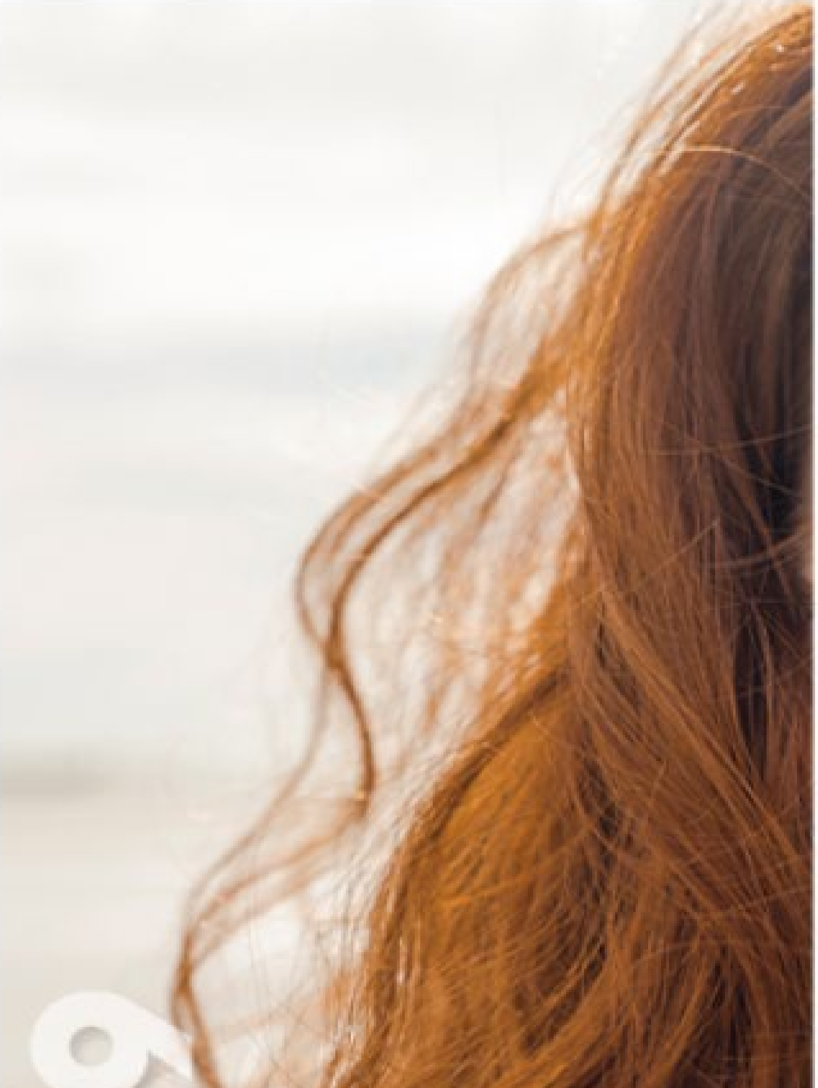

2019
Solvency & Financial
Condition Report


KBC

To the reader

2019 turned out to be a year of challenges for KBC. We had to come up with solutions to deal with far-reaching regulations, new financial players, rapid digitalisation, persistently low interest rates and external factors like Brexit, without being distracted from our main task of helping our clients achieve their dreams and meeting the needs of society. At the same time, further important steps were taken on the sustainability and environment fronts, which you can in full in the Annual Report.

And then we were confronted with the outbreak and spread of coronavirus, which quickly made society's priorities very clear. As an employer and service provider, KBC is doing everything in its power to safeguard the health of its staff and clients, while ensuring that services continue to be provided as usual. We are doing our bit to limit the spread of the virus by allowing as many staff as possible to work from home and by providing clients with advice through a wide range of phone and digital channels. Meanwhile, it is clear that the coronavirus crisis is also having an enormous impact on the economy. At present, we are currently working with the government and other stakeholders to see how we can help deal with the matter at hand. Because, regardless of how the situation pans out, we will continue assuming our responsibility towards society.

Johan Thijs
Chief Executive Officer

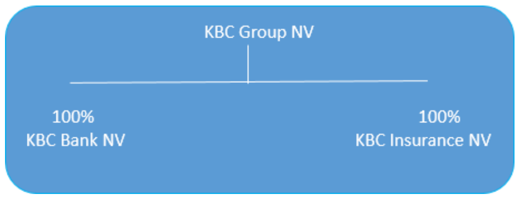
Thomas Leysen
Chairman of the Board of Directors

Company name

KBC Insurance Group contains all consolidated subsidiaries of KBC Insurance NV (mainly the group insurance companies), while KBC Insurance NV refers to the solo (non-consolidated) entity.

Difference between KBC Insurance and KBC Group

KBC Insurance NV is a subsidiary of KBC Group NV. The KBC group's legal structure has one single entity – KBC Group NV – in control of two underlying companies, viz. KBC Bank NV and KBC Insurance NV. All KBC Insurance NV shares are owned (directly and indirectly) by KBC Group NV.



Forward-looking statements

The expectations, forecasts and statements regarding future developments that are contained in this SFCR report are based on assumptions and assessments made when drawing up this report end-March 2020. By their nature, forward-looking statements involve uncertainty. Various factors, in particular the recent Covid-19 crisis, could cause actual results and developments to differ from the initial statements.

Contacts

Investor relations contact details

Kurt De Baenst (General Manager, Investor Relations Office)
IR4U@kbc.be
KBC Group NV, Investor Relations Office, Havenlaan 2, 1080 Brussels, Belgium

Press office contact details

Viviane Huybrecht (General Manager, Corporate Communication/Company Spokesperson)
pressofficekbc@kbc.be
KBC Group NV, Corporate Communication, Havenlaan 2, 1080 Brussels, Belgium

Corporate Sustainability

Filip Ferrante (General Manager, Corporate Sustainability)
csr.feedback@kbc.be
KBC Group NV, Corporate Sustainability, Havenlaan 2, 1080 Brussels, Belgium

Disclosure

In line with its general communication policy, KBC aims to communicate openly with the market about its exposure to risk (see section 4 of this SFCR). Risk management information is therefore provided in a separate section of the 2019 Annual Report of KBC and – more extensively – in this publication.

The most important regulation governing risk and capital management is the Solvency II capital framework applying to insurance entities. Solvency I has been replaced by the fundamentally reformed Solvency II framework, which officially entered into force in January 2016.

Information is disclosed at the highest consolidated level. For more detailed information, please refer to the local disclosures of the entity concerned (for instance, those provided on their websites).

KBC ensures that a representative picture is given at all times in its disclosures. The scope of the reported information – which can differ according to the matter being dealt with – is clearly indicated.

The information provided in this document has not been subject to an external audit. However, the disclosures have been checked for consistency with other existing risk reports and were subjected to a final screening by authorised risk management representatives to ensure quality. In addition, the 2020 Solvency & Financial Condition Report (Activity Year 2019) was distributed to the Group Executive Committee, the Board of Directors, as well as to the Risk & Compliance Committee to ensure appropriate approval was obtained from the management body, as requested under Solvency II.

One-on-one comparison of figures presented in the Annual Report and figures presented in this report cannot always be made due to the different risk concepts used under IFRS and Solvency II. In order not to compromise on the readability of this document, relevant parts of the Annual Report have been reproduced here or, where relevant, clarification is given to explain the differences between the accounting values and the Solvency II values (section 5 of this SFCR).

The Solvency & Financial Condition Report (SFCR) has to be published on a yearly basis by all insurance undertakings and groups. It provides qualitative and quantitative information on the business and performance, the system of governance, the risk profile, the valuation for solvency purposes and capital management of the undertaking.

This report has a harmonised structure that is defined in Annex XX of the Solvency II Delegated Acts Regulation[1] and includes templates defined by the Implementing Regulation[2] that contain quantitative information in the 'Quantitative Reporting Templates (QRTs)'.

All amounts quoted in this report and in the tables are in millions of euros, unless otherwise stated.

This report has been published for some years and therefore comparisons are made with available Solvency II-related data of the previous year.

For the first time there is only one report both for KBC Insurance Group and KBC Insurance NV. Maatschappij voor Brandherverzekering (MVBh) is also included in this report as it was also a separate chapter in the KBC Insurance NV report.

1 Commission Delegated Regulation (EU) 2015/35 of 10 October 2014 (CDR EU 2015_35).

2 Commission Implementing Regulation (EU) 2015/2452 of 2 December 2015 (CIR EU 2015-2452).

Post-balance-sheet events

Significant non-adjusting events between balance sheet date and the date on which the financial statements were approved for publication by the Board of Directors (29 March 2020):

The outbreak and global spread of the coronavirus will exert downward pressure on our results in 2020 (but not have any impact on our financial position at year-end 2019). Given that new government, regulatory and/or sector-related measures are being taken every day, it is impossible at this stage to make a reliable estimate of what the consequences will be for the global economy and, more specifically, for our group. We are, of course, closely monitoring the situation. As always, we are adopting a cautious and conservative approach, even though our solid capital and liquidity positions are such that we are able to withstand extreme scenarios.

Solvency & Financial Condition Report

KBC Insurance Group & KBC Insurance NV SFCR 2020

Activity Year 2019

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Management summary

1 Management summary

ENGLISH VERSION

Highlights in 2019

The KBC Insurance Group (resp. KBC Insurance NV) caters mainly for retail, SME and mid-cap clients. KBC Insurance concentrates on its home markets of Belgium and four countries in Central and Eastern Europe, namely the Czech Republic, Slovakia, Hungary and Bulgaria.

- ✓ All of the material insurance entities are present in KBC's core markets (except for Ireland) and operate according to an integrated bank-insurance model. KBC Group Re is a captive reinsurer providing services out of Luxembourg. KBC Insurance NV accounts for almost 90%[3] of the KBC Insurance Group's overall risk profile;
- ✓ The KBC Insurance Group (resp. KBC Insurance NV) is strongly capitalised in terms of the level and quality of capital. The Solvency II ratio at 31 December 2019 is 202% (resp.215% for KBC Insurance NV), more than double the minimum requirement of 100%;
- ✓ KBC Insurance Group (resp. KBC Insurance NV) has a well-diversified – medium – risk profile, in line with the Risk Appetite Statement (RAS). It benefits from diversified activities that target retail, SME and mid-cap clients across multiple distribution channels;
- ✓ The consolidated result of KBC Insurance Group is 480m EUR in 2019 compared to 469m EUR in 2018, which is an increase of about 10m EUR. The increase compared to last year is primarily caused by a better technical result in both Life and Non-Life businesses, lower taxes and better reinsurance result, largely offset by lower net interest income, a decline in net fee and commission income and higher impairment on shares. For KBC Insurance NV the result 2019 is 352,7m EUR compared to 368m EUR in 2018. This decrease is due to storm damage at the beginning of 2019 and some large claim files;
- ✓ In 2019, earned premiums in Non-Life insurance in KBC Insurance Group were 1.741m EUR, a considerable increase of 9% on the 2018 figure. They grew by 4% in Belgium, by 14% in the Czech Republic, and by 24% in the three other Central and Eastern European markets combined. The increase was recorded in 'car insurance' and in 'property insurance';
- ✓ Earned premiums in Life insurance in KBC Insurance Group amounted to 1.324m EUR in 2019. However, in compliance with IFRS, certain types of Life insurance (i.e. unit-linked products) have been excluded from this figure. If the premium income from these products is included, premium income from the Life insurance business was more than 1,8b EUR, 2% higher than in 2018. Earned premiums in Life insurance grew by 1% at KBC Insurance NV;
- ✓ The combined ratio for Non-Life insurance of KBC Insurance Group came to a healthy 89,9% and to 88,8% (IFRS) for KBC Insurance NV;
- ✓ Operating expenses were 1% lower than in 2018 for KBC Insurance Group. Also for KBC Insurance NV expenses are under control.

3 In terms of Solvency Capital Requirement (SCR).

NEDERLANDSTALIGE VERSIE

Hoogtepunten in 2019

De KBC Verzekeringsgroep (resp. KBC Verzekeringen NV) richt zich voornamelijk op retail-, KMO's en mid-cap-ondernemingen. KBC Verzekeringen concentreert zich op haar thuismarkten in België en vier landen in Centraal- en Oost-Europa, namelijk Tsjechië, Slowakije, Hongarije en Bulgarije.

- ✓ Alle verzekeringsentiteiten zijn aanwezig in de kernmarkten van KBC (behalve voor Ierland) en opereren volgens een geïntegreerd bankverzekeringsmodel. KBC Groep Re is een captive herverzekeraar die diensten aanbiedt vanuit Luxemburg. KBC Verzekeringen NV is goed voor bijna 90% van het globale risicoprofiel van de KBC Verzekeringsgroep;
- ✓ De KBC Verzekeringsgroep (resp. KBC Verzekeringen NV) is sterk gekapitaliseerd in termen van grootte en ook qua kwaliteit van kapitaal. De Solvency II-ratio bedroeg op 31 december 2019 202% (resp. 215% voor KBC Verzekeringen NV), dat is meer dan het dubbele van de minimumvereiste van 100%;
- ✓ KBC Verzekeringsgroep (resp. KBC Verzekeringen NV) heeft een goed gediversifieerde portefeuille met een medium risicoprofiel, dat in lijn is met de RAS (Risk Appetite Statement). De diversificatie tussen activiteiten zowel in retail, in SME alsook bij mid-cap klanten via verschillende distributiekanalen resulteert in positieve resultaten;
- ✓ Het geconsolideerde resultaat van KBC Verzekeringsgroep bedroeg 480m EUR tegenover 469m EUR in 2018, wat neerkomt op een stijging van ongeveer10m EUR. De stijging ten opzichte van vorig jaar is vooral het gevolg van een beter technisch resultaat in zowel het levens- als het schadeverzekeringsbedrijf, lagere belastingen en een beter herverzekeringsresultaat, grotendeels gecompenseerd door lagere netto rentebaten, een daling van de netto provisiebaten en een hogere waardevermindering op aandelen. Voor KBC Verzekeringen NV bedroeg het resultaat 352,7m EUR tegenover 368m EUR in 2018. Deze daling is te wijten aan de stormschade begin 2019 en enkele grote schadegevallen;
- ✓ In 2019 bedroegen de verworven premies in schadeverzekeringen in KBC Verzekeringsgroep in totaal 1.741m EUR, een aanzienlijke stijging van 9% ten opzichte van het voorgaande jaar. Ze stegen met 4% in België, met 14% in Tsjechië en met 24% in de drie andere Centraal- en Oost-Europese markten samen. De stijging werd genoteerd in 'autoverzekeringen' en in 'vastgoedverzekeringen';
- ✓ De verworven premies voor levensverzekeringen in KBC Verzekeringsgroep bedroegen 1.324 m EUR in 2019. In overeenstemming met IFRS zijn bepaalde soorten levensverzekeringen (d.w.z. unit-linked producten) echter niet in dit cijfer opgenomen. Als het premie-inkomen van dergelijke producten wordt meegerekend, bedroeg het premie-inkomen in Leven in totaal meer dan 1,8b EUR, wat 2% hoger is dan in 2018. De verworven premies in Leven stegen met 1% bij KBC Verzekeringen NV;
- ✓ De gecombineerde ratio voor de Niet-Leven activiteiten van de KBC Verzekeringsgroep kwam uit op een gezonde 89,9% en op 88,8% (IFRS) voor KBC Verzekeringen NV;
- ✓ De operationele kosten dalen met 1% in vergelijking met 2018 voor KBC Verzekeringsgroep. Ook voor KBC Verzekeringen NV zijn de kosten onder controle.

Business & performance

2 Business & performance

2.1 Business

2.1.1 Brief presentation of the KBC Insurance Group at year-end 2019

Our area of operation

KBC Insurance is an insurance group catering mainly for retail, SME and mid-cap clients. It concentrates on its home markets of Belgium and four countries in Central and Eastern Europe, namely the Czech Republic, Slovakia, Hungary and Bulgaria.

Main group companies

Belgium	KBC Insurance NV
Czech Republic	ČSOB Pojišt'ovna a.s.
Slovakia	ČSOB Poist’ovňa a.s.
Hungary	K&H Biztosító
Bulgaria	DZI Insurance
Luxembourg	KBC Group Re

Our shareholders

All KBC Insurance NV shares are owned (directly and indirectly) by KBC Group NV. KBC Group NV is a listed company.

Our clients, staff and network

Clients (estimate)	4,9 million
Number of staff (2019 average in FTEs)	3.996
Insurance network	355 agencies in Belgium various distribution channels in Central and Eastern Europe

Our long-term credit ratings (29-11-2019)

	Standard & Poor’s
KBC Insurance NV	A

Management

CEO	Johan Thijs
Chairman of the Board of Directors	Thomas Leysen (Replaced by Koenraad Debackere @ 1/05/2020)

More information

Website	www.kbc.com

Our address

KBC Insurance NV Professor Roger van Overstraetenplein 2 3000 Leuven
Our supervisory authority
National Bank of Belgium De Berlaimontlaan 14 1000 Brussels
Our external auditor
PWC Bedrijfsrevisoren Woluwedal 18 1932 Sint-Stevens-Woluwe

2.1.2 Strategy & business model of KBC Insurance Group

KBC Insurance's strategy is embedded in the strategy of the KBC group, given that we are an integrated bank-insurance group. A summary is provided below of the strategy of the KBC group, where KBC Bank is essentially responsible for the banking business and KBC Insurance for the insurance business. For more detailed information, please see the KBC Group Annual Report for 2019.

How do we create sustainable value?

We want to be able to meet the expectations of all our stakeholders in our core countries and to live up to our commitments. Integrating sustainability in our day-to-day activities is the best guarantee for the creation of long-term value for all these stakeholders.

As an insurer, we enable our clients to operate free of worry and to limit their risks. We work hard every day to provide the best insurance cover at a fair price and we invest in a high-quality claims-handling service, because that will always be the true litmus test of any Non-Life policy. What's more, we use our knowledge of the causes of accidents to develop accident prevention campaigns and we have a long-standing tradition of working with organisations involved in road safety, welfare and victim assistance.

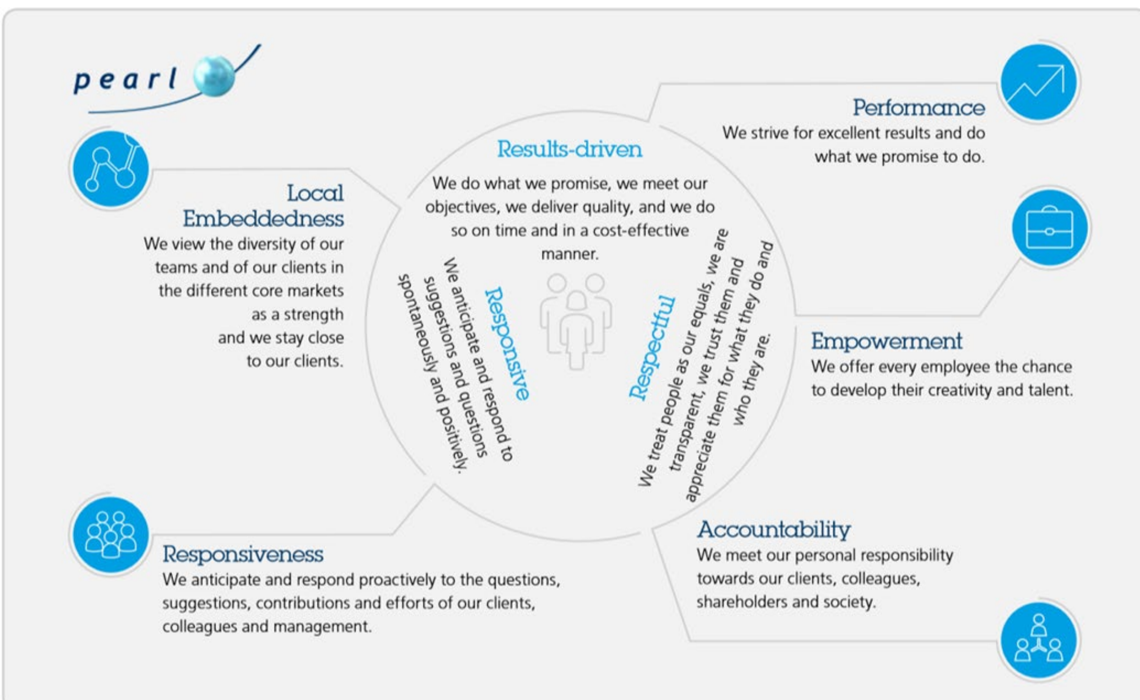
The role we play, especially as an insurer ultimately means that we assume our clients' risks for them. Our highly developed risk and capital management know-how allows us to manage those risks. In the process, we also pay close attention to areas such as cyber risk, anti-corruption measures and climate change risks.

At the same time, we have made a conscious choice to enhance our positive impact on society – where possible – by focusing on areas where we can make a difference as a bank-insurer. The areas in question include financial education, environmental awareness, entrepreneurship and the issue of

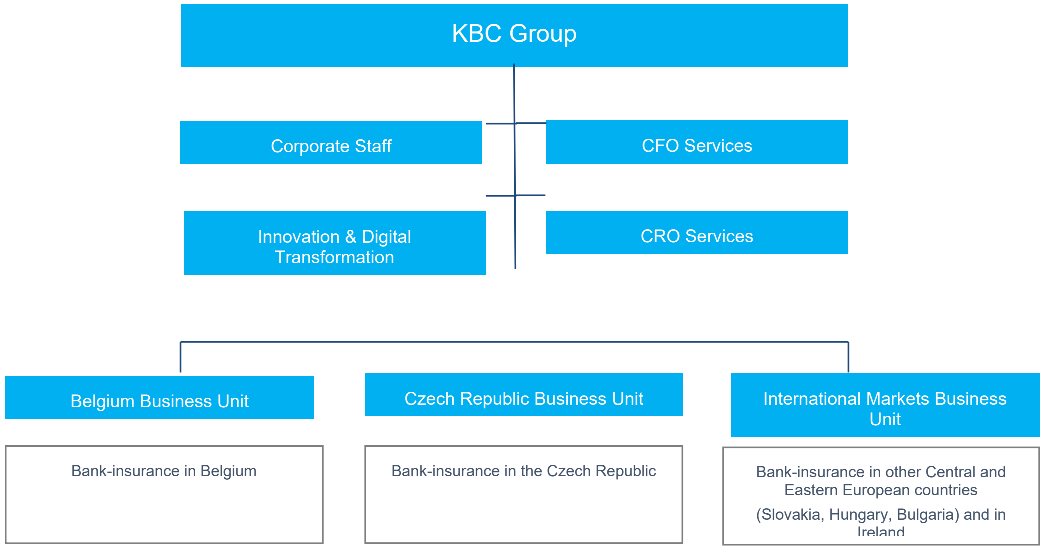
demographic ageing and health. We likewise support social projects that are closely aligned with our business operations and through which we can play our role in society.
What's more, as a major player in each of our core countries, we form part of the local economic and social fabric. We make an important contribution to employment in all our core markets and, as such, recognise that we have a significant direct impact on the lives of our staff. We encourage responsible behaviour on the part of our employees and offer them a fair reward for their work, thereby contributing to the welfare of the countries in which we operate.

What makes us who we are?

We sum up our business culture in the acronym 'PEARL', which stands for **P**erformance, **E**mpowerment, **A**ccountability, **R**esponsiveness and **L**ocal Embeddedness. We also encourage all our employees to behave in a way that is **responsive**, **respectful** and **results-driven**. An explanation of what we mean is given in the diagram.



The Board of Directors is responsible for defining our group's strategy, general policy and risk appetite. It is supported by several specialised committees, namely the Audit Committee, the Risk & Compliance Committee, the Nomination Committee and the Remuneration Committee. Our Executive Committee provides the operational management of the group within the confines of the general strategy approved by the board. Besides the CEO, the Executive Committee includes the Chief Financial Officer (CFO), the Chief Risk Officer (CRO) and the Chief Innovation Officer (CIO) of the group, as well as the CEOs of the three business units.



What differentiates us from our peers? (KBC Group)

Our integrated bank-insurance model

We offer an integrated response to our clients' banking and insurance needs. Our organisation is similarly integrated, with most services operating at group level and the group also managed in an integrated style. Our integrated model offers our clients the benefit of a comprehensive, one-stop financial service that allows them to choose from a wider, complementary and optimised range of products and services. For ourselves, it offers benefits in terms of income and risk diversification, additional sales potential through intensive co-operation between the bank and insurance distribution channels, and significant cost-savings and synergies.

Our strong geographical focus

We focus on our core markets of Belgium, Bulgaria, the Czech Republic, Hungary, Ireland and Slovakia. As a result, we now operate in a mix of mature and growth markets, taking advantage in the latter of the catch-up potential for financial services. We have a limited presence elsewhere in the world, primarily to support activities in our core markets.

Our focus on local responsiveness

We want to build sustainable local relationships with private individuals, SMEs and mid-caps in our core countries. Local responsiveness is very important to us in that regard. It means that we know and understand our local clients better, that we pick up signals effectively and respond to them proactively, that we offer products and services tailored to these local needs, and that we focus on the sustainable development of the different communities in which we operate. Where relevant, we facilitate collaboration among core countries to avoid duplicating our efforts and to offer our clients the best solutions.

Our approach to sustainability

Sustainability is not a separate policy at KBC, but an integral part of our overall business strategy, which is anchored in our day-to-day activities. Our sustainability strategy, which is geared towards the local economy and society, consists of three cornerstones: encouraging responsible behaviour on the part of all our employees, increasing our positive impact on society and limiting any adverse social impact we might have.

Our shareholder structure

A special feature of the KBC Group shareholder structure is the core shareholder syndicate consisting of Cera, KBC Ancora, MRBB and the other core shareholders, which together held roughly 40% of the shares at the end of 2019. These shareholders act in concert, thereby ensuring shareholder stability in our group.

Our strengths				
A well-developed and unique omnichannel bank-insurance and innovative digital strategy, which enables us to respond immediately to our clients' needs	Strong commercial banking and insurance franchises in all our business units	Successful track record of underlying business results	Solid capital position and strong liquidity	Firmly embedded in the local economies of our core countries

Our challenges			
Macroeconomic environment characterised by low interest rates, demographic ageing and geopolitical and climate-related challenges	Stricter regulation in areas like client protection, solvency and the environment	Changing client behaviour, competition and new players in the market	New technologies and cyber crime

In what environment do we operate?

The main challenges facing us are, of course, the economic situation, intensifying competition and technological change, regulation, and cyber and ICT risks. The way in which we are dealing with them is set out below.

The world economy, geopolitical challenges and the environment

The world economy, the financial markets and demographic developments influence our results. Persistently low interest rates have become an important factor in recent years, exerting significant pressure on income and prompting a search for yield. Demographic ageing is also a challenge, for our Life insurance business, for instance. There is a risk, moreover, of corrections in markets where an imbalance may have built up. Geopolitical developments could also have significant implications for the economy and hence our results. The same goes for global health risks, climate change and the transition to a low-carbon society.

How are we addressing them?

- ✓ We ensure in our long-term planning/scenario that our capital and liquidity position is capable of withstanding a negative scenario.
- ✓ The environment and climate change form an important part of our sustainability strategy.
- ✓ We take proactive measures. Examples include adjusting our offering to take account of demographic ageing (such as insurance policies relating to health care) and of demand for sustainable products like Green Bonds and sustainable pension saving.
- ✓ We calculate the potential impact of changes in key parameters and estimate the impact of material events as effectively as possible.
- ✓ We aim to diversify our income sources further to include more fee business, for example, alongside interest income.

Shifting client behaviour and competition

We face strong competition, technological changes and shifting client behaviour. Besides the traditional players, there is intensifying competition from online banks, fintechs, bigtechs and e-commerce in general. This potentially means pressure on cross-sell opportunities and is influencing client expectations, including speed and digital interaction. All this is increasing the significance of digitalisation and innovation within our group and an effective framework for it and creating the need for a resilient, responsive organisation capable of continuously adapting its processes and systems.

How are we addressing them?

- ✓ The creative input and training/diversity of our employees is exceptionally important when it comes to equipping ourselves to deal with competition and technological change.
- ✓ We can draw on an immense volume of data, which enables us to understand more clearly what clients really want. What's more, our integrated model allows us to offer our clients more comprehensive solutions than pure banks or insurers can.
- ✓ We have a process in place to ensure that the business side receives approval efficiently for new product launches. The process also includes a thorough examination of the potential risks. We regularly review all our existing products, so that they can be adapted to take account of evolving client needs or changing circumstances.
- ✓ Research and development have been performed at a variety of group companies as part of a programme to develop new and innovative financial products and services. Over the past few years, we have launched numerous successful mobile and other innovative apps (examples are provided in the 'Our business units' section).
- ✓ Where possible, applications are copied across the group's different home markets. We are also open to partnerships with fintech firms or even sector peers.
- ✓ In addition to innovation and digitalisation, we are working hard to simplify products and processes.

Regulation

Increasing regulation is an issue for the financial sector as a whole. In addition to legislation already in force, such as GDPR, MiFID II, MiFIR and PSD2, it includes the following in the years ahead:

- ✓ The further implementation of the Benchmark Regulation, which entails a thorough reform of the interest-rate benchmarks used for market transactions, credit contracts, accounts and securities issues.
- ✓ The reform of the European Market Infrastructure Regulation (EMIR), which will have an operational impact on our group-wide derivatives trading activities.
- ✓ EU measures to mobilise financial resources for sustainable growth (including a duty to report on environmental, social and governance factors).
- ✓ The draft Regulation on privacy and electronic communication, which is expected in 2020–21 and which will include tighter rules for the use of electronic communication data.
- ✓ Enshrining EU procurement guidelines (EBA, EAVB) in national law.
- ✓ Amendments to the Bank Recovery and Resolution Directive (BRRD2) and the Capital Requirements Regulation (CRR2) and Capital Requirements Directive (CRD5), as well as the ongoing implementation of the Basel IV legislation at both EU and national level.
- ✓ New IFRS, including IFRS 17, which applies to insurance activities and will become effective in a few years' time.

How are we addressing them?

- ✓ We are making thorough preparations for the new regulations. Specialised teams keep close track of the rules and propose the necessary responses in terms of the group's capital planning, for instance.
- ✓ We study the impact of regulations on client behaviour and, where appropriate, adjust our products and processes to take account of shifts in that behaviour.
- ✓ We participate in working groups at sector organisations, where we analyse draft texts
- ✓ A special team focuses on contacts with government and regulators.
- ✓ We produce memorandums and provide training courses for the business side.

Cyber risk and information security

Robust ICT systems are extremely important in an increasingly digital world where hacking and cyber-attacks are a constant threat, with the potential to cause significant financial and reputational harm.

Our focus is on the optimum protection of both our clients and our group itself.

How are we addressing them?

- ✓ We raise our employees' awareness of cyber risks by providing training in areas like phishing and vishing, and fraud in general.
- ✓ We work to achieve highly secure and reliable ICT systems and robust data protection procedures, and we constantly monitor our systems and the environment.
- ✓ We analyse cyber risks from an IT and business perspective, so that we can offer maximum resistance and are able to remedy attacks swiftly and efficiently. We regularly evaluate our action plans and adapt them.
- ✓ A certified Cyber Expertise & Response Team focuses on cyber-crime, informs and assists local entities, tests KBC's defence mechanisms and provides training and cyber-awareness in the group. A group-wide Competence Centre for Information Risk Management concentrates on the risks associated with information security and cyber-crime, and on operational IT risks.
- ✓ We are members of the Belgian Cyber Security Coalition – a knowledge and consultative platform consisting of around 50 public and private-sector enterprises and academics.
- ✓ We also have our entities' cyber risks and defence mechanisms evaluated on an annual basis by an international team of internal information security experts.

Our employees, capital, network and relationships

As a financial group, we draw on many different types of capital, including our employees and our capital base, but also our brands, reputation and capacity to innovate, our relationships with all our stakeholders, our branches, agencies and electronic networks, and our ICT infrastructure.

- ✓ Our employees

Our HR policy features individual focuses in each country, so that we can respond in an optimum way to the local labour market. Our values group-wide, however, are the same and are founded on our PEARL business culture. It is our employees who give it tangible shape each day in all our group's core countries.

Our staff are working together increasingly within multidisciplinary teams. Projects are approached in an agile manner and deliver results in a series of short throughput cycles. This translates into more rapid innovations for our clients. It also encourages our staff to think creatively and to take on new roles, which in turn opens up the prospect of a richer career path aligned with each person's individual talents. We are well aware that this resilience on the part of our employees also enables us to anticipate our client's wishes and respond proactively to increasing digitalisation.

We realise that good managers are key when it comes to bringing out the best in our employees and implementing our strategy successfully. We invest in the training of all managers through leadership programmes that are regularly tested against developments within our company and society. There is an increased focus, for instance, on coaching and progression management.

We view self-development as key to professional growth, along with KBC. Our staff can choose among a wide range of training methods, including e-learning, workplace coaching and traditional courses to acquire new skills. New digital skills certainly form a challenge in that respect.

It remains our firm ambition to make our organisation and staff as future-proof as possible.

We do not make any distinction on the grounds of gender, religion, ethnic background or sexual orientation in our HR, recruitment and promotion policies or remuneration systems.

The application of our HR policy is closely monitored, not only by means of high-quality surveys, but also on the basis of accumulated HR data. We invest in good social dialogue with employee representatives.

We use an operational risk framework to perform an annual review of key risks in the HR process. The implementation and monitoring of legislation forms an important part of this process and we ensure that it is applied strictly in the area of HR.

'People risk' is an important operational risk for human resources, which we closely track in collaboration with our risk department via a 'people risk dashboard'. In a financial sector that is changing very quickly, we would not be able to remain a reference in the European financial sector without the right employees with the right skills. The KBC Group Annual Report contains a table with an overview of the total workforce and a breakdown into various categories.

- ✓ Our capital

Our activities are only possible if we have a solid capital base. At year-end 2019, KBC Group's total equity came to 20,4b EUR. Its capital was represented by 416.394.642 shares at year-end 2019, an increase of 238.966 shares on the previous year, due to the capital increase reserved for staff in December each year. At year-end 2019, KBC Insurance total equity was 3,4b EUR.

KBC Group is the sole shareholder of KBC Insurance. KBC Group shares are held by a large number of shareholders in a number of countries. A group of shareholders consisting of MRBB, Cera, KBC Ancora and the Other core shareholders, constitute KBC Group's core shareholders. A shareholder agreement was concluded between these core shareholders in order to ensure shareholder stability and guarantee continuity within the group, as well as to support and co-ordinate its general policy. To this end, the core shareholders act in concert at the General Meeting of KBC Group NV and are represented on its Board of Directors. The current agreement applies for a ten-year period with effect from 1 December 2014. According to the most recent notifications, the core shareholders own 40% of our shares between them. More information on the KBC Group's shareholder structure can be found in the KBC Group Annual Report. The KBC Insurance share is not traded on the stock market.

- ✓ Our network and our relationships

Alongside staff and capital, our network and relationships are especially important to our activities. An overview of our network can be found under 'Market conditions in our most important countries in 2019'.
Our social and relationship capital comprises all relationships with our clients, shareholders, government, regulators and other stakeholders who enable us to remain socially relevant and to operate as a socially responsible business.

The core of our strategy for the future

Our strategy rests on **four principles**:

- ✓ We place our clients at the centre of everything we do;
- ✓ We look to offer our clients a unique bank-insurance experience;
- ✓ We focus on our group's long-term development and aim to achieve sustainable and profitable growth;
- ✓ We meet our responsibility to society and local economies.

We implement our strategy within a strict risk, capital and liquidity management framework.

To us, corporate sustainability means the ability to live up to the expectations of all our stakeholders and to meet our obligations, not just today but also in the future. Our sustainability strategy consists of financial resilience and three cornerstones:

- ✓ encouraging responsible behaviour on the part of all employees;
- ✓ enhancing our positive impact on society;
- ✓ limiting any negative impact we might have on society.

The client is at the centre of our business culture

We have to earn our clients' trust every day. We work hard to offer them complete, accessible and relevant solutions at a fair price and to achieve an optimum client experience. That means taking their needs rather than our banking or insurance products as our starting point.
We have to adapt constantly to a highly dynamic environment, the changing behaviour and expectations of our clients and new technologies. For that reason, we listen to our clients all the time and keep our finger on the pulse when launching new products. At the same time, we're aware of current issues and developments in society. The insights we gain in this way are vital if we are to grow in line with our clients and community.
We continue to provide a proactive and integrated response to our clients' banking and insurance needs in this more digital world too, in the shape of a comprehensive, one-stop financial service, in which they can choose from a wider, complementary and optimised offering. We are investing around 1,5b EUR in digital transformation between 2017 and year-end 2020 and continue to align our omnichannel distribution network with changing client behaviour.
This approach also entails further internal simplification of processes, systems and products.
Privacy and data protection are an integral part of our profession as a bank-insurer. Digitalisation provides us with a multiplicity of data, which means we know our clients better and can advise them more effectively. But it goes without saying that clients only accept us analysing their data once they already trust us, which is why we have drawn up a carefully thought-out privacy policy.
We expect our employees to communicate in an accessible, clear, understandable and transparent way with our clients.
The most important Key Performance Indicators (KPIs) relating to the client being put at the heart of everything we do, are set out in the KBC Group Annual Report.

We offer our clients a unique bank-insurance experience

As a bank-insurer, we put our clients at the heart of what we do by offering them an integrated range of products and services. We advise them based on needs that transcend pure banking or insurance, including family, the home and mobility. We are organised in such a way that we approach the client with both insurance and banking solutions tailored to their individual needs. After all, our clients don't dream about loans or insurance policies, but about a car, a house, a holiday or a business of their own – things for which they need money. And when they have them, they want to protect them, so they look for insurance too. Thanks to our integrated bank-insurance model, we can offer them an answer to each of those concerns.
We have developed a unique bank-insurance co-operation concept within our group, a model that goes much further than a bank that sells insurance products. It is all about complete back-office integration, which delivers operational and commercial optimisation for both the client and for KBC itself. The roll-out of the model varies from one country to another.
Our bank-insurance model also enables us to achieve various commercial synergies. The most important Key Performance Indicators (KPIs) relating to bank-insurance are set out in the KBC Group Annual Report.

We focus on sustainable and profitable growth

Developing long-term relationships with our clients is crucial if we are to secure our long-term future. Therefore, we do not pursue high short-term returns that come with excessive risks but rather focus on sustainable and profitable growth in the long run.

Sustainable and long-term thinking also means concentrating on the local economies of our core markets. Our geographical footprint remains firmly focused on our core countries. We view our presence in these countries as a long-term commitment and want to consolidate our presence there by means of organic growth or attractive acquisitions, in line with clear and strict strategic and financial criteria.
The pursuit of sustainable and profitable growth also coincides with the search for a diversified income base. In that respect, we want to generate more revenue from the fee business (including fees from asset management activities) and insurance activities, alongside our interest income. We are also diversified in geographical terms: almost half of our net profit, for instance, was already derived in countries other than the Belgium Business Unit in 2019.
We also want to build on the one-stop-shop offering to our clients through partnerships with fintech firms or even sector peers, and to offer services related to bank-insurance.
Moreover, stringent risk management in everything we do is an absolute precondition in terms of guaranteeing sustainability. For more information on this, see 'We aim to achieve our ambitions within a stringent risk management framework'.
The most important Key Performance Indicators (KPIs) relating to sustainable and profitable growth are set out in the KBC Group Annual Report.

Our role in society: to be responsive to society's expectations

We are determined at KBC to pursue a sustainable path – one that puts the client at the centre of what we do and will enable us to satisfy our stakeholders' expectations. We want to establish contact with all our stakeholders and to earn and strengthen their trust by listening to them about the role we can play in society and how we can serve them better.
Wherever possible, we will offer financial solutions that have a positive impact on society and the local economy. We are also focusing on limiting any adverse impact we might have on society and encouraging responsible behaviour on the part of our employees. For that reason, sustainability has been integrated throughout our business operations and is supported by all our employees. Doing business sustainably also means, lastly, that we must have the necessary financial resilience and strictly manage our risks. We constantly pursue a balance, therefore, between healthy profitability and fulfilling our role as a socially responsible business.

- ✓ Aiming to encourage responsible behaviour on the part of all our employees

The basis of responsible behaviour is integrity, which requires honesty, fairness, transparency and confidentiality, as well as a healthy awareness of risk. Integrity and ethical values are also reflected in our 'Code of Conduct for KBC Group Employees'.
We communicate transparently on our rules and policy guidelines, which are published at www.kbc.com/en/policies.

- ✓ Sustainable Development Goals (SDGs)

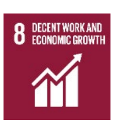
In 2015, the United Nations drew up a development plan with 17 ambitious targets for 2030. We acknowledge our role as an important actor in society and we want to contribute to the economic well-being of companies, private individuals and governments and to support them in achieving better social outcomes. Although the 17 SDGs are all interconnected and relevant, we have selected five goals on which we can have the greatest impact through our core businesses of banking, insurance and asset management. The five goals are set out in the diagram and table below. You can find more information in this regard in our 2019 Sustainability Report, that will be published shortly after the Annual Report on www.kbc.com.

Good health and well-being

We aim to develop banking and insurance products that focus on health, health care and improving quality of life. Our social projects focus on themes like health and road safety. We promote a good work-life balance among our employees.

Affordable and clean energy

We actively contribute to raising the share of renewables in the energy mix. We invest in initiatives in the field of renewable energy and energy efficiency through our banking and insurance activities and have drawn up an exit programme for the financing of non-sustainable energy solutions.



Decent work and economic growth

Our banking and insurance business supports entrepreneurship and job creation and contributes to sustainable economic growth. We support new businesses and invest in innovation and technology through alliances with start-ups and fintechs. We play an important role in protecting basic labour rights, fair pay, equal opportunities and training and development opportunities for all our employees.

Responsible consumption and production

We support the transition to a low-carbon and circular economy. We develop sustainable banking and insurance products and services that meet a range of social and environmental challenges. Sustainable investments are offered as a fully fledged alternative to conventional funds. We endeavour to mitigate our own negative impact on the environment by dealing sustainably with energy, paper, water, mobility and waste and by reducing our greenhouse gas emissions.

Climate action

We apply a strict environmental policy to our loan, investment and insurance portfolios. We develop business solutions that help clients reduce their greenhouse gas emissions and make the transition to a low-carbon economy. We limit our own environmental impact and communicate on that. We seek to address climate-related risks and focus on related opportunities in that area.

- ✓ Aiming to enhance our positive impact on society

We want to enhance our positive impact on society to which end we are focusing on areas in which we, as a bank-insurer, can create added value: financial literacy, entrepreneurship, environmental awareness and demographic ageing and/or health. In doing so, we take account of the local context in our different home markets. We likewise support social projects that are closely aligned with our policy and through which we can play our role in society. These areas are used to incorporate the SDGs into our sustainability strategy and everyday activities. More information and examples are provided in the KBC Annual Report 2019.
We take a closer look elsewhere at our specific approach to climate and human rights.

- ✓ Limiting any negative impact we might have on society

We apply strict sustainability rules to our business activities in respect of human rights, the environment, business ethics and sensitive or controversial social themes. In the light of constantly changing societal expectations and concerns, we review and update our sustainability policies at least every two years. You can find a table with the most important of these policies in the KBC Annual Report 2019.
We take a closer look at our specific approach to climate and human rights later in this section.

We monitor compliance with our sustainability policy in a number of ways:

- Active internal screening of the application of our sustainability policy to our lending, insurance and investment operations;
- A general ESG assessment of the sustainability performance of the relevant companies by external parties, with the emphasis on sustainability strategy and companies' public sustainability strategy and on any recent controversies in which they have been involved.

Examples of measures in the event that infringements are detected:

- Zero tolerance across all our business activities for companies on the blacklist;
- Exclusion of companies that do not comply with the UN Global Compact Principles, as assessed by an external ESG evaluator, for loans, insurance and own assets;
- Enforcement, in consultation with the relevant parties, of an exit strategy or specific conditions on existing credit or insurance relationships and advisory services, and the rejection of new applications.

- ✓ Our sustainability governance

We have anchored sustainability at the different levels within our group, guaranteeing that it receives attention from the highest decision-making bodies while also being broadly integrated into our operations. You can find more details later in this report regarding specific governance in respect of climate change.

The Group Executive Committee reports to the **Board of Directors** on sustainability matters, including policy on climate change.

The **Executive Committee** is the highest level with direct responsibility for sustainability, including policy on climate change. The CFO has been designated as Executive Committee member responsible for climate.

The **Corporate Sustainability Division** is responsible for developing the sustainability strategy and implementing it across the group. The team monitors implementation of the strategy and informs the Executive Committee and the Board of Directors on progress twice per year via the KBC Sustainability Dashboard.
A special team with representatives from different divisions focuses on climate change (Sustainable Finance programme).

The **Internal Sustainability Board** is chaired by the CEO and comprises senior managers from all business units and core countries and the Corporate Sustainability General Manager. The sustainability strategy is drawn up, implemented and communicated under the authority of the Internal Sustainability Board.

The local sustainability departments in each of the core countries support the senior managers on the Internal Sustainability Board with integrating the sustainability strategy and organising and communicating local sustainability initiatives. **CSR committees** in each country supply and validate non-financial information.

Business units and countries: Sustainability is anchored in the core activities.

In addition to our internal organisation, we have set up external advisory boards to advise KBC on various aspects of sustainability. They consist of experts from the academic world:

- An **External Sustainability Board** advises the Corporate Sustainability Division on KBC sustainability policies.
- An **SRI Advisory Board acts as an independent body for the SRI funds and oversees screening of the socially responsible character of the SRI funds offered by KBC Asset Management.**

✓ Our objectives

We also use Key Performance Indicators (KPIs) in the KBC Sustainability Dashboard to see whether we are focusing sufficiently on socially relevant themes and whether we are meeting stakeholder expectations.
The most important Key Performance Indicators (KPIs) relating to our role in society are set out in the KBC Group Annual Report.

Focus on climate

Climate change is one of the greatest challenges facing the world in the 21st century, which is why we have committed ourselves to the transition to a low-carbon society. We recognise that our activities have an impact on the environment and that climate change can affect our business model. We are aware at the same time of the leverage we can exert on behalf of the sustainable development of the planet. For that reason, we will pursue constant progress in our policy and our targets. 2019 saw a milestone in our climate strategy, when we signed up to the Collective Commitment to Climate Action and pursuit of the Paris climate accord targets. We also launched a structural approach to the management and reporting of climate-related risks and opportunities via our Sustainable Finance Programme.

We are convinced that communicating transparently on climate-related effects will encourage the progress needed to limit global warming. In December 2017, therefore, we endorsed the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD).
For more detailed information, see the KBC Group Annual Report 2019.

Focus on human rights

We meet our responsibility to respect human rights, social justice and employment rights throughout the group, and we undertake to respect the letter and the spirit of: (i) the Universal Declaration of Human Rights; (ii) the principles concerning fundamental rights in the eight International Labour Organisation core conventions as set out in the Declaration on Fundamental Principles and Rights at Work; (iii) the UN Declaration on the Rights of Indigenous Peoples; and (iv) the UK Modern Slavery Act, to which end KBC has published a Modern Slavery Statement since 2017. We are also UN Global Compact signatories and have incorporated the ten principles on human rights, labour, environment and anti-corruption in our policies, so that they are applied throughout our activities. We have published our progress since 2006 in the annual UN Global Compact Statement of Continued Support. It goes without saying that we comply with local laws, rules and regulations wherever we operate and with international and regional human rights treaties containing internationally recognised standards by which the business sector must abide. We use the UN Guiding Principles Reporting Framework to monitor our human rights policy, as described in the KBC Group Policy on Human Rights. Our human rights policy applies to our business activities (clients and suppliers) and also to our own internal operations (employees). For more detailed information, see the KBC Group Annual Report 2019.

We aim to achieve our ambitions within a stringent risk management framework

Risk management is an integral part of our strategy and our decision-making process.

- ✓ We perform risk scans to identify all key risks;
- ✓ We define our risk appetite in a clear manner;
- ✓ We translate that into strict limit tracking per activity and business unit;
- ✓ We monitor the risk profile of existing and new products via a New and Active Product Process;
- ✓ We challenge the results of the periodic planning process via stress tests;
- ✓ We have installed independent chief risk officers in all relevant parts of our organisation.

Our 'Three Lines of Defence' model	
1	The business operations side is responsible for managing its risks
2	The second line of defence comprises the control functions, i.e. the risk and compliance functions, which ensure that risks are identified and managed by the business side
3	As independent third line of defence, Internal Audit provides support to the Executive Committee, the Audit Committee and the Risk & Compliance Committee in monitoring the effectiveness and efficiency of the internal control and risk management system

Although the activities of a large financial group are exposed to risks that only become apparent in retrospect, we can currently identify a number of major challenges for our group. As a bank-insurer, we are also exposed to the typical risks for the sector, such as credit risk, market risk, technical insurance risk, liquidity risk, solvency risk and non-financial risks.

Sector-specific risks	How are we addressing them?
Credit risk The potential negative deviation from the expected value of a financial instrument caused by default on the part of a party to a contract, due to the inability or unwillingness of that party to pay or perform, or due to particular measures on the part of political or monetary authorities in a particular country.	• Existence of a robust management framework • Recording impairment charges, taking risk-mitigating measures, optimising the overall credit risk profile, reporting, stress testing, etc. • Limit systems to manage concentration risk in the loan portfolio
Market risk in trading activities The potential negative deviation from the expected value of a financial instrument caused by fluctuations in the level or volatility of market prices, such as interest rates, exchange rates, and share and commodity prices.	• Existence of a robust management framework • Historical VaR method, BPV and basis risk limits, 'greeks' and scenario limits for products with options, stress tests, etc.
Non-financial risks Operational risk is the risk of loss resulting from inadequate or failed internal processes and systems, human error or sudden external events, whether man-made or natural. Compliance risk is the risk of losses or sanctions due to failure to comply with laws and regulations promoting integrity, and with internal policies and codes of conduct reflecting the institution's own values. It includes conduct risk, i.e. the current or prospective risk of losses arising from inappropriate supply of financial services, including cases of wilful or negligent misconduct. Climate risk is the risk associated with the transition to a low-carbon economy and the risk from climate-related physical events that impact our business. Other non-financial risks include reputational risk, business risk and strategic risks.	• Existence of a robust management framework • Group key controls, risk scans, key risk indicators, etc. • Risk scans and developing new methodologies together with external parties • Strict acceptance policy, stress tests, monitoring, etc. .
Market risk in non-trading activities Structural market risks, such as interest risk, equity risk, real estate risk, spread risk, currency risk and inflation risk, are risks inherent to the commercial activity or long-term positions.	• Existence of a robust management framework • Basis Point Value (BPV), sensitivity of net interest income, sensitivity per risk type, stress tests, limit tracking for crucial indicators, etc.
Liquidity risk The risk that an organisation will be unable to meet its obligations on time, without incurring higher-than-anticipated costs.	• Existence of a robust management framework • Drawing up and testing emergency plans for managing a liquidity crisis • Liquidity stress tests, management of funding structure, etc.
Technical insurance risks Risks stemming from uncertainty as to how often insured events will occur and how extensive they will be.	• Existence of a robust management framework • Underwriting, pricing, claims reserving, reinsurance and claims handling policies, etc.

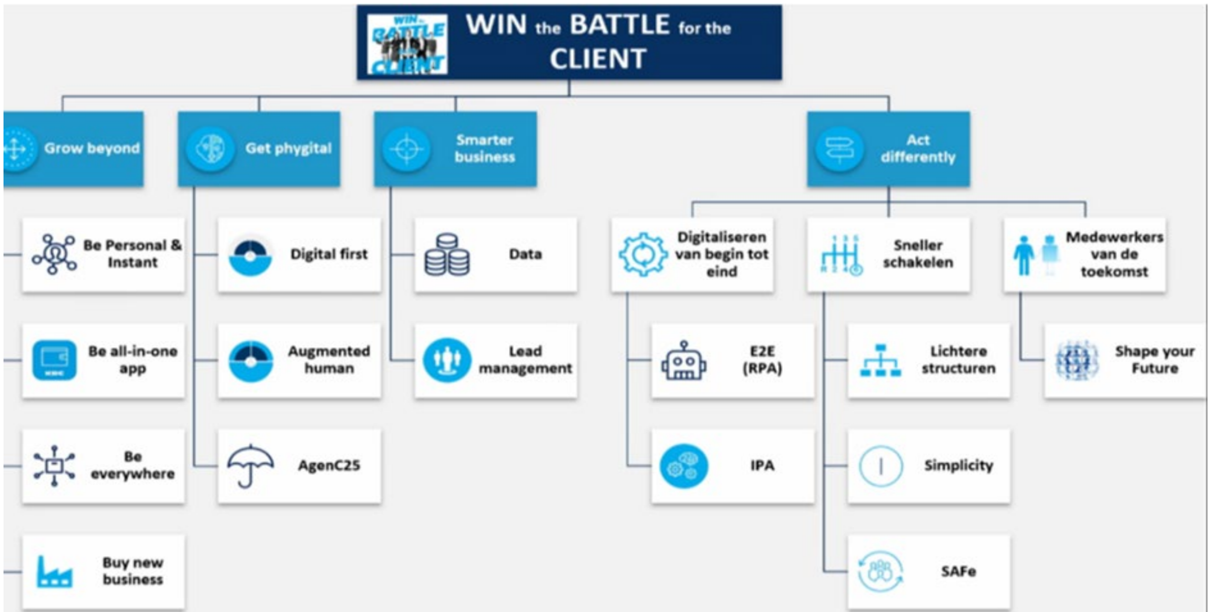
The most important Key Performance Indicators (KPIs) relating to solvency and liquidity are set out in the KBC Group Annual Report.

2.1.3 Strategy & business model of KBC Insurance NV

KBC Insurance NV's strategy is fully aligned with KBC's corporate strategy and centered around the ambition to "Win the battle for the client". The program is built around **4 strategic focus points and underlying principles:**

- ✓ **Grow beyond**: We continue to grow our services via our own channels and those of other parties;
- ✓ **Get phygital**: We aim for an optimal mix of physical and digital customer contact;
- ✓ **Smarter business**: We will work in the commercial segment on the basis of thorough data analysis and lead management;
- ✓ **Act differently**: As KBC employees, we are also evolving and preparing ourselves and our organisation for the future.

It is summarized in the figure below:



IPA = Intelligent Process Automation - SAFe=-Scaled Agile Framework

Figure 1: Overview strategic update KBC Insurance NV

Grow beyond: In order to grow our business we want to use both our own channels and those of other parties. In our own channels we focus on a personal and instant customer experience with a digital service offering when possible and human where needed. We also offer access to third party products and services in our own channels, as a means to attract both customers and prospects to our platform and sales channel. In order to provide a frictionless journey we will use data for on the spot risk assessment & instant personal pricing.

We will also sell our own products via partner channels to ensure that we are present when the customer needs us. We are also looking into opening up our solutions to non-covered claims and prospects to boost revenue. We also remain vigilant to detect investment opportunities in new things that will help us to stay relevant for our customers.

Get phygital: We need to manage the transformation of our distribution model towards a more dynamic digital and physical mix. We will move to a model in which our digital offering becomes the basis, supported and complemented by human aspects where this provides added value to our customers.

The human touch therefore remains indispensable, but also human interaction will be digitally supported in order to offer customers an excellent experience. This is our commitment to the optimal mix of digital and physical customer contact, where our agent as human contact is seamlessly connected to the customer’s digital journey.

Smarter business*:* Customers expect info & tailor-made advice, while changing channel usage diminishes the direct relationship with the customer. Due to these contradictory changes, we need to make smarter use of customer data to obtain better-quality leads. A personalized, relevant lead triggers each individual customer, either directly online or during a conversation with a KBC employee.

Act differently: Our first three strategic objectives are all about preparing our commercial operations for the future. But, to be able to realize these, we will also have to act differently: further simplifying and digitizing, being able to switch gears more quickly and deal flexibly with the changing context, both as an organization and as individuals.

In order to act differently we focus on three aspects related to our internal organization:

End-to-end digitization: We therefore continue to simplify and automate our processes end-to-end. This enables us to work more efficiently and flexibly and achieve our digitization goal. E. g. in claims handling we will enable our customers to steer their claim handling fully digitally while increasing the use of artificial intelligence to speed up the claims process.

Shifting gears more quickly: We also reduce decision levels, work with multi-disciplinary teams and introduce new forms of project work to become even faster and more agile.

Employees of the future: We provide the resources and support so that everyone can take their responsibility to grow and make KBC fully future-proof together. We therefore continue to strengthen the performance culture and leadership capabilities to deal successfully with changes.

2.2 Underwriting results in our home markets

2.2.1 The world economy

The worldwide slowdown in growth that began in 2018 continued in 2019. US protectionism triggered escalating trade disputes and put a damper on global economic sentiment. The drawn-out Brexit negotiations weighed similarly on economic growth in Europe. On the other hand, domestic consumer spending continued to contribute substantially to growth in most regions, thanks primarily to strong labour markets with robust job creation and pay growth and healthy consumer confidence.

Euro area inflation fell again in 2019, due in particular to volatile components like the oil price. Underlying inflation remained broadly constant at a low level. Combined with deteriorating economic performance in the euro area and increasing risks, the ECB revived its policy of quantitative easing in November 2019. The deposit rate was also cut further to -0.50%. Interest rates – especially at the longer end – and rate spreads within the EMU remained very low as a result. The above risks and uncertainties also prompted investors to seek refuge in 'safe haven' debt securities. Consequently, the yield on ten-year German and US government paper recorded a historical low at the end of the summer of 2019.

The European economy then staged a gradual general recovery, making the outlook for 2020 somewhat brighter. Unfortunately, the outbreak and global spread of the coronavirus changed this outlook. It is now generally expected that the world economy will grow at a significantly slower pace in 2020 and that the recovery will start in the second half of the year at the earliest. As an open economy, Europe is quite vulnerable to the direct and indirect economic consequences of the Covid-19 crisis. The policy response to this crisis has been robust. However, the extent to which the measures involved will counteract the slowdown is still largely uncertain.

US economic growth also slowed down in 2019, but remained surprisingly stable in the second half of the year. The positive impact of government stimulation measures and a tax reform in 2017 petered out. What's more, trade conflicts and the deteriorating economic climate put a brake on US activity. The Federal Reserve responded by relaxing its monetary policy once again, cutting its key rate by 25 basis points three times. The unwinding of its balance sheet was also halted earlier than planned. Fearing the economic consequences of the Covid-19 crisis, the Fed surprisingly cut rates again, the first time by 50 basis points in early March 2020 and then by 100 basis points in mid-March 2020. The Fed hopes that, by making this move, it will limit the impact of the Covid-19 crisis on the US economy. In the meantime, budgetary stimulus measures are being taken in the US to supplement the more flexible monetary policy there. The Chinese economy was hit hard by the US-Sino trade war, but will take a much bigger bruising from the Covid-19 crisis and the drastic measures implemented by the Chinese government to fight the virus. The additional stimulus provided by China's government and central bank will soften the downturn only to a limited extent. The gradual recovery of the Chinese economy will support a vigorous economic recovery in Europe, though the continuing slowdown of growth in the US is bad news for Europe's economy too. At present, the European economy can count on some support from lower oil prices caused by the recent oil price war between Saudi Arabia and Russia.

2.2.2 Market conditions in our home countries in 2019

Belgium

Market environment

- The Belgian economy maintained a path of steady but moderate expansion, with real GDP growth of 1,4%.
- Belgian growth was still favourable overall, but supported exclusively by domestic demand.
- Inflation stood at 1,2%, down substantially on its 2018 level.
- Forecast real GDP growth in 2020* of 0,8%.

KBC Group in Belgium

- ✓ Main brands: KBC, KBC Brussels and CBC
- ✓ 355 insurance agencies, electronic channels
- ✓ Estimated 13% share of the market for life insurance and 9% for non-life insurance
- ✓ 3.5 million clients (insurance alone: 0.8 million clients)
- ✓ 29.4b EUR in technical provisions and liabilities under investment contracts

Czech Republic

Market environment

- Real GDP growth eased to 2,4%.
- Consumer spending was supported by wage increases and job creation, but less so than in previous years.
- Inflation averaged 2,6% in 2019.
- Forecast real GDP growth in 2020* of 1,8%.

KBC Group in the Czech Republic

- ✓ Main brand: ČSOB
- ✓ Various distribution channels for insurance, electronic channels
- ✓ Estimated 8% share of the market for life insurance and 8% for non-life insurance
- ✓ 4,2 million clients (insurance alone: 1,6 million clients)
- ✓ 1,7 b EUR in technical provisions and liabilities under investment contracts

Slovakia

Market environment

- Real GDP growth eased to 2,3%.
- The cooling down of industry and a slowdown in German growth had a clearly negative impact on the Slovakian economy.
- Slovakian inflation rose further to 2,8%.
- Forecast real GDP growth in 2020* of 1,9%.

KBC Group in Slovakia

- ✓ Main brand: ČSOB
- ✓ Various distribution channels for insurance, electronic channels
- ✓ Estimated 3% share of the market for life insurance and 4% for non-life insurance
- ✓ 0,6 million clients (insurance alone: 0,4 million clients)
- ✓ 0,3b EUR in technical provisions and liabilities under investment contracts

Hungary	Bulgaria
Market environment	**Market environment**
• Real GDP growth remained strong at 4,9%. • This robust economic performance was the result of a combination of factors, especially the strong monetary stimulus, the absorption of EU funds and fiscal stimuli. • Inflation rose further to 3,4%, at the upper end of the band of one percentage point either side of 3%, which the Hungarian National Bank has set as its target. • Forecast real GDP growth in 2020* of 3,5%.	• Bulgarian real GDP growth remained relatively stable at 3,7% despite a number of challenges for the country, including the economic situation in Turkey. • The average annual increase in Bulgarian consumer prices amounted to 2,4%, due in part to strong wage growth caused by the increasingly tight labour market. • Forecast real GDP growth in 2020* of 2,9%.
KBC in Hungary	**KBC in Bulgaria**
✓ Main brand: K&H ✓ Various distribution channels for insurance, electronic channels ✓ Estimated 3% share of the market for life insurance and 8% for non-life insurance ✓ 1,6 million clients (bank alone: 1,1 million clients) ✓ 0,5b EUR in technical provisions and liabilities under investment contracts	✓ Main brands: UBB and DZI Insurance. ✓ Various distribution channels for insurance, electronic channels ✓ Estimated 23% share of the market for life insurance and 10% for non-life insurance ✓ 1,3 million clients (bank alone: 1 million clients) ✓ 0,3b EUR in technical provisions and liabilities under investment contracts

Table 1: Market conditions in our most important countries

Factoring in the impact of the Covid-19 crisis (27 March 2020): economic forecasts are more than ever subject to considerable uncertainty. We recognise that and take account of different potential scenarios – some more optimistic and others more pessimistic – depending on how the COVID-19 could continue to spread and what the policy responses to it would be. Our most recent base case scenario is based on a longer period of lockdown and more quarantine-related measures being taken in all European countries. This will lead to a very deep economic downturn in the first half of 2020. However, policy measures will underpin the economic recovery at the same time and, therefore, we expect this recovery to be equally as vigorous, starting in the second half of 2020 and continuing in 2021. On an annual basis, this will be reflected in sharp negative GDP growth for 2020, followed by sharp positive growth for 2021. As regards our home markets, we expect the smoothest recovery to be in Belgium thanks to robust automatic stabilisers and intensive ad hoc measures taken by the government.

2.2.3 Coronavirus

The recent emergence of COVID-19 (more commonly known as the 'coronavirus') has required additional attention. At the time this report was being prepared, KBC was monitoring the situation on a daily basis. Business continuity plans and epidemic contingency plans have been activated and are in different phases depending on the KBC group entity concerned. Besides monitoring increased operational risk, we are keeping a very close eye on the related macroeconomic impact, including the impact on KBC's home markets from decreasing GDP growth in China at a time when its economy is already in a fragile state. The financial markets also appear to be highly sensitive to the risks relating to the coronavirus, with stock markets, interest rates and oil prices all falling. A broad range of companies may be directly affected due, for instance, to their reliance on imports or exports, their exposure to vulnerable sectors and – for Central European borrowers – their link with the German economy, leading to a potential worsening of their credit profile. The coronavirus might also affect KBC's insurance business, as pandemics/epidemics are usually covered by our insurance policies, though reinsurance cover is available for mortality risk at KBC Insurance NV.

2.2.4 Profit contribution of the entities in KBC Insurance Group

At year-end 2019 KBC Insurance Group generated a strong result of 462m EUR[4]. The profit contribution of the most material entities is shown in the following table:

(in m EUR)	2019	2018	Change in amount	Change in %
KBC Insurance NV (Belgium)	352,7	368	-15,3	-4%
KBC Group Re (Luxembourg)	16	18,3	-2,3	-13%
ČSOB Pojišťovna a.s. (Czech Republic)	46,7	35,2	11,5	33%
ČSOB Poisťovňa a.s. (Slovak Republic)	10	9,1	0,9	10%
K&H Insurance Zrt. (Hungary)	17,7	14,1	3,6	26%
DZI Insurance (Bulgaria)	17,1	9,9	7,2	73%
Other	2,1	4,1	-2	-49%
KBC Insurance Group	**462**	**459**	**3,6**	**1%**

Table 2: Net Result KBC Insurance Group – breakdown per entity

(in m EUR)	2019	%
KBC Insurance NV (Belgium)	352,7	76,3%
KBC Group Re (Luxembourg)	16	3,5%
ČSOB Pojišťovna a.s. (Czech Republic)	46,7	10,1%
ČSOB Poisťovňa a.s. (Slovak Republic)	10	2,2%
K&H Insurance Zrt. (Hungary)	17,7	3,8%
DZI Insurance (Bulgaria)	17,1	3,7%
Other	2,1	0,5%
KBC Insurance Group	**462**	**100%**

Table 3: Contribution percentage of the entities to KBC Insurance Group profit

4 The net result shown here (462m EUR) is not the same as the net result as shown in the consolidated income statement (480m EUR). The difference between both net results is due to scope/(internal) definition differences.

2.3 Consolidated income statement

2.3.1 Results of KBC Insurance Group

The consolidated income statement of the KBC Insurance Group was as follows:

(in m EUR)	2019	2018	Change in amount	Change in %
Net interest income	462	507	- 44	-9%
Interest income	513	559	- 45	-8%
Interest expense	- 51	- 52	1	-1%
Non-life insurance (before reinsurance)	774	775	- 1	0%
Earned premiums	1 741	1 601	140	9%
Technical charges	- 967	- 826	- 141	17%
Life insurance (before reinsurance)	- 5	- 20	15	-75%
Earned premiums	1 324	1 361	- 38	-3%
Technical charges	- 1 329	- 1 382	53	-4%
Ceded reinsurance result	- 25	- 41	17	-40%
Dividend income	47	53	- 6	-12%
Net result from financial instruments at fair value through profit or loss	103	63	41	64%
of which result on equity instruments (overlay approach)	93	51	42	81%
Net realised result from debt instruments at fair value through OCI	0	1	- 1	-59%
Net fee and commission income	- 349	- 341	- 9	3%
Fee and commission income	165	142	24	17%
Fee and commission expense	- 515	- 483	- 32	7%
Net other income	67	78	- 10	-13%
TOTAL INCOME	1 075	1 074	1	0%
Operating expenses	- 471	- 476	5	-1%
Staff expenses	- 230	- 232	2	-1%
General administrative expenses	- 226	- 230	4	-2%
Depreciation and amortisation of fixed assets	- 15	- 14	- 1	9%
Impairment	- 3	- 2	- 2	114%
on financial assets at AC and at FVOCI	1	3	- 2	-76%
on goodwill	0	0	0	
other	- 4	- 5	0	-10%
Share in results of associated companies and joint ventures	6	19	- 12	-66%
RESULT BEFORE TAX	607	615	- 8	-1%
Income tax expense	- 127	- 145	18	-13%
Net post-tax result from discontinued operations	0	0	0	
RESULT AFTER TAX	480	470	10	2%
attributable to minority interests	0	0	0	-100%
of which relating to discontinued operations	0	0	0	
attributable to equity holders of the parent	**480**	**469**	10	2%
of which relating to discontinued operations	0	0	0	

Table 4: KBC Insurance Group consolidated income statement

Net result

The consolidated result of the KBC Insurance Group is 480m EUR in 2019, as opposed to 469m EUR in 2018.

The increase compared to last year is primarily due to a better technical result in both Life and Non-Life businesses, lower taxes and better reinsurance result, largely offset by lower net interest income, a decline in net fee and commission income, higher impairment on shares.

Overall, earned premiums in Non-Life insurance went up by 8,7%, with all entities recording an increase. Technical charges rose in line with premiums but remained at a low level, due to the absence of any major natural disasters and limited large claims. In addition, the ceded reinsurance result was more negative than in 2018 (fewer recoveries due to fewer large claims). These items were instrumental in achieving the healthy combined ratio of 89,9%.

2.3.1.1 Results from Non-Life insurance business KBC Insurance Group

- ✓ The result (before tax) generated by the Non-Life insurance business for 2019 (255m EUR) was unchanged on its level for 2018.
- ✓ In 2019, earned premiums in Non-Life insurance totalled 1.741m EUR, a considerable increase of 9% on the year-earlier figure. They grew by 4% in Belgium, by 14% in the Czech Republic, and by 24% in the three other Central and Eastern European markets combined. The increase was recorded in 'car insurance' and in 'property insurance'.
- ✓ Technical charges for Non-Life insurance came to -967m EUR in 2019, going up more sharply than premiums, but remaining at an excellent level despite the payments made in relation to storm damage and the higher number of large claims. In addition, 2018 was a favourable year for insurance.
- ✓ General administrative expenses remained virtually unchanged on their year-earlier level.
- ✓ Taking account of higher earned premiums, stable administrative expenses and the increase in technical charges, the combined ratio at group level came to a healthy 89,9% (as opposed to 88,2% in 2018). The combined ratio in all markets was below 95%.

Non-life in %	2019	2018
Net claim ratio	59.4%	56.6%
Net cost ratio (vs written premium)	30.5%	31.6%
Net combined ratio	89.9%	88.2%

Table 5: Non-Life performance ratios (KBC Insurance Group)

2.3.1.2 Results from Life insurance business KBC Insurance Group

- ✓ At 309m EUR, the result (before tax) generated by the Life insurance business was 0,3% higher than the figure for 2018 (30m EUR).
- ✓ In 2019, earned premiums in Life insurance totalled 1.324m EUR, a decline of -3% on the year-earlier figure.
- ✓ Sales of Life insurance (including unit-linked products) were up 2% on the previous year, with guaranteed-rate products rising by just 0,4% (owing to less-attractive guaranteed interest rates and the suspension of Life Future 8 products, and thanks to the inclusion of UBB Life's results for the full year in 2019 as opposed to nine months in 2018). On the other hand, sales of unit-linked products increased by 4% (attributable to robust growth in Belgium that was driven by a lack of investment alternatives for guaranteed-rate products in a low interest-rate environment). This trend was observed mainly in Belgium (guaranteed-rate products up 0%,

unit-linked products up 16%), unlike the Czech Republic, Slovakia and Hungary, where there was a sharp decline in unit-linked products and more or less stable growth of rate-guaranteed products. Bulgaria bucked the trend here, recording strong growth of both guaranteed-rate and unit-linked products. Overall, products offering guaranteed rates accounted for just over 60% of sales in 2019 and unit-linked Life insurance for almost 40% (whereas the share was 61% guaranteed-rate and 39% unit-linked in 2018).

- ✓ The lower expense related to claims incurred was attributable primarily to positive fair value adjustments and, to a lesser extent, to lower 'uprenting' costs due to scaling back the Life Capital portfolio in Belgium and a lower guaranteed interest rate (both recurring and single premium policies), offset to a large extent by higher provisioning for (non-unbundled) unit-linked products relating to premium income and higher claims fees.
- ✓ Investment income was down on its level for 2018, which reflected primarily the decline in interest income, due to falling returns on bonds linked to lower market interest rates and to less dividend income than in 2018. This was partly offset by higher realised gains and lower impairment on shares held in portfolio due to the good year on the stock market.

2.3.1.3 Non-technical result KBC Insurance Group

The non-technical result (43m EUR) in 2019 was down on its year-earlier level and did not include any exceptional items.

2.3.1.4 Income tax expense

The income tax expense for 2019 totalled -127m EUR, or almost 21%, down on its year-earlier level (24% in 2018) which came about primarily on account of higher tax-exempt results on shares.

More information on the 'underwriting performance' of the Group can be found in the Quantitative Reporting Templates:

- ✓ S.05.01 – Premiums, claims and expenses by line of business
- ✓ S.05.02 – Premiums, claims and expenses by country

Because of classification differences between IFRS and Solvency II, QRTs S.05.01 and S.05.02 differ slightly from the figures relating to earned premiums in the table above.

More information on the underwriting policy, performance per business line, and material risk mitigation techniques can be found in the Actuarial Function Report of KBC Insurance Group.

2.3.2 Results of KBC Insurance NV

Scope: contribution IFRS result KBC Insurances in results Business Unit Belgium

2.3.2.1 Results from Non-Life insurance business KBC Insurance NV

(in m EUR)	2019	2018	Change in amount	Change in %
Annual result	195	207	-12	-6%
Technical result	123	142	-19	-13%
Financial result	72	65	7	11%

Table 6: Non-Life result (KBC Insurance NV)

The annual result is 12m EUR lower than last year. The technical result this year is 19m lower than last year. The main effects are listed below:

Negative deltas vs last year are:

- ✓ High impact of major claims (-53m EUR);
- ✓ Last year's release of ageing provisions in Guaranteed Income (-6m EUR);
- ✓ Lower income on recourse (-8,5m EUR mainly caused by higher retroactive corrections (20,4m EUR this year vs 3,9m last year));
- ✓ Higher gross charges of storms (-7m EUR).

This is partly compensated by positive deltas:

- ✓ Higher net earned premiums (+44m EUR) but also higher commissions (-8,5m EUR);
- ✓ Last year's provision for change in methodology of reservation of Permanent disability in general liability (cost of 14m EUR in December);
- ✓ Higher recovery via reinsurer (+24m EUR, main components are recovery of Eberhard storm +9,1m EUR and recovery in multiline +8,6m EUR).

The financial result is 7m EUR better than last year mainly due to higher results on equity (+12,2m EUR in total, explained by lower impairments (+4,2m EUR) and higher net realizations (+8m EUR)) and higher dividend income (+0,6m EUR) partly offset by lower interest income on the bonds portfolio (-5,6m EUR).

Non-life **in %**	**2019**	**2018**
Net claim ratio	58,6%	55,9%
Net cost ratio (vs written premium)	30,6%	31,2%
Net combined ratio	89,2%	87,1%

Table 7: Non-Life performance ratios (KBC Insurance NV)

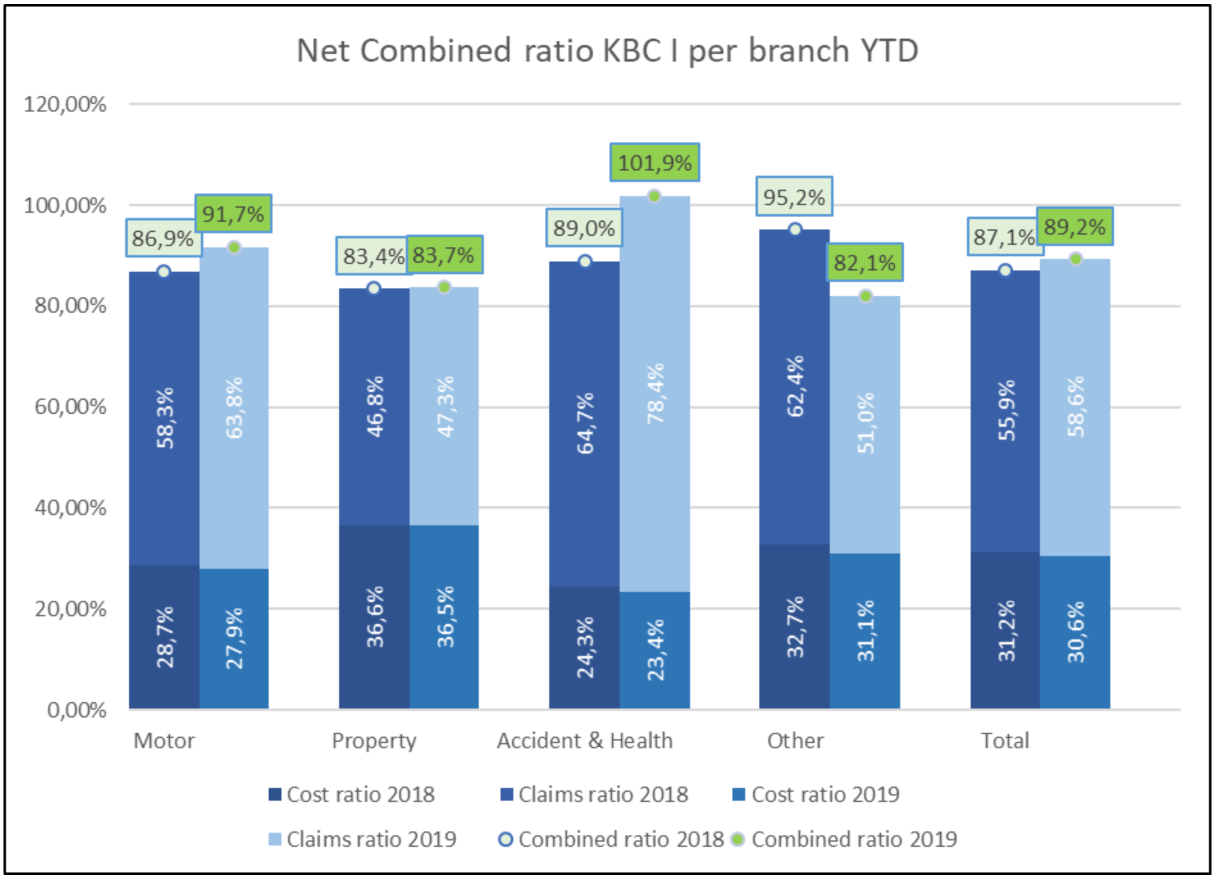


Figure 2: Net Combined ratio KBC Insurance NV per branch

2.3.2.2 Results from Life insurance business KBC Insurance NV

Some definitions:

- ✓ Gross placements = written premiums + internal transfers in +switches in
- ✓ Net placements = gross placements – internal transfers out – switches out - payments (end of term, death)
- ✓ Life investments insurances branch 21 = Life Future 8 + Life Capital + branch 26
- ✓ Riders = mainly guaranteed income (only sold as a rider)
- ✓ Interest margin = interest income – guaranteed interest cost

(in m EUR)	2019	2018	Change in amount	Change in %
Annual result excl. other financial income *(in m EUR)*	141	153	-12	-8%
Other financial results *(in m EUR)*	116	109	7	6%
Annual result *(in m EUR)*	257	263	-5	**-2%**
Expense rate	0,39%	0,39%	0,00%	-0,2%

Table 8 : Results Life (KBC Insurance NV)

For a better understanding of the evolution of the underlying Life results the other financial results are shown on a separate line.

Other financial results:

- ✓ Part of the Life provisions are invested in equity and in trading instruments;
- ✓ Results on the equity (capital gains, dividends, impairments) and trading instruments can be very volatile and explain already some material variances;
- ✓ Therefore we analyze the Life results excluding the results on the equity and trading instruments (= other financial results).

Below the Life result (excl. other financial results) with a breakdown into the Life portfolios.

(in m EUR)	2019	2018	Change in amount	Change in %
Life investment insurances branch 21	-5	-13	8	-64%
Life investment insurances branch 23	50	30	19	64%
Life regular (non investment insurances)	96	125	-29	-23%
Riders (guaranteed income)	0	11	-11	-97%
Annual result excl. other financial income	141	153	-12	-8%

Table 9: Breakdown of the Life result in the different portfolios (KBC Insurance NV)

Life investment insurance branch 21:

(in m EUR)	2019	2018	Change in amount	Change in %
Gross placements	218	281	-63	-23%
Net placements	-480	-692	212	-31%
Results on gross placements	1	1	0	-25%
Results on gross placements (%)	0,30%	0,32%	-0,01%	-3%
Technical provisions EoY	3.369	3.815	-446	-12%
Interest margin on average AuM	9	2	7	354%
Profit dotation on average AuM	-2	-5	3	-57%
Release flashing light provision	1	2	-1	-52%
Additional uprenting re. specific contracts Life Capital (extended guarantee period)	-6	0	-6	
Other results (f.e. redemption fee)	4	2	2	116%
Opex	-12	-15	3	-18%
Annual result Life investements insurances branch 21	-5	-13	8	-64%

Table 10: Life investments branch 21 (KBC Insurance NV)

- ✓ Strong decrease of gross placements as a result of closing down the sales of Life Future 8 (August 2019);
- ✓ Strong decrease of technical provisions: high maturities in Life Capital portfolio in combination with low sales of Life Future 8;
- ✓ Increase of interest income:
  - Increase mainly because of termination payer swaps (Life Capital portfolio);
- ✓ Decrease of profit dotation % on Life Future 8 portfolio;
- ✓ Additional uprenting re. specific contracts Life Capital: extension of interest guarantee period with 3 months for specific impacted contracts;
- ✓ Decrease of OPEX: decrease of cost deposit guarantee fund in line with declining technical provisions.

Life investment insurance branch 23 :

(in m EUR)	2019	2018	Change in amount	Change in %
Gross placements	2.615	2.106	509	24%
Net placements	-165	19	-185	-958%
Results on gross placements	13	11	1	11%
Results on gross placements (%)	0,49%	0,55%	-0,06%	-11%
Technical provisions EoY	13.277	12.649	628	5%
Distribution fee (on total portfolio)	54	38	16	41%
Distribution fee (on total portfolio) (%)	0,41%	0,30%	0,10%	34%
Opex	-17	-19	3	-13%
Annual result life investement insurances branch 23	50	30	19	64%

Table 11: Life investments branch 23 (KBC Insurance NV)

- ✓ Increase of gross placements mainly because of increase of internal transfers (+208m EUR) and switches (+233m EUR); increase of written premiums is limited (+68m EUR);
- ✓ Increase of technical provisions of +628m EUR :
    - negative net placements: -165m EUR
    - fees: -38m EUR
    - positive value corrections: +832m EUR ;
- ✓ Strong increase of distribution fee:
    - higher distribution fee to compensate for a decline in future dividend income from KBC Asset Management caused by a portfolio management reorganization and a changed fee charging method for FOF[5]
    - (internal) dividend income is not shown in figures KBC Insurance NV.

Life regular & riders :

(in m EUR)	2019	2018	Change in amount	Change in %
Premium income life regular	831	820	11	1%
Results on premiums received life regular	1	6	-4	-80%
Results on premiums received life regular (%)	0,13%	0,67%	-0,54%	-80%
Technical provisions EoY	9.909	9.526	382	4%
Mortality result (life regular)	87	91	-4	-5%
Premium income riders (guaranteed income)	49	46	3	7%
Technical charges riders	-35	-22	-13	62%
Commissions riders	-4	-4	0	8%
Net Interest result on average provisions	62	76	-14	-18%
Profit dotation	-13	-10	-3	28%
Release flashing light provision	22	23	-2	-7%
Other results (f.e. redemption fee)	3	2	1	63%
Opex	-75	-71	-4	5%
Annual result Life regular & riders	96	136	-40	-29%

Table 12: Life regular & riders (KBC Insurance NV)

- ✓ Increase in premium income mainly in funeral insurances (+8m EUR); loan balance Insurance (SSV) (+5m EUR) and PSPSE (Private Supplementary Pension for the Self-Employed) (+10m EUR) partly compensated by termination contract Sepia (-15m EUR);
- ✓ Decrease on result on premiums received due to increase of extra commission paid to bank (-5m EUR)
    - extra commission based on growth capital at risk
    - strong growth in 2019 (cfr. high production in mortgage loans due to the termination of 'woonbonus' as from 1/1/2020);
- ✓ Mortality result: result 2019 lower than result 2018 but this is due to a backlog in processing the figures; without the backlog figures are almost equal;

[5] FOF =Funds of funds; these have special cost and fee structures

- ✓ High increase of technical charges riders:
  - lower accounting result in collective guaranteed income due to some severe losses (mostly related to accidents of previous years where % of disability has been substantially increased)
  - if we look at results per accident year the negative technical result of accounting year 2019 is spread over several other accident years resulting in still strong and stable results over time.
- ✓ Decrease of net interest result (-14m EUR);
- ✓ Increase of profit dotation
  - higher cost due to impact of an increasing low renting portfolio
  - total return for client declined .

2.4 Investment performance

2.4.1 Investment performance of KBC Insurance Group

The table below gives some details on the interest income of KBC Insurance Group for 2019 and 2018. The overall trend is that the investment income decreased, as interest income declined, with falling return on bonds linked to the general financial climate of low interest rates, combined with the lower volume of bonds on the balance sheet.

(In m EUR)	2019	2018
Total	**462**	**507**
Interest income	**513**	**559**
Interest income on financial instruments calculated using effective interest rate method		
Financial assets at AC	247	257
Financial assets at FVOCI	239	268
Hedging derivatives	1	1
Financial liabilities (negative interest)	19	15
Other	0	13
Interest income on other financial instruments		
Financial assets MFVPL other than held for trading	0	0
Financial assets held for trading	7	5
Of which economic hedges	6	5
Other financial assets at FVPL	0	0
Interest expense	**-51**	**-52**
Interest expense on financial instruments calculated using the effective interest rate method		
Financial liabilities at AC	-8	-9
Financial assets (negative interest)	-12	-7
Hedging derivatives	-12	-11
Other	-2	-2
Interest expense on other financial instruments		
Financial liabilities hed for trading	-17	-22
Of which economic hedges	-17	-22
Other financial liabilities at FVPL	0	0
Net interest expense relating to defined benefit plans	-1	0

Table 13: Details on Interest Income (KBC Insurance Group)

2.4.2 Investment performance of KBC Insurance NV

Net investment income (excluding unit-linked products) decreased slightly in 2019.

On asset side:
- ✓ Interest income from fixed income instruments dropped due to a lower return on the bond portfolio (lower reinvestment yields on bonds) and general decline in Life Capital portfolio. Total impact: -34m EUR;
- ✓ Equity income increased, there were less impairments on shares as 2019 equity markets strongly outperformed 2018 (+30% vs -10 %), while overall realized gains on shares remained stable in comparison to 2018 as a consequence of the strategy portfolio management. Dividend income dropped slightly. Total impact: + 30m EUR;
- ✓ Lower income on derivatives (swap contracts) due to maturities: - 4m EUR.

On liability side the interest cost and profit sharing remained roughly stable, for an increased total cost of 0,6m EUR.

2.5 Performance of other activities

No other activities are material enough to be included in this SFCR Report.

System of governance

3 System of governance

3.1 Governance, remuneration and fit & proper policy

3.1.1 Governance of KBC Insurance Group

3.1.1.1 Main insurance companies of KBC Insurance Group

The main entities of the KBC Insurance group are:

- ✓ KBC Insurance NV (Belgium);
- ✓ Its subsidiaries:
    - ČSOB Pojišt'ovna a.s. (Czech Republic)
    - ČSOB Poist'ovňa a.s. (Slovak Republic)
    - K&H Insurance Zrt. (Hungary)
    - DZI Life Insurance Jsc (including DZI General Insurance Jsc) (Bulgaria)
    - KBC Group Re (Luxembourg);
- ✓ Its Irish branch.

The activities of the main entities of the KBC Insurance Group are operationally organised in business units:

- ✓ The Belgian activities of KBC Insurance NV are included under the Belgium Business Unit and organised in the KBC Insurance Products Directorate;
- ✓ ČSOB Pojišt'ovna a.s. is part of the Czech Republic Business Unit;
- ✓ ČSOB Poist'ovňa a.s., K&H Insurance Zrt., DZI Life Insurance Jsc (including DZI General Insurance Jsc) are part of the International Markets Business Unit;
- ✓ The Irish branch is part of the International Markets Business Unit;
- ✓ KBC Group Re is part of Group Centre.

3.1.1.2 Shareholder structure and corporate bodies of KBC Insurance NV

3.1.1.2.1 Shareholder structure

Shareholders	Number of shares	Percentage
KBC Group	1.002.016	95,3%
KBC Bank	1	0,0%
KBC Insurance	48.889	4,7%
Total	**1.050.906**	**100,0%**

Table 14: Shareholder structure

3.1.1.2.2 Corporate bodies of KBC Insurance NV

KBC Insurance NV is managed according to a dual model, which draws a distinction between:

- The 'Board of Directors' (BoD), which has the task of setting strategy and supervising operational management;
- The 'Executive Committee' (ExCo), which is responsible for the operational management of the company.

The tasks and functioning of the Board of Directors and the Executive Committee are described in the *Corporate Governance Charter of KBC Insurance NV* (sections 5 and 7). Reference is made several times to this Charter.

The Board of Directors is assisted by the following **advisory committees**:

- The Audit Committee;
- The Risk & Compliance Committee;
- The Remuneration Committee of KBC Group NV;
- The Nomination Committee of KBC Group NV.

The tasks and functioning of Audit Committee and the Risk & Compliance Committee of KBC Insurance NV are described in the Corporate Governance Charter of KBC Insurance NV. The Corporate Governance Charter of KBC Group NV contains the tasks and the rules of procedure of the Remuneration Committee and the Nomination Committee:

- While it is legally not recommended for an insurance company to establish a nomination committee, the KBC group decided to establish such a committee at the level of KBC Group NV, which also operates as a nomination committee for KBC Insurance NV;
- The Remuneration Committee of KBC Group NV (mixed financial holding company and parent of KBC Insurance NV) operates as the remuneration committee of KBC Insurance NV.

3.1.1.3 Internal governance of Belgian activities of KBC Ins and KBC Ins Group

3.1.1.3.1 General remarks

All entities mentioned in 3.1.1.1 have their own governance structure.

The subsidiaries of the KBC Insurance group – ČSOB Pojišt'ovna, a.s. (Czech Republic), ČSOB Poist'ovňa a.s. (Slovakia), K&H Insurance Zrt. (Hungary), DZI Life Insurance Jsc (including DZI General Insurance Jsc (Bulgaria), and KBC Group Re) – are autonomous legal entities. Each one is:

- Managed on a day-to-day basis by an executive body;

- ✓ Supervised by a supervisory body and committees (such as and depending on the country specifics): an Audit, Risk & Compliance Committee, a Remuneration Committee, a Remuneration and Nomination Committee.

KBC Insurance NV established a branch in Ireland to develop Life and Health insurance activities in Ireland.

All the entities develop their strategy and activities within the strategy of the country in which they are active. This country strategy is drawn up in line with the strategy of KBC Group NV and KBC Insurance NV, under the leadership of the Country CEO. The country and insurance strategy, activities and results are reported to:

- ✓ The CEO of their respective business units;
- ✓ The Executive Committee and Board of Directors of KBC Insurance and KBC Group NV.

Mechanisms are in place to ensure that the insurance companies are integrated within their country, their business unit, the KBC Insurance group and the KBC group, that they cooperate and that their activities are monitored.

These mechanisms relate, inter alia, to:

- ✓ The role of the management committees at the level of the Business Units (BU BE and BU IM);
- ✓ The role of the Country Teams;
- ✓ The role of Group Communities;
- ✓ The role of the SGM Group Communities & Insurance;
- ✓ The representation of the shareholders in the supervisory bodies;
- ✓ The role of the control functions and their reporting requirements.

Role of the Country Teams

A Country Team is established in every country (except BU BE) to, inter alia, foster cooperation between the bank and the insurance companies. Each Country Team operates as an advisory body and discusses strategic topics relevant to the entities in each specific country. In addition, it discusses and challenges financial plans and monitors performance.

Role of the Group Communities and the role of the SGM Group Communities & Insurance

The mission of the Group Communities is to foster, stimulate and accelerate the transnational collaboration in the KBC group. This collaboration aims to deliver tangible added value for the entities – make them stronger in the local market – in the domain Insurances and Banking.

The responsibility of the SGM Group Communities & Insurance is twofold: (1) developing and fostering the community working within the business domains Insurances and Banking; and (2) supporting the CEO of the International Markets Business Unit (functional reporting line) in the development of the insurance activities outside Belgium (including representation in the local governance, i.e. representing KBC

Insurance in the various Supervisory Bodies and Audit, Risk & Compliance Committees of all insurance entities (except KBC Insurance NV)).

The role of the control functions at group level and their reporting requirements

Group Risk, Group Compliance and the Group Actuarial Function Holder (at the level of the KBC Insurance Group and the KBC Group) include the findings of insurance subsidiaries - second line of defence functions in their reports, which are submitted to :

- ✓ The Executive Committee of KBC Insurance NV and KBC Group NV;
- ✓ The Audit Committee, the Risk & Compliance Committee and the Board of Directors of KBC Insurance NV and KBC Group NV.

3.1.1.3.2 Governance of the Belgian activities of KBC Insurance NV ("KBC Insurance Products")

Management Committees at the level of the Belgium Business Unit

The insurance activities of KBC Insurance NV (except het branch in Ireland) are included under the Belgium Business Unit. The following management committees have been set up at the level of this business unit:

- ✓ The Belgium Business Unit Management Committee is accountable for designing and proposing the strategy and for managing the execution of the strategy in Belgium Business Unit (BU), fitting the strategy of KBC Group NV and KBC Insurance NV, and, given KBC's bank-insurance strategy, also of KBC Bank NV;
- ✓ The Risk, ALM & Capital Committee, which is dedicated to risk topics and covering all risk types.

The PMSC "V2025" is accountable for monitoring the progress in the implementation of the updated insurance strategy as approved by the Board of Directors dated 19 April 2018 (concretized into the 5 commitments). The Steering Committee gives specific focus to the alignment of the insurance strategy with the implementation plan of the new Business unit Belgium Strategy (June 2019).

The Senior General Manager responsible for the insurance activities of the Belgium Business Unit is a member of these committees.

The Belgium Business Unit reports on its strategy, activities and results to the Executive Committee and to the Board of Directors of both KBC Group NV and KBC Insurance NV.

Management Committees at the level of Insurance Products Belgium

The activities of KBC Insurance Products are part of the Insurance Products Directorate, headed up by a Senior General Manager. This directorate has its own management committees to steer the activities, including:

- ✓ The Insurance Products Management Committee, which manages the KBC Insurance Products Directorate as a whole. It develops the overall strategy of KBC Insurance Products and monitors the business, operational and insurance risk
- ✓ The Insurance Products Risk Management Committee (DVZ Risk), which mission is to anchor the knowledge about SII and the underlying parameters; come to a transparent, documented risk policy; discuss risk related topics; inform about SII; and follow up the SII topics, e.g. parameters, cost allocation, documentation; to support management in ALM matters
- ✓ The Life & Health insurance activities are managed by following committees: a New & Active Product Process Committee, a Risk Management Committee (DVL Risk) and an Operational Management Committee
- ✓ Non-life insurance activities are managed by the following committees: a New & Active Product Process Committee, a Risk Management Committee (DVS Risk) and an Operational Management Committee

Reporting by the control functions

The Risk function, the Compliance function and the Actuarial function (known as the second line of defence) and the Audit function (known as the third line of defence) report their findings on the activities of KBC Insurance Products to:

- ✓ The management of KBC Insurance Products;
- ✓ The Executive Committee of KBC Insurance NV;
- ✓ The Audit Committee, the Risk & Compliance Committee and the Board of Directors of both KBC Group NV and KBC Insurance NV.

3.1.1.3.3 Governance and corporate bodies of the foreign subsidiaries of the KBC Insurance Group

3.1.1.3.3.1 ČSOB Pojišt'ovna a.s –Czech Republic Business Unit

Representatives of the shareholders in ČSOB Pojišt'ovna, a.s

KBC Insurance NV, the sole shareholder of ČSOB Pojišt'ovna a.s, has one representative on the Supervisory Body and one on the Nomination & Remuneration Committee. This representative is the Senior General Manager Group Communities & Insurance.

ČSOB Bank has two representatives on the Supervisory Board, one on the Audit Committee and one on the Nomination & Remuneration Committee. The representatives of ČSOB Bank on the Supervisory Board foster cooperation between ČSOB Bank and the insurance company, in particular by aligning their respective strategies.

Management committees of the insurance company

ČSOB Pojišt'ovna a.s has the following management committees to assist its executive body:

- ✓ New & Active Product Process Committee;
- ✓ Investment Committee;
- ✓ Local Risk & Capital Oversight Committee;
- ✓ Reserving and Parameter Committee.

Reporting by the local control functions

The local Risk function, Compliance function and Actuarial function (known as the second line of defence), and the local Audit function (known as the third line of defence) report their findings on the activities of ČSOB Pojišt'ovna a.s. to:

- ✓ The Board of Directors of the insurance company;
- ✓ The Audit Committee of the insurance company.

3.1.1.3.3.2 ČSOB Poist'ovňa a.s. (Slovakia), K&H Insurance Zrt. (Hungary) and DZI Life Insurance Jsc (including DZI General Insurance Jsc) (Bulgaria) – International Markets Business Unit

Representation of KBC Insurance NV

KBC Insurance NV, the sole shareholder of ČSOB Poist'ovňa a.s., has one representative on the Supervisory Board, i.e. the Senior General Manager Group Communities & Insurance.

It has two representatives on the Remuneration Committee: the CEO of the International Markets Business Unit (member of the Executive Committee of KBC Insurance) and the Senior General Manager Group Communities & Insurance.

It has one representative on the Audit, Risk & Compliance Committee, i.e. the Senior General Manager Group Communities & Insurance.

KBC Insurance NV, the sole shareholder of K&H Insurance Zrt., has two representatives in the Supervisory Board, the Remuneration Committee and the Audit, Risk & Compliance Committee: the CEO of the International Markets Business Unit and the Senior General Manager Group Communities & Insurance. K&H Bank has two representatives on the Supervisory Board and on the Audit, Risk & Compliance Committee.

KBC Insurance NV, the sole shareholder of DZI Life Insurance Jsc, has two representatives on the Supervisory Board, on the Audit, Risk & Compliance Committee and on the Remuneration Committee (the

CEO of the International Markets Business Unit and the Senior General Manager Group Communities & Insurance. The CEO of UBB is also a member of the Remuneration Committee. They have the same mandates in DZI General Insurance Jsc (DZI Life Insurance Jsc being sole shareholder of this company).

Management committees of the insurance subsidiaries

The insurance subsidiaries have their own management committees, which assist their respective executive bodies. These committees consist of:

- ✓ New & Active Product Process committees;
- ✓ Investment committees;
- ✓ Local Risk & Capital Oversight committees. In Hungary, this committee is organised at country level; in Slovakia, this role is performed by the Country Team.

Reporting by the local control functions

The local Risk function, Compliance function and Actuarial function (known as the second line of defence) and the local Audit function (known as the third line of defence) report their findings on the activities to:

- ✓ The management of the insurance subsidiary;
- ✓ The Audit, Risk & Compliance Committee (ARCC) of the insurance subsidiary.

3.1.1.3.3.3 Branch in Ireland

The Irish branch is established to develop Life and Health insurance activities in Ireland.

Taking into account that the branch is legally part of KBC Insurance NV, but is managerially covered by the KBC Ireland Country Team, the governance framework of the branch consists of

- ✓ a Supervisory Body;
- ✓ an Audit, Risk and Compliance body (ARC);
- ✓ a Branch Management Meeting.

Representation of KBC Insurance NV

KBC Insurance NV is represented in the Supervisory Body and the ARC by the CEO of the International Markets Business Unit and the Senior General Manager Group Communities & Insurance. The CRO of Business Unit Belgium and the Actuarial function holder of KBC Insurance NV are invited to the ARC.

The local control functions

The functioning is similar as described above., taking into account that the control functions reporting to the ARC are covered by KBC Insurance NV with the exception of

- ✓ Compliance, which is outsourced to KBC Bank Ireland plc;
- ✓ Risk: the integrated Risk function and operational Risk function are outsourced to KBC Bank Ireland plc.

3.1.1.3.3.4 KBC Group Re

KBC Group Re SA is the internal reinsurance subsidiary belonging to the KBC Group. The company specializes in protecting the KBC Group's bank and insurance entities. It provides (protection) reinsurance for insurers being part of the KBC Group while diversifying and optimizing the group's overall risk retention.

Management structure of KBC Group Re

KBC Group Re is managed by a Board of Directors. The Board of Directors is responsible for developing and approving the strategy and general policy for the company, including a risk, compliance and audit framework, and monitoring their implementation. The Board is also responsible for the appointment of the Managing Director. The Managing Director does also assume the responsibilities and role of 'Dirigeant agréé' as defined in the Luxembourg regulation 'Loi modifiée du 6 décembre 1991 sur le secteur des assurances'.

The Board also acts as Audit, Risk and Compliance Committee (see further).

The Board is composed of at least 3 members (currently 4) appointed by the General Meeting. It consists of 3 non-executive members, i.e. the Senior General Manager responsible for the insurance activities of the Belgium Business Unit, the Senior General Manager in charge of the Group Communities and Insurance Division, a senior manager of the KBC Insurance Products Directorate (BU BE) and the Managing Director.

The Managing Director is the sole Executive Director.

Audit Risk and Compliance Committee

The Audit, Risk and Compliance Committee is not set up as a separate committee: the Board directly exercises its responsibilities regarding those topics within the audit, risk and compliance domains, i.e. the integrity of the financial reporting, the effectiveness of the internal control measures and risk management processes, and the implementation of the compliance rules.

Following persons, or their representative, participate as permanent guests during these Audit Risk and Compliance Committee meetings:

- ✓ The Internal auditor;
- ✓ The Chief Risk Officer (CRO) of the Business Unit Belgium of KBC;
- ✓ The Compliance Officer.

The external auditors are invited at least once a year.

Reporting of the local control functions

The local Risk function, Compliance function and Actuarial function, and the group Audit function report on their findings to the Board of Directors when acting as Audit Risk and Compliance Committee.

Overview of the legal and operational structure

1. KBC Group level

- KBC Insurance Board of Directors
- KBC Insurance Audit Committee
- KBC Insurance Risk & Compliance Committee
- KBC Group Nomination Committee
- KBC Group Remuneration Committee
- KBC Insurance Executive Committee
- Group Insurance Committee
- Asset Liability Committee (ALCO)

2. Business Unit level

CSOB P CZ	CSOB P SK	K&H Ins	DZI Ins/DZI Gen Ins	Irish branch	KBC Ins	KBC Group Re
CZ BU Management Committee	International Markets BU Management Committee				Belgium BU Management	
					Insurance ALM Committee	
					Belgium BU Risk, ALM & Capital Committee (RACC)	
					Maatschappij voor Brandherverzekering	
					see Governance Memorandum MvBH	

3. Legal structure

CSOB P CZ	CSOB P SK	K&H Ins	DZI Ins/DZI Gen Ins	Irish branch	KBC Ins	KBC Group Re
General Meeting	General Meeting	Founder	General Meeting / Single Owner of Capital (SOC)	branch of KBC Insurance NV	Cf. KBC Group level	General Meeting
Supervisory Board	Supervisory Board	Definitive Supervisory Board	Supervisory Board			Board of Directors
Audit Committee	Audit, Risk & Compliance Committee	Audit, Risk & Compliance Committee	Audit, Risk & Compliance Committee			Managing Director
Nomination & Remuneration Committee	Nomination & Remuneration Committee	Nomination & Remuneration Committee	Nomination & Remuneration Committee			
Board of Directors	Board of Directors	Board of Directors	Management Board			

4. Management structure

Committees within Insurance entity

CSOB P CZ	CSOB P SK	K&H Ins	DZI Ins/DZI Gen Ins	Irish branch	KBC Ins	KBC Group Re
NAPP	NAPP	NAPP	NAPP	Supervisory Body	Insurance Products Management Committee	Investment Committee
Investment Committee	Investment Committee	Investment Council	Investment Committee	Audit, Risk and Compliance Body (ARC)	Non-Life Insurance NAPP Committee	
Local Risk & Capital Oversight Committee			Local Risk & Capital Oversight Committee	Branch management meeting	Non-Life Insurance Risk Management Committee	
					Non-Life Insurance Operational Management Committee	
					Life Insurance NAPP Committee	
					Life Insurance Risk Management Committee	
					Life Insurance Operational Management Committee	

Committees at Country level

CSOB P CZ	CSOB P SK	K&H Ins	DZI Ins/DZI Gen Ins	Irish branch	KBC Ins	KBC Group Re
Country team	Country team	Country team	Country team	Country team		
		Local Risk & Capital Oversight Committee				

5. Group Communities & Insurance (part of the general operational unit Innovation and Digital Transformation ("IDT").

- Group Communities & Insurance

Table 15: Overview of the legal and operational structure

3.1.2 Remuneration

Introduced in 2010, the KBC Remuneration Policy defines general remuneration guidelines for all staff and specific remuneration guidelines for those employees who could have a material impact on the risk profile of the company, also known as 'Key Identified Staff'. Continuously changing legislation for financial institutions means that the KBC Remuneration Policy is amended each year. For additional details and background information on the remuneration policy, please see the 'Remuneration report for financial year 2019' section of the KBC Group Annual Report for 2019, which is available at www.kbc.com.
The Compensation Report, on the other hand, provides information on the principles governing remuneration at KBC group level and discloses remuneration figures for financial year 2019 based on European and national legislation. This report is also available at www.kbc.com.

3.1.2.1 Fit & proper policy

The KBC group Suitability Policy was approved by the Board of Directors of KBC Group NV, KBC Bank NV and KBC Insurance NV. It contains the suitability policy for:

- ✓ The Board of Directors;
- ✓ The Executive Committee;
- ✓ The persons in charge of independent control functions, i.e. 'Key Function Holders'.

The Suitability Policy for the non-executive directors of KBC Group NV, KBC Bank and KBC Insurance include the following requirements:

- ✓ The Board of Directors must have sufficient knowledge and expertise of the financial industry and financial markets, and of the banking and insurance activities which are developed within the KBC group;
- ✓ The Board of Directors must have deep knowledge of KBC's strategy and business model and its shareholder structure;
- ✓ The directors must have the capability to understand and critically assess the strategy and its business model, the strategic planning and its implementation, the financial reporting, the organization, the effectiveness of the steps taken with the view to create effective governance, oversight and controls, the management information systems, the impact of technological changes and the digital innovation in the KBC group, the risk, audit and compliance reports and the functioning of the Risk, Audit and Compliance functions, and the reports of the Actuarial function holders and the functioning of the Actuarial function holder;
- ✓ The directors who are appointed to an advisory committee (Audit Committee, Risk & Compliance Committee, Nomination Committee and Remuneration Committee) must have relevant expertise w.r.t. the activities of the committee concerned;
- ✓ All directors, whether executive or not, must have the necessary 'independence of mind'.

The Suitability Policy for the members of the Executive Committee of KBC Group NV, KBC Bank and KBC Insurance includes the following requirements:

- ✓ The Executive Committee as a whole should have deep knowledge and experience relating to finance, risk management, compliance, audit, actuarial analysis, internal control, information management, innovation and technological transformation, change management, organization, societal issues and the legal and regulatory issues;
- ✓ The Executive Committee (ExCo) must have a deep knowledge and experience of the financial industry and of financial markets;
- ✓ The Executive Committee must have a deep knowledge and experience of KBC's strategy and business model, and of the banking and insurance activities which are developed within KBC-group;
- ✓ ExCo members must have the knowledge and experience to lead the KBC group and must have in this respect strategic insight. They should have, depending on their position in the Executive Committee, the knowledge and experience relating to finance, risk management, compliance, audit, actuarial analysis, internal control, information management, innovation and technological transformation, change management, organization, societal issues and the legal and regulatory issues, required to perform their duties individually and, as part of the Executive Committee, to be able to function as a team;
- ✓ ExCo members must have leadership skills in line with the KBC leadership model;
- ✓ ExCo members must have the necessary 'independence of mind';
- ✓ ExCo members live the values of the KBC group.

The process involves the <u>following steps</u>:

- ✓ The Nomination Committee discusses, assesses and advises the Board of Directors regarding the composition of the Board, its advisory committees and the composition of the Executive Committee;
- ✓ It discusses and proposes to the Board the required profile of new directors;
- ✓ It assesses the candidates;
- ✓ It assesses the suitability of the directors (in case of re-appointment) or of the candidate directors (in case of appointment) taking into account the regulatory requirements and the requirements referred to in the aforementioned Suitability Policy. It conducts this assessment based on the files which are prepared for submission to the supervisory body. It assesses the collective suitability of the Board of Directors. It presents its advice to the Board of Directors.

The Suitability Policy for the Key Function Holders of KBC Group NV, KBC Bank and KBC Insurance and the Heads of the foreign branches (a.o. KBC Insurance NV) includes i.a. the following requirements:

- ✓ They must have the appropriate knowledge and experience for the corresponding position and domain, realized or to be realized through education and training (diploma/on the job) or relevant work experience;
- ✓ They must have good communication skills;
- ✓ They must act loyal and responsive;
- ✓ They must have professional behaviour by providing sufficient guarantees to fulfil the position in a conscientious and independent manner, with specific and strong attention to the independence (conflict of interests) and pastimes.

The process involves the following steps:

- ✓ The Corporate HR department discusses, assesses and gives advice to the Executive Committee regarding the appointment of a Key Function Holder;
- ✓ It discusses and proposes to the Executive Committee the required profile of the Key Function Holder;
- ✓ It assesses the candidates;
- ✓ It assesses the fitness and propriety of the Key Function Holders (in case of re-appointment) or of the candidate Key Function Holders (in case of appointment) taking into account the regulatory requirements and the requirements mentioned in the internal policies. It conducts this assessment based on the files which are prepared for submission to the supervisor;
- ✓ It presents its advice to the Executive Committee for approval.

3.2 Risk Management in KBC Insurance Group

3.2.1 Risk governance

Main elements in our risk governance model:

- ✓ The **Board of Directors**, assisted by the Risk & Compliance Committee (RCC), which decides on and supervises the risk appetite – including the risk strategy – each year. It is also responsible for the development of a sound and consistent group-wide risk culture, based on a full understanding of the risks the group faces and how they are managed, taking into account the group risk appetite;
- ✓ The **Executive Committee** – supported by activity-based risk committees – which is the senior management level committee for integrating risk management with risk appetite, strategy and performance goal setting;
- ✓ The **CRO Services Management Committee** and activity-based risk committees mandated by the Executive Committee;
- ✓ **Risk-aware business people** who act as the first line of defence for conducting sound risk management in the group;
- ✓ A **single, independent Risk function** that comprises the Group Chief Risk Officer (Group CRO), local CROs, local Risk functions and the group Risk function. The Risk function acts as (part of) the second line of defence, while Internal Audit is the third line.

Relevant **risk management bodies** and **control functions**:

1. Executive Committee:
   - ✓ makes proposals to the Board of Directors about risk and capital strategy, risk appetite, and the general concept of the risk management framework;
   - ✓ decides on the integrated and risk-type-specific risk management frameworks and monitors their implementation throughout the group;

- ✓ allocates capital to activities in order to maximise the risk-adjusted return;
- ✓ acts as the leading risk committee, covering material issues that are channelled via the specific risk committees or the Group Assets & Liabilities Committee (Group ALCO);
- ✓ monitors the group's major risk exposure to ensure conformity with the risk appetite.

2. Group ALCO (Asset & Liability Committee):
   - ✓ is a business committee that assists the Executive Committee in the domain of (integrated) balance sheet management at group level. It handles matters related to ALM and liquidity risk.

3. Risk committees:
   - ✓ The CRO Services Management Committee supports the Executive Committee in assessing the adequacy of, and compliance with, the KBC Risk Management Framework and defines and implements the vision, mission and strategy for the CRO Services of the KBC group;
   - ✓ The activity-based Group Risk Committees (for lending, markets and insurance, respectively) support the Executive Committee in setting and monitoring limits for these activities at group level. Liquidity and ALM issues related to these activities are addressed by the Group ALCO;
   - ✓ The Group Internal Control Committee (GICC) supports the Executive Committee in monitoring and strengthening the quality and effectiveness of KBC's internal control system.

4. In order to strengthen the voice of the Risk function and to ensure that the decision-making bodies of the business entities are appropriately challenged on matters of risk management and receive expert advice, KBC has deployed independent Chief Risk Officers (CROs) throughout the group according to a logical segmentation based on entity and/or business unit. Close collaboration with the business is assured since they take part in the local decision-making process and, if necessary, can exercise a veto. Independence of the CROs is achieved through a direct reporting line to the Group CRO.

5. Group Risk and Group Credit Risk (known collectively as 'the Group Risk function') have a number of responsibilities, including monitoring risks at an overarching group-wide level, developing risk and capital models (while business models are typically developed by business), performing independent validations of all risk and capital models, developing risk frameworks and advising/reporting on issues handled by the Executive Committee and the risk committees.

6. When appropriate, dedicated working groups comprising risk and business-side representatives are set up to deal with emerging risks or unexpected developments in an integrated way (covering all risk types)

Performance is assessed on a yearly basis as part of the Internal Control Statement.

A simplified schematic of our risk governance model is shown below:

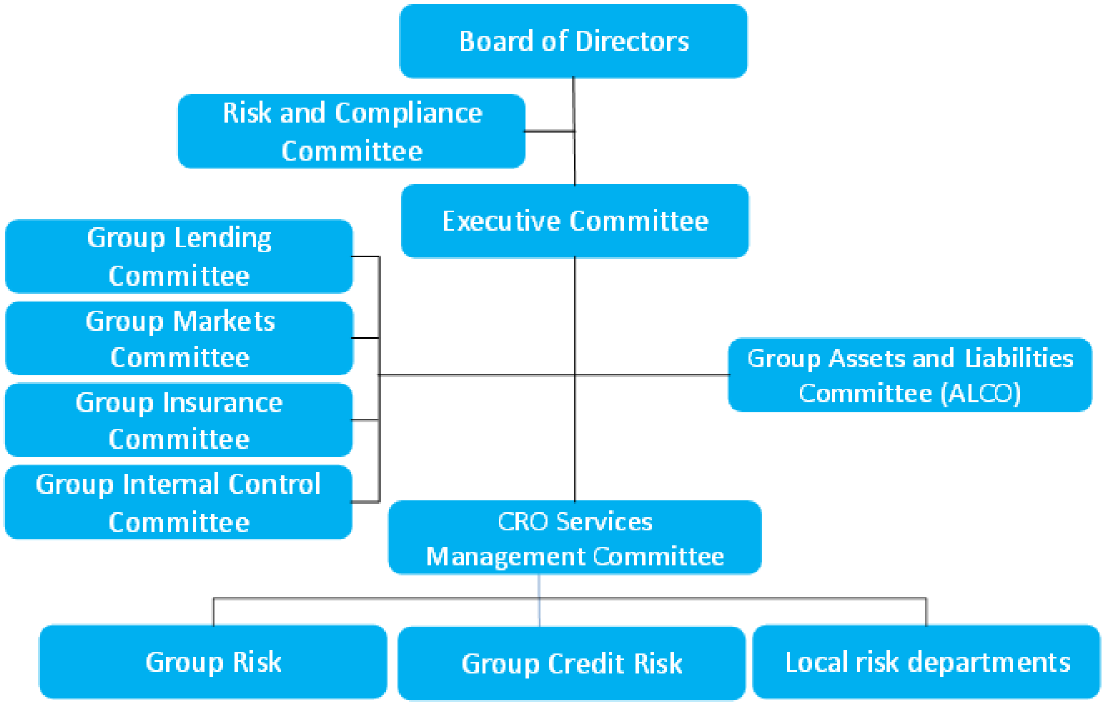


Figure 3: Simplified schematic of our risk governance model

3.2.2 Risk Management Framework (RMF) and building blocks

The changing business environment and the ambitions of the risk strategy need to be reflected in the KBC Risk Management Framework (KBC RMF). The KBC RMF defines the standards for risk management, making sure that the risk management process is uniformly and qualitatively implemented throughout the whole of KBC group. As such, it is also the single point of entry for all documentation on the risk management process within KBC group.

The KBC RMF finds it origin in KBC's overall risk strategy, as defined by the KBC Risk Appetite, which effectively sets the bar for risk management throughout KBC and is formally approved by the Board of Directors (BoD).

As KBC is a Financial Conglomerate (FICO) covering multiple financial sectors and active in a wide range of activities, the KBC RMF combines a holistic, integrated and enterprise-wide view on risk in the Enterprise RMF (ERMF) and a more detailed risk-type specific view in the risk-type specific RMFs. To foster this holistic, integrated and enterprise-wide view on risk, it was decided to merge the Overarching RMF and the Integrated RMF into a new Enterprise RMF. This also

- gives a better view to the RCC/BoD on the KBC RMF, given the increasing regulatory and supervisory expectations on their knowledge of and involvement in processes previously covered in the Integrated RMF;
- reduces overlap between documents.

This is reflected in the structure of the KBC RMF diagram below:

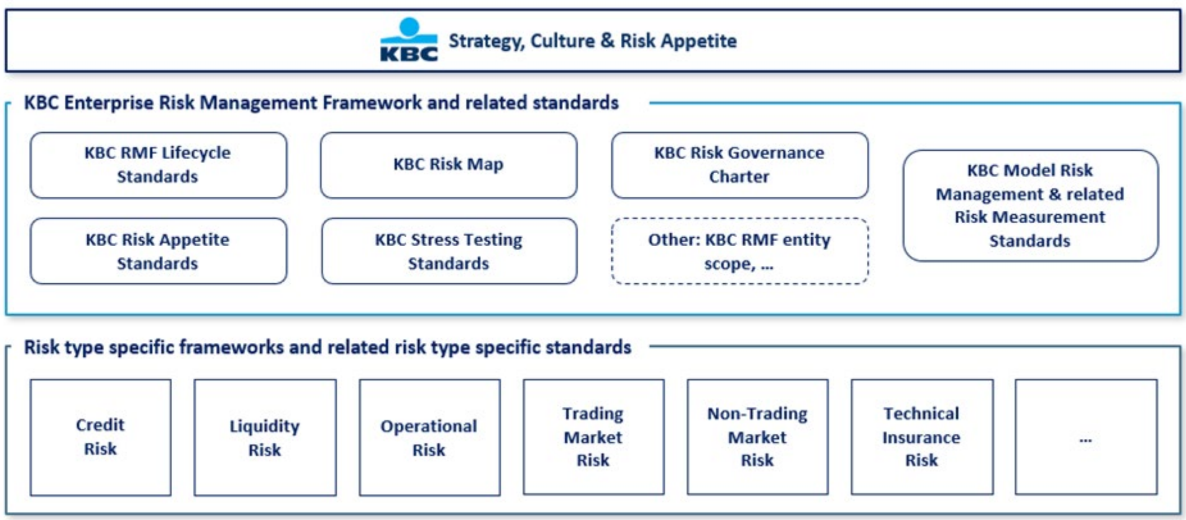


Figure 4: KBC Risk Management Framework

3.2.3 Risk management at KBC Insurance NV

Risk management at KBC Insurance NV is fully aligned with the groups governance and frameworks. The role and responsibilities of the Local Risk departments are similar to those at group level, e.g.

- ✓ Local Risk provides support to local business entities;
- ✓ Local Risk provides assistance to local business entities when implementing the KBC RMF, taking into account local specificities and regulations. Local Risk also monitors and reviews the KBC RMF as locally implemented.

KBC Insurance NV manages and follows up the risk and the related processes within the directorate (NAPP, risk reporting, …). The cooperation with the Local Risk department is a.o. situated in risk meetings:

DVZ Risk (Directie Vergadering Verzekeringen): the mission of the meeting is to:

- ✓ anchor the knowledge about Solvency II and the underlying parameters;

- ✓ discuss ALM Insurance matters;
- ✓ come to a transparent, documented risk policy;
- ✓ follow up Solvency II topics, e.g. parameters, cost allocation, documentation.

DVL /DVS Risk (Directie Vergadering Leven/Directie Vergadering Schade): the mission of the meeting is to:

- ✓ maintain a risk and capital 'governance' (policies, reference framework, delegated authority, process, etc.) for all risk types and to recommend strategic changes thereof to the DVZ risk;
- ✓ ensure the adequacy and the implementation of the risk and capital governance (for all risk types); including informing the DVZ risk about gaps and inefficiencies and taking corrective actions;
- ✓ actively promote the risk and capital agenda;
- ✓ to discuss the validity of transactional risk models prior to the final decision being taken by the Belgium BU CRO. The audit and compliance recommendations are being monitored by the local operational risk manager.

RACC (Risk, ALM and Capital Committee for Business Unit Belgium): the RACC is a specific Management Committee, dedicated to risk topics and covering all risk types. The mission of the meeting is:

- ✓ follow-up: regulatory framework + economic environment;
- ✓ follow-up: audit and compliance recommendations;
- ✓ Risk Strategy: setting the risk appetite; strategic risk, ALM and capital management;
- ✓ Compliance Strategy: setting the compliance boundaries;
- ✓ advising/Sounding Board: risk, ALM and capital proposals from BU Belgium, presented on group risk committees or GEXCO;
- ✓ risk training: providing risk based training for the management of BU Belgium (educational corner);
- ✓ risk awareness: discuss the Top Risk Concerns and their evolution.

3.2.4 Own risk & solvency assessment

The KBC Insurance Group and its insurance and reinsurance subsidiaries conduct an Own Risk and Solvency Assessment (ORSA) to monitor and ensure that business is managed in a sound and prudent way.

KBC's ORSA policy, which is reviewed on an annual basis and brought in line with the most recent ORSA Circular of the National Bank of Belgium, describes the general KBC approach to the ORSA process and its outcome. The ORSA policy describes the objectives and implementation of the ORSA within KBC, highlights its key underlying processes and the roles & responsibilities of the different stakeholders involved.

The ORSA is an integral part of the business strategy and is taken into account on an ongoing basis in the strategic decisions of the KBC Insurance Group and KBC Insurance NV.

All insurance and reinsurance entities pertaining to KBC group are in scope of the ORSA. A differentiated but coherent, consistent and proportionate approach is applied, based on the materiality of the entity. The ORSA processes and reporting are implemented with a high degree of consistency in all material entities of KBC Insurance Group who will have a local or individual ORSA report.

KBC does not require that the non-material entities run the KBC ORSA processes or write an ORSA report. However, the local regulator can impose the need for an ORSA process and reporting.

KBC's ORSA consists of numerous business and risk processes that together contribute to the objectives as set out in the ORSA policy. The reference points for the ORSA are the corporate strategy and the risk appetite objectives. The main processes underlying the regular ORSA are executed on an annual basis and are closely linked to the Strategic Planning Process (Alignment of Planning Cycle or APC) which also follows an annual cycle.

Taking into account the fact that KBC's insurance business is sufficiently mature, this annual periodicity is deemed adequate. The Executive Committee of KBC Insurance can decide to perform an additional ad-hoc ORSA if:

- ✓ major deviations from the business plan (APC) are observed;
- ✓ major changes to the group structure or group composition occur;
- ✓ reclassification of financial assets due to significant changes in the business model.

On a quarterly basis, integrated (insurance) risk reporting reports on: risk signals; the development of the risk profile; results of deep dives, stress & scenario testing. These reports are discussed up to the level of the Executive Committee and the Board of Directors and allow them to manage stress & scenario testing, request (ad-hoc) mid- and long-term risk assessments and review the underpinning ambition and approach.

The annual ORSA process assesses the situation at 31 December and is submitted to the supervisory authority before 30 June of the following year. KBC does not differentiate between the internal and the supervisory ORSA report. Each ORSA report is complemented with an ORSA record which contains all the documents that have been used in the different steps of the ORSA. The local ORSA report of KBC Insurance NV and the ORSA report of KBC Insurance Group of 2019 will be integrated in one document. Detailed analysis (stress testing, assessments) for the local level remains however a vast part of this integrated document.

Based on the outcome of the above processes and assessments, a conclusion is included in the ORSA report that will indicate to what extent the available capital is sufficient to cover the capital requirements. It will link this conclusion to the:

- ✓ changes in the amount and composition of available regulatory capital over the planning horizon and under different economic circumstances;
- ✓ changes in required regulatory capital over the planning horizon, taking into account expected changes to the risk profile of the entity/group;
- ✓ the impact of scenario analyses and sensitivities on required and available regulatory capital.

KBC relies on the Solvency II standard formula to assess its overall solvency needs. An assessment is performed on an annual basis to check whether the standard formula is appropriate in relation to the risk profile of KBC.

3.3 Other key functions of KBC Insurance Group

3.3.1 Actuarial Function

The Actuarial Function is one of the key control functions that is defined in the Solvency II regulatory framework. Solvency II requires an Actuarial Function to be installed in each insurance entity and at insurance group level. Basically, the task of the Actuarial Function is to provide independent assurance to the Board of Directors and the Executive Committee on actuarial matters related to Solvency II. This is done, inter alia, by:

- ✓ Advising on the calculation of the technical provisions (including appropriateness of methodologies, appropriateness and quality of data used, experience analysis);
- ✓ Expressing an opinion on the overall underwriting policy;
- ✓ Expressing an opinion on the adequacy of reinsurance arrangements;
- ✓ Contributing to the effective implementation of the risk management system (risk modelling underlying the SCR calculations, contributing to the ORSA process);
- ✓ Reporting and giving recommendations to the supervisory body of the entity.

Implementation of the Actuarial Function:

- ✓ The Actuarial Function is ultimately reporting accountable to the Board of Directors;
- ✓ An ‘Actuarial Function Holder’ is appointed for every local entity and also at KBC Group level. The Actuarial Function Holder is to be registered on the pay-roll of the entity he/she is representing. Her/his responsibility cannot be outsourced to a party outside the entity;
- ✓ The Actuarial Function Holder coordinates the activities of the Actuarial Function. In general, ‘a function’ is the administrative capacity to undertake particular governance tasks and is – as such - not limited to one specific person or one organizational unit, but can be assigned to several persons or departments subject to an adequate segregation of duties;
- ✓ The Actuarial Function’s basic task is to provide the independent ‘second pair of eyes’ required for the Actuarial Function Holder to meet all the assigned obligations. The Actuarial Function provides input to the Actuarial Function Holder, including forming opinions, proposing recommendations and assisting in writing the Actuarial Function Reports of KBC Insurance Group and KBC Insurance NV.

3.3.2 Compliance Function

With a view to centralisation, consistency and synergy, the Compliance Function of KBC Insurance is exercised by Group Compliance. Group Compliance plays a double role with regard to the domains within the scope of Compliance:

- ✓ An advisory role to support the business entities in implementing and applying requirements, setting up internal procedures and providing necessary training and awareness communication;
- ✓ A monitoring role by performing second-line controls on compliance with requirements.

An Intragroup Service Agreement has been drawn up defining the way this is organised.

Within the Compliance department, there are several technical units, each dealing with specific Compliance domains:

- ✓ Financial Markets, including the rules of conduct in distribution of insurance products and rules on making and providing information;
- ✓ Consumer and Data Protection;
- ✓ Corporate governance;
- ✓ Embargo Management;
- ✓ Anti-Money Laundering (AML) (including OFAC, the Know Your Customer part of FATCA and the Common Reporting Standard, the EU Regulation on information accompanying transfers of funds and tax fraud prevention), financing of terrorism and preventing the funding of the proliferation of weapons of mass destruction;
- ✓ Ethics & Fraud.

The AML and Ethics & Fraud domain are split between a Policy unit and an Investigations unit.

Both the governance of the Compliance Function and its policies within scope, as defined by the Circular on the Compliance Function (Circular NBB_2012_14 d.d. 4 December 2012), satisfy the relevant requirements. In section 5.4 on the Compliance Function, NBB Circular _2016_31 (d.d. 5 July 2016 and the revised version d.d. 13 September 2018) regarding governance of the insurance sector confirms the position reflected in Article 55 of the Act of 13 March 2016 on the status and supervision of insurance and reinsurance undertakings, i.e. the Compliance Function has to focus on integrity and codes of conduct.

Based on the same NBB Governance Circular, two specific additional tasks are included in the Compliance domain. An inventory of the Solvency II-related policies is being drawn up, and the structure of these policies is being put in place to ensure that at least its objectives are included in each policy, the tasks to be performed by the relevant person/function, the applicable reporting processes and the requirement to inform all risk-related and actuarial functions, where relevant. Additionally, Compliance has a coordination task and will check the comprehensibility, consistency and accuracy of governance topics sensu stricto in the RSR report. These governance topics include ownership, management structure, fit &

proper policy, incompatibility of mandates, loans and insurance for managers, independent control functions, remuneration, conflicts of interest and outsourcing.

The legal department of KBC is charged with the task of following up laws and regulations and changes to them in the Solvency II context, as well as communicating to the businesses concerned.

It was key to ensure that crucial pieces of legislation, such as the 4th AML Directive, the GDPR, PRIIPS and IDD, falling under the Compliance domains, were adequately implemented by the businesses within the organisation in 2018-2019.

The Key Function Holder for Compliance at KBC Insurance is the CRO of KBC Insurance, who is also a member of the Executive Committee (ExCo). The Head of the Compliance function of KBC Insurance has a direct reporting line to this member and a functional line with the CEO of KBC Insurance. The Compliance reports are formally submitted every quarter to the ExCo and RCC of KBC Insurance.

Within Compliance, there is also a dedicated Coordinating Compliance Officer who is responsible for coordinating, supporting and following up matters in respect of the Insurance Products Directorate. The Head of Compliance ensures sufficient resources are provided by the department to deal with KBC Insurance. The ExCo of KBC Insurance decides on the annual Compliance plans and submits them to the RCC for confirmation. The Head of Compliance reports to and attends the quarterly meetings of the KBC Insurance RCC. A separate and specific Compliance Charter and Integrity Policy have been drawn up for KBC Insurance, describing the scope, tasks and responsibilities of every party involved at several levels of the organisation. There are two Compliance Risk Managers (CORM) at the level of Insurance Products, one for Life insurance and one for Non-Life insurance. They are not part of the second line of defence (Compliance), but instead are fully incorporated into the business entity. They are facilitators in implementing and following up Compliance issues and, therefore, support the Senior General Manager and General Managers of Insurance Products in their responsibilities with regard to Compliance. The Insurance Products Coordinating Compliance Officer and the CORMs work closely together, have regular meetings and organise reporting to the business entities' management.

3.3.3 Audit Function

The internal Audit Function of KBC Insurance NV is exercised by KBC Group Corporate Audit. It is regulated by NBB Circular NBB_2015_11. The responsibilities of Internal Audit are:

- ✓ To provide independent reasonable assurance to the Board of Directors, the Audit Committee and the Executive Committee on the quality and effectiveness and efficiency of the processes of risk management, internal control and corporate governance that are in place;
- ✓ To support the Board of Directors, the Audit Committee and the Executive Committee in taking up their responsibilities in these processes.

- ✓ To report any serious issues or risks which it becomes aware of and to undertake any required investigations into high-risk situations (e.g. possible fraud, non-compliance with laws, internal guidelines or procedures);
- ✓ To make clear and actionable recommendations which address weaknesses noted during its work and to follow up on the implementation status of these recommendations;
- ✓ To co-ordinate with other audit and review entities, including the Statutory Auditors and the Belgian and local Supervisors, to maximise the efforts of all such entities and to minimise unnecessary overlap and/or disruption. It will hold to this end regular meetings with the Statutory Auditors and with the Supervisors;
- ✓ To carry out any assignment or projects entrusted to it by the Board of Directors, the Audit Committee or the Executive Committee.

To safeguard its independence and objectivity:

- ✓ Internal Audit reports and is accountable to the Audit Committee;
- ✓ The internal audit activity remains free from interference by any part of the organisation, including matters of audit selection, procedures, frequency, timing or report content;
- ✓ The appointment and dismissal of the Head of Internal Audit comes under the authority of the Audit Committee;
- ✓ Internal auditors are, during the exercise of their professional duties, authorised to have direct communication with any member of staff, as well as to access all premises and any records, files or data that are relevant to the performance of an assignment, subject to compliance with local regulations. All members of staff are requested to assist Internal Audit in fulfilling its roles and responsibilities;
- ✓ Internal Audit has the authority to perform assignments on its own initiative in all entities, departments, establishments and functions within its scope, subject to proper reporting to the local Executive and Audit Committees;
- ✓ Internal Audit has the authority to inform directly, and on its own initiative, the Chairman of the Board of Directors or Supervisory Board of the audited entity, the Chairman of its respective Audit Committee, the members of its Executive Committee, its Statutory Auditors or the local Supervisory Authorities;
- ✓ Internal auditors must always be objective and impartial and seek to avoid any conflicts of interest;
- ✓ Internal auditors are not directly involved in the operational organisation of an entity, nor in deciding, developing, introducing or implementing risk management and internal control measures;
- ✓ Internally recruited auditors respect a cooling-off period;
- ✓ Whenever practicable and without jeopardising competence and expertise, internal audit staff will periodically rotate within the internal audit function to boost independence.

The scope of Internal Audit covers all entities, all activities and all divisions, including the various control functions, of KBC Insurance NV. To this end, Internal Audit will periodically – and at least once a year -

examine and evaluate the areas within its scope. The audit plan is defined applying a risk-based approach while ensuring adequate coverage of matters of legal or regulatory interest. The audit plan is supplemented with a statement on the necessary resources to execute the plan. The audit plan is approved by the respective Audit Committees. Deviations from the audit plan must be reported to the respective Audit Committee at least once a year.

The approach followed in performing the audit assignments should be described in resulting audit reports so that their readers can consider the findings against the approach followed. A risk-based approach is used as the primary auditing method. The level of assurance, which may be gained from Internal Audit's work, is relative to the nature and extent of work carried out. It is therefore essential that the auditor involved, when giving a reasoned opinion, documents the nature and the extent of the work undertaken.

The implementation of the audit recommendations is the responsibility of line management, that will communicate the status of this follow-up regularly to Internal Audit, for monitoring purposes.

To facilitate a consistent approach to internal audit across all entities within the KBC Insurance Group, the heads of local internal audit departments are accountable to their supervising Audit Committee and are steered by the Internal Auditor of KBC Group NV. The co-operation between the different internal audit departments is organised in a matrix structure where the competence-based axis intersects with the geographical responsibility axis.

The independence and objectivity of Internal Audit is assured by the KBC Insurance Internal Audit Charter approved by the Board of Directors. The Charter also describes the functioning and organisation of the Internal Audit function.

3.3.4 Internal Control System

Three lines of defence concept

To further improve the Internal Control System within the KBC group, the three lines of defence concept is implemented. The roles and responsibilities of the different actors within the three lines of defence are highlighted in this chapter.

First line of defence: business entities

The first line of defence (business) has full ownership of its risks. It needs to deal with these risks and put the necessary controls in place. This involves allocating sufficient priority and capacity to risk topics, making sure the business self-assessments are of a sufficient quality, and performing the right controls in the right manner.

The table below summarises the roles and responsibilities of the first line of defence.

Function	Description
Strategy and governance	- Create a local business strategy within the defined risk appetite - Are compensated based on performance in relation to risk-adjusted business goals - Locally implement the KBC Risk Management Framework ('KBC RMF') for each risk type within their activity, the Group Compliance Rules and the Group Compliance Monitoring Program

Execution	- Take risk-minded decisions within the playing field for their areas of business
	- Manage their risks (including for outsourced activities and outstanding contractual liabilities) in accordance with the guidelines of the KBC RMF, including
	  o identifying the risks within their business
	  o qualitative and quantitative measurement of these risks
	  o reporting (including analysis, evaluation and presentation)
	  o responding to the risk according to the accountability rules
	    ▪ risk mitigation
	    ▪ risk transfer
	    ▪ risk acceptance
	- Manage the Compliance risk as per the Group Compliance Framework: Group Compliance Charter & Integrity Policy, Group Compliance Risk Appetite as well as the Group Compliance Rules and the Group Compliance Monitoring Program and recommendations

Oversight	- Have an overview via reporting lines of
	  o the actual risk environment and compliance with the playing field
	  o the control environment and compliance with local regulations

Table 16: Roles and responsibilities of the first line of defence

The second line of defence for operational risks consists of the Risk function, the Compliance function, the Legal function, the Tax function, the Finance function and the DQM function

The Risk function, as part of the second line of defence, formulates independent opinions on the risks KBC faces and on the way they are mitigated.

To do this consistently and based on high standards, the Risk function develops, imposes and monitors consistent implementation of methods or frameworks and tools to identify, measure and report on risks. To make sure that its voice is heard, the Risk function also has a veto right, which can be used in the different committees where material decisions are taken.

The table below summarises the roles and responsibilities of the Risk function as part of the second line of defence.

<table>
<tr><th>Function</th><th>Description</th></tr>
<tr><td>Strategy and governance</td><td>- Owns the KBC RMF, including the risk-type specific frameworks.
- Supports the Executive Bodies and/or Business Unit Management Committees (group and local level) in:
o defining the risk appetite which is to be approved by the Boards of Directors of KBC Group, KBC Bank and KBC Insurance and by the local Supervisory Boards;
o translating the risk appetite into the relevant playing field.</td></tr>
<tr><td>Execution</td><td>- Creates, maintains and reviews the KBC RMF, based on regulatory and legal requirements, that clearly defines the responsibilities and tasks of the first and the second-line functions in the KBC RMF.
- Is responsible for the local implementation of the second-line tasks set by the KBC RMF (e.g. integrated risk reporting).
- Actively supports implementation of the KBC RMF in the first line:
o locally through explanation, advice, training, control;
o centrally via training, workshops, etc.
- Challenges and supports the business in managing the risks related to the full lifecycle of their activities and projects.
- Has a veto right in the different committees where material decisions are taken.
Remark:
- Each second line function can also take first line responsibility, e.g. ICAAP/ILAAP/ORSA reporting by the risk function. By doing this, the second-line function is also accountable for the risks related to the activity in question and therefore must define internal controls to guarantee the quality of the result.</td></tr>
<tr><td>Oversight</td><td>- Monitors and challenges the level of implementation of the KBC RMF in the business entities and reports on the overall risk environment to executive management.
- Oversees business entities' compliance with the playing field and escalates if necessary.
- Reports independently on risk matters to the appropriate bodies and risk committees according to the guidelines set out in the KBC RMF.</td></tr>
</table>

Table 17: Roles and responsibilities of the Risk function as part of the 2nd line of defence

The Compliance function, as part of the second line of defence, is positioned as independent function within the KBC group, protected by its specific status, its place in the organisation chart and its reporting lines, and has as prime objective to prevent KBC from running a compliance risk or from incurring loss/damage – regardless of its nature – due to non-compliance with applicable laws, regulations or internal rules that fall either within the scope of the Compliance function or within the areas assigned to it by the EC. Hence, the Compliance function devotes particular attention to adherence to the integrity policy. It performs this second line role by:

- ✓ The identification, assessment and analysis of the risks linked to the Compliance domains, together with the business;

- ✓ An advisory role to support the business entities in implementing and applying requirements, setting up internal procedures and providing necessary training and awareness communication;
- ✓ A monitoring role by performing second-line controls on compliance with requirements and setting up a enhancing and risk based Compliance Monitoring Program.

Due to the specific tasks of each specific function, each second line can also assume first-line accountability, e.g.:

- ✓ tax declarations by Group Tax;
- ✓ financial reporting by Group Finance;
- ✓ calculations of risk metrics by the Risk function;
- ✓ internal capital adequacy assessment process (ICAAP)/internal liquidity adequacy assessment process (ILAAP)/the own risk and solvency self-assessment (ORSA) reporting by Group Risk;
- ✓ filing of suspicious transactions (anti-money laundering) by Group Compliance;
- ✓ personal account dealing by Group Compliance.

By doing this, the second-line function is accountable for the risks related to the activity in question and therefore must define internal controls to guarantee the quality of the result.

Third line of defence: Internal audit

The third line of defence (internal audit) gives assurance to the Boards of Directors that the overall internal control environment is effective and that policies and processes are in place, effective and consistently applied throughout the group.

The table below summarises the roles and responsibilities of the third line of defence.

Function	Description
Strategy and governance	- Independently reports to the Supervisory Bodies, the Executive Bodies, the BU Management Committees, the Audit Committees and Audit, Risk & Compliance Committees - Expresses a reasoned opinion on the functioning of the internal control framework, including the RMF and adherence to risk appetite - Leverages on the proper functioning of the first and second lines of defence
Execution	- Evaluates the functioning of both the first and second lines of defence according to the audit planning approved by the Executive Bodies, the Audit Committees and the Audit, Risk & Compliance Committees - Checks whether risks are managed adequately through all KBC processes - Issues recommendations to remedy risk and control gaps
Oversight	- Monitors and approves the status of audit recommendations

Table 18: Roles and responsibilities of the third line of defence

3.4 Outsourcing

3.4.1 General outsourcing approach at the level of KBC group

KBC group has set the following strategic goals:

- ✓ KBC strives to offer its clients a unique bank-insurance experience;
- ✓ KBC develops the group with a long-term perspective and therefore achieves sustainable and profitable growth and respects solid risk, capital and liquidity boundaries;
- ✓ KBC puts clients' interests at the heart of everything it does and offers them a high-quality service and relevant solutions;
- ✓ KBC takes its responsibility towards society and local economies very seriously and aims to reflect that in its everyday activities.

The outsourcing approach of the KBC group is embedded in the above-mentioned cornerstones:

- ✓ KBC aims to maximise the retention and development of its internal knowledge of all aspects related to the bank-insurance model, as well as the related processes and activities;
- ✓ In particular, functions, processes, activities that include KBC-specific proprietary information, intellectual property rights, trade secrets, know-how creating a competitive market advantage for KBC over its peers ('Core KBC Know-How'), can never be outsourced to a third party, i.e. an entity outside the KBC group ('External outsourcing');
- ✓ To the extent that technological or economic developments justify the outsourcing of some activities, the KBC group strives for a maximal retention of knowledge and control of these activities. Therefore, the KBC group initially turns to the shared services centres (SSC) within the group ('Internal Outsourcing');
- ✓ In the event of outsourcing, KBC aims for the highest possible quality level in order to ensure and guarantee long-term objectives and clients' interests.

3.4.2 Outsourcing principles

The KBC group has an extensive policy on regulated outsourcing. This policy is similarly applicable to internal and external outsourcing. The policy describes the definition of outsourcing as applied within the group, a high level process description, group coordination and central notification, and the monitoring principles.

For every outsourcing file, an outsourcing coordinator has to be appointed. This coordinator has an internal notification duty to a group-wide coordinator. This notification is not only required for new files, but also for material changes in existing outsourced activities and for renewals.

The outsourcing entity is accountable for the risk assessment of an outsourcing initiative. The outsourcing entity is required to write a mandatory risk assessment, accompanied by mandatory advice from the control functions, covering inter alia:

- ✓ Operational risk (as described in the group-wide key controls and zero tolerances);
- ✓ Legal risk (possible legal showstoppers, provided by the (local) legal department);
- ✓ Compliance risk (provided by the (local) Compliance Function);
- ✓ (If applicable) the risks controlled by the Actuarial Function.

Within the group strategy, KBC Insurance develops its own approach on outsourcing. Core values in this approach are client centricity (putting the clients' interest first), maximum synergy and efficiency and drawing on external expertise if this expertise excels internal knowledge or capacities.

An outsourcing policy was approved in December 2018 and is applied on all new outsourcing contracts. The new policy also provides that in the event of a thorough change of an outsourced service the approval procedure will have to be repeated. Therefore it cannot be excluded that some existing contracts may evolve to critical in the future.

3.4.3 Intragroup outsourcing

As already stated in sections 3.3.3 and 3.3.4., a number of control and key functions of KBC Insurance are exercised at group level with a view to fostering centralisation, independence, consistency and synergy.

KBC Group provides the following functions on behalf of KBC Insurance:

- ✓ Audit
- ✓ Compliance
- ✓ Risk
- ✓ Finance
- ✓ Asset/Liability Management (ALM)
- ✓ ICT

All these activities are considered to be critical or important operational functions or activities for KBC Insurance.

In addition, KBC Insurance relies on other KBC entities for specific insurance-related tasks:

- ✓ The contact centre of VAB, a Belgian-based subsidiary of KBC Insurance, provides services related to insurance obligations, covering (non-medical) assistance to persons who encounter difficulties while traveling (includes their property or motor vehicles). VAB receives and adjusts claims, and also provides assistance on behalf of KBC Insurance. VAB also registers claims notified by phone for other Non-Life insurance products and provides primary advice to clients in the name and on behalf of KBC Insurance, and initiates the claims handling process in urgent cases;

- ✓ As regards unit-linked Life insurance policies, KBC Asset Management NV (Belgium) and KBC Asset Management SA (Luxembourg) provide services to KBC Insurance for setting up and managing Luxembourg- and Irish-based investment funds.

KBC Insurance also considers these activities to be critical or important operational functions or activities.

3.4.4 Critical or important operational functions or activities outsourced to external parties

KBC Insurance entrusts its own operational tasks to insurance intermediaries as regards acceptance and claims handling for Non-Life insurance contracts. These activities are only entrusted to Belgian intermediaries, specifically for contracts in which the relationship with the client is maintained.

Outsourcing to tied agents is a standardised process. These agents may perform limited tasks related to the collection of insurance premiums, the settlement of claims (limited in scope) and the provision of green cards. Contracts outsourced to insurance brokers are handled on a case-by-case basis, and may include a wider range of tasks relating to contract management and claims settlement.

KBC Insurance uses the services of a number of Belgian-based, self-employed consulting physicians for specialised medical services (acceptance of certain types of Health and Life insurance, handling claims with complicated medical aspects).

Risk profile

4 Risk profile

4.1 Introduction

KBC Insurance Group and KBC Insurance NV are exposed to a number of typical industry-specific risks such as movements in interest rates, insurance underwriting risk, business risk, operational risks. In this section, we focus on the most material risks KBC Insurance faces.

The KBC Insurance Group Risk Appetite Statement (RAS) reflects the view of the Board of Directors and top management on risk-taking in general and on the acceptable level and composition of risks in coherence with the desired return, in particular. This statement includes a specification of the risk profile and the risk appetite for each risk type into Low risk, Medium risk and High risk.

These high-level risk appetite objectives are the base of the RAS of the local entities and are further specified for different risk types.

This leads to the following risk appetite and risk profile:

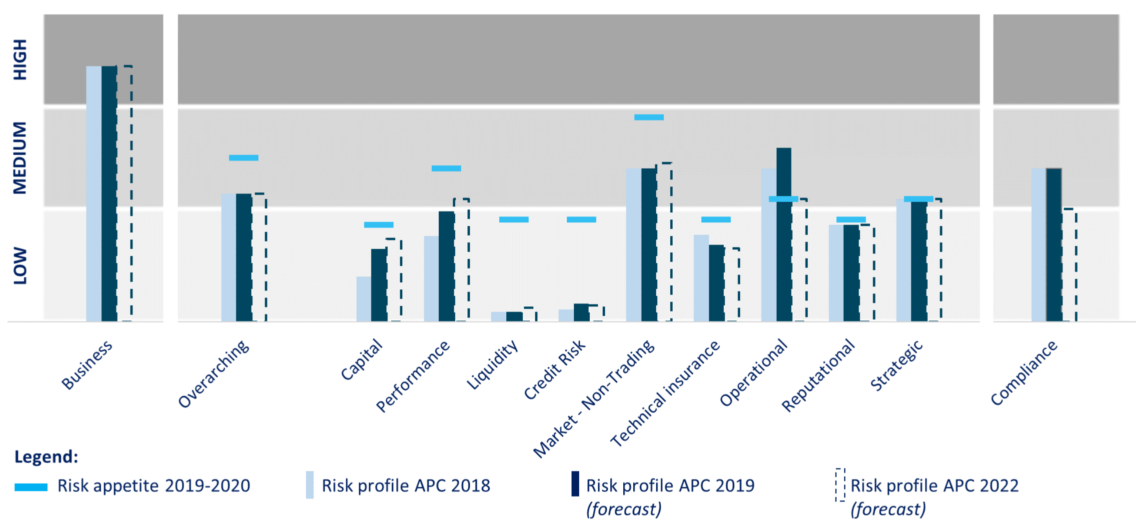


Figure 5: Risk appetite versus risk profile (2019-2022) of KBC Ins Grp & KBC Ins NV

The overarching risk profile of KBC Insurance Group and KBC Insurance NV is expected to remain stable and comfortably within the 'medium' risk appetite over the APC horizon. Though the risk profile of financial risks are increasing, they are compensated by a decreasing risk profile in operational and compliance risk.

Market risk, strategic risk and operational risk (all 'medium') are important drivers in the risk profile of KBC Insurance Group and KBC Insurance NV. It is the ambition to gradually achieve by 2023 the 'low' risk profile for operational risk as well as compliance risk. Actions are ongoing to improve the risk profile of the individual operational sub-risk types. Significant investments and means deployed in automation processes and Artificial Intelligence combined with enhanced qualitative & quantitative Key Risk Indicators, better follow-up of the progress and additional awareness initiatives should contribute to a reduction of the compliance risk profile to ‘low’.

The risk profile of technical insurance risk is low thanks to the strong diversification within insurance underwriting, i.e. a wide range of different insurance product-types that are offered to both retail and small enterprises segments.

The assessment of the overarching risk appetite and risk profile is not only based on the individual risk types, but also the anchor points of KBC’s playing field are taken into account (i.e. capital, performance and liquidity) which are all expected to increase slightly over the APC horizon. The risk profile of performance is expected to increase to the lower end of medium, as the impact of the improving Non-Life combined ratio is counterbalanced by the performance of the total Life insurance portfolio which is under pressure in the current low interest rate environment. The margin on new business is however expected to improve during the APC horizon, and is closely followed up at local level as well as group level.

Based on the final 2020 top risks for KBC Group , the risk profile, the Solvency II SCR materiality and the SCR underpinning exercise, the following ranking of 5 most material risks is defined for both KBC Insurance Group and KBC Insurance NV:

1. Strategic risk
2. Market risk – spread risk
3. Market risk – interest rate risk
4. Market risk – equity risk
5. Operational risk

4.2 Underwriting risk

4.2.1 Introduction

The 'underwriting risk' or 'technical insurance risk' stems from uncertainty regarding the frequency and severity of insured losses. All these risks are kept under control through appropriate underwriting, pricing, claims reserving, reinsurance and claims handling policies of line management and through independent insurance risk management.

The management of the technical insurance risk strategy is the responsibility of the Executive Committee of KBC Insurance Group, assisted by the Group Insurance Committee (GIC), which has representatives from both the business side and the Risk function.

Adequate procedures are enforced throughout the KBC Insurance Group to ensure sound, quality underwriting, provided with good overall profitability, within the prescribed retention limits, and in adherence to the group and local risk appetite.

The insurance entities focus mainly on the segments of retail and small enterprises i.e. Private Persons, the Self-Employed and Small and Medium-Sized Enterprises (SMEs). Through the wide range of insurance products that are offered to these clients, an important degree of diversification is reached. Where larger risks are taken in portfolio, or when risks could accumulate to a larger scale, risk mitigation is achieved through the purchase of reinsurance cover.

Although insurance underwriting is not performed at group level, the KBC Group control-functions nevertheless play an important role as regards underwriting performance. More specifically, the KBC Group Risk Management function and the Actuarial function closely monitor the underwriting rules and underwriting performance, or the profitability calculations that are performed for all the insurance and reinsurance entities.

Adequate procedures are in place to ensure that the quality of underwriting is high and overall profitability sound, within the prescribed retention limits and in line with the group and local risk appetite:

- ✓ The Risk Appetite Statement describes the level of risk that can be accepted for each risk type, defines the risk limits and how this is to be translated into business operations;
- ✓ A limits framework defines the maximum exposures that can be borne by the group and, based on those limits, more detailed ones are specified for the local entities. This limits framework is reviewed on a yearly basis. Compliance checks are conducted annually to see whether these retention limits are adhered to;
- ✓ A uniform, group-wide 'New and Active Product Process' (NAPP) screens and formally decides on each product before it can be launched in the market;
- ✓ The performance indicators and adequacy of the technical provisions are constantly monitored.

Group Risk is responsible for providing support with regard to local implementation and the functional direction of the insurance risk management process of the insurance subsidiaries.

The insurance risk management framework is designed primarily around the following building blocks:

- ✓ Adequate identification and analysis of material insurance risks by, inter alia, analysing new emerging risks, concentration or accumulation risks, and developing early warning signals;
- ✓ Appropriate risk measurements and use of these measurements to develop applications aimed at guiding the company towards creating maximum shareholder value. Examples include best estimate valuations of insurance liabilities, ex post economic profitability analyses, natural catastrophe and other Life, Non-Life and Health exposure modelling, stress testing and internal required capital calculations;
- ✓ Stress testing and sensitivity analysis;
- ✓ Regular reporting and follow-up of the risk measurements in insurance risk report;
- ✓ Determination of insurance risk limits and conducting compliance checks, as well as providing advice on reinsurance programs.

The following risk aspects have an important impact on the underwriting risk profile of an insurance company:

- ✓ **Concentration risk:**

  Main concentration risk that can be observed for the underwriting risk:

  - Natural catastrophe risks (storms, floods, earthquakes, etc.);
  - Non-natural catastrophe risks or 'man-made' catastrophe risks (e.g. pandemic events, big losses, etc.);
  - Concentration risks linked to specific activities (e.g. nuclear risk, terrorism risks).

  The possible concentration risk at KBC Insurance Group level is also assessed. Exposure can be aggregated at group level in different ways:

  - Via accumulation exposure across different entities (e.g. a storm hitting several domestic KBC markets);
  - Via internal reinsurance when direct entities cede important parts of their exposure to KBC Group Re, which keeps the risk in own retention or further cedes the pooled risk to the external reinsurance market;
  - Via credit exposure to reinsurance counterparties.

  KBC Group risk management has developed a model for assessing the group-wide exposure to all Non-Life insurance risks, including natural hazards. This model measures the most material Non-Life insurance risks (catastrophe and premium & reserve risk) for all group insurance and reinsurance companies, with account being taken of outward reinsurance (external and intra group). The resulting concentration risk exposures are used to check compliance with the limit frameworks (group and local level) based upon which adequate reinsurance coverage can be bought.

- ✓ **Risk mitigation**

Besides strict underwriting guidelines that should guarantee sound underwriting, reinsurance is bought to support the strategic objectives as formulated in the Risk Appetite Statement. In order to achieve the objectives, the reinsurance policy of the KBC Insurance Group stipulates that every material insurance entity has to acquire reinsurance protection to ensure that its net exposure remains within the bounds of the risk retention limit framework.

The insurance portfolios are protected against the impact of large claims or the accumulation of losses (risk concentration) by means of reinsurance contracts. We divide these reinsurance programmes into three main groups, i.e. property insurance, liability insurance and personal insurance, and we re-evaluate and renegotiate them every year. Most of our reinsurance contracts are concluded on a non-proportional basis, which provides cover against the impact of large claims or loss events. The independent insurance risk management function is also responsible for advising on the restructuring of the reinsurance programmes. This approach has resulted in optimising the retention of the KBC group particularly in respect of its exposure to natural catastrophe risk, but also in respect of other lines of business.

Major reinsurance programmes on the property and liability of KBC direct insurance companies are centralised via KBC Group Re. These reinsurance programmes are re-evaluated and renegotiated every year.

Best estimate valuations of insurance liabilities

As part of its mission to independently monitor insurance risks, the group and local Risk function regularly carries out in-depth studies. These indicate that the Non-Life technical provisions at subsidiary level are sufficient. The value of technical provisions equals the sum of a Best Estimate and a Risk Margin. The Best Estimate corresponds to the discounted future cashflows of the insurance obligations. A Risk Margin is added to ensure that the value of the technical provisions is equivalent to the amount an insurance company would require to take on the obligations of the insurance company. The adequacy of provisions is checked per business line at subsidiary level and the overall adequacy is assessed at subsidiary level for all business lines combined.

In addition, the main group companies conduct Liability Adequacy Tests (LAT) that meet local and IFRS requirements for the Life technical provisions. We make calculations using prospective methods (cashflow projections that take account of lapse rates and a discount rate that is set for each insurance entity based on local macroeconomic conditions and regulations), and build in extra market-value margins to deal with the factor of uncertainty in a number of parameters.

For Life business also the Value of New business (VNB)/Value of Business In force (VBI) are calculated which are both widely used industry standards to measure the profitability of the Life insurance operations. With this group-wide methodological framework a reference throughout KBC Insurance Group was provided.

Also for KBC Insurance NV underwriting risk reflects the risk in relation to the perils covered and the processes used in the conduct of business arising from Non-Life, Life or Health insurance obligations.

The most important consideration in the assessment of the technical insurance risk profile is the stability of the technical-financial result. This is supported by KBC Insurance NV's nature as a diversified retail insurer. As such, KBC Insurance NV can rely on a broad client, product and intermediary base to absorb risks at different levels. This is realized by:

- ✓ Offering a full product range, including all important Life and Non-Life products;
- ✓ Focusing on retail clients, providing services to a large number of private persons, SMEs and the self-employed;
- ✓ Operating through tied agents and bank branches, who deal exclusively with KBC Insurance NV. Hence, all policies of a client that is serviced by a KBC agent are placed with KBC Insurance NV;
- ✓ Being active on the full Belgian territory through a fine-meshed network, that also comprises the KBC bank branches.

These elements result in diversification, geographically as well as over a large number of clients, different branches and products.

4.2.2 Life insurance risk

In the tables below, an overview is provided of the KBC Insurance Group's best estimate provisions for the Life business at end of year 2019.

Life Business - Best Estimates end of year 2019		
Line of business (in m EUR)	**Best Estimate** (gross of reinsurance recoverables)	%
Total Best Estimate Life excluding Health and Unit Linked	15.747	51%
Total Best Estimate Health similar to Life	567	2%
Total Unit Linked Best Estimate and value as a whole	14.404	47%
Total Best Estimate provisions Life (incl. Health similar to Life and Unit Linked)	**30.718**	**100%**

Table 19: Life business KBC Ins Grp – Best Estimates (gross of reinsurance) EOY 2019

Compared with last year (total best estimate provision for the Life business, including Health similar to Life and Unit-linked: 28.987m EUR), the Life business' risk exposure has increased with 6% at group level. The majority of the premium volume is still written in Belgium (including both the guaranteed-rate and Unit-Linked businesses).

Gross written premium Life (in m EUR)	2019		2018	
	Gross Written Premium	%	Gross Written Premium	%
KBC Insurance NV (Belgium)	1.486	82%	1.422	80%
ČSOB Pojišťovna a.s. (Czech Republic)	227	13%	259	15%
ČSOB Poisťovňa a.s. (Slovak Republic)	39	2%	48	3%
K&H Insurance Zrt. (Hungary)	34	2%	39	2%
DZI Insurance (Bulgaria)	16	1%	18	1%
Total	**1.802**	**100%**	**1.786**	**100%**

Table 20: Life business KBC Ins Grp – gross written premium -split per entity EOY 2019

Premium volume in total for Life increased in 2019 with 1%, as shown in the table above. This was mainly driven by an increase in KBC Insurance NV. In all other CEE entities a decrease was observed.

Gross written premium (in m EUR)	2019			2018		
	Unit-Linked	Non Unit-Linked	Total	Unit-Linked	Non-Unit linked	Total
KBC Insurance NV (Belgium)	491	994	1.486	423	999	1.422
ČSOB Pojišťovna a.s. (Czech Republic)	175	53	227	206	53	259
ČSOB Poisťovňa a.s. (Slovak Republic)	18	21	39	28	21	48
K&H Insurance Zrt. (Hungary)	22	12	34	27	12	39
DZI Insurance (Bulgaria)	0	16	16	0	17	18
Total	**706**	**1.096**	**1.802**	**684**	**1.102**	**1.786**

Table 21: Life business KBC Ins Grp – gross written premium - EOY 2019

As the table indicates, the growth in Life premium is due to the Unit Linked products; we observe a small decrease in Non-Unit Linked products.

4.2.3 Non-Life insurance risk

An overview of the KBC Insurance Group's best estimate provisions for the Non-Life business at end of year 2019 is provided in the tables below.

Non-Life Business - Best Estimates end of year 2019		
Line of business (in m EUR)	**Best Estimate** (gross of reinsurance recoverables)	%
Total Best Estimate excluding Health non similar to Life	1.574	87%
Total Best Estimate Health non similar to Life	244	13%
Total Best Estimate provision Non-Life (incl. Health non similar to Life)	**1.818**	**100%**

Table 22: Non-Life business KBC Ins Grp – Best Estimates EOY 2019

The graph below shows how the gross written premium (GWP) volume has developed over the past few years. The steady increase in Non-Life GWP volumes is in line with expectations, i.e. a stable moderate growth that is expected to continue in the coming years.

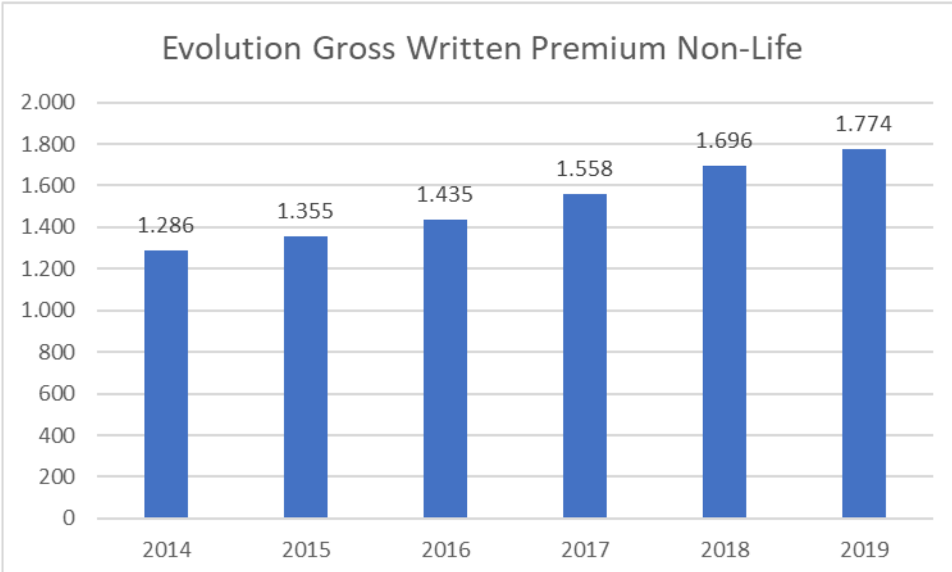


Figure 6: Non-Life business KBC Ins Grp - Evolution gross written premium

The table below illustrates the premium split per entity for the Non-Life portfolio.

Gross written premium Non-Life (in m EUR)	2019		2018	
	Gross Written Premium	%	Gross Written Premium	%
KBC Insurance NV (Belgium)	1.130	64%	1.142	67%
ČSOB Pojišťovna a.s. (Czech Republic)	284	16%	251	15%
ČSOB Poisťovňa a.s. (Slovak Republic)	52	3%	48	3%
K&H Insurance Zrt. (Hungary)	159	9%	119	7%
DZI Insurance Life (Bulgaria)	21	1%	19	1%
DZI Insurance Non-Life (Bulgaria)	128	7%	117	7%
KBC Group Re	-	0%	-	0%
Total	**1.774**	**100%**	**1.696**	**100%**

Table 23: Non-Life business KBC Ins Grp - gross written premium– split per entity EOY 2019

Premium volume in total for Non-Life increased in 2019 with 4,5%, as shown in the table above. This was mainly driven by an increase in the CEE entities and a small decrease in KBC Insurance NV.

4.2.4 Conclusion

Combining the qualitative and quantitative assessments of the Life, Non-Life and Health technical insurance risks results in a 'low' risk profile, as was the risk profile of last year.

4.3 Market risk

4.3.1 Introduction

The process of managing our structural exposure to market risks (including interest rate risk, equity risk, real estate risk, foreign exchange risk and inflation risk) is also known as Asset/Liability Management (ALM).

'Structural exposure' encompasses all exposure inherent to our commercial activity or to our long-term positions. Trading activities are consequently not included. Structural exposure can also be described as a combination of:

- ✓ Mismatches in the insurance activities between liabilities in the Non-Life and Life businesses and the corresponding covering assets;
- ✓ The risks associated with holding an investment portfolio for the purpose of (re)investing shareholders' equity;
- ✓ The structural currency exposure stemming from the activities abroad (investments in foreign currency, results posted at branches or subsidiaries abroad, foreign exchange risk linked to the currency mismatch between the insurer's liabilities and its corresponding investments).

The management of the ALM risk strategy at KBC is the responsibility of the GExCo, assisted by the Group ALCO, which has representatives from both the business side and the Risk function.

Managing the ALM risk on a daily basis starts in the first line with risk awareness at Group Treasury and the local treasury functions. The treasury departments measure and manage this market risk within the playing field defined by the risk appetite. KBC's ALM limits are approved at two levels.

- ✓ On the one hand limits at the level of KBC Insurance Group for interest rate risk, equity risk, real estate risk and foreign exchange risk, which are approved by the Board of Directors (BoD);
- ✓ On the other hand limits at the level of the solo entities for interest rate risk, equity risk, real estate risk and foreign exchange risk, which are approved by the Group Executive Committee (GExCo). Together this forms the playing field for KBC's solid first line of defence for ALM risk.

KBC's second line of defence is the responsibility of Group Risk and the local risk departments. Their main task is to measure ALM risks and flag up current and future risk positions. A common ALM Risk Management Framework (Non-Trading Market Risk Management Framework or NTMRMF), an ALM rulebook and shared group measurement infrastructure ensures that these risks are measured consistently throughout the group. The NTMRMF and ALM Rulebook have been drawn up centrally by Group Risk and are applicable for all entities.

The main building blocks of KBC's ALM Risk Management Framework are:

- ✓ A broad range of risk measurement methods such as Basis-Point-Value (BPV), interest rate gap analysis, key rate report (i.e. BPV per time bucket) and economic sensitivities;
- ✓ Net interest income (NII) simulations performed under a variety of market scenarios. Simulations over a multi-year period are used in budgeting and risk processes;
- ✓ Capital sensitivities arising from investment book positions that impact available regulatory capital (e.g. bonds that are classified as fair value through other comprehensive income);

- ✓ Stress testing and sensitivity analysis.

Risk profile vs risk appetite Market risk

The Risk Appetite Statement (RAS) for market risk, as defined by the BoD, is translated into concrete ALM limits, drilled down to the solo entity level. These ALM limits are monitored and reported on a quarterly basis. The medium risk appetite of the KBC Insurance Group (resp. KBC Insurance NV) for market risk is defined based on 4 (resp. 5) ALM limits i.e.

- ✓ A primary BPV limit;
- ✓ A primary equity limit (nominal);
- ✓ A primary real estate limit (nominal);
- ✓ A FX (foreign exchange) limit;
- ✓ An additional 'Net Recourse on Repo Funding' limit (nominal) for KBC Insurance NV.

There were no limit breaches at the level of KBC Insurance Group nor KBC Insurance NV during 2019.

4.3.2 Interest rate risk

One of the most important risks for insurance undertakings in the current low yield environment is interest rate risk. The negative impact of low yields on available capital is rather straightforward, given the longer tenor of liabilities compared to assets and the increased impact of the convexity effect[6] following from these persistent low yields.

The main technique used to measure interest rate risks in the ALM view is the +10 BPV method, which measures the extent to which the net asset value of the portfolio would change if interest rates were to go up by 10 basis points across the entire interest rate term structure. A negative (positive) BPV figure indicates a decrease (increase) in the net asset value of the portfolio.

Interest (Swap +10 BPV) limit *KBC Insurance Group (in k EUR)*	+10 Swap BPV		
	31/12/2018	31/12/2019	Absolute Change
KBC Insurance Group	**14.249**	**12.998**	**-1.250,73**
KBC Insurance NV	16.040	15.060	-980
KBC Group Re	-1.103	-1.136	-33
K&H Insurance	-533	-664	-131
CSOB P SK	-42	179	221
CSOB P CZ	262	434	172
DZI	-375	-874	-499

Table 24: KBC Ins Grp - Impact of a parallel 10 BPV increase in risk-free IR curve

[6] Relatively speaking, a parallel 10 base point shock to the interest curve is more significant when interest rates are lower. Therefore, the existing increase in interest rate sensitivity, measured by the BPV, is not necessarily a consequence of actively taking more interest rate risk.

KBC also uses other techniques such as interest rate gap analysis, key rate reports (i.e. BPV per time bucket), the duration approach, scenario analysis and stress testing (both from a regulatory capital perspective and from a net interest income perspective).

Where the group's insurance activities are concerned, the fixed-income investments for the Non-Life reserves are invested with the aim of matching the projected pay-out patterns for claims, based on extensive actuarial analysis or well-considered cyclical benchmark profiles.

The Non-Unit-Linked Life activities (branch 21 insurance) combine a guaranteed interest rate with a Discretionary Participation Feature (DPF or profit sharing). The main risks to which the insurer is exposed as a result of such activities are a low-interest-rate risk (i.e. the risk that return on investments will drop below the guaranteed level) and a risk that the investment return will not be sufficient to give clients a competitive profit sharing rate. The risk of low interest rates is managed via a cash flow-matching policy, which is applied to that portion of the Life insurance portfolios covered by fixed-income securities. Unit-Linked Life insurance investments (branch 23 insurance) are not dealt with here, since this activity does not entail any material market risk for KBC.

The tables below summarise the exposure to interest rate risk in the Life insurance activities, according to the ALM view for KBC Insurance Group (resp. KBC Insurance NV). The interest rate sensitive assets and liabilities, relating to Life insurance business offering guaranteed rates, are grouped according to the expected timing of cash flows. It should be stressed that the Life insurance liabilities are not only covered by the interest rate sensitive assets which are shown in underlying tables. Next to these interest rate sensitive assets, the balance sheet also contains:

- ✓ Interest rate sensitive assets in surplus, i.e. assets that are not linked to any insurance liabilities;
- ✓ Interest rate insensitive assets, such as equity & real estate investments, which in general are held to cover the long-term insurance liabilities (i.e. liabilities with a term of 10 to 15 years or higher).

Interest rate risk per end of December 2018						
(in m EUR)	Expected Cash Flows (undiscounted)					
(except for duration, expressed in years)	0-5 years	5-10 years	10-15 years	15-20 years	> 20 years	Total
Fixed-income assets backing liabilities, guaranteed component	6.978	4.388	1.679	1.597	799	15.442
Liabilities guaranteed component	5.513	3.923	2.338	2.008	2.606	16.389
Difference in expected cash flows	1.465	465	-659	-411	-1.807	-947
Mean duration of assets						6,55
Mean duration of liabilities						9,20

Interest rate risk per end of December 2019						
(in m EUR) *(except for duration, expressed in years)*	Expected Cash Flows (undiscounted)					
	0-5 years	5-10 years	10-15 years	15-20 years	> 20 years	Total
Fixed-income assets backing liabilities, guaranteed component	7.073	3.797	1.923	1.875	880	15.548
Liabilities guaranteed component	5.599	3.602	2.358	1.789	2.978	16.326
Difference in expected cash flows	1.474	195	-435	86	-2.098	-778
Mean duration of assets						7,29
Mean duration of liabilities						10,03

Table 25: KBC Ins Grp - Expected undiscounted interest rate sensitive CF's for Life insurance

Interest rate risk per end of December 2018						
(in m EUR) *(except for duration, expressed in years)*	Expected cash flows (undiscounted)					
	0-5 years	5-10 years	10-15 years	15-20 years	> 20 years	Total
Fixed-income assets backing liabilities, guaranteed component	6.312	4.079	1.552	1.463	753	14.159
Liabilities guaranteed component	5.336	3.711	2.202	1.891	2.398	15.539
Difference in expected cash flows	976	368	-650	-428	-1.645	-1.379
Mean duration of assets						6,63
Mean duration of liabilities						9,16

Interest rate risk per end of December 2019						
(in m EUR) *(except for duration, expressed in years)*	Expected cash flows (undiscounted)					
	0-5 years	5-10 years	10-15 years	15-20 years	> 20 years	Total
Fixed-income assets backing liabilities, guaranteed component	6.361	3.557	1.704	1.742	833	14.196
Liabilities guaranteed component	5.432	3.402	2.226	1.674	2.753	15.487
Difference in expected cash flows	928	155	-522	68	-1.920	-1.291
Mean duration of assets						7,43
Mean duration of liabilities						9,95

Table 26: KBC Ins NV - Expected undiscounted IR sensitive CF's for Life

As mentioned above, the main interest rate risk for the insurer is a downside one. KBC adopts a liability-driven ALM approach focused on mitigating the interest rate risk in accordance with KBC's risk appetite. For the remaining interest rate risk, we adhere to a policy that takes into account the possible negative consequences of a sustained decline in interest rates, and have built up an adequate supplementary buffer.

Table 27: Breakdown of the Non-unit-linked Life reserves by guaranteed IR – KBC Ins Grp & Table 28: Breakdown of the Non-unit-linked Life reserves by guaranteed IR – KBC Ins NV below show the evolution of the Life insurance reserves (i.e. mathematical reserves at 4Q2019) broken down by the corresponding interest rate guarantee. Note that all mathematical reserves linked to interest rate guarantees above 2,5% have substantially decreased during 2019, with the exception of the reserves linked to guarantees of 5% or higher. The latter is primarily caused by specific Life insurance portfolios in the CE insurance undertakings (i.e. ČSOB P SK & ČSOB P CZ), for which this very high interest rate guarantee is not only applicable to the existing reserves, but is contractually also applicable to new premiums.

Life Insurance Reserves by Interest Rate Guarantee *(in m EUR)*	31/12/2018		31/12/2019		Change	
	Amount Reserve	Proportion (%)	Amount Reserve	Proportion (%)	Absolute	Relative
5,00% and higher	413,37	3,05%	418,87	3,11%	5,51	1,33%
More than 4,25% up to and including 4,99%	1.208,27	8,90%	1.108,13	8,22%	-100,14	-8,29%
More than 3,50% up to and including 4,25%	683,76	5,04%	624,29	4,63%	-59,47	-8,70%
More than 3,00% up to and including 3,50%	1.389,92	10,24%	1.345,38	9,98%	-44,55	-3,20%
More than 2,50% up to and including 3,00%	820,80	6,05%	505,25	3,75%	-315,55	-38,44%
More than 0,00% up to and including 2,50%	8.826,36	65,05%	9.264,79	68,74%	438,43	4,97%
0,00%	225,98	1,67%	211,34	1,57%	-14,64	-6,48%
Total	**13.568,47**	**100,00%**	**13.478,06**	**100,00%**	**-90,41**	**-0,67%**

Table 27: Breakdown of the Non-unit-linked Life reserves by guaranteed IR – KBC Ins Grp

Life Reserves - Split by interest rate guarantee (in m EUR)	*EoY 2018*		*EoY 2019*	
	Reserves	*proportion Reserves*	*Reserves*	*proportion Reserves*
5.00% and higher	1,78	0,01%	2,97	0,02%
More than 4.25% up to and including 4.99%	1208,27	9,42%	1108,13	8,69%
More than 3.50% up to and including 4.25%	678,12	5,28%	619,78	4,86%
More than 3.00% up to and including 3.50%	1389,92	10,83%	1345,38	10,55%
More than 2.50% up to and including 3.00%	709,12	5,53%	384,11	3,01%
More than 0.00% up to and including 2.50%	8688,55	67,71%	9136,54	71,66%
0.00%	156,35	1,22%	153,63	1,20%
Total	**12832,11**	**100,00%**	**12750,54**	**100,00%**

Table 28: Breakdown of the Non-unit-linked Life reserves by guaranteed IR – KBC Ins NV

In 2018 it was decided to widen the interest rate gap (increase BPV by 5m EUR), anticipating an expected revival of the interest rate environment in the near future. Widening the interest rate gap in 2018 has increased the interest rate sensitivity of the liabilities, compared to the sensitivity of the assets, making the balance sheet more sensitive towards downward interest rate movements.

The 2019 treasury strategy was focussed on maintaining the current interest rate gap and if the interest rate environment would allow for it (i.e. if the interest rates would surpass certain levels), it was planned to gradually do additional investments to anticipate reinvestment risk of the coming years.

4.3.3 Credit spread risk

From an ALM perspective, KBC manages the credit spread risk for inter alia the sovereign portfolio by monitoring the extent to which the value of the sovereign bonds would change if credit spreads were.

Spread Risk Sensitivity 4Q2019	*+100bp Spread BPV (in m EUR)*	*Proportion of total +100bp Spread BPV*
KBC Core Countries	**-528,4**	**53,7%**
Belgium	-412,2	41,9%
Czech Republic	-52,6	5,3%
Hungary	-8,9	0,9%
Slovakia	-22,9	2,3%
Bulgaria	-13,1	1,3%
Ireland	-18,7	1,9%
Southern Europe	**-70,3**	**7,1%**
Greece	0,0	0,0%
Portugal	-11,1	1,1%
Spain	-19,5	2,0%
Italy	-39,7	4,0%
Other Countries	**-384,9**	**39,1%**
France	-213,8	21,7%
Poland	-15,7	1,6%
Germany	-35,6	3,6%
Austria	-23,4	2,4%
Netherlands	-11,5	1,2%
United States	0,0	0,0%
Rest	-84,9	8,6%
TOTAL	**-983,7**	**100%**

Table 29: Spread Risk sensitivity (+100bp) of sovereign bonds at 4Q2019 – KBC Ins Grp

Spread Risk Sensitivity 4Q2019	*+100bp Spread BPV (in m EUR)*	*Proportion of total +100bp Spread BPV*
KBC Core Countries	**-449,7**	**50,7%**
Belgium	-409,9	46,2%
Czech Republic	-0,4	0,0%
Hungary	0,0	0,0%
Slovakia	-19,9	2,2%
Bulgaria	-1,7	0,2%
Ireland	-17,8	2,0%
Southern Europe	**-68,0**	**7,7%**
Greece	0,0	0,0%
Portugal	-10,1	1,1%
Spain	-18,9	2,1%
Italy	-39,0	4,4%
Other Countries	**-370,0**	**41,7%**
France	-211,2	23,8%
Poland	-14,0	1,6%
Germany	-35,6	4,0%
Austria	-23,2	2,6%
Netherlands	-11,2	1,3%
United States	0,0	0,0%
Rest	-74,8	8,4%
TOTAL	**-887,7**	**100%**

Table 30: Spread Risk sensitivity (+100bp) of sovereign bonds at 4Q2019 – KBC Ins NV

4.3.4 Equity risk

The ALM strategies for the insurance business are based on a risk-return evaluation, taking into account the market risk attached to open equity positions.

Underlying tables give a view on the breakdown of the equity portfolio by sector for KBC Insurance Group (resp. KBC Insurance NV), showing a well-diversified portfolio with the largest exposure towards the industrial and financial sector.

Breakdown Equity Portfolio by Sector	*31/12/2018*	*31/12/2019*
Industrial	35,1%	41,8%
Financial	23,5%	22,5%
Consumer cyclical	11,9%	10,8%
Consumer non-cyclical	10,3%	9,3%
Basic materials	5,4%	4,2%
Energy	5,8%	4,1%
Communication	2,7%	2,7%
Utilities	1,8%	2,6%
Real estate	3,3%	1,5%
Other and not specified	0,2%	0,4%
Total	**100%**	**100%**

Table 31: Breakdown equity portfolio (excl. strategic participations) by sector – KBC Ins Grp

Breakdown Equity Portfolio by Sector	*31/12/2018*	*31/12/2019*
Industrial	35,3%	42,5%
Financial	21,9%	20,6%
Consumer cyclical	12,7%	11,9%
Consumer non-cyclical	10,3%	9,1%
Energy	6,1%	4,5%
Basic materials	5,4%	4,1%
Utilities	1,9%	2,9%
Communication	2,6%	2,4%
Real estate	3,5%	1,7%
Other and not specified	0,2%	0,4%
Total	**100%**	**100%**

Table 32: Breakdown equity portfolio (excl. strategic participations) by sector – KBC Ins NV

4.3.5 Real estate risk

KBC Insurance NV has a real estate portfolio, which is held as an investment for Non-Life reserves and long-term Life activities. The real estate exposure is viewed as a long-term hedge against inflation risk and as a way of optimising the risk/return profile of these portfolios.

The tables below provide an ALM view on the sensitivity of economic value to fluctuations in the property markets.

Real Estate limit KBC Insurance Group *(in m EUR)*	Real Estate Shock (25%)		Absolute Change	Relative Change
	31/12/2018	31/12/2019		
KBC Insurance Group	81,5	98,1	16,6	20,4%

Table 33: Impact of a 25% drop in real estate prices – KBC Ins Grp

Real Estate limit KBC Insurance NV *(in m EUR)*	Real Estate Shock (25%)		Absolute Change	Relative Change
	31/12/2018	31/12/2019		
KBC Insurance NV	78,4	95,1	16,7	21,3%

Table 34: Impact of a 25% drop in real estate prices – KBC Ins NV

4.3.6 Foreign exchange or currency risk

As currency risk is measured against the local reporting currency, it is important to understand that the currency risk at the level of the KBC Insurance Group is perceived differently than the currency risk at the level of the solo insurance entities, which are reporting in a non-euro currency, i.e.:

- ✓ ČSOB Pojišťovna a.s. (CZ), reporting in CZK;
- ✓ K&H Biztosító Zrt., reporting in HUF;
- ✓ DZI Life Insurance Jsc , reporting in BGN;
- ✓ DZI General Insurance Jsc, reporting in BGN.

We pursue a prudent policy as regards our structural currency exposure, essentially seeking to avoid currency risk through FX hedging.

The current FX hedging strategy makes a distinction between three sources of FX risk, i.e.:

- ✓ FX risk stemming from strategic participations:
  KBC Insurance NV has a full strategic participation in all the underlying (re)insurance entities of the KBC Insurance Group[7]. The value of these strategic participations is determined by the net asset value (NAV) of the respective (re)insurance undertakings, of which some are denominated in a foreign currency[8].
- ✓ FX risk stemming from the equity portfolio:
  The equity positions (excl. strategic participations) are not hedged, but the FX expected return, risk and volatility is an inherent part of the assessment to invest in non-euro equities. Based on historical analysis, no strong economic reasons were found to systematically hedge this type of FX risk.
- ✓ FX risk stemming from the remaining portfolio (primarily fixed-income securities such as bonds and foreign currency denominated insurance liabilities). All of the remaining portfolio is cash flow hedged via cross-currency swaps.

4.3.7 Inflation risk

Inflation – as an economic parameter – indirectly affects the Life of companies in many respects, in much the same way as other parameters do (e.g. economic growth or the rate of unemployment). It is not easily quantifiable as a market risk concept. However, certain financial products or instruments have a direct link with inflation and their value is directly impacted by a change in market expectations.

The KBC Insurance Group is directly exposed to inflation risk, linked to either insurance claim accident years or to insurance claim development years, i.e.:

- ✓ Inflation linked to accident years: If a similar claim (e.g. the exact same car and damage) would happen later in time (e.g. five years later), would this impact the claim amount?
- ✓ Inflation linked to development years: If claim amounts are not paid out immediately (e.g. delayed or spread over time), would this impact the claim amount?

A specific example is workmen's compensation insurance, where particularly in the case of permanent or long-term disabilities, an annuity benefit is paid to the insured person (with the annuity being linked to inflation by law).

The inflation risk inherently linked to the insurance activities of the KBC Insurance Group is regularly assessed and accordingly mitigated through:

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7 KBC Group Re (LU), K&H Biztosító Zrt (HU), ČSOB Poist'ovňa a.s. (SK), ČSOB Pojišt'ovna a.s. (CZ), DZI Life Insurance Jsc (BG) DZI General Insurance Jsc (BG).

8 In scope: K&H Biztosító Zrt (HU), denominated in HUF & ČSOB Pojišt'ovna a.s. (CZ), denominated in CZK.
Although DZI Life Insurance Jsc and DZI General Insurance Jsc are denominated in BGN, no separate FX hedge is put in place given the pegging of the BGN to the EUR.

- ✓ Correct price setting mechanisms;
- ✓ Investment in inflation-linked assets to hedge the inflation risk on the liability side, i.e.
    - Short- and mid-term inflation risk is hedged through inflation-linked bonds.
    - Long-term inflation risk is hedged through equity and real estate exposure.

4.4 Credit risk

Credit risk is the potential negative deviation from the expected value of a financial instrument arising from the non-payment or non-performance by a contracting party (for instance a borrower), due to that party's insolvency, inability or lack of willingness to pay or perform, or to events or measures taken by the political or monetary authorities of a particular country (country risk). Credit risk thus encompasses default risk and country risk, but also includes migration risk, which is the risk for adverse changes in credit ratings.

We manage our credit risk at both transactional and portfolio level. Managing credit risk at the transactional level means that we have sound practices, processes and tools in place to identify and measure the risks before and after accepting individual credit exposures. Limits and delegations are set to determine the maximum credit exposure allowed and the level at which acceptance decisions are taken. Managing the risk at portfolio level encompasses, inter alia, periodic measuring and analysing of risk embedded in the consolidated loan and investment portfolios and reporting on it, monitoring limit discipline, conducting stress tests under different scenarios and taking risk mitigating measures.

PLS limits and monitoring

From a KBC Group perspective, next to the banking entities, also the (re)insurance entities are limited in taking credit concentration risk in their portfolios by the Portfolio Limit System (PLS). This PLS has been in use for many years, and limits are monitored per asset class.

For the following 4 asset classes, concentrations are limited for the (re)insurance entities within KBC Group:

- ✓ ***PLS Sovereigns***: limits are set on the nominal amount of credit exposure (direct credit lending, as well as bond investments) to central and federal country authorities, central banks and government-sponsored export credit agencies;
- ✓ ***PLS Sub-National Governments***: limits are set on the nominal amount of credit exposure (direct credit lending, as well as bond investments) to regional authorities, provincial authorities, cities, municipalities, public welfare bodies, inter-municipal associations and other entities for which the Sub-National Government is financially responsible (e.g., a hospital controlled/managed by a municipality is in scope, while other hospitals are out of scope). A ratings-based approach is followed, i.e. decreasing nominal limits for more risky credit ratings. Besides these single name concentration limits (i.e. PLS), limits on the maximum allowed Sub-National Government exposure per country are also in place;
- ✓ ***PLS Financial Institutions***: limits are set on the Loss Given Default (LGD) amount of any type of investment in a financial institution by the (re)insurance entities. Again a ratings-based approach is followed, i.e. decreasing LGD limits for lower credit (more risky) ratings. These LGD limits are further translated into nominal limits for operational purposes in the business;
- ✓ ***PLS Corporates and Non-Bank Financial Institutions*:** limits are set on the Loss Given Default irrecoverable (LGD(irr)) amount of all credit-risk-bearing assets (bonds and their equivalent). Here, too, a ratings-based approach is followed, i.e. decreasing LGD(irr) limits for lower external credit ratings (with a zero limit for non-investment grade counterparties).

PLS limit breaches are monitored ex-post on a quarterly basis.

Reinsurance programs

Reinsurance contracts with reinsurance companies are always negotiated by the reinsurance department. In selecting reinsurance undertakings, price is never the only parameter, but KBC also takes into account knowledge transfer, the availability of tools & processes, as well as the financial security and stability of the reinsurance undertakings.

On a quarterly basis all (re)insurance entities of KBC Insurance Group report the status of the reinsurance recoverables by counterparty to the Group Credit Risk Directorate (GCRD). GCRD calculates the group accumulation by counterparty and checks this against the limits set in the Portfolio Limit System. All possible breaches are reported to the Extended Credit Committee.

4.5 Liquidity risk

Liquidity risk is the risk that an organisation will be unable to meet its payment obligations as they come due, without incurring unacceptable losses.

The principal objective of our liquidity management is to enable the core business activities of the KBC Insurance Group to continue to generate revenue, even under adverse circumstances.

An insurance entity's liquidity is managed by matching cashflows but is also managed through monitoring the Investment Policy amongst others by ensuring that sufficient investments are made in liquid assets. As a result, insurance entities are less sensitive for 'real' liquidity risk.

The nature of liquidity risk of insurance entities is not comparable to that of banking entities, mainly because of the different structure of the asset/liability profile. Banking activities normally have to cope with assets that have longer tenors than the corresponding liabilities. Insurance activities typically have assets that are shorter and much more liquid than the corresponding liabilities.

KBC has developed a Liquidity Risk Management Framework for Insurance entities (LRMF-I). This allows for an enhanced risk management practice including identification, measurement, reporting and response and follow-up on liquidity risk for Insurance entities. Within liquidity risk for the insurance entities, the distinction is made between liquidity risk of Non-Life and Life insurance activities.

4.5.1 Non-Life liquidity risk

Within the Non-Life insurance business, liquidity risk could arise if a catastrophe (e.g. natural disaster) would take place leading to huge claims and thus large cash demands. The cash outflows will typically take place over a longer time horizon (i.e. assessment of damage, legal procedures, etc.) and certain levels of claims are covered by re-insurance contracts.

KBC's reinsurance policy states that sufficient claims payment clauses have to be negotiated to ensure that the risk related to a timing mismatch between claims' payments and reinsurance recoverable is as much as possible restricted. More specifically, reinsurance contracts should include provisions allowing to make a request for immediate claim payment for large losses outside the usual accounting periods ('cash loss' clauses). In order to follow up on these (remaining) risks the (re)insurance exposure point risk will be assessed in the near future. Furthermore, the worst case exposure to liquidity risk will be analysed including the impact of re-insurance versus the default of re-insurance counterparties under a specific scenario and the quantity and quality of the options to cover outflows in the above scenario (e.g. liquid asset buffer, liquidity lines received, etc.).

4.5.2 Life liquidity risk

The Life insurance business could be confronted with liquidity risk as a result of:

- ✓ Changing market circumstances (e.g., movement in rates, competition, etc.) leading to a surge in early redemptions;
- ✓ Changing regulatory environment (e.g., change in beneficial tax regime) leading clients to switch to other non-insurance products (market-wide scenario);
- ✓ An idiosyncratic scenario where clients question the insurance company's creditworthiness and reduce their exposure;
- ✓ A pandemic-like scenario;
- ✓ A combination of the above (combined scenario).

These scenarios could result in a mass lapse of the portfolio. In all of these scenarios, the insurance company should have an adequate liquidity buffer (cash, liquid assets, contingent credit lines, etc.) to cope with these cash outflows. Apart from the idiosyncratic scenario, the time horizon in which the cashflows will take place, is expected to be rather long (i.e. longer than one month), hence reducing the risk of not being able to meet the liabilities at an acceptable cost (e.g. the market value of the assets will be lower than normally expected in the event of idiosyncratic stress situations). Furthermore and especially in the case of KBC Insurance NV, clients will lose their fiscal advantage in case of early surrender. Surrender risk is therefore partially mitigated through fiscal rules. The liquidity risk attached to Life insurance activities is assessed by an internal stress test ratio, as defined in the LRMF.

4.5.3 Contingent liquidity risk

Liquidity risk can also arise from off-balance sheet exposure at the insurance entities. Collateral agreements for derivative and non-derivative transactions could give rise to liquidity risk when it is required to post additional collateral in adverse market circumstances. These contingent outflows will materialise in the portfolios where the transactions are concluded. However, the off-balance sheet exposure that could give rise to liquidity risk in stressed market circumstances, is rather limited for KBC Insurance Group as well as KBC Insurance NV.

4.6 Operational risk

Operational risk is the risk of loss resulting from inadequate or failed internal processes and systems, human error or sudden external events, whether man-made or natural. Operational risks include non-financial risks such as information and compliance risks, but exclude business, strategic and reputational risks.

Managing operational risk

We have a single, global framework for managing operational risk across the entire group. The Group Risk function is the primary responsible for defining the operational risk management framework. The development and implementation of this framework is supported by an extensive operational risk governance model covering all entities of the group.

The main tasks of the Competence Centre for Operational Risk are to:

- ✓ Define the operational risk management framework and the minimum standards for operational risk management processes for the group;
- ✓ Inform senior management and oversight committees of the operational risk profile;
- ✓ Provide oversight on independent risk investigations and challenges of the internal control environment where needed;
- ✓ Provide oversight and advice on the effectiveness of controls executed to reduce operational risk;
- ✓ Create an environment where risk specialists (in various areas, including information risk management, business continuity and disaster recovery, compliance, anti-fraud, legal, tax and accounting matters) can work together (setting priorities, using the same language and tools, uniform reporting, etc.). The Competence Centre for Operational risk consists of independent risk experts both at group and local level.

The operational risk profile of KBC Insurance is put at medium and though the overall operational risk profile will decrease significantly, it is expected to remain medium. This ambition is reflected in the operational risk management framework which further specifies the playing field and specifically monitors all aspects of operational risk. The key domains are:

- ✓ Business Continuity risk
- ✓ Fraud risk
- ✓ Information Security risk
- ✓ IT risk
- ✓ Legal risk
- ✓ Model risk
- ✓ Outsourcing/3rd party risk
- ✓ Process risk
- ✓ Personal & Physical Security risk

Internal Control Environment

In its yearly statements on the overall quality of KBC's Internal Control System (ICS) , the GExCo is of the opinion that the control system at the end of 2019 is largely up to standards. In specific areas (continued) improvements are needed in view of the overall risk appetite of the KBC Insurance Group with appropriate actions defined or ongoing.

This opinion is based on the evaluation of the opinions of the businesses and local Risk Department per process, the evaluation of the review by the Audit Department, as well as the evaluation of the controls in the domains covered by the Compliance Department.

Cyber risk

Information security and cyber security remain a top priority in 2019, as reports show that cyber threats are still on the rise. The risk profile is therefore assessed as medium for the entire KBC Insurance Group. An “Information Security” process is installed ensuring that information, data, processes and systems are protected against the risk of loss, misuse, unauthorized disclosure or modification, inaccessibility, inaccuracy and damage of information and also against a breach of regulation or other duties.

4.7 Other material risks

4.7.1 Strategic risk

Strategic risk is the risk caused by not taking a strategic decision, by taking a strategic decision that does not have the intended effect or by not adequately implementing strategic decisions.

KBC is confronted with high and growing uncertainty and ambiguity in its business environment which, combined with numerous transformation and regulatory projects, is putting pressure on the execution of the strategy. Due to this, strategic risk was identified as the n°1 most material risk to which KBC Insurance Group and KBC Insurance NV are exposed to. The risk profile of strategic risk is set to 'medium' based on expert opinion. A strong process is in place to manage this risk and to define strategic priorities, which supports management (in a context of strict cost control & pressure on income) to find the right balance between transformation initiatives, regulatory projects and the business as usual. There are no limits or targets related to strategic risk. Nevertheless, changes in the external environment are monitored and reported to the BoD.

KBC has sound processes to monitor evolutions in the outside world and identify the potential threats to our business model; and to respond to these by means of the strategy. Processes regarding strategic risk management are strong and awareness about the challenges for the insurance business is high. Business is acting on these challenges to its business model by means of its strategy.

A point of attention for the execution of the strategy of KBC Insurance NV is that it requires the implementation of several transformation and digitalization projects, while simultaneously a large amount of regulation that is issued by different parties has to be implemented as well. All these projects draw from the same, limited pool of expert resources; and have to be absorbed by the existing organization, on top of the business as usual. Business has to match these new developments to a complex IT infrastructure that has been developed and built upon over time.

The regulation mentioned earlier impacts the business of insurers in many ways:

- ✓ Regulation regarding consumer protection and privacy implies a large change for distribution channels;
- ✓ Regulation w.r.t. cost transparency in insurance distribution reinforces the rise of online sales and may put additional stress on margins.

The preservation of a level playing field between classic insurers and fintech based companies is of utmost importance to the sustainability of the business model. Existing legislation will have to be adapted to take the new possibilities offered by the digital economy into account.

4.7.2 Compliance risk

Compliance risk is the risk of losses or sanctions due to failure to comply with laws and regulations presenting an integrity dimension and with internal policies and codes of conduct reflecting the institution's own values, as defined in the Group Compliance Framework. It includes conduct risk, i.e. the current or prospective risk of losses arising from inappropriate supply of financial services, including cases of wilful or negligent misconduct. This covers aspects of both hard law and soft law.

No risk appetite is set for compliance risk, as KBC aims to comply with all laws and regulation in the compliance domain (included in the Integrity Policy) taking particularly account of conduct risk and the integrity dimension as non-compliance could lead to sanctions and impact on our reputation.

A Compliance Strategy was enforced during 2019 to make Group Compliance future proof, to enhance KBC Group's culture & awareness regarding compliance and to move to one Compliance Function group-wide. Meanwhile, Group Compliance has set up priorities. A large part of the Compliance efforts towards insurance will continue to be concentrated on :

- ✓ Anti-Money Laundering (AML);
- ✓ Insurance Distribution Directive (IDD);
- ✓ General Data Protection Regulation (GDPR).

4.7.3 Business risk

Business risk is the risk arising from changes in external factors (the macroeconomic environment, regulations, client behaviour, competitive landscape, socio-demographic environment, climate, etc.) that impact the demand for and/or profitability of our products and services.

Business risk is an inherent consequence of being in business. As business risk is driven by external factors, no risk appetite is set for business risk. Given the high pace of change in the outside world, the challenging competitive and macro-economic environment and the increasing regulatory pressure, the uncertainty in which the entire industry operates is high. Therefore, the risk profile of business risk has been set to high.

Business and strategic risks are assessed as part of the strategic planning process, starting with a structured risk scan that identifies the top financial and non-financial risks. Exposure to the identified business and strategic risks is monitored on an ongoing basis. Besides the risk scan, business and strategic risks are continually monitored by means of risk signals being reported to top management. In addition, these risks are discussed during the aligned planning process and are quantified under different stress test scenarios and long-term earnings assessments.

The main elements considered for business risk at KBC Insurance NV are:

- ✓ The rise of new technologies, changing customer behaviour, consumer protection regulation and a distribution landscape that is more and more becoming digital pose new opportunities and threats. These elements may lead to disintermediation by putting pressure on the classic distribution model where the distributor builds up a strong relation with his customer. Key for the insurance industry is the ability to adapt to a rapidly changing world with multiple factors that challenge the business model;
- ✓ The continued low interest rate environment weighs on the profitability of the Life insurances, despite that interest rates slightly improved compared to their lowest point. Low bond yields make it very difficult to offer an attractive proposition to new clients, and also put the yields of reinvestment of maturing assets that cover existing contracts under pressure. The resulting search for yield and the abundant liquidity in the market drives up the prices of assets and causes risk premiums to decrease, leading to concerns whether risks are still adequately rewarded and the fear for asset bubbles;
- ✓ Different geopolitical factors, such as trade wars, the uncertain outcome of the Brexit, Italian budget discussions, … will continue to add uncertainty to the financial markets and may weigh on economic growth.

4.7.4 Reputational risk

Reputational risk is the risk arising from loss of confidence by or negative perception on the part of stakeholders – be it accurate or not – that can adversely affect a company's ability to maintain existing, or establish new, business/customer relationships and have continued access to sources of funding.

One of KBC's main assets is to have and maintain a strong reputation. To manage reputational risks, which are often secondary in nature, KBC sets a strict risk appetite on all its risks, promotes corporate social & environmental responsibility, aims for sustainable growth and actively manages incidents if they occur. KBC Group actively monitors external stakeholders' confidence and expectations and performs a yearly reputation survey to benchmark itself to its peers. GExCo monitors Net Promoter Scores (NPS), reputation and employee engagement metrics versus internal targets.
In order to avoid major reputational damage, KBC has installed a procedure not to do business with blacklisted companies.

Reputation risk at KBC Insurance NV remains on the same level as last year and remains within the boundaries of a low risk appetite. It cannot be underpinned through a metric and this assessment is the result of expert judgment. The most important considerations for reputational risk are:

- ✓ The overall operational risk, which is assessed as medium, but will improve due to the projects named earlier. The process improvements in the Life domain, with less manual interventions, reduce the chances of operational errors and consequent reputational damage to occur. Also the improvements w.r.t.. SLA's in the processing of insurance contracts have a beneficial effect on the reputational risk.
- ✓ The fact that the company works with external partners (eco-systems, outsourcing activities). Those partners however are well screened and (for the moment) rather limited.
- ✓ Claims handling. However, as KBC has a policy to be 'close to the client', possible incidents will have a rather limited overall impact;

- ✓ Branch 23 products, in which the client bears the investment risk, may also be a source of reputational risk. However, the management considers this risk mitigated as Branch 23 distribution is compliant with the stringent Mifid regulation;
- ✓ Furthermore, a sound New and Active Product Process (NAPP) working is in place to mitigate the risks and risks that originate at KBC Bank are kept in check by the agreements between the insurer and the bank and asset management, and monitoring of these agreements.

4.8 Other information

Sensitivity analysis & stress testing on Solvency II required capital

Risk sensitivity and stress-testing exercises are set up to uncover risks that would otherwise remain unidentified and also to allow us to observe how risk measurements change under stressed conditions. These sensitivity exercises are performed on a regular basis.

Stress testing is an important risk management tool that adds value both to strategic processes and to day-to-day risk management (risk identification, risk appetite and limit setting, ...). As such, stress testing is an integral part of our risk management framework, and an important building block of ORSA (the Own Risk and Solvency Assessment).

Stress tests are performed internally within the insurance group or at local entity level or are initiated on a regular basis by the regulator (EIOPA7[9] or local regulators). KBC also performs ad hoc integrated stress tests to test its vulnerability for specific risks and potential adverse conditions that may arise.

[9] European Insurance and Occupational Pensions Authority

Valuation for solvency purposes

5 Valuation for solvency purposes

The following tables provides both the Solvency II value used in the economic balance sheet and the accounting (IFRS/BGAAP) value for each material class of assets and liabilities. A description of how this value is determined can be found in the sections below.

A more detailed composition of the Solvency II values can be found in the QRT S.02.01 - Balance Sheet.

KBC Insurance Group:

Economic balance sheet 31/12/2019 - Assets (in m EUR)	**IFRS Value**	**Solvency II Value**	***Difference***
Goodwill & intangible assets	135	0	*-135*
Deferred tax assets	5	0	*-5*
Property (other than for own use)	136	240	*103*
Participations and related undertakings	274	264	*-10*
Equity Instruments	1.341	1.341	*0*
Bonds	17.878	18.869	*990*
Derivatives	1	1	*0*
Deposits other than cash equivalents	488	619	*131*
Assets held for index-linked and unit-linked funds	14.477	14.477	*0*
Loans & mortgages	2.290	2.513	*223*
Reinsurance recoverables	123	84	*-39*
Own shares	0	203	*203*
Other	705	620	*-85*
Total Assets	**37.853**	**39.230**	***1.377***
Economic balance sheet 31/12/2019 - Liabilities (in m EUR)	**IFRS Value**	**Solvency II Value**	***Difference***
Technical provisions -non-life	2.834	2.166	*-668*
Technical provisions - Life (excl. Index-linked and unit-linked)	14.475	16.783	*2.307*
Technical provisions - Index-linked and unit-linked	14.585	14.479	*-106*
Deferred tax liabilities	332	254	*-78*
Derivatives	47	49	*2*
Subordinated Loan (Tier2)	0	500	*500*
Other	1.650	1.644	*-6*
Total Liabilities	**33.923**	**35.875**	***1.951***
Excess Assets over Liabilities	**3.930**	**3.356**	***-574***

Table 35: Economic balance sheet 31/12/2019 - KBC Insurance Group

KBC Insurance NV:

Economic balance sheet 31/12/2019 - Assets (in m EUR)	BGAAP Value	Solvency II Value	*Difference*
Goodwill & intangible assets	0	0	*0*
Deferred tax assets	0	0	*0*
Property (other than for own use)	127	226	*99*
Participations and related undertakings	847	1.206	*359*
Equity Instruments	939	1.247	*308*
Bonds	14.877	16.763	*1.886*
Derivatives	1	0	*-1*
Deposits other than cash equivalents	454	582	*128*
Assets held for index-linked and unit-linked funds	13.319	13.319	*0*
Loans & mortgages	2.282	2.503	*222*
Reinsurance recoverables	108	88	*-20*
Own shares	203	203	*0*
Other	330	351	*21*
Total Assets	**33.488**	**36.489**	***3.001***
Economic balance sheet 31/12/2019 - Liabilities (in m EUR)	**BGAAP Value**	**Solvency II Value**	***Difference***
Technical provisions -non-life	2.494	1.702	*-791*
Technical provisions - Life (excl. Index-linked and unit-linked)	13.905	15.925	*2.020*
Technical provisions - Index-linked and unit-linked	13.426	13.345	*-81*
Deferred tax liabilities	3	123	*120*
Derivatives	13	40	*27*
Subordinated Loan (Tier2)	500	500	*0*
Other	1.778	1.494	*-284*
Total Liabilities	**32.119**	**33.131**	***1.012***
Excess Assets over Liabilities	**1.369**	**3.358**	***1.989***

Table 36: Economic balance sheet 31/12/2019 - KBC Insurance NV

The Table 37 gives a clear overview on how for KBC Insurance Group the **IFRS value** for 'excess assets over liabilities' is reconciled with the Solvency II value for 'excess assets over liabilities'. The following parts of this section provide a more detailed view on the underlying methodological differences.

Reconciliation IFRS equity & assets over liabilities Solvency II (in m EUR)	
IFRS equity	**3.422**
Valuation differences between IFRS and Solvency II	
of which: deduction intangible assets (after tax)	-128
of which: valuation difference participations	-10
of which: valuation difference real estate at fair value (after tax)	86
of which: valuation difference fair value loans & receivables (after tax)	266
of which: valuation difference fair value amortised cost bonds (after tax)	749
of which: valuation difference reinsurance recoverables	-32
of which: valuation difference technical liabilities (after tax)	-1.255
of which: treasury shares	203
of which: volatility adjustments	104
of which: other	-50
Assets over liabilities Solvency II	**3.356**

Table 37: Reconciliation IFRS equity & assets over liabilities Solvency II - KBC Ins Grp

The main differences between IFRS and Solvency II valuations per asset class are:

- ✓ **Goodwill and intangible** assets are valued at zero under Solvency II. Under IFRS software (27m EUR) and goodwill (108m EUR) are included as well. Goodwill includes the goodwill paid on companies included in the scope of consolidation and in relation to the acquisition of activities and mainly relates to the acquisition of DZI Insurance and ČSOB Pojišt'ovna a.s. (CZ);
- ✓ The higher **net deferred tax liability** under Solvency II compared to IFRS is due to the deferred tax liabilities calculated on the difference between the IFRS and Solvency II balance sheet. The difference between Solvency II and IFRS assets is higher than the difference on the liability side, increasing deferred tax liabilities;
- ✓ **Property (other than for own use)** is valued at fair value under Solvency II, while under IFRS it is measured at initial cost minus accumulated depreciation and impairment losses. Value for which the property could be sold between knowledgeable willing parties in an arm's length transaction is much higher than the IFRS accounting value;
- ✓ **Equity instruments** are measured at fair value, both under IFRS as under Solvency II. Therefore, the difference between both views is minimal;
- ✓ **Bonds** are (mainly) valued using 2 valuation methods under IFRS:
    - Over 70% is valued at fair value through other comprehensive income (FVOCI), meaning the Solvency II value (fair value) equals the IFRS value.
    - A small 30% of the bonds is valued at amortized cost under IFRS, causing the difference between the IFRS view (amortized cost) and Solvency II view, where these bonds are also measured at fair value. Given the low interest rate environment, the fair value on these bonds is higher than the amortized cost value.
- ✓ **Assets held for Index-Linked and Unit-Linked funds** are equal under IFRS and Solvency as both are measured at fair value. On liability side, a difference is noticed for Index-Linked and Unit-Linked TPs between IFRS and Solvency as management fees are included under Solvency II;
- ✓ **Deposits other than cash equivalents** are measured at amortized cost under IFRS and at fair value under Solvency II. Due to the decrease in interest rates, the Solvency II (fair) value is higher than the IFRS value;
- ✓ **Loans and mortgages** are valued at amortized cost under IFRS. Under Solvency II, these are valued at fair value. Fair value of these loans is higher than the amortized cost value given the lower interest rates;
- ✓ **Own Shares/treasury shares**: KBC Insurance NV has 203m EUR of treasury shares. Under IFRS equity (i.e. excess of assets over liabilities under IFRS) treasury shares are deducted from equity, meaning they are not part of the balance sheet. Under Solvency II treasury shares are reported on the Economic Balance Sheet as an asset. For determining the Available Own Funds under Solvency II, the treasury shares are deducted from the Excess of assets over liabilities.

Technical Provisions under Solvency II consist of a best estimate and a risk margin. Best estimates corresponds to the probability-weighted average of future cashflows, which are discounted using the risk free rate and volatility adjustment. The risk margin is calculated using the Solvency Capital Requirement, the cost-of-capital as determined by the regulator and the risk free rate curve. IFRS technical provisions consists of different types of provisions (see 5.2 Technical provisions).

For KBC Insurance NV the Table 38 gives a clear overview of how the **BGAAP value** for 'excess assets over liabilities' is reconciled with the Solvency II value for 'excess assets over liabilities'. The following parts of this section provide a more detailed view on the underlying methodological differences (in m EUR).

Reconciliation IFRS equity & assets over liabilities BGAAP Solvency II (in m EUR)	
Share capital	65
Share premium	1.086
Reserves	218
IFRS parent shareholder's equity	**1.369**
BGAAP equity	**1.369**
Valuation differences between IFRS and Solvency II	
of which : valuation difference real estate at fair value (after tax)	74
of which: valuation difference participations	359
of which: valuation difference fair value equity	308
of which: valuation difference fair value amortised cost bonds (after tax)	1.422
of which: valuation difference fair value loans & receivables (after tax)	261
of which: valuation difference reinsurance recoverables	-15
of which: valuation difference technical liabilities (after tax)	-861
of which: other	441
Assets over liabilities Solvency II	**3.358**

Table 38: Reconciliation IFRS equity & assets over liabilities Solvency II - KBC Ins NV

- ✓ **Property (other than for own use)** is measured at fair value under Solvency II which explains the difference as under BGAAP property is measured at initial cost minus accumulated depreciation. The fair value (for which the property could be sold between knowledgeable willing parties in an arm's length transaction) is much higher than the BGAAP accounting value;
- ✓ **Holdings in related undertakings, including participations** are valued under SII based on the net asset value according the economic balance for insurance companies and for non-insurance companies the net asset value is based on their IFRS financial statements. In BGAAP participating shares are recognized at acquisition costs less impairments, if any;
- ✓ **Equity instruments** are measured at fair value under IFRS and Solvency II and measured at cost (i.e. acquisition costs less impairments, if any) under BGAAP;
- ✓ **Bonds** are under Solvency II valued at fair value determined according to what is stipulated under IFRS13 Fair value. In BGAAP the bonds are valued at amortized costs less impairment, if any;
- ✓ **Assets held for index-linked and unit-linked funds** are equal under Solvency II and BGAAP as both are measured at fair value;
- ✓ **Deposits other than cash equivalents** are measured at amortized cost under BGAAP and at fair value under Solvency II. Due to the decrease in interest rates, the Solvency II (fair) value is higher than the BGAAP value;
- ✓ **Loans and mortgages** are valued at amortized cost under BGAAP. Under Solvency II, these are valued at fair value. Fair value of these loans is positive given the lower interest rates;
- ✓ **Own Shares/treasury shares**: KBC Insurance NV has 203m EUR of treasury shares. Under Solvency II and BGAAP treasury shares are reported on the Economic Balance Sheet as an asset. For determining the Available Own Funds under Solvency II, the treasury shares are deducted from the Excess of assets over liabilities. In BGAAP an undistributable reserve as part of equity is being created;
- ✓ **Technical provisions** under Solvency II consist of a best estimate and a risk margin. Under the statutory accounts these are accounted for according to BGAAP; including the mathematical reserves, the unearned premium reserve, the claims reserve (incl. IBNR), the flashing light reserve and the equalization reserve etc.;

- ✓ **Pension benefit obligations** are recognized under Solvency II in compliance with IAS19 employee benefits. Under BGAAP these Pension benefit obligations for the Defined Benefit Plans are not recognized;
- ✓ **Deferred tax liabilities** are recognized under Solvency II in compliance with IAS12 income taxes and are mainly the result of the non-realized gains included in the fair value of the bonds. Valuation differences on the technical provisions offset each other and as such impact on deferred tax is neglectable. In BGAAP, deferred taxes are not recognized;
- ✓ **Derivatives** fulfil the criteria of hedging instrument under BGAAP and as such are valued on a pro-rata temporis basis. For Solvency II derivatives are values on fair value basis;
- ✓ **Other liabilities** under BGAAP include the foreseen dividend pay-out for an amount of 156m EUR and the fund for future appropriation of 158m EUR.

5.1 Assets – material classes of assets

5.1.1 Solvency II value

5.1.1.1 Goodwill

Goodwill should be valued at zero *(Delegated Regulation (EU) 2015/35, Art. 12)*.

5.1.1.2 Deferred taxes

Deferred taxes, other than deferred tax assets arising from the carry forward of unused tax credits and the carry forward of unused tax losses, are valued on the basis of the difference between the Solvency II values and the values ascribed to assets and liabilities as recognised and valued for tax purposes *(Delegated Regulation (EU) 2015/35, Art. 15).*

5.1.1.3 Bonds, Equity Instruments and Loans & mortgages

- ✓ For Solvency II purposes, 'Bonds', 'Equity instruments' and 'Loans & mortgages' are valued at the amount for which they could be exchanged between knowledgeable willing parties in an at arm's length transaction. This definition is in line with the IFRS definition of fair value;
- ✓ KBC defines 'fair value' as 'the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date'. Fair value is not the amount that an entity would receive or pay in a forced transaction, involuntary liquidation or distressed sale. A deviation from IFRS is however applicable for the valuation of financial liabilities, as Solvency II explicitly imposes that the fair value may not reflect the own credit risk (Delegated Regulation (EU) 2015/35, Article 14;
- ✓ All internal valuation models used at KBC are validated by an independent Risk Validation Unit. In addition, the Executive Committee has appointed a Group Valuation Committee (GVC) to ensure that KBC and its entities meet all the legal requirements for measuring financial assets and liabilities at fair value. The GVC monitors consistent implementation of the KBC Valuation Framework, which consists of various guidelines, including the Group Market Value Adjustments Policy and the Group Parameter Review Policy. The GVC meets at least twice a quarter to approve significant changes in valuation methods (including, but not limited to, models, market data and inputs) or deviations from group policies for financial assets and liabilities measured at fair value. The committee is made up of members from Finance, Risk Management and the Middle Office. Valuation uncertainty measurements are made and reported to the GVC every semester. Lastly, certain fair values generated by valuation models are challenged by a team set up specifically for this purpose;
- ✓ Market value adjustments are recognised on all positions that are measured at fair value to cover close-out costs, adjustments for less liquid positions or markets, mark-to-model-related valuation adjustments, counterparty risk and funding costs. Credit value adjustments (CVAs) are used when

measuring derivatives to ensure that the market value of the derivatives is adjusted to reflect the credit risk of the counterparty. In making this adjustment, both the mark-to-market value of the contract and its expected future fair value are taken into account. These valuations are weighted based on the counterparty credit risk that is determined using a quoted credit default swap (CDS) spread, or, if there is no such spread, on the counterparty credit risk that is derived from bonds whose issuers are similar to the derivative counterparty in terms of rating, sector, geographical location and seniority of the exposure. A funding value adjustment (FVA) is a correction made to the fair value of derivatives in order to ensure that the (future) funding costs or income attached to entering into and hedging such instruments are factored in when measuring the value of the instruments;

- ✓ The IFRS9 fair value hierarchy prioritises the valuation techniques and the respective inputs into three levels;
- ✓ The fair value hierarchy gives the highest priority to 'level 1 inputs'. This means that, when there is an active market, quoted prices have to be used to measure the financial assets or liabilities at fair value. Level 1 inputs are prices that are readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency (and that are quoted in active markets accessible to KBC). They represent actual and regularly occurring market transactions on an arm's length basis. The fair value measurement of financial instruments with quoted prices is based on a mark-to-market valuation derived from currently available transaction prices. No valuation technique (model) is involved;
- ✓ If there are no price quotations available, the reporting entity establishes fair value using a model based on observable or unobservable inputs. The use of observable inputs needs to be maximised, whereas the use of unobservable inputs has to be minimise;
- ✓ Observable inputs are also referred to as 'level 2 inputs' and reflect the assumptions market participants would use in pricing the asset or liability based on market data obtained from sources independent of the reporting entity. Observable inputs reflect an active market. Examples of observable inputs are the risk-free rate, exchange rates, stock prices and implied volatility. Valuation techniques based on observable inputs include discounted cash flow analysis, reference to the current or recent fair value of a similar instrument, or third-party pricing, provided that the third-party price is in line with alternative observable market data;
- ✓ Unobservable inputs are also referred to as 'level 3 inputs' and reflect the reporting entity's own assumptions about the assumptions that market participants would use in pricing the asset or liability (including assumptions regarding the risks involved). Unobservable inputs reflect a market that is not active. For example, proxies and correlation factors can be considered to be unobservable in the market;
- ✓ The valuation methodology and the corresponding classification in the fair value hierarchy of the most commonly used financial instruments are summarised in the table below. This table provides an overview of the level in which the instruments are generally classified, but exceptions are possible. In other words, whereas the majority of instruments of a certain type are within the level indicated in the table, a small portion may actually be classified in another level;

	Instrument type	Products	Valuation technique
Level 1	Liquid financial instruments for which quoted prices are regularly available	FX spots, exchange traded financial futures, exchange traded options, exchange traded stocks, exchange traded funds, liquid government bonds, other liquid bonds, liquid asset backed securities (ABS) in active markets	Mark-to-market (quoted prices in active markets)
Level 2	Plain vanilla/liquid derivatives	(Cross-currency) interest rate swaps (IRS), FX swaps, FX forwards, forward rate agreements (FRA), inflation swaps, dividend swaps, commodity swaps, reverse floaters, bond future options, interest rate future options, overnight index swaps (OIS), FX resets	Discounted cashflow analysis based on discount and estimation curves (derived from quoted deposit rates, FX swaps and (CC)IRS)
		Caps & floors, interest rate options, European & American stock options, European & American FX options, forward starting options, digital FX options, FX strips of simple options, European swaptions, constant maturity swaps (CMS), European cancellable IRS, compound FX options	Option pricing model based on observable inputs (e.g., volatilities)
		Credit default swaps (CDS)	CDS model based on credit spreads
	Linear financial assets (without optional features) – cash instruments	Deposits, simple cashflows, repo transactions	Discounted cashflow analysis based on discount and estimation curves (derived from quoted deposit rates, FX swaps and (CC)IRS)
	Asset backed securities	Medium liquid asset backed securities	Third-party pricing (e.g., lead manager); prices corroborated by alternative observable market data, or using comparable spread method
	Debt instruments	KBC IFIMA own issues (liabilities)	Discounted cashflow analysis and valuation of related derivatives based on observable inputs
	Linear financial liabilities (cash instruments)	Loans, commercial paper	Discounted cashflow analysis based on discount and estimation curves (derived from quoted deposit rates, FX swaps and (CC)IRS)
Level 3	Exotic derivatives	Target profit forwards, target strike forwards, Bermudan swaptions, digital interest rate options, quanto interest rate options, digital stock options, Asian stock options, barrier stock options, quanto digital FX options, FX Asian options, FX European barrier options, FX simple digital barrier options, FX touch rebates, double average rate options, inflation options, cancellable reverse floaters, American and Bermudan cancellable IRS, CMS spread options, CMS interest rate caps/floors, (callable) range accruals, outperformance options, auto-callable options	Option pricing model based on unobservable inputs (e.g., correlation)
	Illiquid credit-linked instruments	Collateralised debt obligations (notes)	Valuation model based on correlation of probability of default of underlying assets
	Private equity investments	Private equity and non-quoted participations	Based on the valuation guidelines of the European Private Equity & Venture Capital Association (EVCA)
	Illiquid bonds/asset backed securities	Illiquid bonds/asset backed securities that are indicatively priced by a single pricing provider in an inactive market	Third-party pricing (e.g., lead manager), where prices cannot be corroborated due to a lack of available/reliable alternative market data
	Debt instruments	KBC own issues (KBC IFIMA)	Discounted cashflow analysis and valuation of related derivatives based on unobservable inputs (indicative pricing by third parties for derivatives)

5.1.1.4 Property (other than for own use)

Property other than for own use is valued at the amount for which they could be exchanged between knowledgeable willing parties in an at arm's length transaction under Solvency II.

5.1.1.5 Assets held for index-linked and unit-linked funds

Assets held for Index-Linked and Unit-Linked contracts (classified in line of business 31 (branch 23) as defined in Annex I of Delegated Regulation (EU) 2015/35), are measured at fair value.

5.1.1.6 Deposits other than cash equivalents

Deposits other than cash equivalents are measured at fair value. The same principles are applied as discussed for 'Bonds', 'Equity instruments' and 'Loans & mortgages'.

5.1.1.7 Own shares

This is the total amount of own shares held directly by the group (also referred to as 'Treasury shares' under IFRS). The amount of own shares is deducted from the excess of assets over liabilities when determining the available capital as illustrated in section 7.2. Basic own funds.

5.1.2 IFRS value for KBC Insurance Group

To determine the IFRS value, reference can be made to the IFRS valuation rules applicable within KBC as included in the Annual Report of KBC Group Consolidated – Notes on the accounting policies – Note 1 2: Summary of significant accounting policies.

5.1.2.1 Goodwill

Goodwill is defined as any excess of the cost of the acquisition over the acquirer's interest in the fair value of the identifiable assets acquired and liabilities and contingent liabilities assumed at the date of acquisition. It is recognised as an intangible asset and is carried at cost less impairment losses. Goodwill is not amortised, but is tested for impairment at least once a year or if there is either internal or external evidence for doing so. An impairment loss is recognised if the carrying amount of the cash-generating unit to which the goodwill belongs exceeds its recoverable amount. Impairment losses on goodwill cannot be reversed. For each new business combination, KBC has to choose whether to measure minority interests at fair value or as their proportionate share of the acquiree's net identifiable assets. This choice determines the amount of goodwill recognised.

5.1.2.2 Deferred taxes

Deferred tax assets are recognised for all deductible temporary differences between the carrying value of assets and liabilities and their tax base, and for carry forward of unused tax losses and for carry forward unused tax credits, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences can be utilised. KBC calculates deferred tax assets for carry forward unused tax losses. When estimating the period over which tax losses can be used against future taxable profits, KBC uses projections for a period between eight to ten years.

5.1.2.3 Bonds, Loans & Mortgages, Equity Instruments and Derivatives

KBC applies all the requirements of IFRS 9 as from 1 January 2018, except for the hedge accounting transactions which continued to be accounted for in accordance with IAS 39.
On initial recognition of a financial asset, KBC first assesses the contractual terms of the instrument in order to classify it as an equity or debt instrument. An equity instrument is defined as any contract that evidences a residual interest in another entity's net assets. In order to satisfy this condition, KBC reviews whether the instrument includes no contractual obligation for the issuer to deliver cash or exchange financial assets or financial liabilities with another entity under conditions that are potentially unfavourable to the issuer.
Any instruments which do not meet the criteria of equity instruments are classified as debt instruments by KBC.

Debt instruments
When KBC concludes that the financial asset is a debt instrument, then on initial recognition, it can be categorised in one of the following categories:

- ✓ Mandatorily measured at fair value through profit or loss (FVPL);
- ✓ Designated at initial recognition at fair value through profit or loss (FVO);
- ✓ Fair value through other comprehensive income (FVOCI);
- ✓ Amortised cost (AC);
- ✓ Fair value through profit or loss – overlay approach (only possible for debt instruments held in an activity connected with the insurance activity which do not pass the SPPI test) (FVI).

Debt instruments have to be classified in the **FVPL** category when (i) they are not held in business model whose objective is to hold assets to collect contractual cash flows or within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets or alternatively (ii) they are held in such business model but the contractual terms of the instrument give rise on specified dates to cash flows that are not solely payments of principal and interest on the principal amount outstanding.
Further, KBC may in some cases, on initial recognition, irrevocably designate a financial asset that otherwise meets the requirements to be measured at AC or at FVOCI as at fair value (**FVO**) if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise.

A debt instrument is measured at **FVOCI** only if it meets both of the following conditions and is not designated as at FVO:

- ✓ the asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets;
- ✓ and the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

A debt instrument is measured at **AC** only if it meets both of the following conditions and is not designated as at FVO:

- ✓ the asset is held within a business model whose objective is to hold assets to collect contractual cash flows;
- ✓ the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

A debt instrument is categorised as **FVI** when it is held in respect of a business activity that is connected to contracts in scope of IFRS 4 and if it is measured at fair value through profit or loss applying IFRS 9 but would not have been measured at fair value through profit or loss in its entirety in accordance with IAS 39 and for which KBC elected using the overlay approach. Regarding the application of the overlay approach more information is provided in section *"Overlay approach"* below.
Loans and advances are debt instruments held by the institutions that are not securities and are in general measured at amortised cost.

Equity instruments
Financial equity instruments are categorised in one of the following categories:

- ✓ Mandatorily measured at fair value through profit or loss (FVPL);
- ✓ Equity instruments elected for fair value through other comprehensive income (FVOCI);
- ✓ Equity instruments held under an activity connected with the insurance activity, KBC applies the fair value through profit or loss – overlay (FVI);

KBC can designate equity instruments of the insurance activity in the FVI category, until the effective date of IFRS 17. The equity investments that KBC Insurance activity classifies as FVI shall meet both of the following criteria:

- ✓ it is measured at fair value through profit or loss applying IFRS 9 but would not have been measured at fair value through profit or loss in its entirety applying IAS 39;
- ✓ it is not held in respect of an activity that is unconnected with insurance contracts.

Regarding the application of the overlay approach more information is provided in section "*Overlay approach"* below.

Derivatives
KBC can recognise derivative instruments either for trading purpose or as hedging derivatives. Derivatives can have asset or liability positions depending on their actual market value.

- ✓ **Trading derivatives**
  Derivative instruments are always measured at fair value and KBC makes a distinction as follows:

- Derivatives that are held with a hedging intent but for which hedge accounting cannot be or is not applied (economic hedge): Hedging instruments can be acquired with the intention of economically hedging an external exposure but without the application of hedge accounting. The interest component on these derivatives is recognised under *"Net Interest Income"* while all other fair value changes are recognised under *"Net result from financial instruments at fair value through profit or loss";*
- Derivatives held without hedging intent (trading derivative): KBC entities can also enter into a derivative position without any intention to hedge economically a position. Such activity can relate to closing / selling an external position in the near term or for short-term profit taking purposes. All fair value changes on such derivatives are recognised under *"Net result from financial instruments at fair value through profit or loss".*

✓ **Hedging derivatives**
Hedging derivatives are derivatives which are specifically designated in a hedge relationship. The accounting process of the such derivatives are detailed in the section *"Hedge Accounting – Hedging Instrument"*.

Overlay approach
In accordance with the amendment to IFRS 4 issued in September 2016, KBC decided to use the overlay approach to overcome the temporary consequences of the different effective dates of IFRS 9 and IFRS 17 (replacing IFRS 4). Accordingly, KBC uses the overlay approach which reclassifies from the income statement to OCI the extra volatility related to the adoption of IFRS 9. The reclassified amounts are recognised in the overlay reserve within equity.
The overlay approach is applied for the financial assets of KBC's insurance activity that are eligible. The eligibility is based on the following criteria:

- ✓ Assets that are measured at FVPL applying IFRS 9 which would not have been measured at FVPL in its entirety applying IAS 39;
- ✓ All assets except those held in respect of an activity that is unconnected with contracts within the scope of IFRS 4.

Financial assets can be designated under the overlay approach until the instrument:

- ✓ is derecognised;
- ✓ when it is no longer held in respect of an activity that is connected with insurance contracts;
- ✓ when at the beginning of any annual period KBC decides not applying the overlay approach for that particular instrument;
- ✓ Until IFRS 17's effective date.

The application of the overlay approach requires retaining certain IAS 39 accounting policies for financial assets which are the following:

- ✓ Impairment on equity instrument: equity instruments held by the insurance activity of KBC were typically classified as AFS under IAS 39, under IFRS 9 they are classified at FVPL. The designation under the overlay approach requires applying the IAS 39 impairment on equity instruments. By using the overlay approach, all fair value changes are recognised in the overlay reserve but when the decline is significant (more than 30%) or prolonged (more than one year) compared to the acquisition cost then the fair value loss is recognised in the income statement. Any further decrease is also recognised directly in the income statement while increases are recognised in the overlay reserve;

- ✓ Recognition of gain and losses in the income statement upon disposal of equity instruments: by designating the equity instruments connected to KBC's insurance activity under the overlay approach upon the sale of the equity instruments the accumulated overlay reserve in OCI is recycled to the income statement ensuring same results as under IAS 39;
- ✓ Impairment on debt instrument: The KBC methodology for the calculation of Incurred But Not Reported (IBNR) impairments on non-defaulted debt securities booked at amortized cost (HTM and L&R) is based on the Basel II IRB Advanced models with an emergence period of 1,5 months (no PIT factor is applied). No IBNR impairments are calculated for debt securities at fair value (AFS).

5.1.2.4 Property (other than for own use)

Property other than for own use or investment property is defined as a real estate property either built, purchased or acquired under a finance lease by KBC, which is held to earn rentals or capital appreciations rather than used by KBC for the supply of services or for administrative purposes.
Investment property is initially recognised at cost (including directly attributable costs). KBC subsequently measures investment property at initial cost minus accumulated depreciation and impairment losses.

5.1.2.5 Assets held for index-linked and unit-linked funds

Assets held for index-linked and unit-linked funds are recognised as investment contracts in financial assets mandatorily at fair value through P&L other than Held For Trading (MFVPL).

5.1.2.6 Deposits other than cash equivalents

Deposits other than cash equivalents are measured at amortised cost.

5.1.2.7 Own shares

If an entity reacquires its own equity instruments, those instruments ('treasury shares') are not recognised as an asset on the balance sheet but should be deducted from equity instead.

5.1.3 BGAAP for KBC Insurance NV

To determine the BGAAP value reference can be made to the BGAAP valuation rules applicable within KBC Insurance NV as included in the Annual Accounts of KBC Insurance NV in note 20 of the BGAAP valuation rules.

Under BGAAP assets and liabilities are measured at costs and no fair valuing is applied within the statutory accounts of KBC Insurance.

5.1.3.1 Formation expenses, intangible and tangible assets

Formation expenses are charged directly to the profit and loss account unless the Board of Directors decides otherwise.
Intangible fixed assets whose useful lifetime is limited are depreciated over five years unless the Board of Directors decides otherwise. Systems software is depreciated at the same rate as hardware and is therefore depreciated over a period of three years. Software other than systems software is depreciated over five years. Core systems with a longer useful life are depreciated straight line over an eight-year period. Core systems are types of standard software, including back-end data applications, for processing operations during the day and updates of the general ledger balances on the mainframe.
All tangible fixed assets are recognised at acquisition cost, less accumulated depreciation. They are recorded at acquisition cost, including ancillary, directly allocable costs (acquisition costs, non-deductible VAT etc.).
The rates of depreciation are determined on the basis of the anticipated useful economic life of the item and are applied according to the straight-line method. All tangible fixed assets are depreciated on an accruals basis from the time they are available for use. The ancillary costs are written off over the life of the asset. A write-down is charged for ancillary costs on the acquisition of land.

5.1.3.2 Equity shares

Participating interests and shares that are considered financial fixed assets are recognised at acquisition costs. Write downs are applied only in the event of a lasting impairment in or loss of value, established on the basis of the financial position, the profitability and the prospectus of the company concerned.
Impairment charges are written back immediately the stock market price rises, albeit to no more than the acquisition value.
Listed shares are recognised at acquisition cost and impaired if the stock market price is sustainably (> 1 year) or significantly (> 30%) lower than the book value, showing that the impairment is sufficiently lasting in nature. The impairment charge is then equal to the difference between the carrying value and the stock market price. Impairment charges are reversed immediately when the stock market price rises, albeit to no more than the acquisition value.
Unlisted shares are written down in the event of a lasting diminution in value or impairment justified by the state, profitability or prospects of the company in which the holdings, shares or profit-share certificates are held.

5.1.3.3 Bonds

Fixed-income securities are recognised at amortised costs and interest is recognised according to the effective interest method.

The fixed-income securities are impaired according to the principles that apply for the valuation of granted loans. When market value are declining below acquisition value, an impairment is recognised when there is uncertainty as to whether all or part of the receivable or security will be paid when due.
Fixed-income treasury securities (under ‘other financial investments’) serving to support liquidity are impaired if their market value is lower than the book value.
Impairment is booked on real estate certificates if their market value is less than their acquisition cost (LOCOM). These impairment charges are written back where the market value rises, up to a maximum of the acquisition cost of the underlying security.

5.1.3.4 Loans and advances

Loans and advances are recorded in the balance sheet for the outstanding principal amount, plus the interest past due and sundry costs to be paid by the customers. Loans classified as irrecoverable and doubtful, specific write-downs are posted on a case-by-case basis in order to cover the losses which are considered certain or likely to ensue on the outstanding loans.

5.1.3.5 Assets held for index-linked and unit-linked funds

Assets held for index-linked and unit-linked funds are recognised as investment contracts in financial assets mandatorily at fair value through P&L other than Held For Trading (MFVPL).

5.1.3.6 Deposits other than cash equivalents

Deposits other than cash equivalents are measured at amortised cost.

5.1.3.7 Own shares

If an entity reacquires its own equity instruments, those instruments (‘treasury shares’) are recognised as an asset on the balance sheet and an undistributable reserve is recognised for the same amount as part of equity.

5.2 Technical provisions

5.2.1 Solvency II value

5.2.1.1 Technical provisions in general

In general, the technical provisions on the Solvency II economic balance sheet have to be calculated as the sum of a best estimate and a risk margin:

- ✓ The **best estimate** corresponds to the probability-weighted average of future cashflows, taking into account the time value of money, using the relevant risk-free interest rate term structure;
- ✓ The **risk margin** is calculated by determining the cost of providing an amount of eligible own funds equal to the Solvency Capital Requirement necessary to support the insurance and reinsurance obligations over their lifetime. The cost of capital rate is defined by the regulator, and is set at 6%.

An exception to the requirement to calculate a best estimate and a risk margin is made for insurance obligations for which the value can be replicated reliably using financial instruments for which a reliable market value is observable. The value of the technical provisions associated with these future cash flows shall be determined 'as a whole' (i.e. no separate calculation of best estimate and risk margin), based on the market value of the financial instruments.

Technical provisions Life in general relate to those insurance liabilities that are 'pursued on similar technical basis to that of Life insurance', even if they are not Life insurances from a pure legal perspective. In practice the classification into Life resp. Non-Life liabilities is based on the actuarial techniques used for calculating the technical provisions. This split up, specific for the Solvency II regulation framework, entails some classification differences with the IFRS balance sheet.

For calculation of the best estimate, within the Life respectively Non-Life obligations, the contracts have to be split up in so called 'homogeneous risk groups'. These are group of contracts with similar characteristics and dynamics, for which the same assumptions can be used when projecting the insurance cash flows in the future.

In order to obtain the best estimate which corresponds to the probability-weighted average of future cashflows, the best estimate calculation must take into account all uncertainties in the cash flows. Note however that an allowance for uncertainty does not mean that additional margins should be included in the best estimate.

Including these uncertainties requires particular cashflow characteristics to be accounted for in the valuation methodology. This gives rise to specific assumptions on the uncertainty surrounding a number of factors, including the following:

- ✓ the timing, frequency and severity of insured events;
- ✓ claim amounts and the period needed to settle the claims;

- ✓ the amount of expenses;
- ✓ policyholder behaviour;
- ✓ expected future developments such as future demographic, legal, medical, technological, social, environmental developments including inflation, both entity- and portfolio-specific. For example, in a particular country, this may include changes as a result of legislation, tax measures or the cost of care;
- ✓ interdependency between two sources of uncertainty.

When calculating the best estimate, a projection of the estimated future cashflows is made.
The cashflows are subsequently discounted using the risk free interest rate term structure, as set-up and provided by the regulator. The volatility adjustment (VA) can be added to this curve in order to compensate the spread movements of the assets.
The VA is designed to protect insurers with long-term liabilities from the impact of volatility on the insurers' solvency position. The VA is based on a risk-corrected spread on the assets in a reference portfolio. It is defined as the spread between the interest rate applying to the assets in the reference portfolio and the corresponding risk-free rate, minus the fundamental spread (which represents default or downgrade risk). The VA is provided and updated by EIOPA and can differ for each major currency and country.

5.2.1.2 Technical provisions (Life business)

When projecting future cashflows for Life obligations, so-called 'similar to Life techniques' are used.
In principle, these Life obligation cashflow projections are made on a policy-by-policy basis. Only in situations when such a calculation is unpractical policies can be grouped together and the methodology is then applied to the group of policies. This grouping is subject to strict conditions (for instance, it must give approximately the same results as a calculation made on a policy-by-policy basis).
The following cashflows should be taken into account when generating the best estimate of Life insurance obligations:

The **cash inflows** should at least include the gross premiums (after tax) included in the contract boundaries at the valuation date. It should be noted that contract boundaries may in some cases not be the same for IFRS and Solvency II.
In addition, all cashflows resulting from these premiums are taken into account, e.g., expenses, commissions and guarantees.
Investment returns (interests earned, dividends, etc.) are not taken into account. In the case of unit-linked contracts, only the risk premiums related to the non-hedgeable portion of the liabilities are taken into account.

The **cash outflows** must include at least:

- ✓ Benefit payments to policyholders and beneficiaries. The benefit cash outflows should include (non-exhaustive list):
    - Maturity benefits
    - Death benefits
    - Disability benefits
    - Surrender benefits

  - Annuity payments
  - Profit sharing bonuses (e.g., financial or mortality profit sharing)
  - Payments with respect to additional riders
- ✓ Claims payments incurred by the insurer in providing contractual benefits that are paid in kind (if they exist).
- ✓ Expenses that are incurred in servicing insurance obligations, such as: administrative expenses, investment management expenses, claims management expenses, acquisition expenses, overhead expenses. The projection of expenses has to include future expected inflation.

The cashflow projection method also includes options and guarantees that are related to the contract.

A **contractual option** is defined as a right to change the benefits, to be exercised at the discretion of its holder (generally the policyholder), on terms that are established in advance. Thus, in order to trigger an option, a deliberate decision of its holder is necessary. Examples of such options are:

- ✓ Surrender value option: the policyholder has the right to fully or partially surrender the policy and receive a pre-defined lump sum amount;
- ✓ Paid-up policy: the policyholder has the right to stop paying premiums and change the policy status to paid-up. Payments may not be reactivated in the future;
- ✓ Dormancy option: the policyholder has the right to partially or completely stop paying premiums, but with the option to reactivate the payments in the future;
- ✓ Annuity conversion option: the policyholder has the right to convert a lump-sum survival benefit into an annuity at a pre-defined minimum rate of conversion;
- ✓ Policy conversion option: the policyholder has the right to convert from one policy to another at pre-determined terms and conditions;
- ✓ Extended coverage option: the policyholder has the right to extend the coverage period when the original contract expires, without having to produce further evidence of health.

The contractual options within the business of KBC Insurance NV which are pre-determined in the contract include the following;

- ✓ Surrender value option;
- ✓ Paid-up policy option.

The derivation of the specific paid-up and surrender probabilities is set out in separate documents describing the lapse parameters. These are further elaborated in chapter 8 of the BEL Manual.

A **financial guarantee** is present when there is the possibility to pass losses to the undertaking or to receive additional benefits as a result of changed financial variables (e.g., investment return of the underlying asset portfolio, performance of indices, etc.). In the case of guarantees, the trigger is generally automatic (the mechanism would be set in the policy's terms and conditions) and thus not dependent on a deliberate decision of the policyholder.

The following is a non-exhaustive list of examples of common financial guarantees embedded in Life insurance contracts:

- ✓ Guaranteed invested capital: include a capital guarantee of the initial investment amount, usually up to a set percentage. This can be considered as a 0% interest rate guarantee.
  e.g. a guaranteed return of investment in unit-linked funds;
- ✓ Guaranteed minimum investment return: minimum interest rate is guaranteed.
  e.g., investment insurance with a guaranteed minimum return plus a variable – but not guaranteed – profit sharing amount;
- ✓ Minimum guaranteed benefits: e.g., return of initial investment.

If contracts are expected to benefit from profit sharing, this profit sharing must also be included in the projection of the cashflows.

KBC Insurance NV has the following Life insurance contracts where the financial guarantee is embedded in the contract:

- ✓ Contract with a guaranteed minimum interest return.

KBC Insurance NV also has contracts where the benefits are based on a declaration of KBC and the timing or the amount of the benefits is at its own discretion:

- ✓ Contracts with profit sharing

Where insurance and reinsurance contracts include financial guarantees, contractual options or future discretionary benefits, the present value of cash flows arising from those contracts may depend both on the expected outcome of future events and developments and on how the actual outcome in certain scenarios could deviate from the expected outcome. The methods used to calculate the best estimate should take such dependencies into account.

At KBC we calculate in the time value of financial options and guarantees (TVOG), both the optionality of lapse (contractual option) and profit sharing (financial option) as they are correlated (both depending on economic scenarios).

More specifically the embedded optionality is coming from:

- ✓ Future profit sharing to the policy holder, which is based on the return of the own asset portfolio;
- ✓ Lapse behaviour (currently only full surrenders, but might also be dormancy in the future), which is linked to the economic environment (10Y OLO).

According to the Solvency II regulatory framework, obligations arising from Health insurance must be assigned to 'Health SLT' (similar to Life techniques) if the actuarial methods used to calculate these cashflow projections are similar as the ones mentioned in this subchapter.

The tables below give an overview for KBC Insurance Group and KBC Insurance NV of the best estimate provisions of the Life lines of business, gross of ceded reinsurance, measured according to the Solvency II valuation principles above.

KBC Insurance Group:

Line of business (in m EUR)	Best Estimate gross of reinsurance recoverables (in m EUR)	%
Total Best Estimate Life excluding Health and Unit Linked	**15.747**	**51,3%**
30 Insurance with profit participation	15.754	51,3%
32 Other Life insurance	-23	-0,1%
34 Annuities stemming from NL not related to health	16	0,1%
36 Life reinsurance	0	0,0%
Total Best Estimate Health similar to Life	**567**	**1,8%**
29 Health reinsurance	191	0,6%
33 Annuities stemming from NL related to health	376	1,2%
Total Unit linked Best Estimate and value as a whole	**14.404**	**46,9%**
31 Index-linked and unit linked insurance	14.404	46,9%
Total Best Estimate provision Life (incl. Health similar to Life and Unit Linked)	**30.718**	**100,0%**
Split up in solvency 2 lines of business of the best estimate provisions Life gross of ceded reinsurance, situation 31.12.2019		

Table 39: Best estimates per Solvency II Line of business - KBC Insurance Group

KBC Insurance NV:

Line of business (in m EUR)	Best Estimate gross of reinsurance recoverables (in m EUR)	%
Total Best Estimate Life excluding Health and Unit Linked	**14.961**	**51,9%**
30 Insurance with profit participation	14.961	51,9%
32 Other Life insurance	0	0,0%
34 Annuities stemming from NL not related to health	0	0,0%
36 Life reinsurance	0	0,0%
Total Best Estimate Health similar to Life	**568**	**2,0%**
29 Health reinsurance	194	0,7%
33 Annuities stemming from NL related to health	373	1,3%
Total Unit linked Best Estimate and value as a whole	**13.281**	**46,1%**
31 Index-linked and unit linked insurance	13.281	46,1%
Total Best Estimate provision Life (incl. Health similar to Life and Unit Linked)	**28.810**	**100,0%**
Split up in solvency 2 lines of business of the best estimate provisions Life gross of ceded reinsurance, situation 31.12.2019		

Table 40: Best estimates per Solvency II Line of business - KBC Insurance NV

5.2.1.3 Technical provisions (Non-Life business)

The same general principles as outlined in 'Technical provisions (Life business)' apply to Non-Life obligations.
When projecting future cashflows for Non-Life obligations, so called 'similar to Non-Life techniques' are used.
Specifically for Non-Life obligations, Solvency II requires calculations to be performed separately for 'premium provisions' and 'provisions for claims outstanding':

- ✓ The **premium provisions** relate to claim events occurring after the valuation date and during the remaining in-force period (coverage period) of existing policies held by the undertaking.
  The calculation of the gross BE of the premium provision relates to:
    - All expected future premiums for existing policies
    - All future claim payments for existing policies
        - Arising from future events
        - Past the valuation date
        - That will be insured under the insurer's existing policies that have not yet expired
    - Expenses (allocated and unallocated claims expenses, as well as ongoing administration of in-force policies, acquisition costs, overhead expenses, investment management expenses) related to the above
- ✓ The **provisions for claims outstanding** relate to claim events that have already occurred but that are not settled yet, regardless of whether the claims arising from these events have been reported or not.

Both types of provisions are calculated according to different (standard) actuarial techniques.

The **premium provision** is calculated on the assumption that the portfolio of policies in a certain line of business is stable enough, so that claims experience from the past can be used to make predictions of claims that will occur in the future. In addition, the assumptions regarding the timing of future cashflows are based on past claims experience.

For the **claims provisions**, different techniques are used depending on the claim sizes (attritional, large and extra-large claims). An estimate is also made for those claims that have already occurred but which have not yet been reported at valuation date. The best estimate for claims outstanding also includes provisions for claim handling costs, both internal and external costs.

It should be noted that provisions for annuities stemming from Non-Life contracts form part of the Life technical provisions.

According to the Solvency II regulatory framework, obligations arising from Health insurance must be assigned to 'Health NSLT' (non-similar to Life techniques) if the actuarial methods used to calculate these cashflow projections are similar as the ones mentioned in this subchapter.

The tables below provides an overview of the best estimate provisions of the Non-Life and the Health non-similar to Life lines of business, gross of ceded reinsurance, measured according to the Solvency II valuation principles above.

KBC Insurance Group:

Line of business (in m EUR)	Best Estimate gross of reinsurance recoverables (in m EUR)	%
	1.574	**86,6%**
Motor vehicle liability insurance	814	44,8%
Other Motor Insurance	83	4,6%
Marine, aviation and transport insurance	4	0,2%
Fire and other damage to property insurance	184	10,1%
General liability insurance	362	19,9%
Credit and suretyship insurance	0	0,0%
Legal Expenses insurance	90	4,9%
Assistance	10	0,5%
Miscellaneous financial loss	10	0,5%
Proportional Motor Vehicle Liability reinsurance	0	0,0%
Proportional Other Motor insurance reinsurance	0	0,0%
Proportional Marine, aviation and transport reinsurance	0	0,0%
Proportional Fire and other damage to property reinsurance	1	0,1%
Proportional General liability reinsurance	2	0,1%
Proportional Credit and suretyship reinsurance	0	0,0%
Proportional Legal Expenses reinsurance	0	0,0%
Proportional Miscellaneous financial loss reinsurance	-1	0,0%
Non-Proportional Casualty reinsurance	15	0,8%
Non-Proportional Property reinsurance	0	0,0%
Non-Proportional Marine, aviation and transport reinsurance	0	0,0%
	244	**13,4%**
Medical Expense insurance	14	0,8%
Income Protection insurance	0	0,0%
Workers' Compensation insurance	227	12,5%
Proportional Medical expense reinsurance	0	0,0%
Proportional Income Protection reinsurance	1	0,0%
Proportional Workers' compensation reinsurance	1	0,1%
Non-Proportional Health Reinsurance	1	0,1%
	1.818	**100%**
Breakdown by Solvency II lines of business of the best estimate Non-Life provisions gross of ceded reinsurance (situation at 31.12.2019)		

Table 41: Best estimates per Solvency II Line of business - KBC Insurance Group

<u>KBC Insurance NV</u>:

Line of business (in m EUR)	Best Estimate gross of reinsurance recoverables (in m EUR)	%
	1.161	**82,4%**
Motor vehicle liability insurance	576	40,9%
Other Motor Insurance	30	2,1%
Marine, aviation and transport insurance	0	0,0%
Fire and other damage to property insurance	122	8,7%
General liability insurance	323	22,9%
Credit and suretyship insurance	0	0,0%
Legal Expenses insurance	90	6,4%
Assistance	6	0,4%
Miscellaneous financial loss	7	0,5%
Proportional Motor Vehicle Liability reinsurance	0	0,0%
Proportional Other Motor insurance reinsurance	0	0,0%
Proportional Marine, aviation and transport reinsurance	0	0,0%
Proportional Fire and other damage to property reinsurance	1	0,1%
Proportional General liability reinsurance	1	0,0%
Proportional Credit and suretyship reinsurance	0	0,0%
Proportional Legal Expenses reinsurance	0	0,0%
Proportional Miscellaneous financial loss reinsurance	0	0,0%
Non-Proportional Casualty reinsurance	5	0,4%
Non-Proportional Property reinsurance	0	0,0%
Non-Proportional Marine, aviation and transport reinsurance	0	0,0%
	249	**17,6%**
Medical Expense insurance	13	0,9%
Income Protection insurance	7	0,5%
Workers' Compensation insurance	227	16,1%
Proportional Medical expense reinsurance	0	0,0%
Proportional Income Protection reinsurance	1	0,1%
Proportional Workers' compensation reinsurance	1	0,1%
Non-Proportional Health Reinsurance	0	0,0%
	1.410	**100%**

Breakdown by Solvency II lines of business of the best estimate Non-Life provisions gross of ceded reinsurance (situation at 31.12.2019)

Table 42: Best estimates per Solvency II Line of business - KBC Insurance NV

5.2.1.4 Technical provisions (total)

The following tables present the gross best estimate, the risk margin and the reinsurance recoverables of the KBC Insurance Group and KBC Insurance NV, consistent with the figures on the Economic Balance Sheet at end of year 2019.
The best estimates and reinsurance recoverables are discounted at the EIOPA risk free rate, including the volatility adjustment as described in the previous paragraphs:

KBC Insurance Group:

Line of business (in m EUR)	Best Estimate - gross of reinsurance	Risk Margin	Reinsurance Recoverables
Technical Provisions - Non-Life	**1.818**	**348**	**99**
Non-Life (excl. Health)	1.574	286	95
Health (similar to Non-Life)	244	62	5
Technical Provisions - Life (incl. Index-Linked & Unit-Linked)	**30.718**	**544**	**-15**
Life (excl. Health and IL & UL)	15.747	394	-11
Health (similar to Life)	567	75	-4
Index-Linked & Unit-Linked	14.404	75	0
Total Technical Provisions	**32.536**	**893**	**84**

Table 43: Technical provisions - KBC Insurance Group

KBC Insurance NV:

Line of business (in m EUR)	Best Estimate - gross of reinsurance	Risk Margin	Reinsurance Recoverables
Technical Provisions - Non-Life	**1.411**	**292**	**108**
Non-Life (excl. Health)	1.162	236	103
Health (similar to Non-Life)	249	55	5
Technical Provisions - Life (incl. Index-Linked & Unit-Linked)	**28.810**	**460**	**-20**
Life (excl. Health and IL & UL)	14.961	323	-14
Health (similar to Life)	568	73	-7
Index-Linked & Unit-Linked	13.281	64	0
Total Technical Provisions	**30.221**	**752**	**88**

Table 44: Technical provisions - KBC Insurance NV

5.2.2 IFRS value for KBC Insurance Group and BGAAP value for KBC Insurance NV

5.2.2.1 Provisions for unearned premiums and unexpired risk

For the primary business, the provision for unearned premiums is in principle calculated on a daily basis, based on the gross premiums.

For inward treaties, i.e. reinsurance business received, the provision for unearned premiums is calculated for each contract separately on the basis of the information communicated by the ceding undertaking and, where necessary, supplemented on the basis of the company's own experience regarding the evolution of the risk over time.
The provision for unearned premiums for the Life insurance business is recorded under the provision for the Life insurance group of activities.

5.2.2.2 Life insurance provision

Except for Unit-Linked Life insurance products, this provision is calculated according to current actuarial principles, with account being taken of the provision for unearned premiums, the ageing reserve, the provision for annuities payable but not yet due, etc. In principle, this provision is calculated separately for every insurance contract.
For accepted business (if any), a provision is constituted for each individual contract, based on the information supplied by the ceding undertaking and supplemented, where necessary, by the company's own past experience.
Besides the rules set out below, an additional provision is set aside as required by law. The following rules apply:

- ✓ **Valuation according to the prospective method**. This method is applied for the provisions for conventional Non-Unit-Linked Life insurance policies, modern Non-Unit-Linked universal Life insurance policies offering a guaranteed rate of interest on future premium payments and for the provision for extra-legal benefits for employees in respect of current annuities. Calculations according to prospective actuarial formulas are based on the technical assumptions made in the contracts;
- ✓ **Valuation according to the retrospective method**. This method is applied for the provision for modern Non-Unit-Linked universal Life insurance policies and for the provision for extra-legal benefits for employees in respect of new supplementary premium payments. Calculations according to retrospective actuarial formulas are based on the technical assumptions made in the contracts, though no account is taken of future payments.

5.2.2.3 Provision for claims outstanding

For **claims reported**, the provision is in principle measured separately in each case, taking into account the known facts in the claims file, on the basis of the amounts still due to the injured parties or beneficiaries, plus external costs of settling claims. Where benefits have to be paid in the form of an annuity, the amounts to be set aside for that purpose are calculated using recognised actuarial methods.

For '**claims incurred but not reported**' at balance sheet date, an IBNR (Incurred But Not Reported) provision is set aside. In the primary business, this IBNR provision is based on a lump sum per class of insurance depending upon past experience and the trend in the insured portfolio. For extraordinary events, additional amounts are added to the IBNR provision.

For **'claims incurred but not enough reserved'** at balance sheet date, an IBNER (Incurred But Not Enough Reserved) provision is set aside if the adequacy procedures demonstrate that the other claims provisions are insufficient to meet future liabilities. This provision contains amounts for claims which have already been reported but which, for technical reasons, could not yet be recorded in the claims file. Where appropriate, a provision is set aside on a prudent basis for possible liabilities arising for claims files already closed.
A provision for the **internal cost of settling claims** is calculated at a percentage that is based on past experience.

Additional provisions are also constituted as required by law, such as supplementary workmen's compensation provisions.

5.2.2.4 Provision for profit sharing and rebates

This heading includes the provision for the profit share that has been allocated but not yet awarded at the end of the financial year for both the group of Life insurance activities and the group of Non-Life insurance activities.

5.2.2.5 Liability Adequacy Test

A Liability Adequacy Test is performed to evaluate current liabilities, detect possible deficiencies and recognise them in profit or loss.

5.2.2.6 Equalization and catastrophe provision for KBC Insurance NV

All amounts in the equalisation and catastrophe provision are allocated to offsetting non-recurring underwriting losses in the years ahead, equalising in the loss ratio and covering special risks.

5.2.2.7 Ceded reinsurance and retrocession

The effect of reinsurance business ceded and retrocession is entered as an asset and calculated for each contract separately, supplemented where necessary by the company's own past experience regarding the evolution of the risk over time.

5.2.3 Evolution of the differences in technical provisions between Solvency II and IFRS value

When looking at the evolution of the differences between Solvency II and IFRS value over 2019, the main differences arise mostly from volatility adjustment and interest rate changes:

- ✓ The risk free interest rates also decreased over the horizon, leading to an additional difference of -990m EUR;
- ✓ During 2019, the volatility adjustment decreased from 24bp to 4bp. This decrease led to a lower discounting curve for the Best Estimates under Solvency II compared to previous year. Due to this, the differences caused by the volatility adjustment decreased from -270m EUR last year to -209m EUR this year;
- ✓ Other evolutions are in the opposite direction (369m EUR) and mainly consist of changes in the risk margin (116m EUR).

5.3 Other liabilities

5.3.1 Solvency II value

Deferred taxes

Deferred taxes, other than deferred tax assets arising from the carry forward of unused tax credits and the carry forward of unused tax losses, are valued on the basis of the difference between the Solvency II values and the values ascribed to assets and liabilities as recognised and valued for tax purposes *(Delegated Regulation (EU) 2015/35, Art. 15)*

5.3.2 IFRS value for KBC Insurance Group

To determine the IFRS value reference can be made to the IFRS valuation rules applicable within KBC, as included in the Annual Report of KBC Group Consolidated – Notes on the accounting policies – Note 1 2: Summary of significant accounting policies.

5.3.2.1 Deferred taxes

Deferred tax liabilities are recognised for all taxable temporary differences between the carrying amount of an asset or liability and its tax base. They are measured using the tax rates that are substantially enacted at the reporting date and expected to be in effect on realisation of the assets or settlement of the liabilities to which they relate and which reflects the tax consequences that would follow from the manner in which the entity expects to recover or settle the carrying amount of the underlying asset or liability at the balance sheet date.

5.3.2.2 Financial Liabilities

Financial instruments or their component parts are classified as liabilities or as equity in accordance with the substance of the contractual arrangements on initial recognition and the definitions of financial liabilities and equity instruments. A financial instrument is classified as a liability if:

- ✓ KBC has a contractual obligation to deliver cash or another financial asset to the holder or to exchange another financial instrument with the holder under conditions that are potentially unfavourable to KBC;
- ✓ KBC has a contractual obligation to settle the financial instrument in a variable number of its own equity instruments.

A financial instrument is classified as an equity instrument if both of the conditions are not met and in that case is covered under the section *"Equity".*

- ✓ **Financial liabilities held for trading**
  Held-for-trading liabilities are those incurred principally for the purpose of generating a profit from short-term fluctuations in price or dealer's margin. A liability also qualifies as a trading

liability if it belongs to a portfolio of financial instruments held for trading separately by the trading desk and for which there is a recent pattern of short-term profit-taking.

Trading liabilities can include derivative liabilities, short positions in debt and equity instruments, time deposits and debt certificates. In connection with derivative liabilities KBC makes similarly distinction between trading and hedging derivatives as in case for derivative assets.

Initially, held-for-trading liabilities are measured at fair value. At the end of the reporting date, trading liabilities are measured at fair value. Fair value adjustments are always recorded in the income statement.

- ✓ **Financial liabilities upon initial recognition designated by the entity at fair value through profit or loss**

  IFRS 9 allows measuring a (group of) financial liability(s) on initial recognition at fair value, whereby fair value changes are recognized in profit or loss except for fair value changes related to the changes in own credit risk which are presented separately in OCI. The fair value designation is used by KBC for the following reasons:

  - Managed on a FV basis: KBC designates a financial liability or group of financial liabilities at fair value when these are managed and their performance are evaluated on a fair value basis. It is used to account for (unbundled) deposit components (i.e. financial liabilities not including a discretionary participation feature)
  - Accounting mismatch: Fair value option can be used when the use eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise from measuring assets or liabilities or recognising the gains and losses on them on different bases.
  - Hybrid instruments: A financial instrument is regarded as a hybrid instrument when it contains one or more embedded derivatives that are not closely related to the host contract. The fair value option can be used when it is not possible to separate the non-closely related embedded derivative from the host contract and then the entire hybrid instrument can be designated at fair value. This results that both the embedded derivative and the host contract are measured at fair value. KBC uses this option when, for example, structured products contain non closely related embedded derivatives, in which case both the host contract and the embedded derivative are measured at fair value.

- ✓ **Financial liabilities measured at amortised cost**

  KBC classifies most of its financial liabilities under this category, also those used to fund trading activities, when the trading intent is not present in the financial liabilities (e.g. issued bonds).

  These financial liabilities are initially measured at cost, which is the fair value of the consideration received including transaction costs. Subsequently they are measured at amortised cost, which is the amount at which the funding liability was initially recognised minus principal repayments and plus or minus the cumulative amortisation of any difference between that initial amount and the maturity amount. The difference between the amount made available and the nominal value is recorded on an accruals basis as an interest expense. Interest expenses accrued, but not yet paid, are recorded under accruals and deferrals.

5.3.3 BGAAP value for KBC Insurance NV

To determine the BGAAP value reference can be made to the BGAAP valuation rules applicable within KBC, as included in the Annual Accounts of KBC Insurance NV– Note 20 on the accounting policies.

5.3.3.1 Deferred taxes

Under BGAAP deferred taxes are not recognised.

5.3.3.2 Financial Liabilities

Financial liabilities are measured at amortised cost.

5.4 Alternative methods for valuation

Not applicable to the KBC Insurance Group.

Capital management

6 Capital Management

The solvency of KBC Insurance Group is calculated on the basis of Solvency II, conform the pillar 1 requirements. KBC Insurance Group is subject to the Solvency II regime as well as all its insurance subsidiaries. To determine solvency at group level, the accounting consolidation method is used. An overview of all undertakings in the scope of the group can be found in QRT 32.01.

A solvency ratio of 100% is required as a minimum by the regulator. Within KBC, the capital management process aims at reaching an optimal balance between regulatory requirements, rating agencies views, market expectations and management ambitions. It is a key management process relating to all decisions on the level and composition of the capital, both at group level and towards our subsidiaries.

An important process in this context is the Alignment of Planning Cycles (APC). This yearly process aims to create an integrated three-year plan in which the strategy, finance, treasury and risk perspectives are collectively taken into account. In this process, the risk appetite of the group is set and cascaded by setting risk limits at entity level. The APC is not only about planning, it is also about closely monitoring the execution of the plan in all its aspects. Such monitoring is reflected in dedicated reports, drawn up by the various Group functions.

In addition to APC, KBC Insurance Group and its (re)insurance subsidiaries conduct an Own Risk and Solvency Assessment (ORSA) on a regular basis, in accordance with Solvency II requirements. The aim of the ORSA is to monitor and ensure that business is managed in a sound and prudent way and that the KBC Insurance Group is adequately capitalised in view of its risk profile and the quality of its risk management and control environment. The ORSA process draws to a large extent on the same 'core processes' as the ICAAP and includes APC, risk appetite setting and ongoing business, risk and capital management processes. Where necessary, these processes are enhanced to take account of the specific nature of the (re)insurance activities and to comply with Solvency II requirements.

6.1 Solvency II ratio

6.1.1 KBC Insurance Group

As also stated in the 'Capital adequacy' section of the Annual Report, the Solvency II ratio of KBC Insurance Group amounted to 202% at the end of 2019, which is a decrease of 15pp compared to year-end 2018. KBC Insurance Group does not use any of the transitional measures.
The main drivers of the year-on-year evolution of the Solvency II ratio (including volatility adjustment) are:

- ✓ **Decreasing interest rate curves**: for 2019 a drop of 38bps at the 10 year point is observed. Interest rates on the long term have decreased more than on the short term, resulting in a flatter curve and an overall negative impact on the ratio;
- ✓ **Lower European sovereign spreads** (Italy, Spain, Belgium) and **lower corporate spreads** leading to a lower volatility adjustment (from 14bps to 6bps) which has had a (small) negative impact on the ratio;
- ✓ The **Solvency II review** of 2018 has been taken into account in the 2019 figures: no longer capital for spread risk needs to be held for loans that are fully guaranteed by an RGLA (Regional Government and Local Authorities), positively impacting the Solvency II ratio (+12pp). Next to that the **parameter updates** in 2019 lead to a combined drop of 4pp on the ratio. Main updates were related to lapses, expenses and profit sharing;
- ✓ **Increase in equity markets** (EUROSTOXX 600 increased by 23%). The negative impact of the symmetric adjustment however leads to a decrease of the Solvency II ratio;
- ✓ **Business decisions:** The swaps which were used to mitigate the currency risk of the non-EUR participations have been terminated leading to a higher SCR Currency and a lower Solvency II ratio (-2pp).

(in m EUR)	**31/12/2018**	Interest rates	Share prices & purchases	Spreads & VA	Impact RGLA	Model & parameter update	Other	**31/12/2019**
Available	**3.590**	-5	174	-180	0	-134	51	**3.496**
Required	**1.651**	46	134	46	-108	-57	15	**1.727**
SII ratio	**217%**	-6%	-6%	-15%	12%	-1%	1%	**202%**

Table 45: Evolution in components of the SII ratio (KBC Insurance Group)

Solvency, KBC Insurance Group (including volatility adjustment)		
(in m EUR)	31/12/2018	31/12/2019
Own funds	**3.590**	**3.496**
Tier 1	3.090	2.996
IFRS parent shareholders' equity	2.728	3.422
Dividend pay-out	-132	-156
Deduction of intangible assets and goodwill (after tax)	-124	-128
Valuation differences (after tax)	341	-196
Volatility adjustment	313	104
Other	-35	-49
Tier 2	500	500
Subordinated loans	500	500
Solvency Capital Requirement (SCR)	**1.651**	**1.727**
Solvency II ratio	**217%**	**202%**
Solvency surplus above SCR	1.939	1.769

Table 46: Own funds, SCR & SII ratio (KBC Insurance Group)

In the table above, the line valuation differences contains -among other things- the valuation differences between IFRS and Solvency II for the assets as well as for the liabilities. This item has decreased considerably over 2019 because of the decrease in interest rates which has a higher impact on the liabilities compared to the assets.

6.1.2 KBC Insurance NV

As also stated in the ‘Capital adequacy’ section of the Annual Report, the Solvency II ratio of KBC Insurance NV amounted to 215%, which is an decrease of 15% compared to year-end 2018. KBC Insurance NV does not use any of the transitional measures.

The main drivers of the year-on-year evolution of the Solvency II ratio (including volatility adjustment) are the same as those for KBC Insurance Group. (See 6.1.1 KBC Insurance Group).

Solvency, KBC Insurance NV (including volatility adjustment)		
(in m EUR)	31/12/2018	31/12/2019
Own funds	**3.626**	**3.499**
Tier 1	3.126	2.999
BGAAP parent shareholders' equity	1.368	1.369
Dividend pay-out	-132	-156
Valuation differences (after tax)	1.370	1.246
Volatility adjustment	171	98
Other	349	441
Tier 2	500	500
Subordinated loans	500	500
Solvency Capital Requirement (SCR)	**1.576**	**1.630**
Solvency II ratio	**230%**	**215%**
Solvency surplus above SCR	2.050	1.869

Table 47: Own funds (KBC Insuance NV)

The line other contains:

- ✓ The valuation difference between BGAAP and Solvency II for derivatives;
- ✓ The amount in the Funds for Future Allocation (128m EUR in 2018 and 158m EUR in 2019), which is zero under Solvency II and reported as other liability in BGAAP;
- ✓ Profit appropriation: profit premium and dividend to be paid are part of the other liabilities in the BGAAP balance sheet, while these are not included in the Solvency II economic balance sheet.

6.2 Own funds

6.2.1 Basic own funds

KBC Insurance Group

The total available capital of KBC Insurance Group amounted to 3.496m EUR at end of year 2019. This amount comprises solely basic own fund items, which are eligible to cover the Solvency Capital Requirement and the Minimum Capital Requirement.

More information about 'Own funds' can be found in QRT S.23.01.- Own Funds.

(in m EUR)	31/12/2018	31/12/2019	Nominal change
Share capital	65	65	0
Share premium	1.086	1.086	0
Reconciliation reserve	1.939	1.845	-94
Excess assets over liabilities	3.425	3.356	-69
Expected dividend payments	-132	-156	-24
Own shares	-203	-203	0
Other own fund items	-1.151	-1.151	0
Tier 1 capital	**3.090**	**2.996**	**-94**
Tier 2	500	500	0
Tier 2 capital	**500**	**500**	**0**
Total available basic own funds	**3.590**	**3.496**	**-94**

Table 48: Composition of Capital - KBC Insurance Group

Tier-1 capital amounted to 2.996m EUR at end of year 2019, down 94m EUR on its year-earlier level, due to a decrease in excess of assets over liabilities (-69m EUR - more details below) and due to the difference in dividend pay-out (-24m EUR).

Decrease in excess of assets over liabilities with 69m EUR is caused by a higher increase in liabilities compared to the increase in assets:

- ✓ Lower interest rates (from 4Q18 until 3Q19) leading to a higher value of both assets and liabilities. However as the liabilities are more sensitive to the interest rate change, they increase more, resulting in a lower available capital;
- ✓ Parameter updates (-134m EUR) lead to increased liabilities and a lower available capital.
- ✓ Lower spreads lead to higher values assets, but as this also leads to a lower Volatility Adjustment, liabilities increase even more;
- ✓ This is all partly compensated by an increase in the value of equity, due to the higher equity markets.

Tier-2 capital consists of a 10-year, subordinated, Solvency II-compliant tier-2 loan granted by KBC Group to KBC Insurance for a nominal amount of 500m EUR on 18 March 2015.

Economic balance steet (m EUR)	31/12/2018	31/12/2019
Investments (other than assets held for index-linked and unit linked funds)	20.414	21.453
Equities	1.211	1.341
Bonds	17.970	18.869
Government bonds	11.973	12.726
Corporate bonds	5.988	5.944
Other bonds	9	199
Other investments	1.233	1.243
Assets held for index-linked and unit linked funds	13.685	14.477
Loans & mortgages	2.479	2.513
Cash & equivalents	325	156
Other	589	631
Total assets	**37.492**	**39.230**
Technical provisions - non-life	2.036	2.166
Best estimate	1.728	1.818
Risk margin	308	348
Technical provisions - life (excl. index-linked and unit linked funds)	15.757	16.783
Best estimate	15.384	16.314
Risk margin	373	469
Technical provisions index-linked and unit linked funds	13.699	14.479
Debt owed to credit institutions	1.034	1.040
Other	1.540	1.407
of which Deferred tax liabilities	376	254
Total liabilities	**34.066**	**35.875**
Excess of assets over liabilities	**3.425**	**3.356**

Table 49: Economic balance sheet - KBC Insurance Group

KBC Insurance NV

The total available capital of KBC Insurance NV amounted to 3.499m EUR at 31 December 2019. This amount comprises solely basic own fund items, which are eligible to cover the Solvency Capital Requirement and the Minimum Capital Requirement.

More information about 'Own funds' can be found in QRT S.23.01.01.

(in m EUR)	31/12/2018	31/12/2019	Nominal change
Share capital	65	65	0
Share premium	1.086	1.086	0
Surplus funds	128	158	
Reconciliation reserve	1.848	1.691	-157
Excess assets over liabilities	3.462	3.358	-103
Expected dividend payments	-132	-156	-24
Own shares	-203	-203	0
Other own fund items	-1.278	-1.308	-30
Tier 1 capital	**3.126**	**2.999**	**-127**
Tier 2	500	500	0
Tier 2 capital	**500**	**500**	**0**
Total available basic own funds	**3.626**	**3.499**	**-127**

Table 50: Composition of available basic own funds - KBC Insurance NV

Tier-1 capital amounted to 2.999m EUR at year-end 2019, down 127m EUR on its year-earlier level, due to movements in excess of assets over liabilities, caused mainly by a decrease in excess of assets over liabilities (-103m EUR more details below) and due to the difference in dividend pay-out (-24m EUR).

Tier-2 capital consists of a 10-year, subordinated, Solvency II-compliant tier-2 loan granted by KBC Group to KBC Insurance for a nominal amount of 500m EUR on 18 March 2015. The year-on-year changes in tier-2 capital were due to the changes in fair value of this loan.

The decrease in excess of assets over liabilities with 103m EUR is caused by a higher increase in liabilities compared to the increase in assets:

- ✓ Lower interest rates (from 4Q18 until 3Q19) leading to a higher value of both assets and liabilities. However as the liabilities are more sensitive to the interest rate change, they increase more, resulting in a lower available capital.
- ✓ Parameter updates lead to increased liabilities and a lower available capital.
- ✓ Lower spreads lead to higher values assets, but as this also leads to a lower Volatility Adjustment, liabilities increase even more.
- ✓ This is all partly compensated by an increase in the value of equity, due to the higher equity markets.

Economic balance steet (*in m EUR*)	31/12/2018	31/12/2019
Investments (other than assets held for index-linked and unit linked funds)	19.180	20.109
Equities	1.148	1.247
Bonds	16.000	16.763
Government bonds	10.451	11.037
Corporate bonds	5.541	5.527
Other bonds	8	198
Other investments	2.032	2.099
Assets held for index-linked and unit linked funds	12.622	13.319
Loans & mortgages	2.468	2.503
Cash & equivalents	213	69
Other	468	489
Total assets	**34.951**	**36.489**
Technical provisions - non-life	1.637	1.702
Best estimate	1.376	1.411
Risk margin	262	292
Technical provisions - life (excl. index-linked and unit linked funds)	14.924	15.925
Best estimate	14.610	15.529
Risk margin	314	396
Technical provisions index-linked and unit linked funds	12.656	13.345
Debt owed to credit institutions	1.034	1.040
Other	1.237	1.118
of which Deferred tax liabilities	247	123
Total liabilities	**31.489**	**33.131**
Excess of assets over liabilities	**3.462**	**3.358**

Table 51: Economic balance sheet - KBC Insurance NV

6.2.2 Ancillary own funds

No ancillary own funds are taken into account, as these funds are not available.

6.2.3 Material differences between equity

KBC Insurance Group
In the table below, a reconciliation is made between IFRS equity as shown in the financial statements of KBC Insurance Group and the excess of assets over liabilities according to Solvency II.

Reconciliation IFRS equity & assets over liabilities Solvency II	
(in EUR m)	**31/12/2019**
Share capital	65
Share premium	1.086
Treasury Shares	-203
Revaluation reserve debt securities (FVOCI)	781
Revaluation reserve equity instruments (FVOCI)	12
Revaluation reserve equity instruments (overlay approach)	350
Hedging reserve	0
Remeasurement of defined benefit obligations (after tax)	2
Reserves	841
Translation differences	10
Net profit of the year (IFRS)	480
IFRS parent shareholder's equity	**3.422**
Minority interest	0
IFRS equity	**3.422**
Valuation differences between IFRS and Solvency II	
of which: deduction intangible assets (after tax)	-128
of which: valuation difference participations	-10
of which: valuation difference real estate at fair value (after tax)	86
of which: valuation difference fair value loans & receivables (after tax)	266
of which: valuation difference fair value amortised cost bonds (after tax)	749
of which: valuation difference reinsurance recoverables	-32
of which: valuation difference technical liabilities (after tax)	-1.255
of which: treasury shares	203
of which: other	-50
Assets over liabilities Solvency II	**3.252**
Volatility adjustment (VA)	104
Assets over liabilities Solvency II, incl. VA	**3.356**

Table 52: Reconciliation IFRS & Solvency II - KBC Insurance Group

The reason for the valuation differences between IFRS equity according to the financial statements and the excess of assets over Liabilities according to Solvency II as shown in the table, are explained in chapter 5 Valuation for solvency purposes.

KBC Insurance NV

In the table below, a reconciliation is made between BGAAP equity as shown in the financial statements of KBC Insurance NV and the excess of assets over liabilities according to Solvency II.

Reconciliation BGAAP equity & assets over liabilities BGAAP	
(in m EUR)	31/12/2019
Share capital	65
Share premium	1.086
Reserves	218
BGAAP equity	**1.369**
Valuation differences between BGAAP and Solvency II	
of which : valuation difference real estate at fair value (after tax)	74
of which: valuation difference participations	359
of which: valuation difference fair value equity	308
of which: valuation difference fair value amortised cost bonds (after tax)	1.422
of which: valuation difference fair value loans & receivables (after tax)	261
of which: valuation difference reinsurance recoverables	-15
of which: valuation difference technical liabilities (after tax)	-861
of which: other	441
Assets over liabilities Solvency II	**3.358**

Table 53: Reconciliation BGAAP - KBC Insurance NV

The reasons for the valuation differences between BGAAP equity according to the financial statements and the excess of assets over liabilities according to Solvency II, as shown in the table, are explained in chapter 5 Valuation for solvency purposes.

6.2.4 Forward looking view on available capital

For the forward looking view according on available capital for KBC Insurance NV and KBC Insurance Group according to the company's strategy (APC) is referred to the ORSA report of KBC Insurance Group 2020.

6.3 Diversification effects

KBC Insurance Group

The calculation of the Solvency II capital requirement for the KBC Insurance Group is based on method 1 (the accounting-consolidation based method). In this method, the standard formula for the calculation of the Solvency Capital Requirement (SCR) is applied to the consolidated assets and liabilities. The following table shows the total SCR for the KBC Insurance Group as the sum of the SCR for its underlying material entities[10], compared to the result of the group SCR calculated according to the accounting-consolidation based method.

m EUR	31/12/2019
KBC Insurance NV	1.497
KBC Group Re	70
DZI Insurance	49
CSOB P SK	27
CSOB P CZ	121
K&H	48
Stand-alone SCR	**1.812**
KBC Insurance Group	**1.727**
Diversification effect	-85

Table 54: Diversification effects at the level of KBC Insurance Group – end of year 2019

Due to the composition of the KBC Insurance Group, where KBC Insurance NV accounts for most of the overall risk profile and capital requirements, the potential sources for diversification (such as geographical diversification) are limited (85m EUR) and do not manifest themselves in a material way in the group calculation.

[10] In order to avoid double counting, the SCR of KBC Insurance NV and DZI Insurance already excludes the value of participations in other insurance undertakings part of KBC Insurance Group.

6.4 Solvency Capital Requirement & Minimum Capital Requirement

In the standard formula, the SCR is calculated as the sum of different components. KBC Insurance Group uses the distinguishable components (SCR Market Risk, SCR Counterparty Risk, SCR Life Risk, SCR Health Risk, and SCR Non-Life Risk) to calculate the Basic SCR (BSCR). Because there is some risk of overlap between the different components, diversification reduces the risk involved and the related SCR. After calculating the Basic SCR, three components are added in order to calculate the total SCR. These three elements are the Loss Absorbing Capacity of the Technical Provisions, the Loss Absorbing Capacity of the Deferred Taxes and the SCR Operational Risk.

- ✓ The Loss Absorbing Capacity of the Technical Provisions (LAC TP) is calculated according to Art. 206 of the Delegated Regulations 2015-35 and takes into account any legal, regulatory or contractual restrictions in the distribution of future discretionary benefits;
- ✓ The adjustment for the Loss Absorbing Capacity of the Deferred Taxes (LAC DT) is calculated according to Art. 207 of the Delegated Regulations 2015-35, whereby a decrease in deferred tax liabilities or an increase in deferred tax assets results in a negative adjustment for the loss-absorbing capacity of deferred taxes. If this adjustment is positive, the adjustment is nil.

6.4.1 Solvency Capital Requirement 31/12/2019

KBC Insurance Group

The waterfall chart below shows the major components of the SCR, which stands at 1.727m EUR. The SCR Market Risk (1.389m EUR) is clearly the biggest contributor to the SCR. SCR Life Underwriting Risk (689m EUR) and SCR Non-Life underwriting Risk (579m EUR) are second and third, respectively. It should be noted that the total SCR for the underwriting risk accounts for 50% of undiversified basic Solvency II Pillar 1 capital.

More information on this matter can be found in QRT S.25.01 - Solvency Capital Requirement - Only Standard Formula.

Total eligible own funds to meet the group SCR amounted to about 3.496m EUR, which gives a Solvency II ratio of about 202%. This ratio is well above the minimum 100% required by the Delegated Regulations 2015-35.

The Minimum Capital Requirement (MCR) at group level is equal to the sum of the MCRs of the entities. At 31/12/2019, 5 out of 7 local entities reached the cap of the MCR, being 45% of their own SCR, including the two most material entities (KBC Insurance NV and ČSOB Pojišt’ovna a.s. (CZ)). Therefore, the evolution of the MCR will mainly follow the evolution of the SCR of the local entities.

At the KBC Insurance Group, the focus is more on the SCR than the MCR in follow-up, because it is the most stringent risk measure of the two:

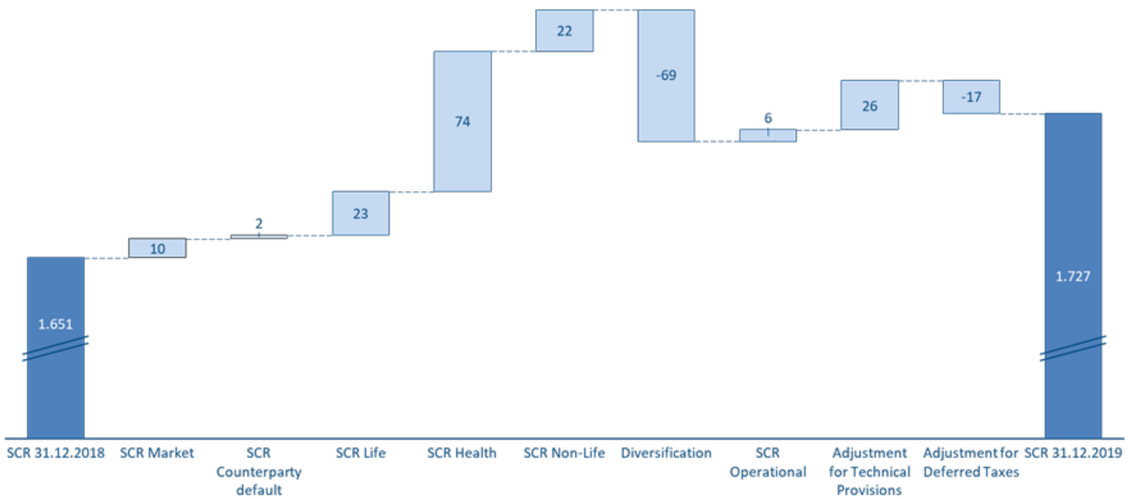

Figure 7: Waterfall diagram SCR - KBC Insurance Group

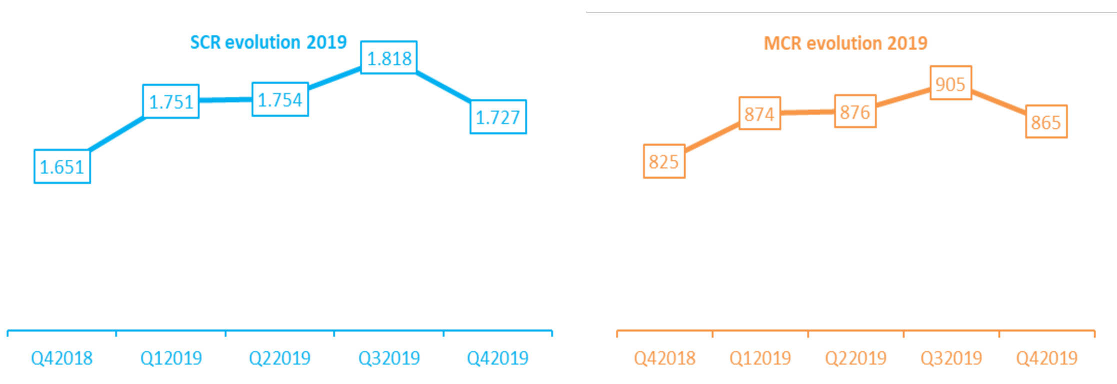

Figure 8: Evolution SCR in 2019 - KBC Insurance Group

(in m EUR)	2018	2019	Nominal change
SCR Non-Life	557	579	22
SCR Health	190	264	74
SCR Life	666	689	23
SCR Market risk	1.379	1.389	10
SCR Counterparty default risk	111	114	2
TOTAL SCR before diversification	**2.904**	**3.034**	**131**
Diversification benefits	-922	-991	-69
TOTAL SCR before diversification	**1.982**	**2.043**	**61**
SCR Operational Risk	129	135	6
Adjustment loss absorbing effect TP	-105	-79	26
Adjustment deferred taxes	-356	-373	-17
TOTAL after diversification and adjustments	**1.651**	**1.727**	**76**

Table 55: Evolution sub SCR - KBC Insurance Group

The SCR of KBC Insurance Group increases over 2019 with 76m EUR, largely driven by the lower interest rate environment. Main underlying movements are:

- ✓ Exemption on spread risk for loans that are fully guaranteed by an RGLA (Regional Government and Local Authorities), leading to a decrease of 108m EUR on total SCR (after diversification);
- ✓ This drop in market risk is compensated by increases in equity risk linked to the improved equity markets and by increases in SCR currency due to the decision to no longer hedge the currency risk of non-EUR participations;
- ✓ Increases in underwriting risks are largely driven by the low interest rate environment. This is reinforced by a material increase of SCR Health largely driven by parameter & model updates as well as portfolio evolutions.

KBC Insurance NV

The SCR of KBC Insurance NV increases with 54m EUR. The main reasons for movements in the SCR/MCR are completely in line with the clarifications given for KBC Insurance Group.

The waterfall chart below (in m EUR) shows the major components of the SCR, which stands at 1.630m EUR. The SCR Market Risk (1.421m EUR) is clearly the biggest contributor to the SCR. SCR Life Underwriting Risk (593m EUR) and SCR Non-Life underwriting Risk (455m EUR) are second and third, respectively. It should be noted that the total SCR market risk accounts for 46% of undiversified basic Solvency II Pillar 1 capital.

More information on this matter can be found in Quantitative Reporting Template (QRT) S.25.01.21.

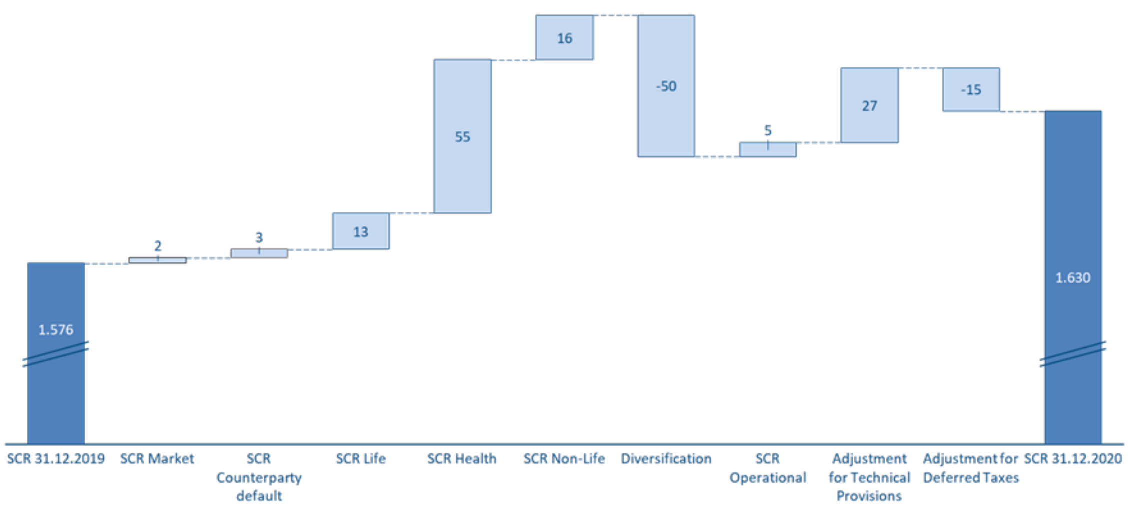

Figure 9 : Waterfall diagram SCR - KBC Insurance NV

The charts below focus on how the Solvency Capital Requirement (SCR) and Minimum Capital Requirement (MCR) change over time. The figures are in millions of euros:

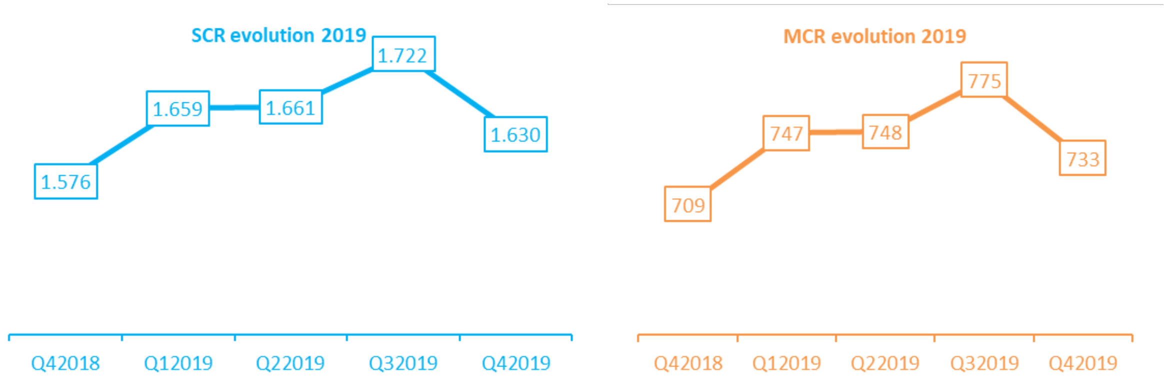

Figure 10: Evolution SCR in 2019 - KBC Insurance NV

(in m EUR)	2018	2019	Nominal change
SCR Non-Life	439	455	16
SCR Health	198	253	55
SCR Life	581	593	13
SCR Market risk	1.419	1.421	2
SCR Counterparty default risk	87	89	3
TOTAL SCR before diversification	**2.723**	**2.811**	**88**
Diversification benefits	-814	-864	-50
TOTAL SCR before diversification	**1.909**	**1.947**	**38**
SCR Operational Risk	112	116	5
Adjustment loss absorbing effect TP	-106	-80	27
Adjustment deferred taxes	-339	-354	-15
TOTAL after diversification and adjustments	**1.576**	**1.630**	**54**

Table 56: Evolution sub SCR - KBC Insurance NV

The SCR of KBC Insurance NV increases over 2019 with 54m EUR, largely driven by the lower interest rate environment. Main underlying movements are the same as those of KBC Insurance Group.

6.4.2 Forward looking

Over the business planning horizon the SCR is expected to remain fairly stable. Details can be found in the ORSA report of KBC Insurance Group.

6.5 Use of the duration-based equity risk sub-module in the calculation of SCR

Due to the demands of the National Bank of Belgium, and noting that the requisite ring-fenced funds do not exist in Belgium, the Solvency Capital Required calculation method using a duration based equity is not applicable.

6.6 Differences between the standard formula and any internal model used

The KBC Insurance Group has opted to calculate the Solvency Capital Requirements based on the standard formula (without any simplifications), rather than calculating them with a self-developed (partial) internal model. Therefore, further information has not been included here.

KBC Insurance NV has opted to calculate the Solvency Capital Requirements based on the standard formula (without any simplifications), rather than calculating them with a self-developed (partial) internal model. Therefore, further information has not been included here.

6.7 Non-compliance with the MCR and non-compliance with the SCR

As KBC Insurance Group and KBC Insurance NV have not faced any form of non-compliance with either the Minimum Capital Requirement or the Solvency Capital Requirement during the reporting period, further information has not been included.
As demonstrated by the various sensitivities calculated as part of the ORSA process , we also expect compliance with Minimum and Solvency Capital Requirement under adverse circumstances in the forward looking view.

6.8 Use of undertaking specific parameters

KBC Insurance Group and KBC Insurance NV did not opt to use undertaking specific parameters to calculate the Solvency Capital Requirements. Therefore, further information has not been included here.

6.9 Any other information

No other information to be included.

7 Solvency and Financial Condition Report MVBh

SFCR

Maatschappij voor Brandherverzekering CV (MVBh)

Based on situation as at 31 December 2019

7.1 Introduction

Insurance activities of KBC Insurance NV in Belgium include their reinsurance subsidiary Maatschappij voor Brandherverzekering CV (MVBh), a fire reinsurance company, which is discussed in this section.

In general the policies which are applicable to KBC Insurance NV are applicable as well to MVBh, taking into account the limited nature, small scale and simplicity of the risks inherent in its business.

Name, legal form and address
Maatschappij voor Brandherverzekering CV
Professor Roger Van Overstraetenplein 2
3000 Leuven (Belgium)
Our supervisory authority
National Bank of Belgium
De Berlaimontlaan 14
1000 Brussels
Our external auditor
PWC Bedrijfsrevisoren
Woluwedal 18
1932 Sint-Stevens-Woluwe
Representative: Tom Meuleman

7.2 Business and performance

7.2.1 Business

Business model

Local insurers, characterised by the very local nature of their activities, still have a role to play in society and therefore remain socially relevant since they belong to a local community's social network that mutualises its risks. Their risk profile is generally defensive and well under control. They are very often legally incorporated as 'mutual insurance association' or in some cases as 'insurance cooperative'.

These mutual insurers actually only write policies against fire damage and ancillary perils for 'simple risks' (together with the minor liability and legal expenses insurance cover that can typically be included in these fire policies), mainly located in their local municipality or neighbouring municipalities in West and East Flanders.

MVBh was incorporated on April 10th 1917, as published in the enclosures to the Belgian Official Gazette dated May 21st 1917, charter n°. 1763. Its mission is to conclude reinsurance contracts against fire damage and ancillary perils with the above-mentioned local insurers, in order to allow them to maintain their cooperative structure.

MVBh accepts 100% of technical insurance risks of these local insurers. Since underwriting results of all affiliated insurers are mutualised within MVBh, a stable revenue stream for local insurers can be generated through yearly profit participation.

KBC Insurance NV is MVBh's largest shareholder, holding 24.799 shares, out of a total of 27.525 (slightly more than 90%). The remaining shares (slightly less than 10%) are owned by 34 local insurers.

MVBh is a reinsurance cooperative ("coöperatieve vennootschap"). Characteristic for cooperative companies is that their shareholders are clients or providers as well. KBC Insurance NV provides MVBh with insurance products, premium rates, underwriting policy, claims settlement policy, claims reserving policy, policy and claims administration processes and -systems, 1st line actuarial function, end user computing, retrocession, inward and outward reinsurance administration.

MVBh's size is small since reinsurance activities are limited to local insurers which do not (yet?) grow in number and have limited growth opportunities due to their local character.

Since insurance cooperative "Pittemse Brandverzekering CVBA" has become shareholder and client of MVBh in the course of 2019, to MVBh's knowledge there are no other remaining mutual insurance associations or insurance cooperatives, in scope of MVBh's business model, actively in business, which are currently not part of MVBh's cooperative structure. MVBh's board of directors has initiated a debate about tactical and strategic profitable growth opportunities. Following considerations and questions are on the agenda:

- ✓ Which measures can be taken to incentivize these 34 mutual associations and insurance cooperatives to grow, professionalise, rejuvenate and modernize their local management structure where needed (modernisation of local bye-laws, creation of local websites, digitally unlock conclusion and management of insurance policies, marketing initiatives, …)?
- ✓ Cooperative entrepreneurship in general receives increased public interest. How can we support new initiatives relative to cooperative insurance and put the latter "on the map" again (e.g. in cooperation with Cera, KBC-I NV and KBC-I's insurance agents)?

MVBh's organisation has been kept very simple due to the simplicity of its activities as well as its small size, without compromising its risk management. MVBh is supported not only by KBC Insurance NV, but also KBC Bank NV and KBC Group NV (finance, accounting, tax, ALM management, legal, data quality, human resources, business continuity, risk, compliance, 2nd line actuarial function, internal audit).

MVBh pays proper compensation for services received, in line with KBC group's transfer pricing principles and practices.

7.2.2 Underwriting performance

The following table has been derived from statutory financial statements and demonstrates the historical underwriting profitability of the company:

	2015	2016	2017	2018	2019
Gross earned premium *(in k EUR)*	6.736	7.246	7.278	7.365	7.959
Gross earned premium (100%)	100,0%	100,0%	100,0%	100,0%	100,0%
Gross incurred losses	-29,5%	-34,1%	-20,4%	-26,0%	-31,7%
Change in equalization reserves	-0,6%	3,7%	-7,5%	0,0%	-1,1%
Profit participation to clients	-20,0%	-24,8%	-20,1%	-20,0%	-17,4%
Expenses and commissions	-25,5%	-25,2%	-25,5%	-25,1%	-25,1%
Gross technical balance	**24,4%**	**19,6%**	**26,5%**	**28,9%**	**24,7%**
Other items	0,0%	-0,3%	-0,1%	-0,1%	0,0%
Investment income and expenses	5,4%	6,8%	11,2%	0,8%	1,5%
Gross technical - financial balance	**29,8%**	**26,1%**	**37,6%**	**29,6%**	**26,1%**
Retrocession balance	-24,0%	-21,3%	-26,6%	-26,6%	-24,5%
Net balance	**5,9%**	**4,8%**	**11,0%**	**3,0%**	**1,6%**

Table 57: Statutory financial statement, underwriting profitability (MVBh)

7.2.3 Investment performance

The following information has been copied from statutory financial statements:

(in k EUR)	2015	2016	2017	2018	2019
Investment income					
Dividends	64	67	63	4	36
Fixed income	149	139	121	99	84
Term deposits	2	1			
Subtotal	**216**	**207**	**184**	**103**	**120**
Impairment reversals	52	130	161	40	70
Realized capital gains	185	369	697	58	2
Other	0	0	0	11	15
Subtotal	**453**	**706**	**1.042**	**212**	**206**
Investment expenses					
Asset management expenses	7	13	14	6	5
Investment management expenses	26	27	28	31	20
Impairments	54	45	2	70	0
Realized capital losses	0	129	182	46	65
Subtotal	**87**	**214**	**226**	**153**	**89**
Investment income, net of expenses	**366**	**492**	**816**	**59**	**117**
Average statutory balance sheet total	**11.423**	**12.259**	**13.133**	**13.544**	**13.675**
Return on average balance sheet total	**3,2%**	**4,0%**	**6,2%**	**0,4%**	**0,9%**

Table 58: Investment performance (MVBh)

7.3 System of Governance

7.3.1 Legal management structure

Dual structure

MVBh is managed according to a dual model, which draws a distinction between:

- The '**board of directors**', which has the task of setting strategy, determining general policy, supervising operational management and performing acts which are reserved to the board of directors in accordance with applicable legislation and MVBh's bye-laws.
- The '**executive committee**', which is responsible for the operational management of the company.

The board of directors is composed of at least seven directors, who are nominated by the general assembly. The board of directors is composed of (three) executive directors, who constitute the executive committee and are in charge of MVBh's operational management, and non-executive directors (four of which represent the mutual associations – MVBh shareholders, the other representing KBC Insurance NV). They are exclusively natural persons.

The non-executive directors, who are therefore no members of the executive committee, always constitute a majority within the board of directors. The chairman of the board of directors is a non-executive director.

The board of directors assumes final accountability for MVBh. Therefore the board of directors determines and controls more specifically:

- MVBh's strategy and objectives;
- the risk policy, including general risk tolerance limits.

Moreover, the board of directors oversees the executive committee and its functioning.

The executive committee is composed of three executive members of the board of directors (natural persons) together constituting a board. They are nominated and dismissed by the board of directors.

The executive committee is accountable for elaborating, executing and pursuing the strategy decided upon by the board of directors, taking into account MVBh's values, risk appetite and policies.

Committees

Based upon article 52 of the Insurance and Reinsurance Supervision Act dated 13 March 2016, the tasks assigned to the Audit Committee, the Remuneration Committee and the Risk Committee are executed by the board of directors of MVBh as a whole.

7.3.2 Operational management structure

MVBh has no employees on its payroll. Activities which are not performed by members of the Executive committee, are performed by KBC Group NV, KBC Bank NV and KBC Insurance NV staff.

7.3.3 (Regulated) outsourcing

The outsourcing approach of MVBh is embedded in the approach of KBC Group and KBC Insurance NV. With the aim of providing its clients the best possible service, MVBh appeals to the knowledge and efficiency present in the Belgian-based entities of KBC Group. No activities or functions are outsourced to external parties.

KBC Group NV provides audit, risk management, finance and tax services. The compliance function is not formally outsourced; necessary guidance and support from KBC Group NV, Group Compliance directorate is, however, provided. MVBh’s CRO is accountable for the Risk function and takes up some of the concerned tasks and activities. However, others are formally outsourced to KBC Group NV’s risk management directorate.

KBC Insurance NV supports MVBh with the following services:

- ✓ Underwriting, acceptance of insurance policies;
- ✓ Administration of insurance policies;
- ✓ Settlement of claims reported by the mutual insurers and insurance cooperatives (both from administrative and content-wise perspective);
- ✓ Network expertise and support provided to business managers of the mutual insurers and insurance cooperatives;
- ✓ Administration of incoming and outgoing reinsurance contracts;
- ✓ End user computing services;
- ✓ Actuarial tasks in execution of the calculation of the solvency position.

The first three services are performed by KBC Insurance NV as part of a retrocession agreement between MVBh and KBC Insurance NV, and are therefore not to be considered as regulated outsourcing.

MVBh considers all these activities to be critical or important functions or activities.

The Executive committee’s chairman oversees and coordinates the activities which are related to outsourcing, except those relative to outsourced 2nd line of defence management activities which are coordinated by MVBh’s CRO.

7.3.4 Independent control functions

General

MVBh's internal control system is based upon the **three lines of defence** concept:

- ✓ The CEO and deputy CEO, assisted by the relevant parties to which functions, activities or operational tasks have been assigned or outsourced, as 1st line of defence, have full ownership of their risks.
- ✓ The CRO, who also takes accountability for the compliance and actuarial functions, assisted by the relevant parties to which some of the relating activities or tasks have been outsourced, or which provide necessary guidance, constitute the 2nd line of defence.
- ✓ The internal and external audit functions constitute the 3rd line of defence.

The persons executing the independent control functions are independent of the operational functions of MVBh. They report at least twice a year directly to the board of directors about the execution of their task and inform the Executive Committee.

Risk management function, compliance function and actuarial function

In accordance with article 56, §3, 2nd subsection, 2° of the Insurance and Reinsurance Supervision Act, the head of the risk management function is a member of the Executive Committee of MVBh. This Executive committee member is the acting Chief Risk Officer (CRO), is actively involved in determining MVBh's risk strategy and all policy decisions having a significant impact on the risks and can provide a full picture of the whole range of risks MVBh is exposed to (key function holder).

The risk management function within MVBh is partially outsourced to KBC Group NV, under the general supervision of the CRO of MVBh.

This person also takes accountability for the compliance and actuarial functions. These three independent control functions are executed independently from one another.

The compliance function ascertains that MVBh, the directors, employees (if any) and authorized representatives comply with legal and regulatory provisions regulating the reinsurance activity (in particular the rules with respect to integrity and behaviour applying to this activity).

The compliance function also assesses potential consequences of changes in the legal framework for MVBh's activities and identifies and assesses compliance risks.

The actuarial function ascertains that MVBh uses an adequate underwriting methodology, coordinates and controls the calculation of the technical provisions and provides an opinion on MVBh's retrocession programme, in accordance with article 59 of the Insurance and Reinsurance Supervision Act.

Internal audit function

The board of directors has approved MVBh's current internal audit charter on December 2nd, 2019.

For internal audit MVBh relies on the corporate audit directorate of KBC Group NV. The internal audit function provides the board of directors and Executive Committee with an independent assessment of the quality and effectiveness of the internal controls, risk management and governance system of MVBh.

The person who is accountable for the internal audit function or the person designated for these purposes, communicates his findings and recommendations with the board of directors and Executive Committee.

7.3.5 Remuneration policy

The KBC remuneration policy applies to KBC insurance entities group-wide. The policy consists of remuneration principles that reflect the Solvency II directive 2015/35, including a governance structure and decision-making processes with the involvement of the internal control functions.

The principles are being applied for all staff and 'identified staff', meaning the members of KBC Insurance NV's board of directors, its Executive Committee, those responsible for the independent control functions and all other staff whose activities could have a material impact on the risk profile of KBC Insurance NV. These identified staff members are identified through an effective identification process.

The remuneration principles promote sound and effective risk management and effectively prevent remuneration arrangements which encourage excessive risk-taking, through several mechanisms in the remuneration process such as the risk gateway, the use of quantitative risk adjusted measures such as the risk adjusted profit, risk objectives etc. The remuneration principles consist of measures to prevent conflicts of interest and are aligned with the strategy, business and risk appetite of KBC Insurance group and the underlying entities.

Members of MVBh's Executive Committee receive a fixed remuneration. There is no variable component.

Apart from a pension plan for MVBh's chairman of the Executive Committee there are no supplementary pension or early retirement schemes for the members of the administrative, management or supervisory body and other key function holders.

7.3.6 Fit & proper requirements

MVBh's requirements concerning skills, knowledge and expertise applicable to the persons who effectively run MVBh or have other key functions as well as its process for their appointment and assessing their fitness and propriety are identical to the ones determined at KBC group level.

No loans, credits or suretyships have been granted to members of the board of directors (whether smaller or larger than 100.000 EUR).

7.4 Risk Profile

7.4.1 Underwriting risk

MVBh only writes reinsurance business with local Belgian mutual insurers and limits underwriting to fire business and allied perils. Reinsurance is on a 100% quota–share basis.

Mutual insurers only write policies against fire damage and ancillary perils for 'simple risks' (together with the minor liability and legal expenses insurance cover that can typically be included in these fire policies), mainly located in their local municipality or neighbouring municipalities in West and East Flanders.

Underlying policies relative to product offering, underwriting, pricing, reserving and claims settlement are copied from the ones applied by KBC Insurance NV.

Underwriting limits, in terms of sums insured, as defined by the inward reinsurance contracts, must be strictly applied.

Technical insurance risk represents a significant part of all risks within MVBh. Moreover, technical insurance performance is the decisive factor in determining how much profit is returned by MVBh to clients–mutual insurers. Therefore, limiting volatility of technical insurance performance is key.

The reinsurance portfolio, gross of proportional retrocession, is adequately protected by non-proportional retrocession cover, in terms of deductible, limit and amount of cover on an annual basis, against the consequences of large individual claims or claims in risk concentrations.

Due to the local character of MVBh's ceding companies–local insurers, risk locations may be geographically highly concentrated. These concentrations are mapped on a regular basis. As explained in the previous paragraph, ensuing risks are adequately retroceded.

MVBh monitors the underwriting performance of individual mutual insurers, and encourages individual mutual insurers to eliminate systematic underperformance, compared to their peers.

MVBh conducts portfolio checks on (at least) a yearly basis, aiming at controlling compliance with the above-mentioned policies, monitoring evolution of claims ratios of individual local insurers, and detecting and rectifying potential errors and mistakes.

MVBh pays appropriate attention to opinions of the actuarial function holder, and takes appropriate measures, if necessary.

MVBh's exposures to natural catastrophes (i.e., windstorm, flood and earthquake), man-made catastrophes, as well as large individual fire claims, are analysed on a regular basis and reported to the board of directors (cf. ORSA report).

Within the framework of the annual internal control statement process, an assessment is made of the implementation status of the Risk Management Framework for technical insurance risk. Items which are identified for improvement must be tackled systematically.

7.4.2 Market risk

Market risks represent a significant part of overall risks which MVBh is exposed to, triggered by (i) the investment of shareholders' funds and (ii) differences between risk profiles of cash–flows, originating from reinsurance liabilities on the one hand and assets, covering reinsurance liabilities on the other hand. Being exposed to market risks is an inevitable consequence of operating in the (re)insurance business.

Creating sustainable shareholder value from managing these market risks is <u>not</u> MVBh's core expertise. Therefore MVBh must rely on KBC–group's expertise with respect to market risk and investment portfolio management. So–called "ALM limits" must be set specifically for MVBh. Compliance with these limits is reported on every meeting of the board of directors.

7.4.3 Credit risk

Counterparty default risk on issuers of financial instruments is managed within the 'ALM limits' framework mentioned above, relying on KBC group's expertise with respect to credit risk management.

MVBh's credit risk largely stems from counterparty default risk exposure to KBC Insurance NV, originating from retrocession contracts. KBC Insurance NV is indeed MVBh's preferred retrocessionaire.

Although credit risk is quite significant within MVBh's overall risk profile because of counterparty default risk exposure to KBC Insurance NV, MVBh accepts this risk.

7.4.4 Liquidity risk

This risk may emerge when a catastrophic event occurs which generates high incurred claims in the reinsurance portfolio, more specifically when a time gap occurs between the moment MVBh is expected to pay these claims to its ceding companies on the one hand, and the moment the retroceded part can be recovered from the retrocessionaire on the other hand.

This risk has been neutralised by the retrocession contract through a clause which foresees the possibility for MVBh to request cash claims from its retrocessionaire once a contractually determined threshold has been exceeded.

7.4.5 Operational risk

MVBh endorses the group-wide framework for non-financial risk management and business continuity management.

In as far as relevant for MVBh, non-financial risk management tools such as group key controls, internal control statement, competition compliance program, etc. are applied.

For its business continuity plan, MVBh is obviously highly dependent on KBC Insurance NV and KBC group.

MVBh analyses the adequacy of business processes both systematically and on an ad-hoc basis.

Compliance with the group-wide framework for non-financial risk management and business continuity management is ascertained by an adequate execution of the local operational risk manager's and business continuity manager's roles. Guidance and steering for the execution of these roles is provided by the KBC Belgium Business Unit's risk management and crisis management departments.

Audit recommendations are executed in a timely and correct manner.

7.4.6 Other material risks

Business risk

Portfolio growth depends to a large extent on local insurers' business managers' willingness to place business with the local insurer. Professional relationship management with these local business managers is key.

MVBh's development is very closely linked to local Belgian mutual insurers' development. Should, for example, their survival be compromised due to unrealistically high regulatory obligations, MVBh's future would inevitably be jeopardized.

The Insurance and Reinsurance Supervision Act imposes strict requirements on (re)insurance undertakings to ensure their solvency. Should mutual insurers have to comply with these requirements, they would inevitably have to cease business. Fortunately, the bill allows for a 'soft' regime in a number of cases, including for 'small' insurers.

Mutual insurers (i.e., MVBh's clients) have assumed the regime of 'small' insurers, which reinsure 100% of their insurance obligations, entailing a huge simplification of their solvency regime i.e.:

- ✓ The Insurance and Reinsurance Supervision Act is (quasi) not applicable;
- ✓ The insurance undertaking must submit an application file for registration with the National Bank of Belgium (NBB) and demonstrate it complies with all required conditions;
- ✓ NBB must approve the application for registration;
- ✓ Once approved, the insurance undertaking will be listed on a specific register to be published on NBB's website;
- ✓ NBB may decide at its discretion to further regulate all additional information requirements, either on an individual or a general basis.

Application files for registration have been submitted by the mutual insurers to the NBB in 2017, and approved by the NBB. They are now listed on the NBB's website.

Reputation risk

The reputation of MVBh is a strategic asset of the firm. We aim to protect and grow our reputation in the eyes of our clients by managing our business in a responsible manner.

MVBh champions a strong compliance culture and has zero tolerance for any intentional violation of mandatory legal norms that are sanctioned with criminal penalties against our company, its directors or employees or administrative measures which could result in the revocation, suspension, modification or nonrenewal of the licenses issued to MVBh.

Regular reporting to the KBC Group Compliance division is done in compliance with Group Compliance Rules.

Concentration risk

KBC Insurance NV is MVBh's preferred reinsurer. MVBh is also exposed to KBC Bank, through current, savings and investment accounts, as well as, potentially, term deposits and other securities. KBC Insurance NV and KBC Bank NV maintain close (commercial) relationships. Potential impact on MVBh of ensuing contagion risk is adequately monitored and kept under control.

The global limit relative to counterparty default risk, withheld in the ALM limit framework, applies to KBC group as a whole. On top of that comes exposure to KBC Insurance generated by MVBh's retrocession programme, as well as exposure to KBC Bank due to current and savings accounts which are held by MVBh with KBC Bank in view of its daily operations. Outstanding balances of these accounts are kept at a minimum level to ensure smooth daily operations. Surpluses are transferred to KBC Asset Management, and from then onwards fall within the global limit relative to counterparty default risk.

7.5 Valuation for Solvency Purposes

7.5.1 Assets

Valuation bases for solvency purposes

These are identical to the ones used by KBC Insurance NV. Actual values can be found in QRT S.02.01.02.

Valuation bases in statutory financial statements

Impairments

For both financial fixed assets and unlisted shares, recorded under 'other financial assets', impairments are entered in the books in case of durable depreciations in value.

Listed shares are impaired in case their market value is sustainably (longer than one year) or significantly (more than 30%) lower than their book value, demonstrating that the depreciation in value is sufficiently durable.

The resulting impairments equal the difference between book value and market value.

The recorded impairments are reversed as soon as the market value is higher again, up to the purchase value at maximum.

For treasury investments, impairments are recorded when the realisation value of the investment at balance sheet date is lower than the purchase value.

For the other receivables and fixed income securities, impairments are recorded when reimbursement at maturity date is fully or partially uncertain or at risk.

Impairments are not maintained if, at fiscal year–end, they are higher than when based upon a current assessment, in accordance with the standards used at the time the impairments were recorded.

Provisions for risks and costs

At fiscal year–end, all foreseeable risks and charges which originated during the fiscal year are provisioned for, in accordance with the provisions of the Royal Decree of 17 November 1994.

Technical provisions

The technical provisions for claim payments to be made in the future are calculated per claim or per contract, taking known elements of the file into account.

Revaluations

Financial fixed assets as well as investment securities can be revalued when they show a certain and permanent capital gain compared to their purchase value.

Actual values can be found in template SE.02.01.16.

Other

In case of sale of securities the accounting value of sold securities is determined in accordance with a system of individualization of these securities. Gains or losses are taken immediately in P&L.

7.5.2 Technical provisions

Valuation bases and methods

In general, expected future cash flows related to reinsurance liabilities have been calculated and documented by KBC Insurance NV's Non-Life actuarial department in accordance with technical provisions guidelines as provided by KBC Group and taking into account the Risk Measurement Framework of KBC. We will briefly describe the **main principles**.

Pre-claim versus post-claim Non-Life obligations

For Non-Life obligations, separate cash-flow projections are made relative to:

- ✓ claim events that are expected to occur after the valuation date and during the remaining in-force period of existing contracts (pre-claim liabilities);
- ✓ claim events that have already occurred but that are not settled yet, regardless of whether the claims arising from these events have been reported or not (post-claim liabilities).

Gross liabilities versus retrocession recoverables

- ✓ Cash-flow projections are initially made on a gross basis, without deduction of retrocession recoverables;
- ✓ Retrocession recoverables are valued separately. They are included on the asset side of the economic balance sheet, and are calculated separately for Non-Life pre-claim and post-claim expected cash flows. Their valuation allows for expected losses due to counterparty default (i.e., the reinsurer); the impact thereof is however negligible.

Segmentation into homogeneous risk groups

Reinsurance liabilities have been grouped according to the nature of their risks, and calculations have been done separately for fire and allied perils (including natural catastrophes), general third-party liability ensuing from insured buildings, and legal expenses linked to the latter. These homogeneous risk groups have a one-to-one link with Solvency II lines of business (LOB) 19, 20 and 22:

- ✓ LOB 19 – proportional Non-Life reinsurance – fire and other damage to property insurance;
- ✓ LOB 20 – proportional Non-Life reinsurance – general liability insurance;
- ✓ LOB 22 – proportional Non-Life reinsurance – legal expenses insurance.

Where required by Solvency II regulations (i.e., if both parties are committed), future premiums on existing contracts are taken into account in valuing current liabilities. All contracts incept at 1 January, with a minimum 3-month cancellation period, ending on 30 September. Tacit renewal of these reinsurance contracts implies both parties are committed; therefore, in this case, at 31 December, the next generation of reinsurance contracts is within scope of the valuation of reinsurance liabilities.

Technical provisions are calculated according to the 'Mark to Model' method; i.e., a theoretical 'transfer value' is calculated at which the liabilities would be valued when transferred to another company. This includes the calculation of the:

- ✓ discounted best estimate of liabilities: models are used to generate cash-flow projections. The present value is then calculated at the risk-free discounting yield curve;
- ✓ risk margin: in such a manner as to ensure that the value of the technical provisions is equivalent to the amount that (re)insurance undertakings would be expected to require in order to take over and meet the (re)insurance obligations. It is calculated according to the cost of capital approach; i.e., the present value of the cost of holding expected required capital during the remaining lifetime of the liabilities.

At present only deterministic calculations are made.

The matching adjustment referred to in Article 77b of Directive 2009/138/EC, the volatility adjustment referred to in Article 77d, the transitional risk-free interest rate term structure referred to in Article 308c and the transitional deduction referred to in Article 308d are either not relevant or not applied.

Overview of Solvency II technical provisions

The enclosed table provides an overview, as at 31 December 2019 of Solvency II technical provisions (cf. also QRT S.17.01.02):

- ✓ broken down into pre-claim and post-claim obligations;
- ✓ broken down into gross and retroceded obligations;
- ✓ per Solvency II line of business.

All amounts in the SOLVENCY II columns are expressed in terms of 'liabilities'; i.e., a negative liability represents an asset. Gross pre-claim liabilities are negative since they represent the economic profit expected to be generated by the 2020 generation of inward reinsurance contracts.

The risk margin is very high compared to the discounted best estimate of gross liabilities. However, the latter is composed of a positive value for the discounted best estimate of gross post-claim liabilities, and a negative one, almost compensating the positive one, for the best estimate of gross pre-claim liabilities. This negative value reflects the economic profits expected to be generated by the 2020 generation of inward reinsurance contracts; these expected economic profits are of course uncertain, and the risk margin, part of which covers the pre-claim liabilities, represents the amount that (re)insurance undertakings would be expected to require in order to take over and meet the (re)insurance obligations.

Note that the risk margin is relevant only with respect to gross liabilities. A breakdown is available along the line of business criterion only.

As explained in MVBh's risk appetite statement, for the profit sharing policy to be achieved a net economic return any one accident year T, ex–ante, based on the Solvency II best estimate, as at 31/12/(T–1), of net pre–claim insurance liabilities, expressed as a % of net reinsurance premium, of close to 0% has to be targeted. At 31/12/2019 this is actually the case since overall net pre-claim reinsurance liabilities are almost equal to zero (i.e. 541 EUR).

Comparison between Solvency II and statutory valuation

The enclosed table also compares Solvency II with statutory technical provisions.

Provisions for unexpired risks as at 31 December 2019 don't figure in the statutory balance sheet since (almost) all underlying policies have a principal premium due date at 1 January. As reinsurance contracts are renewed as at 1 January 2020, the Solvency II economic balance sheet contains pre-claim liabilities related to these renewed contracts.

The equalisation reserves do not figure in the Solvency II economic balance sheet.

All amounts in the SOLVENCY II and STATUTORY columns are expressed in terms of 'liabilities'; i.e., a negative liability represents an asset.

A negative (STATUTORY MINUS SOLVENCY II) figure represents a statutory deficiency whereas a positive figure represents a statutory redundancy, compared to the Solvency II economic balance sheet.

Since statutory valuation bases are very prudent, not surprisingly, gross liabilities represent a statutory redundancy.

However, retroceded liabilities represent a statutory deficiency since:

- ✓ the statutory balance sheet doesn't contain pre-claim liabilities towards MVBh's retrocessionaire, whereas the Solvency II economic balance sheet does, since in Solvency II, gross pre-claim obligations are expected to generate a profit, all of which will be due to the retrocessionaire;
- ✓ post-claim retrocession recoveries are overestimated in the statutory balance sheet, compared to the Solvency II economic balance sheet.

Liabilities, net of retroceded obligations, represent a statutory redundancy, compared to the Solvency II economic balance sheet.

	(in k EUR)	SOLVENCY II				STATUTORY (BGAAP)			STATUTORY (BGAAP) MINUS SOLVENCY II			
	Reinsurance liabilities	*Pre-claim*	*Post-claim*	*Risk margin*	*Total*	*Pre-claim*	*Post-claim*	*Total*	*Pre-claim*	*Post-claim*	*Risk margin*	*Total*
Gross	LOB 19 (Fire)	-1.265	1.338	305	378	0	1.723	1.723	1.265	385	-305	1.345
	LOB 20 (GTPL)	-10	10	0	-0	0	19	19	10	8	-0	19
	LOB 22 (LA)	-6	23	0	17	0	21	21	6	-2	-0	4
	Equalization reserves					1.711		1.711	1.711			1.711
	Total	**-1.282**	**1.371**	**305**	**395**	**1.711**	**1.763**	**3.473**	**2.992**	**391**	**-305**	**3.079**
Retroceded	LOB 19 (Fire)	1.250	-1.235		15	0	-1.378	-1.378	-1.250	-143		-1.393
	LOB 20 (GTPL)	21	-10		10	0	-19	-19	-21	-9		-29
	LOB 22 (LA)	11	-23		-12	0	-21	-21	-11	2		-9
	Total	**1.282**	**-1.268**		**14**	**0**	**-1.418**	**-1.418**	**-1.282**	**-150**		**-1.432**
Net	LOB 19 (Fire)	-14	102	305	393	0	345	345	14	242	-305	-48
	LOB 20 (GTPL)	10	0	0	10	0	0	0	-10	-0	-0	-10
	LOB 22 (LA)	5	0	0	5	0	0	0	-5	-0	-0	-5
	Equalization reserves					1.711		1.711	1.711			1.711
	Total	**1**	**103**	**305**	**408**	**1.711**	**345**	**2.055**	**1.710**	**242**	**-305**	**1.647**

Table 59: Overview of SII and statutory (BGAAP) TP's as at 31/12/2019 (MVBh)

7.5.3 Other liabilities

Valuation bases are identical to the ones used by KBC Insurance NV.

7.6 Capital Management

7.6.1 Own funds

We refer to QRT S.23.01.01 to show that total unrestricted tier 1 basic own funds of 10.174.040 EUR are eligible and available to meet SCR and MCR. There are no ancillary own funds.

The origins of differences with statutory own funds are listed in the following table:

	SE.02.01.16 *(in k EUR)*	Solvency II value	Statutory accounts value	Difference
	Own funds	10.174	8.129	2.045
	Foreseeable dividends	2	2	0
	Difference	10.172	8.126	2.045
Assets	Listed equities	1	1	0
Assets	Collective investments undertakings	2.350	2.199	151
Assets	Government bonds	3.095	2.918	178
Assets	Corporate bonds	4.436	4.316	121
Assets	Reinsurance recoverables	-14	1.418	-1.432
Liab.	Technical provisions	395	3.473	-3.079
Liab.	Deferred tax liabilities	51	0	51
	TOTAL [ASSETS - LIABILITIES]			**2.045**

Table 60: Differences between Solvency II and statutory valuations (MVBh)

7.6.2 Solvency Capital Requirement and Minimum Capital Requirement

MVBh's SCR calculations are based upon the standard formula. No (partial or full) internal model is used. As shown in QRT S.25.01.21, the SCR as at 31 December 2019 amounts to 2.716.405 Eur giving rise to a solvency ratio of 374% of SCR.

Non-Life underwriting risk (1.326.652 EUR), market risk (1.220.931 EUR), counterparty default risk (841.648 EUR), and operational risk (238.770 EUR) are the largest risks MVBh is exposed to.

No simplified calculations, nor undertaking-specific parameters are used.

The MCR is considerably higher than the SCR i.e. 3.600.000 EUR (as shown in QRT S.28.01.01), giving rise to a solvency ratio of 283% of MCR.

The Solvency II ratio with respect to the SCR is of course higher than the Solvency II ratio with respect to the MCR. When considering the solvency ratios, the SCR is less relevant in our case.

List of abbreviations

8 List of abbreviations

(3)LOD	(Three) Line(s) Of Defence
(A)RCC	(Audit,) Risk & Compliance Committee
(G)ExCo	(Group) Executive Committee
(N)SLT	(Non-) Similar to Life Techniques
ABS	Asset-Backed Security
AFH	Actuarial Function Holder
AFS	Available For Sale
ALCO	Asset Liability Committee
ALM	Asset-Liability Management
AML	Anti-Money Laundering
APC	Alignment of Planning Cycles
BE	Best Estimates
BoD	Board of Directors
BPV	Basis Point Value
CDS	Credit Default Swap
CEO	Chief Executive Officer
CFO	Chief Financial Officer
CMS	Constant Maturity Swaps
CORM	Compliance Risk Manager
CRO	Chief Risk Officer
CVA	Credit Value Adjustment
DPF	Discretionary Participation Feature
DTL	Deferred Tax Liabilities

EBS	Economic Balance Sheet
EIOPA	European Insurance and Occupational Pensions Authority
EOY	End Of Year
EPIFP	Expected Profits Included in Future Premiums
EU	European Union
FATCA	Foreign Account Tax Compliance Act
FIFV	Financial liabilities designated at Fair Value through profit or loss
FRA	Forward Rate Agreements
FX	Foreign exchange
GDPR	General Data Protection Regulation
GIC	Group Insurance Committee
GICC	Group Internal Control Committee
GLC	Group Lending Committee
GMC	Group Markets Committee
G-RISK	Group Risk
GVC	Group Valuation Committee
GWP	Gross Written Premium
HFT	Held For Trading
HR	Human Resources
HTM	Held To Maturity
IAS	International Accounting Standard
IBNER	Incurred But Not Enough Reserved
IBNR	Incurred But Not Reported
ICO	Intercompany
ICT	Information & Communication Technology

IDD	Insurance Distribution Directive
IFRS	International Financial Reporting Standards
IM MC	International Markets Management Committee
IR(R)	Interest Rate (Risk)
IT	Information Technology
L&R	Loans & Receivables
LAC DT	Loss Absorbing Capacity Deferred Taxes
LAT	Liability Adequacy Test
LGD(irr)	Loss Given Default (irrecoverable)
LoB	Line of Business
LRMF(i)	Liquidity Risk Management Framework (insurance)
LTG	Long Term Guarantee
MCR	Minimum Capital Requirement
MiFID	Markets in Financial Instruments Directive
MRBB	Maatschappij voor Roerend Bezit van de Boerenbond cvba
NAPP	New and Active Product Process
NBB	National Bank of Belgium
NII	Net Interest Income
NL	Non-Life
NPS	Net Promoter Scores
NSL	Non Similar to Life
OFAC	Office of Foreign Assets Control
OIS	Overnight Index Swaps
ORSA	Own Risk & Solvency Assessment
P&L	Profit & Loss

PD	Probability of Default
PLS	Portfolio Limit System
PRIIPS	Packaged Retail and Insurance-based Investment Products
PWC	PriceWaterhouseCoopers
QRT	Quantitative Reporting Template
Risk ManCo	Risk Management Committee
RM	Risk Margin
RMF	Risk Management Framework
ROE	Return On Equity
S&P	Standard & Poor’s
SA	Symmetric Adjustment
SCR	Solvency Capital Requirements
SFCR	Solvency and Financial Condition Report
SII	Solvency II
SII SF	Solvency II Standard Formula
SME	Small and Medium-sized Enterprises
SRI	Socially Responsible Investing
SSC	Shared Service Centres
T1/T2	Tier 1 / Tier 2
TP	Technical Provisions
TRIP	Terrorism Reinsurance and Insurance Pool
VA	Volatility Adjustment
VaR	Value At Risk

Glossary

9 Glossary

3 LOD (Three Lines of Defence)

The 3 LOD model ensures the resilience of KBC's risk and control environment and safeguards the sustainability of our business model going forward. In this model, Business acts as the first line of defence, Risk as one of the second lines and Internal Audit as the third line. They all work together in order to prevent big impact losses for the KBC group.

Annuity

A contract that provides a series of regular payments (both amount and timing) by the insurer (amount payable / benefit) under specified conditions for a specified period of time.

An annuity may begin at a specified time after the issuing of the contract (deferred annuity), or following a specified trigger such as death or disability, e.g. orphans' benefits or disability annuities. Annuity benefits under an insurance contract typically end upon the death of the insured person, or cease upon recovery of the insured from disability or after a predefined period. Coverage may relate to one or two persons, respectively single-Life or joint-Life.

The contract can be funded by the policyholder by means of a single premium or through a series of instalments. The amount of regular payments to the beneficiary may be fixed or not, i.e. variable or fixed annuity, certain or temporary. Annuity contracts are sold on an individual and group basis.

Asset-liability management (ALM)

The ongoing process of formulating, implementing, monitoring and revising strategies for both on-balance-sheet and off-balance-sheet items, in order to achieve an organisation's financial objectives, given the organisation's risk tolerance and other constraints.

Best Estimate

The best estimate shall correspond to the probability-weighted average of future cash-flows, taking account of the time value of money (expected present value of future cash-flows), using the relevant risk-free interest rate term structure.

The calculation of the best estimate shall be based upon up-to-date and credible information and realistic assumptions and be performed using adequate, applicable and relevant actuarial and statistical methods.

The cash-flow projection used in the calculation of the best estimate shall take account of all the cash in- and out-flows required to settle the insurance and reinsurance obligations over the lifetime thereof.

BPV (Basis Point Value)

The measure that reflects the change in the net present value of interest rate positions, due to an upward parallel shift of 10 basis points (i.e. 0,10%) in the zero coupon curve.

Business risk

Business risk is the risk arising from changes in external factors that impact the demand for and/or profitability of our products and services. Risk factors that are taken into consideration include the macroeconomic environment, the regulatory framework, client behaviour, the competitive landscape and the socio-demographic environment.

Business risk is assessed on the basis of structured risk scans. Strategic risk is the risk caused by not taking a strategic decision, by taking a strategic decision that does not have the intended effect or by not adequately implementing strategic decisions.

Carrying amount

The amount at which an asset or liability is recognised in the balance sheet.

Linked to IAS 36.6 (impairment of assets), IAS 16.6 (property, plant and equipment) and IAS 38.8 (intangible assets).

This value is not necessarily the same as historic cost, e.g. because the carrying amount takes into account depreciation or could be a fair value.

Catastrophe risk

The risk that a single event, or series of events, of major magnitude, usually over a short period (often 72 hours), leads to a significant deviation in actual claims from the total expected claims.

The notion of catastrophe risk is per definition relative to the financial position of the individual insurer and any significance will need to be defined in mathematical terms. The exact definition of what constitutes a catastrophe hence varies per insurer.

Credit risk

Credit risk is the potential negative deviation from the expected value of a financial instrument arising from the non-payment or non-performance by a contracting party (for instance, a borrower, guarantor, insurer or re-insurer, counterparty in a professional transaction or issuer of a debt instrument), due to that party's insolvency, inability or lack of willingness to pay or perform, or to events or measures taken by the political or monetary authorities of a particular country (country risk). Credit risk thus encompasses default risk and country risk, but also includes migration risk, which is the risk for adverse changes in credit ratings.

DPF (Discretionary Participation Feature)

Part of the annual profit that is attributed to the policyholders of an insurance contract.

EAD (Exposure At Default)

The amount expected to be outstanding if an obligor defaults. At the time of default, it is equal to the actual amount outstanding, and therefore is no longer an expectation.

EBS (Economic Balance Sheet)

Balance sheet statement based on one of those accounting approaches using market-consistent values for all current assets and current obligations relating to in-force business, including off-balance sheet items.

Depending on the reporting approach different items can be recognised or not recognised in the balance sheet, as well the definition of a current resource or obligation can vary from approach to approach. The economic balance sheet provides the market-consistent value of the shareholder equity.

EIOPA (European Insurance and Occupational Pensions Authority)

The successor to the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS), EIOPA is part of the European System of Financial Supervision consisting of three European Supervisory Authorities and the European Systemic Risk Board. It is an independent advisory body to the European Parliament and the Council of the European Union. EIOPA's core responsibilities are to support the stability of the financial system, transparency of markets and financial products, as well as the protection of insurance policyholders, pension scheme members and beneficiaries.

EL (Expected Loss)

The expected value of losses due to default over a specified horizon. EL is typically calculated by multiplying the Probability of Default (a percentage) by the Exposure At Default (an amount) and Loss Given Default (a percentage). It is always considered 'an expectation' due to the 'Probability of Default' factor.

Eligible capital

Capital (either on or off-balance sheet) which, under regulatory rules, may be taken into account (fully or partially) in determining the insurer's available capital for solvency purposes.

Equity risk

The risk of a change in value caused by deviations of the actual market values of equities and/or income from equities from their expected values

Fair value

The amount for which an asset could be exchanged or a liability settled between knowledgeable, willing parties in an arm's length transaction. Market-consistent value or fair value is based on relative pricing or the 'no arbitrage' argument.

Foreign exchange risk

The risk of a change in value caused by the fact that actual foreign currency exchange rates differ from those expected.

Foreign exchange risk can arise if the assets and liabilities of an insurer are not in the same currency, or if contracts for administrative and other services are contracted in a currency different to the currency implied in the premium determination.

Guaranteed benefit

Payments or other benefits to which a particular policyholder or investor has an unconditional right that is not subject to the contractual discretion of the issuer.

The unconditional right of the policyholder implies that no condition is subject to the insurer's discretion, nor to insurer's performance. Hence, a guaranteed benefit, or its determination, is contractually stipulated without any ability of the insurer to influence that benefit, neither by discretion nor by its performance. Accordingly, a guarantee is a risk bearing feature, since the amount to be paid might deviate from the earnings of the insurer, without the ability of the insurer to avoid that.

Health insurance

Generic term applying to all types of insurance indemnifying or reimbursing for losses (e.g. loss of income) caused by illness or disability, or for expenses of medical treatment necessitated by illness or disability.

IBNR (Incurred but not Reported) reserves

IBNR is the abbreviation of incurred but not reported reserves (IBNR), these are the reserves for claims that become due with the occurrence of the events covered under the insurance policy, but have not been reported yet.

Inflation risk

The risk of a change in value caused by a deviation of the actual market-consistent value of assets and/or liabilities from their expected value, due to inflation, e.g. price inflation, wage inflation, etc., leading to an unanticipated change in insurance cost and/or impact of an insurance contract, e.g. with respect to contract limits.

Insurance contract

A contract under which one party (the insurer) accepts significant insurance risk from another party (the policyholder) by agreeing to compensate the policyholder or its beneficiary if a specified uncertain future event (the insured event) affects the policyholder.

Insurance risk

The potential negative deviation from the expected value of an insurance contract or pension claim (or a portfolio thereof).

Interest rate risk

The potential negative deviation from the expected value of a financial instrument or portfolio thereof due to changes in the level or in the volatility of interest rates.

Lapse risk

The potential negative deviation from the expected value of an insurance contract or a portfolio thereof due to unexpected changes in policy lapses. Note that the term surrender risk refers specifically to contracts with surrender value.

LGD (Loss Given Default)

The loss a bank expects to experience if an obligor defaults, taking into account the eligible collateral and guarantees provided for the exposure. It can be expressed as an amount or as a percentage of the EAD (Exposure At Default). At the time of default, the loss experienced is a loss of the actual amount outstanding, thus no longer an expectation.

Life insurance

Category of insurance contracts for which the benefit payment is based on the occurrence of death, disability, or critical illness of the insured within the specified coverage term, or on the life status of the insured at maturity.

Life insurance offers life and/or death coverage of the insured in the form of a single or multiple (as well regular in case of an annuity) lump sum payments to a beneficiary.

Health insurance products are often sold as a rider to a (group) Life contract. In *sensu stricto* these are not Life insurance, because they do not relate to the occurrence of death.

Liquidity risk

Liquidity risk is the risk that an organisation will be unable to meet its payment obligations as they come due because of the inability to liquidate assets or obtain adequate funding (liability liquidity risk) or the risk that it cannot easily unwind or offset specific exposures without significantly lowering market prices because of inadequate market depth or market disruptions (asset liquidity risk).

Market risk

The potential negative deviation from the expected value of a financial instrument (or portfolio thereof) due to changes in the level or volatility of market prices.

Market value

The cost that would be incurred or the gain that would be realised if an outstanding contract was replaced at current market prices (also called replacement value).

MVA (Market Value Adjustment)

IFRS-inspired adjustments or reserves recognised on positions at fair value. MVAs cover close-out costs, adjustments for less liquid positions or markets, counterparty exposure resulting from OTC derivatives, model-linked valuation adjustments, operation-related costs, as well as transaction- specific adjustments.

Mark-to-Market

The act of assigning a market value to an asset

MCR (Minimum Capital Requirement)

The capital level representing the final threshold that triggers ultimate supervisory measures in the event that it is breached.

Non-Life insurance

Generic term used to refer to all types of insurance business other than Life insurance, including for example Property insurance, Liability insurance, Motor insurance, Accident insurance, and Health insurance.

Operational risk

The potential negative deviation from the expected value of the organisation resulting from inadequate or failed internal processes and systems, human error or sudden external events, whether man-made or natural. Operational risk excludes business, strategic and reputational risk.

ORSA (Own Risk and Solvency Assessment)

The Own Risk and Solvency Assessment covers the entirety of the processes and procedures employed for identifying, assessing, monitoring, managing, and reporting on the short- and long-term risks a (re)insurance undertaking faces or may face, and for determining the own funds necessary to ensure that the undertaking's overall solvency needs are met at all times.

PD (Probability of Default)

The probability that an obligor will default within a one-year horizon.

Risk appetite

Risk appetite, as defined by the Board of Directors, is the amount and type of risk that KBC is able and willing to accept in pursuit of its strategic objectives. While the ability to accept risk is limited by financial (e.g., available capital) and non-financial regulatory and legal constraints, the willingness to accept risk depends on the interests of various stakeholders (shareholders, creditors, employees, management, regulators, clients, etc.). Risk appetite aims to find the right balance of satisfaction for all stakeholders.

Risk margin

A generic term, representing the value of the deviation risk of the actual outcome compared with the best estimate, expressed in terms of a defined risk measure

The term 'risk margin' in the context of Solvency II refers to the amount above the best estimate liability.

RWA (Risk-Weighted Asset)

An exposure weighted according to the 'riskiness' of the asset concerned. 'Riskiness' depends on factors such as the probability of default by the obligor, the amount of collateral or guarantees and the maturity of the exposure.

Solvency II

Solvency II is a project, initiated by the European Commission in 2001, and resulted in the European directive 2009/138/ EC of 25/11/2009 (Solvency II) which establishes capital requirements and risk management standards that apply across the EU and affect all areas of an insurer's operations. Solvency II aims to move away from the idea that 'one approach fits all' and thus encourages companies to manage risk in a way which is appropriate to the size and nature of their business in order to provide protection to policyholders by reducing the risk of insolvency to insurers.

SCR (Solvency Capital Requirement)

The amount of capital to be held by an insurer to meet the Pillar I requirements under the Solvency II regime.

Spread risk

The risk of a change in value due to a deviation of the actual market price of credit risk from the expected price of credit risk.

Underwriting risk

The risk of a change in value due to a deviation of the actual claims payments from the expected amount of claims payments (including expenses).

Total underwriting risk for Non-Life insurance includes the total of claims risk and expense risk for claims. For Life insurance it includes the total of lapse, surrender, and biometric risks, as well as expense risk for claims

VaR (Value At Risk)

The unexpected loss in the fair value (= difference between the expected and worst case fair value), at a certain confidence level and with a certain time horizon.

Annex

10 Annex

10.1 Transactions with related parties

Transactions with related parties, excluding key management (in millions of EUR)	2019 Parent entities with joint control	2019 Subsidiaries and other entities of group	2019 Associated companies	2019 Joint ventures	2019 Other	2019 Total	2018 Parent entities with joint control	2018 Subsidiaries and other entities of group	2018 Associated companies	2018 Joint ventures	2018 Other	2018 Total
Assets	1	608	14	3	10	637	4	622	14	46	2	687
Loans and advances	0	476	0	0	0	476	0	497	0	0	0	497
Equity instruments (including investments in associated companies and joint ventures)	0	53	14	3	0	70	0	50	14	46	2	112
Other	1	80	0	0	10	91	4	75	0	0	0	79
Liabilities	502	1 114	0	0	0	1 616	501	1 150	0	0	0	1 651
Deposits	0	1 040	0	0	0	1 040	0	1 034	0	0	0	1 034
Other financial liabilities	500	0	0	0	0	500	500	0	0	0	0	500
Other	2	75	0	0	0	76	0	116	0	0	0	117
Income statement	- 108	66	0	0	0	- 42	- 107	28	0	- 5	0	- 84
Net interest income	- 8	153	0	0	0	145	- 8	146	0	0	0	138
Interest income	0	165	0	0	0	165	0	154	0	0	0	154
Interest expense	- 8	- 12	0	0	0	- 20	- 8	- 8	0	0	0	- 16
Earned premiums, insurance (before reinsurance)	0	0	0	0	0	0	0	0	0	0	0	0
Technical insurance charges (before reinsurance)	0	0	0	0	0	0	0	0	0	0	0	0
Dividend income	0	0	0	0	0	1	0	2	0	0	0	2
Net fee and commission income	0	- 84	0	0	0	- 84	0	- 122	0	- 5	0	- 127
Fee and commission income	0	103	0	0	0	103	0	50	0	0	0	50
Fee and commission expense	0	- 186	0	0	0	- 186	0	- 172	0	- 5	0	- 177
Net other income	1	33	0	0	0	34	2	34	0	0	0	36
General administrative expenses	- 100	- 37	0	0	0	- 137	- 101	- 32	0	0	0	- 133
Undrawn portion of loan commitments, financial guarantees and other commitments												
Given by the group	0	0	0	0	0	0	0	0	0	0	0	0
Received by the group	0	5 122	0	0	0	5 122	0	0	0	0	0	0

Table 61: Transactions with related parties

10.2 Transactions with key management

Transactions with key management (members of the Board of Directors and Executive Committee) (in millions of EUR) (*)	2019	2018
Total (*)	0,4	0,4
Breakdown by type of remuneration		
Short-term employee benefits	0,4	0,4
Post-employment benefits	0,0	0,0
Defined benefit plans	0,0	0,0
Defined contribution plans	0,0	0,0
Other long-term employee benefits	0,0	0,0
Termination benefits	0,0	0,0
Share-based payments	0,0	0,0
Stock options (units)		
At the beginning of the period	0,0	0,0
Granted	0,0	0,0
Exercised	0,0	0,0
Composition-related changes	0,0	0,0
At the end of the period	0,0	0,0
Advances and loans granted to key management and partners	0,0	0,0

(*) Remuneration to key management or partners of the consolidating company on the basis of their activity in that company, its subsidiaries and associated companies, including the amount of retirement pensions granted to former key management staff on that basis.

Table 62: Transactions with key management

10.3 List of Tables

10.4 List of Figures