Enterprise risk management report

"Our risk profile reflects our freedom from legacy constraints and organisational complexity. As we transition from the start-up phase, at this time of enhanced opportunity, we have established a business that is ready to grow"

Enterprise risk management in a modern, legacy-free environment

At launch in December 2020, Conduit set out to be a modern, forward-looking organisation where risk management is integral to our culture, guiding strategic and operational plans.

The Company's increasing maturity in 2022 was such that we have been able to revisit and evolve key policies with minor refreshes to the Risk Policy, Stress and Scenario Testing Policy and Commercial Insurer's Solvency Self-Assessment Policy, alongside the evolution of the Underwriting Guidelines and formalisation of our Pricing Policy. I'm happy to report that our objective to have risk management integral to what we do is being delivered upon.

The risk function has provided quarterly reporting to the Board and/or Board Committees addressing our response to risk, compliance with risk appetite and tolerance statements, key risk indicators, and the response to any risk events or near-misses.

Our deployment of portfolio management tools gained pace and robustness in 2022, across both underwriting and investments, with analysis also supported by the maturing and increased adoption of our underwriting pricing tool which provides rich data for the analysis of rate adequacy and movement.

Similarly, our toolset to manage operational cyber threats also matured during the year, working in collaboration with our cloud-based system providers and technology partners. Our work on key risk indicators progressed during the year, but further work remains.

Emerging risk has also been a consideration during 2022, with an emerging risk register maintained and substantive discussions held on this topic as part of the strategy sessions of the Board, notably including various considerations associated with climate risk and cyber risk.

Our risk profile reflects our freedom from legacy constraints and relative organisational simplicity, with systems developed to ensure transparency and auditability in all our activities. This, together with our limited appetite for investment risk, allows a focus on underwriting, which is the core of our business.

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Risk profile

Conduit Re is well capitalised and has now completed the baseline operational build-out, with staffing increasing from 41 to 54 during 2022, as it transitions from start-up to being an established business. Further operational growth is now expected to be supportive of organic business growth.

Underwriting risk is the risk that we seek and is our primary risk. During 2022, we increased the operational and modelling support to our underwriters. We conducted a proof of concept on a more advanced approach to casualty accumulations. We plan to further advance this in 2023 with potential to expand to certain specialty classes. This will bring a similar level of sophistication as our aggregation control toolset for property, and natural-catastrophe-exposed specialty business.

Conduit Re maintains a balanced portfolio of reinsurance classes, geographical exposures and strict limits on our exposures to natural-catastrophe s and man-made loss events. Recognising the current favourable market conditions, we have accelerated our exposure appetite growth, to be deployed if market conditions support.

Our target gross exposure, per our 2023 business plan and 2022 business plan, for our largest single peril/region combinations at the 1 in 100 and 1 in 250 return periods increased from $131.2 million to $190.3 million and from $202.2 million to $249.0 million respectively. The same combinations on a net basis increased from $54.2 million to $65.0 million and from $77.9 million to $98.7 million. These targets are calibrated to 1 July viewpoints, for a first occurrence, and may change. Our actual gross modelled exposures at 1 July 2022 were broadly in line with plan while our net exposure was lower, due to the availability of competitive outwards reinsurance.

We buy high-quality outwards reinsurance to manage peak exposures and use reinsurers who are individually approved by our Counterparty Security Committee.

We seek to minimise other risks including investment risk, where our primary aim is to protect capital, and operational risk, where our simple corporate and organisational structure supports risk containment.

By starting life as a public company, we are less exposed to the short-term growth pressures that can be faced when private capital providers are motivated by seeking a liquidity event in the medium term. We are focused on long-term performance and building our business in a way that is sustainable and compatible with our responsible ESG values.

The overall risk policy and enterprise risk framework have remained relatively stable during 2022, with continued work on tools, risk indicators and the commencement of work on our internal capital model.

Our summary risk appetite and exposures are set out on the next pages.

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Risk category	Relative appetite/preference	Trend	Commentary
Overall – capital adequacy	Low We maintain capital to support a minimum rating of A– by AM Best and to provide a surplus over the regulatory enhanced capital requirement of twice that prescribed as an early warning buffer by the BMA.	↔	AM Best affirmed our A– rating and we have substantial capital to deploy. The value of our available assets has been reduced by mark-to-market losses but is expected to recover as held assets approach maturity.
Underwriting – premium	High This is the risk we seek in order to generate return. The risk is managed by seeking a target portfolio based on our view of rate adequacy and target diversification, supported by event and/or aggregate retrocessional protections.	↗	After a market-loss heavy 2022, industry capacity is expected to be constrained and this can lead to greater volatility. There is opportunity to take on the same, or greater, risk at improved rate.
Underwriting – exposure and aggregations	Medium We underwrite catastrophe-exposed reinsurance through our property and specialty classes, and business exposed to other aggregations, notably across casualty lines. We seek to understand and manage our exposures generally to a lower level than our Bermuda peer group.	↗	Overall, our portfolio has been slightly less exposed to catastrophe losses than we initially planned, but a volatile market and decreased market risk capacity increase risk.
Underwriting – reserve	Medium We underwrite a mix of classes including those where reserves take time to develop. We seek to minimise reserve risk through rigorous data analytics using market data, and benefit from an external loss reserve specialist review.	↔	Our current reserves have been impacted by elevated catastrophe losses, but the absence of legacy means the impact of inflation is limited. The volatility of reserve risk reduces as our overall book grows.
Investment – market and liquidity	Low Our primary aim is to protect capital and, consequently, we have a low appetite to expose our capital base to investment losses and a low appetite for volatility.	↘	Our limited risk portfolio has meant that our investment performance has performed favourably in comparison to peers. Our strategy remains unchanged with mark-to-market losses expected to substantially unwind over time.

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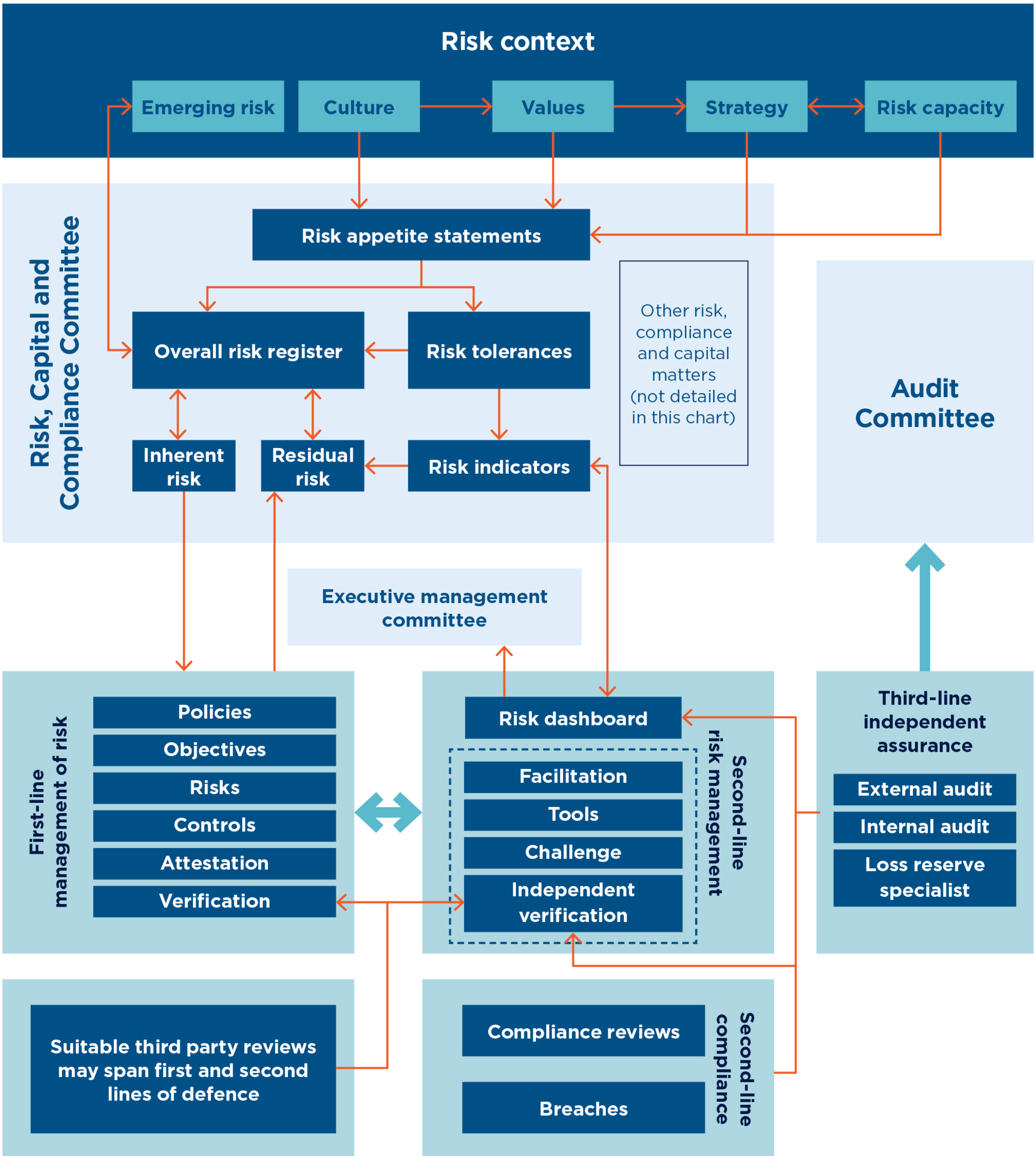
Risk category	Relative appetite/preference	Trend	Commentary
Credit	Low We use reinsurance to provide protection and therefore select reinsurers who provide limited credit risk.	↔	All retrocessionaires continue to be high quality and approved by the Counterparty Security Committee.
Operational and systems	Low We seek to minimise our operational risk within the context of operating as a reinsurer. We seek to attract and retain high-quality staff and gain competitive advantage by use of high-quality and integrated systems.	↘	Our operational risks have continued to decrease as we transition from the start-up phase and we expect this to continue as we mature.
Strategic	Low We seek to manage risk by keeping a clear and focused strategy as a single balance sheet reinsurer based in one location.	↘	We have executed on strategy to date and favourable market conditions further reduce strategic risk.
Reputational	Low A focus on maintaining and enhancing brand and franchise value with support from the ESG Committee, established by the holding company board.	↔	Public coverage is favourable to date and good progress is being made on transparency on ESG-related matters, with our first ESG Report to be published alongside this Annual Report and Accounts.
Legal, regulatory and litigation	Very low We seek to minimise our legal, litigation and regulatory risk by investing in our systems and people. We have no appetite for censure by regulators and tax authorities.	↘	The initial period of elevated risk during start-up phase has passed. The rate of change on global fiscal initiatives and political volatility in key locations we are exposed to appear to have reduced, providing a more stable environment.

Overall enterprise risk management framework and risk governance



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Risk governance

The Board is required under The UK Code to establish procedures to manage risk, oversee the internal control framework, and determine the nature and extent of the principal risks the Company is willing to accept in the context of achieving its long-term strategic objectives. To this end, the Board is supported by the CHL Audit Committee and the CRL Board and committees, most notably the CRL Risk, Capital and Compliance Committee.

The Board prescribes risk preferences that guide the CRL Board and committees as they establish risk appetite and tolerance statements. The Board also monitors the effectiveness of the overall enterprise risk management framework, leveraging the work undertaken by the CRL Board and committees.

CHL directors are invited to attend CRL Board and committee meetings and are provided with the associated materials and minutes. In addition, four CHL independent Non-Executive Directors also serve as Directors on the CRL Board.

CRL operates under a 'three lines of defence' risk management model, with the CRO reporting directly to the CRL Board's Risk, Capital and Compliance Committee. This reporting includes regular reporting of compliance with risk appetite and tolerance statements, emerging risks, risk event reports, key risk indicators and the solvency self-assessment. Membership of this committee includes directors who also serve on the boards of both CHL and CRL.

The risk function provides independent challenge and oversight of the identification, measurement, management and monitoring of risk by the first line of defence, supporting the CRL Risk, Capital and Compliance Committee and the CHL Board.

Day-to-day oversight of the management of risk by the first line of defence and the independent challenge provided by the second line is supported by the CEO and the Executive Committee.

Outputs from other second line of defence functions (Compliance and Actuarial) and from the third line (Internal Audit, External Audit and the Independent Loss Reserve Specialist) are fed back into the overall risk assessment. Regular meetings between the second-line functions and Internal Audit commenced during 2022. Outputs from all such functions may be used, where appropriate, to support independent validation, alongside the risk function's own reports and those of other independent third parties.

The capital management aspects of the risk framework have, to date, focused primarily on rating agency and regulatory requirements, with significant buffers being held. Development of our own internal capital model commenced in late 2022 and is expected to continue through 2023.

Conclusion

Overall, I remain confident that the management of risk is progressing in line with the initial vision set out with first-line ownership of risks: a small, focused risk team working closely with, now deepened, actuarial, modelling and data resources.

During 2022, my own responsibilities were expanded to also specifically address how we respond to climate and sustainability across our operations. This is very much complementary to my existing role as CRO, with our approach to climate and sustainability, like risk, being integral to how we work on a day-to-day basis.

Looking ahead to 2023, I expect a continuation of the market volatility we have seen in 2022. My view is that our now well-established operational capability and growing portfolio are well positioned to carefully embrace the market opportunity.

Andrew Smith
CRO
3 March 2023