Habib Insurance Company Limited

Risk Management Policy and Guidelines

Table of contents

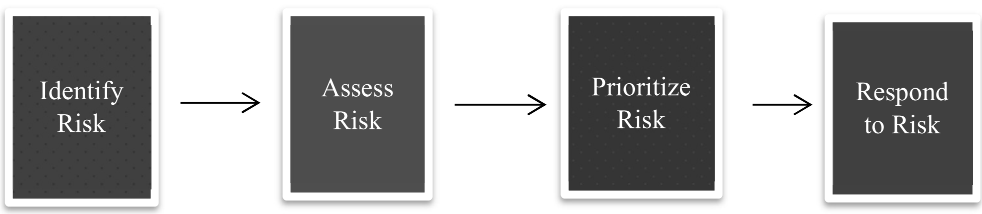
RISK MANAGEMENT POLICY AND GUIDELINES

The success or failure of an insurance company is directly dependent on the effective risk management. The business of insurance entails artful assumption and management of a risk under different classes of insurance business. Risk management involves the art of carefully determining the **risk appetite or risk tolerance** in correlation to treaty capacity, risk accumulation and capital adequacy. HIC risk policy captures the essence of risk management, not only the insurance risk but also the operational risks that can cause material impact on the organization.

Given the imperatives of risk management, the process has been strategized as below:

1. MANAGING RISK IN INSURANCE

Risk Process Flow Diagram:



Identify risks

The risk (or event) identification process precedes risk assessment and produces a comprehensive list of risks organized by risk category viz. insurance, financial, operational, strategic, compliance and sub-category (market, credit, liquidity, etc.) for business units and corporate functions. At this stage, it is important to understand the holistic nature of risks making up the enterprise's risk profile.

Assess risks

Assessing risks consists of assigning values to each risk. This is to be accomplished in two stages where an initial screening of the risks is performed using qualitative techniques, followed by a more quantitative analysis for complicated risks.

Prioritize risks

Risk prioritization is the process of determining risk management priorities by comparing the level of risk against predetermined target risk levels and tolerance thresholds. Risk is viewed not just in terms of financial impact and probability, but also subjective criteria such as health and safety impact, reputational impact and vulnerability.

Respond to risks

The results of the risk assessment process then serve as the primary input to risk responses whereby response options are examined (accept, reduce, share, or avoid), cost-benefit analysis performed, a response strategy formulated, and risk response plans developed.

The insurance risk is predominantly dependent on the happening of an event that triggers a claim. These risks are managed through an effective underwriting strategy, adequate reinsurance arrangements and proactive claims handling. The underwriting strategy aims to minimize insurance risks with a balanced portfolio mix to avoid risk accumulation.

2. ***OPERATIONAL RISK***

RISK HIERARCHY

The risk management environment is established under the corporate framework and is assigned to senior management i.e, COO and Head of Reinsurance.

Following key factors should be considered while underwriting risks:

1. Pricing risk i.e. premiums sufficient to absorb claims
2. Natural calamities (e.g., floods; severe storms; tornados; etc.) and the risk accumulation in a location
3. Which calamities have occurred in the past? How frequently? Was the damage minor, moderate, or severe?
4. Which calamities are most likely to occur in a region and the probable impact?
5. How vulnerable is the accumulation to each of the above identified hazards? Would the potential damage be catastrophic or manageable?
6. Common hazards? (e.g., water leaks; fire; blackout; etc.)
7. Clients should be encouraged for application of deductibles in policies against some reduction in premiums
8. Review of the past claims history of the client

COMMERCIAL PROPERTY INSURANCE				
PERIL	**LOCATION**	**DESCRIPTION**	**PROBABILITY/ CHANCE OF OCCURRENCE**	**ACTION**
Fire Strict compliance to the underwriting manual must be ensured	Islamabad Lahore Karachi	Low severity-High Frequency	1% up to 5%	More Properties may be insured as risk is moderate to minimal, subject to safe housekeeping as per industries standards
Earthquake	Western Baluchistan KPK and Southeastern Sindh	High	5% up to 10%	Avoid RISK ACCUMULATION at one location
Atmospheric Disturbance	Urban Areas	Minimal to Medium	1% up to 5%	This peril may be given if required
Allied Perils	Western Baluchistan and KPK	High	1% up to 5%	Large housing schemes should be avoided
Burglary	Islamabad	Low	<5%	More Properties may be insured as risk is minimal
Cash in Safe/Transit	Urban Areas	High	>10%	This cover may be given in conjunction with other business
	Islamabad	Low	<10%	Deductible should be applied
	Rural Areas	Low	<5%	Deductible should be applied

HOME INSURANCE

PERIL	LOCATION	DESCRIPTION	PROBABILITY /CHANCE OF OCCURRENCE	ACTION
Fire	Islamabad Lahore Karachi	Low	1% up to 10%	Concrete Structure commonly used in Pakistan less prone to fire and may be insured
Atmospheric Disturbance	Islamabad Lahore Karachi	Medium High Medium	<10% 20% or greater <10%	Rain damage in low lying areas causes extensive damage. Past history must be considered before underwriting
Earthquake	Islamabad Lahore Karachi	High Low Low	10% <10% <10%	Risk accumulation in Islamabad to be carefully monitored
Burglary	Islamabad Lahore Karachi	Low Low Medium	<10% 10% up to 15% 15% up to 25%	Limit the cover upto 20% of the total property sum insured

MARINE INSURANCE

PREFERRED			**NON-PREFERRED**
Office equipment, Electronics, Garments, Spare Parts, Rice, Yarn, Toys, Cement in bags, Sugar in bags, packed tea, Cars, Sports goods etc	Inland Transit Import & Export	High Medium	- Inland transit to and from Afghanistan - Import from any African Port - Arms & ammunitions - Live Stock

AUTO INSURANCE			
RISK	**IMPACT**	**MITIGATION**	**ACTION**
Flooding, earthquake riots and strikes	Medium	CAT Cover desired	To obtain CAT cover
Third Party Liability	Medium	Cap the Third Party liability limit Avoid Third Party cover on Commercial Vehicles, buses etc.	Max. Cap to be Rs. 100k
Vehicle associated with Politicians and lawyers	High	Avoid such risks as these may create problems	To be put on Decline List
Theft Only cover for vehicles	Medium	Install tracking devices	Avoid offering this cover

Considering the above tables, it is not advisable to insure large number of houses in Islamabad as the city is more prone to earthquake. A single event of catastrophe will result in large number of damages. Similarly, Lahore and Islamabad experience heavy rains and wind storms every year. Hence, possibility of rain damages should also not be ignored. Properties like Filling Stations, shops, small factories usually sustain losses due to heavy rains. However, most of the time, quantum of these losses is not on a higher side.

REINSURANCE & COINSURANCE RISK

The Company's arrangement of reinsurance or coinsurance is diversified such that it is neither dependent on a single reinsurer nor the operations of the Company are substantially dependent upon any single reinsurance contract. The Company obtains reinsurance cover from companies with sound financial health and rating. Reinsurance arrangements in place include treaty and facultative arrangements, including catastrophe cover. The effect of such reinsurance arrangements is that the Company may not suffer ultimate net insurance losses beyond the Company's risk appetite.

RISK	IMPACT	MITIGATION
Liquidation of Reinsurer or Coinsurers	High	Dealing with leading companies having A+ rating by PACRA/JCR-VIS for local insurance companies and A+ by S&P or AM Best for international reinsurers. Assign exposure limits for each Company

OTHER RISKS

RISK	IMPACT	MITIGATION
Wrong selection of Surveyor	Medium to High	Continuous monitoring the panel of Surveyor
Misuse of data by an employee terminated	High	Immediate blocking system rights Newspaper advertisement in case of key employees

REPUTATIONAL RISK MANAGEMENT

The Company's reputation is at risk when our stakeholders have adverse perceptions, regardless of whether those perceptions are grounded in fact or not. Stakeholders' expectations change constantly, and so reputational risk is dynamic.

Whilst there is no procedure or process to follow for avoidance of reputational risk, the following guidelines should be adapted:

1. Build Goodwill amongst customers, employees, regulator and other stakeholders

2. Monitor Social Media

3. Timely and efficient resolution of crises

3. ***FINANCIAL RISK***

SOLVENCY RISK

RISK	**MITIGATION**
Changes in regulatory requirements And Inefficient allocation of Assets compromising maximum admissibility under the solvency calculation	Placement of funds in funds managed by Asset management companies to keep adequate solvency margins Be alert of Assets that may be disallowed in future Endeavour to keep the credit period below 45 days to improve solvency position. Prepare Quarterly solvency margin calculations as increase in Earned Premium is direct consequence in increasing the solving margin requirement. Investment in Land and Building is allowed for solvency purpose calculation at 25%. Prior to making any investment in properties solvency calculations must be conducted to ensure adequacy. Loans including loans to related parties are kept at minimal as only 1 to 2% is allowed for solvency purposes. Balances with, shares, loans or any amount due from related party is not allowed under solvency. These to be kept at minimal. Vehicles, office equipment and furniture and fixtures are not allowed under solvency.

INVESTMENT RISK

RISK	MITIGATION
Stocks and marketable securities	To comply with Board policy on investments
Bank deposits/ term deposits	"AAA" rated banks - Cap of Rs.200 million per bank "AA" rated banks - with Cap of Rs.150 million per bank "A" rated banks Cap of Rs.75 million per bank
Mutual Funds	Exposures should be managed based on credit rating of the Asset Management Company and Funds and Company and Fund wise cap should be assigned

Managing the Risk under Investments

Managing Default Risk

Default risk may be minimized by investing in government securities bank deposits that are considered risk-free from a default standpoint. Investments in AAA securities are also considered almost risk-free, however per company cap must be assigned to have a balanced and diversified portfolio.

Fixed Deposit Certificates

This is considered the safest form of investment. Although profit rate is comparatively lower but provides a regular income on monthly/ quarterly basis. Hence, it would be easier to decide how to further utilise the income generated from such investment

Credit & Liquidity Risk

Credit Risk may be mitigated by monitoring credit exposures and undertaking transactions with a large number of counterparties in various industries. To mitigate Liquidity Risk, funding sources should be diversified and the investment portfolio should comprise a healthy balance of cash, cash equivalents and market securities.

Market Risk

Company is exposed to market risk with respect to its investments. This risk can be limited by maintaining a diversified portfolio and by monitoring the key factors that affects market movements.

Interest Rate Risk

To minimize interest rate risk, it is advisable to keep the maturity of deposits in line with the cash flow requirements of the Company to avoid penalties of cashing before maturity.

THE CORPORATE RISK

An effective corporate structure should include the following:

Have clear accountability and expectations which will help to achieve business objectives and ensure decisions are coordinated and consistent with stated risk appetite and policy.	Compliance to the Underwriting guidelines
Appropriate allocation and communication of roles, responsibilities & accountabilities across the business, and the setting of appropriate rules and processes for risk based decision making and reporting.	Conduct of periodic internal audits
All relevant parties to understand their roles, responsibilities and accountabilities, including what is expected of them and their authority for decision and reporting (i.e. each relevant individual can explain who they are accountable to, in what manner and how the risk appetite and policy applies to their role	Compliance to Organogram
All relevant parties to understand the relationships and associated tasks between key business and functional areas, share relevant information and take account of all relevant and significant factors to make informed decisions.	Compliance to the Authority limits as approved by the Board of Directors
Have a commonly agreed and understood terminology and language for risk that complement the organization's culture and business practice, used by, and readily available to, all members of the organization.	Risk assumption is restricted as per the treaty limits and takaful arrangement.

Ensure that appropriate risk information flows around the organization on a timely basis, and that there are processes in place to escalate risk issues. To be effective, escalation processes should be accessible to all, have clearly laid out procedures, trigger points and escalation points; and enable escalation through authority levels	Monthly MIS and Financials are presented highlighting any trigger points.

CURRENCY RISK

The Company needs to minimize its foreign currency risk to protect the negative impact of exchange rate fluctuations on transactions, both committed and anticipated. Although the Company is currently less exposed to foreign currency risk, but with anticipated growth in commercial lines business, the foreign currency risk would be required to be managed effectively.

The Company's exposures to Currency risk will be managed in the following manner:

1. The Chief Financial Officer will keep abreast of the evolution of foreign exchange rate fluctuations, expert market analysis, commentary and other information on forecasted rates available from reliable sources such as major financial institutions

2. The Chief Financial Officer will prepare forecasts of foreign currency requirements

3. Where significant foreign currency requirements are identified and their timing is fairly certain, the Chief Financial Officer will assess the feasibility and the desirability of entering into a hedging arrangement

4. All significant forward contracts, options and other instruments used to hedge a foreign currency exposure will be negotiated

5. The Chief Financial Officer will establish the annual foreign currency planning rates for the USD, EUR and GBP in conjunction with the Corporate Plan

6. The Company can engage in hedging arrangements based on identified needs only and not for speculative reasons

7. The Company will prepare an analysis of the year's foreign currency trades comparing them to the planning rates and the prevailing market rates to gain knowledge and perspective for use in implementing management strategies

4. ***ERRORS & OMISSIONS RISK***

Risk	Impact	Mitigation
Taking exposure without adequate reinsurance	High	GIS should restrict the posting rights of policies above treaty limits
Unaccounted cover notes	High	Daily monitoring of unaccounted / outstanding cover notes
Error in communicating correct and complete underwriting details to the reinsurer	High	The document should be reviewed by a person other than the one who has prepared
Risk inspection not carried out	Medium to High	For new clients, risk inspection should be mandatory prior to underwriting the risk For existing clients, risk inspection should be carried out periodically
Late/ Non intimation of claim to the reinsurer	Medium to High	Regular review of Claim Intimation Report
Non-compliance of laws	Medium to High	Checklist should be in place and signed off by the department head
Omission to mention applicable clauses / warranties e.g., Bank Mortgage Clause, Subject to No Loss Clause	Medium to High	The document should be reviewed by a person other than the one who has prepared
System passwords not changed frequently	Medium to High	Monitor password changes through logbook
Omission in recording purchase and sale transactions of shares	Medium to High	Daily monitoring of investment report

5. IDENTIFICATION OF KEY RISK

Any of the risk mentioned above may become a "Key Risk" if the amount involved exceeds 10% of the Total Equity.

6. ***IT RISK***

Risk	Mitigation
Hacking Unauthorized Email / system access	Change password periodically Restrict unauthorized access Install updated Malware / Firewall Monitor & swift action on Alerts generated by the system
Hardware Failure Data inaccessible Data Loss & Corruption Fire, Disasters	Having a Disaster Recovery & Business Continuity Plan in place which should be reviewed & tested periodically
Information Theft Virus Transmission	Restrict use of external Devices Restrict use of emails other than the official email Monitoring of user emails
Integration failure - Change in Operating system / Hardware / Release update (Database Patches)	Test the changes in the system before being operational Maintain Log Files
Leakage of information due to Disposal of Hardware	Make sure data is removed from storage devices before disposal
Accuracy of Data backup	Back up data should be checked periodically by restoring it in the system
Unauthorised access to server room	Camera Monitoring Authorised Access System
Power failure	Installation of UPS & Auto Start Generator Email Alerts from UPS Physical guard available on premises
Fire & Temperature Control in the Server Room	Install Room Temperature Control device with Alert service Smoke Detector & Fire extinguisher
Remote unauthorised access to Servers	Install Virtual Private Network (VPN) Install Firewalls
Unattended User PC / Software	Activate session expiry