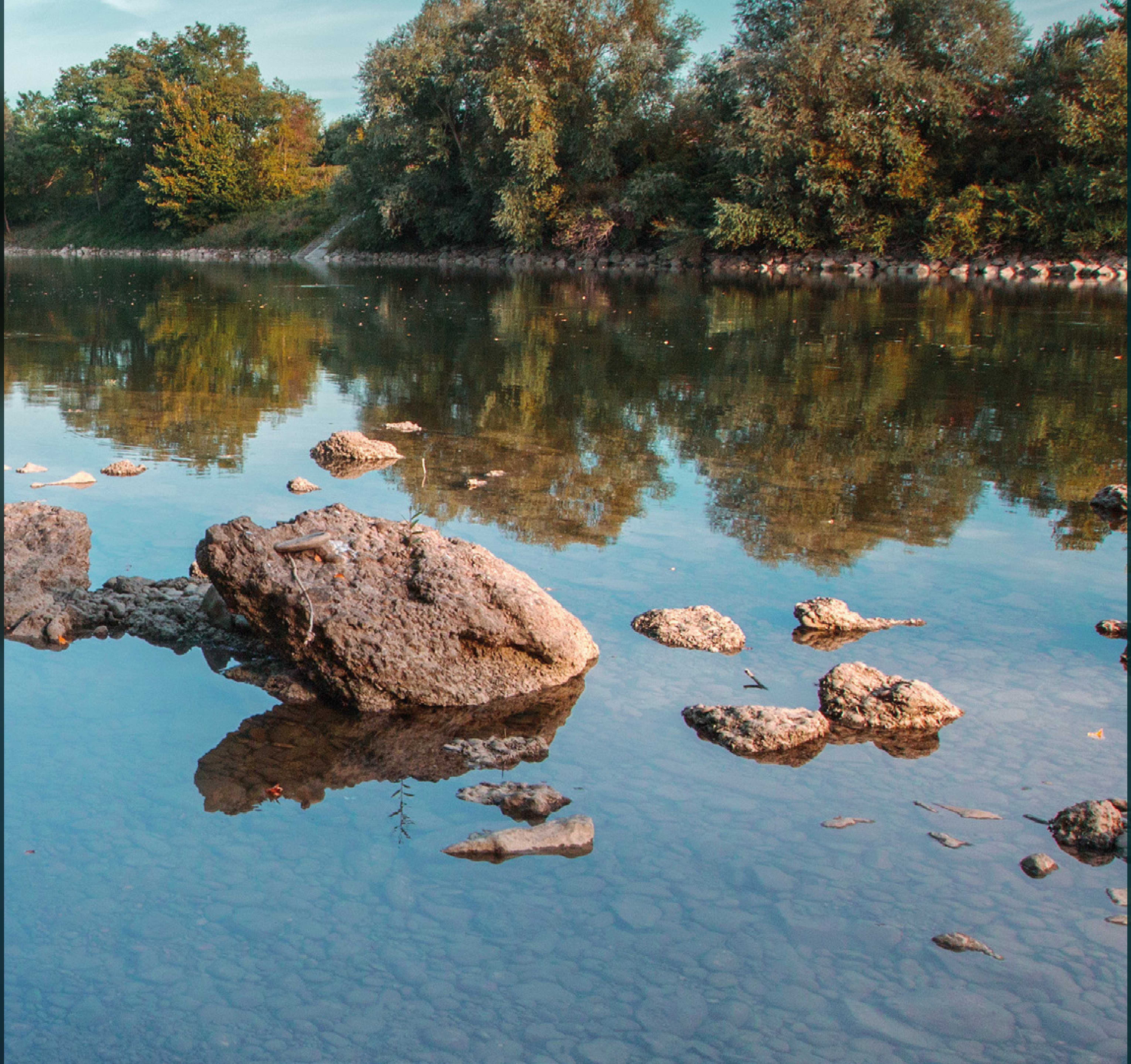
11 Risk management[84]



CONTENTS

84 GRI 102-11.

Below we describe the risk and capital management systems and the significant risks to which the Sava Insurance Group is exposed. These areas will be presented in more detail also in the solvency and financial condition report of Sava Re as at 31 December 2021 with auditor assurance, which will be posted on the Company's website on 26 April 2022, and in the solvency and financial condition report of the Sava Insurance Group as at 31 December 2021 with auditor assurance, which will be published on the Sava Re website on 19 May 2022.

11.1 Risk management system

The Sava Insurance Group management is aware that risk management is key to achieving operational and strategic objectives and to ensuring the long-term solvency of the Group. Therefore, the Group is continuously upgrading its risk management system at both the Group company and Group levels.

In recent years, the Sava Insurance Group has expanded its services with the integration of non-insurance companies. The risk management system is therefore based on Solvency II requirements, but additionally takes into account the legal specifics of non-insurance companies. The risk management system in these companies is adapted according to the business activities of each of them and the scope of these activities and risks to which a company is exposed.

The Group companies' risk culture and awareness of the risks to which they are exposed is essential to the security and financial soundness of the companies and the Group as a whole. To establish good risk management practices, the Group promotes a risk management culture with appropriately defined remuneration for employees, employee training, and relevant internal information flow at the individual company and Group levels.

The Sava Insurance Group has implemented a risk strategy that defines the Group's risk appetite and policies that cover the entire framework of risk management, own risk and solvency assessments, and risk management for each risk category. Based on the Group's risk strategy and policies, individual Group companies set up their own risk strategies and policies, taking into account their specificities and local legislation. The adequacy of policies underpinning the risk management system is examined annually. The risk strategy is prepared in line and simultaneously with the strategic plan.

The risk management system at the individual company and Group levels is subject to continuous improvement. Particular attention is paid to:

- clearly-expressed risk appetite in the framework of the risk strategy and on this basis also operational limits;
- development of own risk assessment models and upgrading of the own risk and solvency assessment (hereinafter: ORSA),
- integration of the ORSA and risk strategy in the framework of business planning and shaping of the business strategy,
- integration of risk management processes into business processes,
- systematic upgrading of the internal control environment, adjustment of processes to new activities, monitoring of the occurrence of untoward events,
- establishment of adequate risk management standards in all Group companies depending on the scope, nature and complexity of business transactions and related risks.

CONTENTS

11.1.1 Risk management organisation

Systematic risk management includes an appropriate organisational structure and a clear delineation of responsibilities.

The efficient functioning of the risk management system is primarily the responsibility of the Sava Re management board and the management board of each individual subsidiary. To ensure efficient risk management, the Group uses a three lines of defence model, which clearly segregates responsibilities and tasks among the lines:

- The first line of defence constitutes all organisational units with operational responsibilities (development, sales, marketing and insurance management, provision of insurance services, financial operations, accounting, controlling, human resources and others).
- The second line of defence consists of three key functions (the risk management function, actuarial function, compliance function) and the risk management committee, if set up in the company.
- The third line of defence consists of the internal audit function.

The Group's risk management system has been set up based on the top down principle, taking into account the specificities of each individual company.

The management board of each company plays a key role and bears ultimate responsibility for the effectiveness of established risk management processes and their alignment with the Group's standards and the applicable legislation. In this regard, the management board is primarily responsible for:

- setting the risk strategy and approval of risk tolerance limits and operational limits,
- adopting policies relating to the risk management system,
- implementing effective risk management processes in the Company,
- monitoring operations in terms of risk and providing input for risk-based decision making.

The supervisory board of each individual company approves the risk strategy, risk management policies and the appointment of key function holders in the risk management system. In addition, the supervisory board analyses periodic reports relating to risk management. A risk committee has been set up within the supervisory board of the parent company to provide relevant expertise and support in the risk management process in the Company and in the Group.

The first line of defence of each individual Group company involves all company employees responsible for ensuring that operational tasks are performed in a manner that reduces or eliminates risks. Additionally, risk owners are responsible for individual risks listed in the risk register. Line managers are responsible for ensuring that the operational performance of the processes for which they are responsible are conducted in a manner that reduces or eliminates risks, and that the frameworks laid down in the risk strategy are observed. The first line of defence is also responsible for monitoring and measuring risks, the preparation of data for regular reporting on individual areas of risk, and the identification of new risks.

Each Group company has set up the following three key functions as part of the second line of defence: the actuarial function, risk management function, and compliance function. In addition, the Group's large members have in place a risk management committee. The members of the risk management committee and key function holders are appointed by the management board; key function holder appointments additionally require the consent of the supervisory board. Each individual company ensures the independence of the key functions, which are organised as management support services and report directly to the management board. Their roles and responsibilities are defined in the policy of each key function or in the risk management policy that defines the risk management function.

The risk management function of each individual company is mainly responsible for setting up effective risk management processes and for the coordination of risk management processes already in place at the company or Group level. It is involved in all stages of the processes of identification, assessment, monitoring, management and reporting of risks. It is also involved in the preparation of the risk strategy and the setting of risk tolerance limits. The risk management function regularly reports to the risk management committee (if set up), the management and the supervisory boards, the risk committee (Sava Re) and the Group's risk management function holder, and works in cooperation with the risk management function on an ongoing basis. Furthermore, it offers support to the management board in decision-making (including in relation to the strategic decisions such as corporate business strategy, mergers and acquisitions, and major projects and investments).

CONTENTS

The main tasks of the actuarial function in the risk management system comprise expressing an opinion on the underwriting policy, expressing an opinion on the adequacy of reinsurance arrangements, and independent verification and challenging of technical provision calculations, including assumptions, methods and expert judgment areas. The actuarial function of each individual company works in cooperation with the Group's actuarial function.

The main duties of the compliance function relating to the risk management system are: identification, management and reporting of any instances of non-compliance with regulations, including monitoring of the legal environment, analysis of existing processes regarding their compliance with internal and external rules, and any changes in regulations.

Apart from the key functions, the second line of defence at Sava Re also consists of a risk management committee that addresses risks at the Company and Sava Insurance Group levels. Such a committee also operates in some (larger) subsidiaries. The committee includes the key representatives of the first line of defence and the management board with regard to the company's risk profile. The holders of other key functions of the risk management system are also invited to attend meetings of the committee. The committee is primarily responsible for monitoring the risk profiles of the Group and individual companies, analysing risk reports and issuing recommendations to the management board.

The third line of defence consists of the internal audit function. Employees of the Sava Re internal audit department also perform the internal audit function for other Slovenian subsidiaries under outsourcing arrangements, while other subsidiaries have their own internal audit departments. The internal audit function operates at the individual company and Group levels and is completely independent from the business operations and other functions. In 2021, Group Internal Auditing was introduced in the entire Sava Insurance Group, including in non-EU based Group companies. In the context of the risk management system, the internal audit function holders are responsible for the independent analysis, verification, and assessment of the performance and effectiveness of internal control and risk management systems.

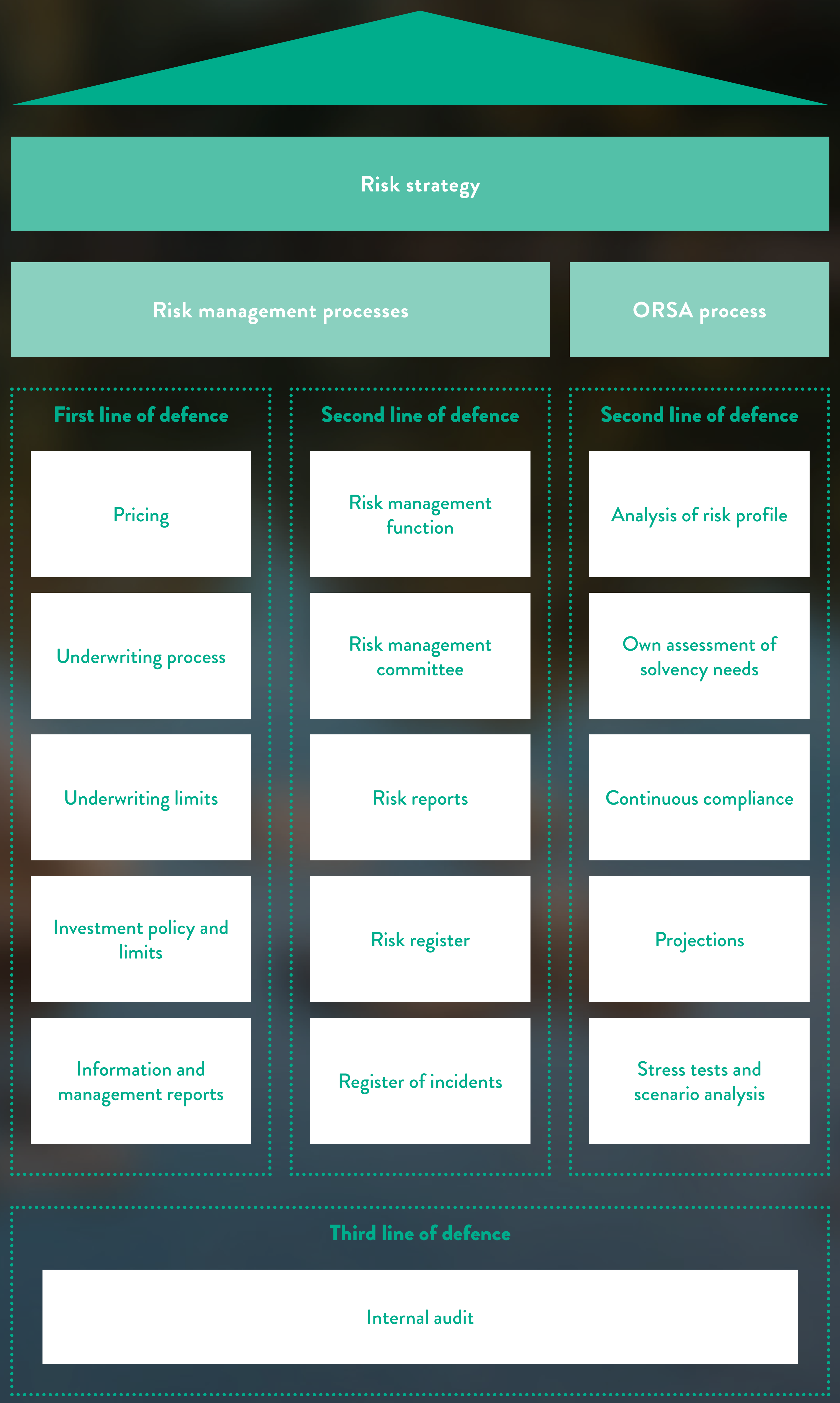
Good practices from Sava Re's risk management model and the organisation of risk management are also transferred to other Group companies.

11.1.2 Components of the risk management system

Risk management is integrated into all stages of business management and is composed of the following key elements:

- risk strategy,
- risk management processes within the first and second lines of defence, and
- the ORSA process.

The Group's risk management system is presented in the diagram below.



CONTENTS

11.1.2.1 Risk strategy

The Group seeks to operate in compliance with its business strategy and meet the key strategic objectives while maintaining an adequate capital level. With this in mind the management board, with the consent of the Sava Re supervisory board, approved the Sava Insurance Group risk strategy for 2020–2022 in 2020, taking into account its risk-bearing capacity. Each individual Group company drafts its own risk strategy by taking into account the Group's risk strategy. The Group document sets:

- the company's risk appetite,
- key indicators, and
- risk tolerance limits.

The key areas on which risk appetite is based are:

- the solvency ratio,
- the profitability of operating segments,
- the volatility of operating results by operating segment, and
- liquidity indicators.

Each individual Group company sets its own risk strategy, risk tolerance limits and operational limits based on the Group's risk appetite. Risk tolerance limits are limits set for individual risk categories included in individual companies' risk profiles, determining approved deviations from planned values. These limits are set based on the results of the sensitivity analysis, stress tests and scenarios, and professional judgment.

Individual Group companies set operational limits, such as (re)insurance underwriting limits and investment limits, in order to ensure that the activities of the first line of defence are carried out in accordance with the set risk appetite. In addition, each Group company ensures that it has in place well-defined and established escalation paths and management actions in the case of any breach of operational limits.

For periodic monitoring of compliance with the risk strategy, individual Group companies define a minimum set of risk measures for each risk category to allow for monitoring of the Group's and each Group company's current risk profile and capital position. These risk measures are regularly monitored at the Group and individual company levels.

11.1.2.2 Risk management processes

Risk management processes are inherently connected with and incorporated into the basic processes conducted at the individual company and Group levels. All organisational units are involved in risk management processes.

The chief risk management processes are:

- risk identification,
- risk assessment (measuring),
- risk monitoring,
- determining appropriate risk control measures (risk management), and
- risk reporting.

Risk identification

Risk management processes are incorporated into all three lines of defence of the risk management process. The roles of individual lines of defence are defined in the risk management policy. Risk management processes are also integrated into the decision-making system. All important and strategic business decisions are also evaluated in terms of risk.

In the process of risk identification, each individual Group company identifies the risks to which it is exposed. The key risks compiled in each company's risk register, constituting the company's risk profile, are reviewed on a regular basis and new risks are added if so required. Risk identification at the Group level is conducted in the same way.

CONTENTS

Risk identification in individual Group companies and at Group level is both a top-down and a bottom-up process. The top-down risk identification process is conducted by the risk management function, the risk management committee and the management board of each Group company. Such identification of new and emerging risks is based on monitoring of the legal and business environment, market developments and trends, and expert knowledge. This approach is mainly used with strategic risks, such as reputational risk and regulatory risk.

Bottom-up risk identification takes place in individual organisational units and with risk owners (first line of defence). A Group company's risk thus identified is categorised and incorporated into the relevant monitoring, measuring, managing and reporting processes.

Risk identification is performed on an ongoing basis, especially as part of business planning and any major projects and business initiatives such as launching of a new product, investment in a new class of assets, acquisitions and other.

Risk assessment (measurement)

The Group has in place regular risk assessment (measurement) processes for all the risks to which individual companies or the Group are exposed. Both qualitative and quantitative methods are used to measure risk. A modelling department has been set up on the Sava Insurance Group level, which develops quantitative models for Group-wide risk assessment.

Risks are thus measured:

- using the Solvency II standard formula,
- by calculating the overall solvency needs within the own risk and solvency assessment (ORSA),
- by conducting and analysing stress tests and scenarios,
- through qualitative risk assessment in the risk register,
- using various risk measures allowing simplified measurement and monitoring of the current risk profile.

Risk monitoring

Risk monitoring is conducted at several levels: at the level of individual organisational units and risk owners, risk management departments, the risk management committee, the management board, the supervisory board's risk committee (Sava Re) and at the supervisory board level of each Group company. In addition, each Group company's risk profile is monitored at the Group level in terms of impact on the Group's risk profile. A standard set of risk measures is defined for risk monitoring, and Group companies follow it on a regular basis. Both risks and risk management measures are subject to monitoring and control. Adverse events and appropriate corrective measures to prevent the recurrence of an individual event are also monitored.

Risk management

The management board of each Group company is responsible for risk management and the use of various risk management techniques and actions. In its decisions, the management board takes into account the cost benefit aspect of actions as well as recommendations, if any, issued by the risk management committee and key functions.

Whenever the need arises to adopt a new risk control measure, the relevant company conducts an analysis of the measure in terms of economic and financial viability. Elimination or mitigation of individual risks must be more cost effective than mitigation of the potential impact should the risk materialise, taking into full account the probability of such an event and all its implications.

In practice, it is already in the business planning process that a Group company examines the impact of the business strategy on its capital position, both with regard to the regulator as well as with regard to the own risk and solvency assessment. If during the financial year, decisions are taken that have a significant impact on the risk profile but have not been assessed in terms of risk during the business planning process, the relevant company assesses the impact of such decisions on its risk profile and capital adequacy, and verifies compliance with the risk appetite. If a business decision could have a significant impact also on the Group's risk profile, such impact on the Group's risk profile and capital adequacy is also assessed. If any business decision fails to comply with the risk appetite or any risk tolerance limit is exceeded, the company is required to document such deviation and take relevant action to resolve the situation.

CONTENTS

Risk reporting

Periodic risk reporting has been set up at the large Group companies and at the Group level. Risk owners report on each risk category to the risk management function, including a predetermined set of significant risk measures and qualitative information. Based on this, the risk management function in cooperation with risk managers prepares a risk report covering each individual company's entire risk profile. The report is first discussed by the company's risk management committee (if the company has one), followed by the management board, risk committee (Sava Re) and the company's supervisory board. Finally, a company's risk management function submits the report to the Group's risk management function.

11.1.2.3 Own risk and solvency assessment

In addition to these risk management processes, EU-based Group (re)insurance companies and the Group also perform an ORSA, which is defined in the own risk and solvency assessment policy. ORSA is a process that includes the identification of the differences between a company's or the Group's risk profile and the assumptions of the standard formula, the own assessment of solvency needs, capital adequacy projections, stress tests and scenarios, and the establishment of the link between the risk profile and capital management. In ORSA, all material risks, whether quantifiable or not, are assessed that may have an impact on the operations of the Group or a Group company from either an economic or a regulatory perspective. The 2022 ORSA also includes climate change risk considered and assessed qualitatively, and two climate scenarios.

As a rule, the ORSA process is conducted annually; an ad hoc ORSA is performed in the event of a significant change in the risk profile. EU-based Group insurers and the Group report to the regulator on the ORSA (at least) on an annual basis. Every year, ORSA is more closely integrated with other processes, in particular with risk and capital management and business planning. The Group's risk management committee and company management boards are actively involved in the ORSA throughout the process. Employees from different departments take part in the process, as we wish to obtain as complete and updated a picture of a company's risk profile as possible.

The primary objective of the ORSA is to better understand own risk profile and the standard formula, and to analyse the impact of the changes in the risk profile on capital adequacy over the next three years. ORSA is an integral part of the decision-making process conducted to ensure that the key decisions and the business strategy are adopted with consideration of risks and associated capital requirements. Based on ORSA results we also check the compliance of the business strategy with the risk strategy. This establishes the link between the business strategy, the risks taken in the short, medium and longer term, and the capital requirements arising from those risks and capital management.

CONTENTS

11.2 Capital management

The capital management policy lays down objectives and key activities related to capital management. Capital management is inseparable from the risk strategy, which defines the risk appetite.

The Group's capital management objectives are:

- solvency, in the range of the optimal long-term capitalisation as defined in its risk strategy;
- adequate degree of financing flexibility;
- ability to achieve adequate profitability for operating segments that tie up capital;
- ability to achieve an adequate return on equity or adequate dividend yields for shareholders.

The Group manages its capital to ensure that each Group company has available, on an ongoing basis, sufficient funds to meet its obligations and regulatory capital requirements. The composition of own funds held to ensure capital adequacy must comply with regulatory requirements and ensure an optimal balance between debt and equity capital. The amount of own funds of each Group company and the Group must be sufficient, at all times, to meet the statutory solvency capital requirement, as well as to satisfy the requirements of its target credit rating and other objectives of any Group member or the Group.

An important input element of capital management and business planning is the Group's risk strategy, including the risk appetite set out therein. The Group's risk strategy defines levels of capital adequacy. These levels serve as the basis for determining the capital adequacy of each Group company.

The Group risk strategy in conjunction with capital adequacy is defined so as to meet regulatory requirements and the requirements of rating agencies, and to ensure that the parent company has sufficient excess capital to cover any potential capital needs of subsidiaries in the event of a major stress scenario materialising in any of them. To this end, excess of eligible own funds is determined over the statutorily required.

As provided by the risk strategy, all Group subsidiaries must have, on an ongoing basis, a sufficient amount of capital available to meet solvency requirements. In addition, Group subsidiaries subject to the Solvency II regime must have sufficient capital to absorb small to medium fluctuations in the SCR and own funds, which may result from the standard formula methodology and the possibility of small and medium stresses and stress scenarios materialising.

11.3 Material risks of the Sava Insurance Group

The Sava Insurance Group and Group members are exposed to the following risks:

- Underwriting risks arising from (re)insurance contracts. These are associated with the risks covered under (re)insurance contracts and with directly related activities.
- Market risk related to volatile prices of financial instruments, market prices of other assets and participations in other companies.
- Credit risk arising from non-performance and changes in the credit rating of securities issuers related to the investment portfolio of Group companies, and of reinsurers, intermediaries and other business partners who have outstanding liabilities to the Group companies.
- Operational risk associated with inadequate or inefficient internal processes, people and computer systems, or from external events.
- Liquidity risks related to loss resulting from insufficient liquid assets when liabilities become due or increased costs of realisation of less liquid assets.
- Strategic risk associated with achieving the Company's strategic plans, and reputational risk, including any implications.

Individual risks are described in detail in the notes to the financial statements of the Sava Insurance Group and Sava Re (section 17.6 "Risk management").

CONTENTS