Operating and financial review

Group Chief Financial Officer's report

QBE achieved a strong rebound in profitability during 2021, reflecting a material improvement in underwriting earnings despite heightened catastrophe experience. Favourable market conditions and a focus on targeted growth supported a 22% increase in our premium base. We enter 2022 with real momentum.

Gross written premium (US$M)

18,457

22% from 2020

Net earned premium (US$M)

13,408

10% from 2020

Statutory underwriting profit (loss) (US$M)

1,138

2020 (869)

Financial performance

QBE reported a statutory net profit after tax of $750 million compared with a loss of $1,517 million in 2020.

Adjusted cash profit after tax improved to $805 million from a loss of $863 million in the prior year and equates to a return on equity of 10.3%.

The statutory underwriting profit improved to $1,138 million (which included a $301 million risk-free rate benefit) from a loss of $869 million (which included a $381 million risk-free rate charge) in 2020, notwithstanding increased catastrophe claims and further adverse prior accident year claims development.

Gross written premium increased 22% as a result of premium rate increases, improved retention and strong new business growth. Growth in our Crop business was particularly strong, supported by higher commodity prices and targeted organic initiatives.

The statutory combined operating ratio improved to 93.7% from 104.2% in 2020, reflecting significant COVID-19 claims in the 2020 result and improved current accident year profitability.

The benefits of increased operating efficiency more than offset a material increase in catastrophe claims.

Crop reported a combined operating ratio of 92.7% compared with 95.0% in the first half and 98.2% in 2020. Underwriting profit increased to $87 million from $14 million in 2020.

The Group's statutory expense ratio improved to 13.6% from 15.0% in the prior year, reflecting further cost savings from the operational efficiency program coupled with operating leverage due to strong premium growth.

We are now well into the next phase of our operating efficiency journey, including the rationalisation and modernisation of our IT estate, which is expected to contribute to an expense ratio of 13% by 2023. In addition to cost efficiencies, digitisation and modernisation are expected to drive sustained improvement in operating capacity and business agility.

As we approach our 13% expense ratio target, we expect to increasingly reinvest incremental operating efficiencies to capitalise on longer-term growth opportunities.

Financial strength and capital management

QBE's capital position strengthened during the year, notwithstanding very significant organic growth.

QBE's indicative APRA PCA multiple increased to 1.81x at 31 December 2021. Excluding GBP327 million of subordinated debt intended to be redeemed, the indicative pro forma APRA PCA multiple was 1.75x, up from 1.72x at the end of 2020, and at the higher end of our 1.6–1.8x target range.

The improvement in the regulatory capital position primarily reflects strong organic earnings generation during the year.

We have revised our measure of gearing from debt to equity to debt to total capital to align with the approach underpinning our external debt covenants. Debt to total capital was 26.9% at 31 December 2021. Excluding the subordinated debt intended to be redeemed, pro forma gearing improved to 24.1% from 25.8% at the end of 2020, and is within the Group's 15–30% target range.

The probability of adequacy (PoA) of net outstanding claims reduced slightly to 91.7% from 92.5% at the end of 2020, but remains towards the top end of our 87.5–92.5% target range.

Investment performance and strategy

The total investment return for the year was 0.4% and compared with 0.9% in 2020.

During the year the Group held a modestly short asset duration relative to outstanding claims liabilities. With the significant steepening in yield curves, the Group generated a pre-tax profit of $41 million as a result of this tactical curve positioning.

Our investment approach remains conservative, with 94% of our cash and investments in high quality fixed income securities and the remaining 6% in risk assets, primarily unlisted property and infrastructure.

In 2022, we will gradually move towards our long-term strategic asset allocation benchmark of 15% exposure to risk assets, including equities, high yield and emerging market debt, and private credit.

Statutory net profit (loss) after tax (US$M)

750

2020 (1,517)

Adjusted cash profit (loss) ROE

10.3%

2020 (10.9)%

Summary income statement and underwriting performance

FOR THE YEAR ENDED 31 DECEMBER	STATUTORY 2021 US$M	STATUTORY 2020 US$M	ADJUSTMENTS CTP 2021 US$M	ADJUSTMENTS COVID 2021 US$M	ADJUSTMENTS COVID 2020 US$M	MANAGEMENT BASIS 2021[1,2] US$M	MANAGEMENT BASIS 2020[1] US$M
Gross written premium	**18,457**	14,643	**–**	**4**	(42)	**18,453**	14,685
Gross earned premium	**17,035**	14,008	**–**	**4**	(42)	**17,031**	14,050
Net earned premium	**13,408**	11,708	**(365)**	**(6)**	(77)	**13,779**	11,785
Net claims expense	**(8,371)**	(8,934)	**349**	**141**	(560)	**(8,861)**	(8,374)
Net commission	**(2,070)**	(1,891)	**19**	**2**	9	**(2,091)**	(1,900)
Underwriting and other expenses	**(1,829)**	(1,752)	**–**	**2**	(27)	**(1,831)**	(1,725)
Underwriting result	**1,138**	(869)	**3**	**139**	(655)	**996**	(214)
Net investment income on policyholders' funds	**77**	142	**–**	**–**	–	**77**	142
Insurance profit	**1,215**	(727)	**3**	**139**	(655)	**1,073**	(72)
Net investment income on shareholders' funds	**45**	84					
Financing and other costs	**(247)**	(252)					
Loss on sale of entities and businesses	**–**	(2)					
Share of net loss of associates	**(7)**	(5)					
Restructuring and related expenses	**(72)**	(104)					
Amortisation and impairment of intangibles	**(21)**	(466)					
Profit (loss) before income tax	**913**	(1,472)					
Income tax expense	**(156)**	(39)					
Profit (loss) after income tax	**757**	(1,511)					
Non-controlling interests	**(7)**	(6)					
Net profit (loss) after income tax	**750**	(1,517)					
KEY RATIOS	**%**	**%**				**%**	**%**
Net claims ratio (ex risk-free rate)	**64.6**	73.1				**66.5**	67.9
Prior accident year claims development	***(1.1)***	*3.1*				***1.4***	*3.1*
Risk margin (release) charge	***(0.6)***	*2.9*				***0.7***	*0.4*
Net commission ratio	**15.5**	16.1				**15.2**	16.1
Expense ratio	**13.6**	15.0				**13.3**	14.6
Combined operating ratio (ex risk-free rate)	**93.7**	104.2				**95.0**	98.6
Combined operating ratio	**91.5**	107.4				**92.8**	101.8
Insurance profit (loss) margin	**9.1**	(6.2)				**7.8**	(0.6)

1 Excludes estimated impact of COVID-19 on Group underwriting results.

2 Excludes transaction to reinsure CTP liabilities which, although immaterial to profit overall, materially impacts year-on-year comparison of net earned premium and underwriting ratios.

Cash profit and dividends

Reconciliation of cash profit

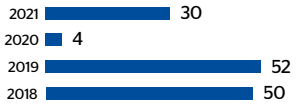
FOR THE YEAR ENDED 31 DECEMBER	2021 US$M	2020 US$M
Net profit (loss) after tax	**750**	(1,517)
Amortisation and impairment of intangibles after tax [1]	**53**	455
Write-off of deferred tax assets	**–**	120
Write-off of capitalised IT assets	**–**	27
Net cash profit (loss) after tax	**803**	(915)
Restructuring and related expenses after tax	**52**	75
Net loss on disposals after tax	**–**	2
Additional Tier 1 capital coupon accrual	**(50)**	(25)
Adjusted net cash profit (loss) after tax	**805**	(863)
Return on average shareholders' equity – adjusted cash basis (%)	**10.3**	(10.9)
Basic earnings (loss) per share – adjusted cash basis (US cents)	**54.6**	(60.7)
Dividend payout ratio (percentage of adjusted cash profit) [2]	**41%**	N/A

1 $50 million of pre-tax amortisation expense is included in underwriting expenses (2020 $50 million).

2 Dividend payout ratio is calculated as the total A$ dividend divided by adjusted cash profit converted to A$ at the period average rate of exchange.

Dividends per share (A¢)

30



Dividend payout (A$M)

443

Dividends

The Board has reassessed the Group's dividend policy and now expects to pay out 40%–60% of adjusted cash profit annually. This revised approach will better support the Group's growth ambitions and provide flexibility to manage the dynamics of the global insurance cycle.

The final dividend for 2021 is 19 Australian cents per share, compared with the nil 2020 final dividend.

The final dividend will be 10% franked and is payable on 12 April 2022. The Dividend Reinvestment Plan and Bonus Share Plan will be satisfied by the issue of shares at a nil discount.

The combined 2021 interim and final dividend of 30 Australian cents per share is up substantially from 4 Australian cents per share in 2020 and equates to a total payout of A$443 million or 41% of adjusted cash profit.

The payout for the current period balances the need to reward shareholders while retaining capital flexibility to support the near-term growth outlook and the normalisation of risk settings in our investment portfolio.

Significant items impacting the underwriting result

The summary income statement on the preceding page shows the statutory result excluding the following items to more clearly present underlying performance.

CTP reinsurance

During 2021, the Group entered into a transaction to reinsure Australian CTP prior accident year liabilities which reduced net earned premium and net claims expense by $365 million and $349 million respectively, while positively impacting commission expense by $19 million.

While not materially impacting profit, the transaction impacts year-on-year comparison of net earned premium and underwriting ratios.

COVID-19

The result included a COVID-19 benefit of $139 million compared with a charge of $655 million in 2020, mainly due to a $140 million risk margin release reflecting reduced uncertainty with respect to business interruption, LMI and trade credit claims outcomes.

In addition, a current accident year charge of $63 million was offset by favourable prior accident year claims development of $64 million.

The current accident year charge included North America claims (mainly accident & health (A&H), professional liability and workers' compensation) and a modest second half charge for potential Australian business interruption claims.

Prior accident year claims development included adverse development in North America which was more than offset by favourable development in International as well as positive development in business interruption, LMI, CTP and trade credit in Australia Pacific.

While QBE separately identified obvious COVID-19 impacts, there could be other less significant impacts, both positive and negative, that were not readily identifiable or quantifiable.

Further commentary in relation to COVID-19 is included in Note 1.2.3 on page 88 of this Annual Report.

Unless otherwise stated, the Group and business commentary following excludes the impact of COVID-19 and the 2021 CTP reinsurance transaction.

Segment underwriting performance

Combined operating ratio

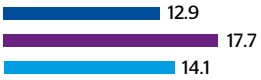
95.0%

Net claims ratio

66.5%

Net commission ratio

15.2%



Expense ratio

13.3%

- North America
- International
- Australia Pacific

North America

North America reported a combined operating ratio of 102.9%, down from 112.7% in 2020.

Excluding further disappointing adverse prior accident year claims development, the current accident year combined ratio improved to 99.2% from 103.7% in 2020.

Significantly higher catastrophe costs, which included Winter Storm Uri and Hurricane Ida, were more than offset by an improvement in the ex-cat claims ratio and the combined commission and expense ratio as a result of premium rate increases, cost savings and favourable operating leverage.

Despite drought conditions in parts of the Mid West, Crop recorded a combined operating ratio of 92.7%, down from 98.2% in 2020. Strong premium growth and higher commodity prices contributed to a materially improved expense ratio.

International

International delivered another strong result reporting a combined operating ratio of 90.6%, down from 91.3% in 2020.

Excluding favourable prior accident year claims development, the current accident year combined ratio increased to 91.8% from 89.6% in the prior year.

Materially higher catastrophe costs more than offset further improvement in the combined commission and expense ratio. Both the insurance and reinsurance businesses were impacted by elevated catastrophe claims which included Storm Bernd as well as Winter Storm Uri and Hurricane Ida in the US.

The ex-cat claims ratio increased slightly with the benefit of further premium rate increases on the attritional claims ratio more than offset by strengthened IBNR assumptions, especially with respect to large individual risk claims.

European insurance and Asia recorded improved underwriting results relative to the prior year while QBE Re was impacted by heightened catastrophe costs and adverse prior accident year claims development.

Australia Pacific

Australia Pacific reported a strong combined operating ratio of 91.4%, down from 92.8% in 2020.

Excluding adverse prior accident year claims development, the current accident year combined ratio improved to 88.8% from 93.3% in the prior year.

Although elevated relative to the prior year, catastrophe claims costs reduced as a percentage of net earned premium.

The ex-cat claims ratio and the combined commission and expense ratio improved further, supported by premium rate increases, cost control and favourable operating leverage.

LMI reported a greatly improved combined operating ratio of 35.4%, down from 62.3% in the prior year. The strong residential property market and buoyant employment conditions contributed to the improved underwriting result.

FOR THE YEAR ENDED 31 DECEMBER	GROSS WRITTEN PREMIUM		NET EARNED PREMIUM		COMBINED OPERATING RATIO		INSURANCE PROFIT (LOSS) BEFORE INCOME TAX	
	2021 US$M	2020 US$M	2021 US$M	2020 US$M	2021 %	2020 %	2021 US$M	2020 US$M
North America	**6,289**	4,775	**3,965**	3,351	**102.9**	112.7	**(23)**	(488)
International	**6,958**	5,856	**5,545**	4,812	**90.6**	91.3	**716**	265
Australia Pacific	**5,215**	4,079	**4,265**	3,626	**91.4**	92.8	**446**	252
Corporate & Other	**(9)**	(25)	**4**	(4)	**–**	–	**(66)**	(101)
Group management basis	**18,453**	14,685	**13,779**	11,785	**95.0**	98.6	**1,073**	(72)
Risk-free rate impact	**–**	–	**–**	–	**(2.2)**	3.2	**–**	–
NSW CTP reinsurance	**–**	–	**(365)**	–	**(0.2)**	–	**3**	–
COVID-19 impact	**4**	(42)	**(6)**	(77)	**(1.1)**	5.6	**139**	(655)
Group statutory	**18,457**	14,643	**13,408**	11,708	**91.5**	107.4	**1,215**	(727)

Premium income and pricing

Gross written premium (US$M)

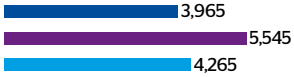
18,453

21% from 2020

Net earned premium (US$M)

13,779

12% from 2020



- North America
- International
- Australia Pacific

Average renewal premium rate increase

Group

+9.7%

North America	+10.7%
International	+10.2%
Australia Pacific	+8.3%

Group

Gross written premium increased 26% to $18,453 million from $14,685 million in the prior year.

On a constant currency basis, gross written premium increased 21% reflecting rate increases, organic growth and improved retention coupled with especially strong growth in Crop.

Excluding Crop, gross written premium growth was 17% on the same basis.

The Group achieved an average renewal premium rate increase of 9.7% compared with 9.8% in 2020.

Excluding premium rate increases and Crop, constant currency growth was 10% for the year, up from 1% in 2020 and 7% during the first half of 2021.

North America

North America reported a 32% increase in gross written premium, underpinned by an average renewal premium rate increase of 10.7% compared with 10.2% in 2020.

Excluding Crop, gross written premium grew 20%, mainly due to premium rate increases and growth in financial lines, programs (property and specialty) and retail (middle market).

Crop premium grew 51% as a result of significantly higher commodity prices coupled with strong organic growth.

Excluding premium rate increases and Crop, growth was 14%.

International

International reported a 15% uplift in gross written premium, underpinned by a 10.2% premium rate increase compared with 12.8% in the prior year.

European insurance (financial lines, property and liability) and QBE Re achieved strong top-line growth of 29% and 26% respectively, while the UK and International markets grew by 15% and 10% respectively. Asia contracted by 2% due to significantly reduced travel insurance business.

Excluding premium rate increases, growth was 6%.

Australia Pacific

Australia Pacific reported a 17% increase in gross written premium reflecting an 8.3% premium rate increase compared with 5.4% in 2020.

Growth in commercial lines, home, motor and LMI was partly offset by moderation in CTP and the impact of the economic slowdown in the Pacific Islands.

Excluding premium rate increases, growth was 11%.

Reinsurance expense

Reinsurance expense increased 44% to $3,252 million from $2,264 million in the prior year.

Much of the increase reflects growth in more heavily reinsured portfolios including Crop, North America financial lines (where growth is being supported by a 50% quota share) and LMI (where the current accident year quota share was increased to 50%) as well as additional (largely government) reinsurance on trade credit & surety.

Average renewal premium rate increases

FOR THE YEAR ENDED 31 DECEMBER	2021 %	2020 %	2019 %	2018 %
North America	**10.7**	10.2	5.7	3.8
International	**10.2**	12.8	6.0	4.1
Australia Pacific	**8.3**	5.4	7.3	7.2
Group	**9.7**	9.8	6.3	5.0

Foreign exchange rates

FOR THE YEAR ENDED 31 DECEMBER		2021		2020	
		PROFIT OR LOSS	BALANCE SHEET	PROFIT OR LOSS	BALANCE SHEET
Australian dollar	A$	**0.751**	**0.727**	0.688	0.771
Sterling	£	**1.375**	**1.353**	1.283	1.368
Euro	€	**1.182**	**1.138**	1.140	1.222

Underwriting expenses, commission and tax

Expense ratio

13.3%

2020 14.6%

Net commission ratio

15.2%

2020 16.1%

Tax rate

17.1%

2020 (2.6)%

Underwriting and other expenses

The Group's expense ratio improved to 13.3% from 14.6% in the prior year, reflecting disciplined cost management (albeit assisted by modest non-recurring savings) coupled with operating leverage as a result of strong premium growth.

North America reported significant improvement due to cost savings and operating leverage driven by strong premium growth, especially in Crop.

International and Australia Pacific also enjoyed a modest reduction in their expense ratios as a result of cost control coupled with positive operating leverage.

Net commission

The net commission ratio reduced to 15.2% from 16.1% in 2020, primarily due to business mix.

Growth in Crop, where commissions are reimbursed by the US Government, and in classes protected by quota share such as financial lines and LMI, beneficially impacted net commission expense in North America and Australia Pacific.

International's commission ratio improved due to profit commissions coupled with additional reinsurance on trade credit.

Income tax expense

QBE's effective statutory tax rate was 17.1% compared with a negative 2.6% in the prior year and reflects the mix of corporate tax rates in the countries where we operate, with profits in the North American tax group offset by previously unrecognised tax losses.

The prior year tax rate was impacted by the non-deductible impairment of goodwill and corresponding write-off of deferred tax assets.

During the year, QBE paid $88 million in corporate income tax globally, net of a $3 million refund in Australia which reduced our dividend franking account, the balance of which stood at A$54 million as at 31 December 2021. The franking account balance will enable the Group to fully frank A$126 million of dividends.

Having regard to QBE's franked AT1 distribution commitments, the dividend franking percentage is expected to remain around 10% for the foreseeable future.

Operational efficiency

Underwriting and other expenses (US$M)

1,831

Stable on 2020[1]

Expense ratio

13.3%

1 Constant currency basis.

We have made good progress on the next phase of our efficiency journey targeting an expense ratio of 13% by 2023.

We are making steady progress on the rationalisation and modernisation of our IT estate, with our exposure to end-of-life technology reducing in line with plan through a structured program of systems upgrades and decommissioning work underway in each of our divisions.

Automation of testing and infrastructure operations is ongoing and delivering gradual improvement in quality and efficiency. As an example, 50 simple infrastructure automations delivered to date are estimated to save in excess of 3,750 person days per annum.

We are nearing completion of the transition from our Sydney data centre to a co-located facility and, as part of this process, have commenced active migration of existing legacy applications to cloud based infrastructure.

The Group transitioned to a new contract relationship with our main IT service provider earlier in the year which is already delivering material benefits, including reduced development and operational service costs as well as increased contract flexibility and protection.

Our digital capability continues to improve with digitisation and automation of claims processes and innovation driving improved customer and partner experience, particularly in Australia, Asia and North America.

During the year we consolidated our real estate footprint in Australia and North America in line with new working practices. We also achieved a meaningful reduction in third party consulting costs and simplified divisional organisational structures, particularly in North America.

These measures are supporting reinvestment into key areas of strategic growth and helping to unlock greater operating leverage in our business as well as improving the expense ratio.

The expected cost of the restructure is approximately $150 million over three years, including a $72 million charge recognised in the current year that was not reported as part of the Group's underwriting expenses.

Claims

Ex-cat claims ratio

57.4%

Catastrophe claims ratio

6.6%

- North America
- International
- Australia Pacific

Incurred claims

Excluding the impact of changes in risk-free rates used to discount net outstanding claims, the net claims ratio improved to 66.5% from 67.9% in the prior year.

This was primarily driven by improvement in the ex-cat claims ratio and a reduced level of adverse prior accident year claims development, which were partly offset by an increase in the net cost of catastrophe claims.

The major components of the Group's net claims ratio are discussed hereafter.

Ex-cat claims

The ex-cat claims ratio improved to 57.4% from 58.8% in the prior year, primarily due to premium rate increases in excess of claims inflation and reduced claims settlement costs, albeit partly offset by a strengthened current accident year IBNR allowance.

The ex-cat claims ratio in North America improved to 66.7% from 69.3% in the prior year (57.1% from 60.2% excluding Crop) reflecting premium rate increases in excess of claims inflation and reduced severity of claims experience in aviation.

Despite the strong premium rate environment, International's ex-cat claims ratio increased marginally to 53.1% from 52.8%, with the benefit of premium rates in excess of claims inflation more than offset by stronger IBNR assumptions in long-tail classes.

Australia Pacific's ex-cat claims ratio improved to 54.2% from 56.6% in the prior year, reflecting the benefit of premium rate increases in excess of claims inflation coupled with continued refinements to risk selection and claims management initiatives.

Weighted average risk-free rates

CURRENCY		31 DECEMBER 2021	30 JUNE 2021	31 DECEMBER 2020	31 DECEMBER 2019	31 DECEMBER 2018
Australian dollar	%	**1.12**	**0.68**	0.41	1.11	2.06
US dollar	%	**1.44**	**1.35**	0.82	1.95	2.74
Sterling	%	**0.86**	**0.72**	0.07	0.80	1.08
Euro	%	**(0.33)**	**(0.30)**	(0.59)	(0.08)	0.23
Group weighted	%	**0.87**	**0.73**	0.30	1.05	1.66
Estimated risk- free rate benefit (charge)	US$M	**301**	**205**[1]	(381)	(231)	13

1 Estimated risk-free rate benefit for the six months to 30 June 2021.

Catastrophe claims

The net cost of catastrophe claims increased to $905 million or 6.6% of net earned premium compared with an allowance of 5.7% and a net cost of 5.8% in 2020.

Catastrophe costs included Winter Storm Uri, Hurricane Ida, Storm Bernd, Cyclone Seroja and widespread flooding and storm losses in Australia.

The world experienced another costly year of natural catastrophes in 2021 and, most notably, the US experienced its third most costly year on record. At $36 billion, Hurricane Ida resulted in one of the largest individual losses ever recorded.

Catastrophe experience can be intensified by the effects of climate change. In that context, we continue to analyse hazard and claims trends while reviewing our exposure to properly balance the risk we face against the need to achieve an appropriate return on the capital required to support that risk. As a consequence, we are currently reducing our exposure to North American hurricane risk.

Weighted average risk-free rates

As tabled on the preceding page, the currency weighted average risk-free rate used to discount net outstanding claims liabilities increased to 0.87% at 31 December 2021 from 0.30% at 31 December 2020.

Risk-free rates increased materially across all currencies resulting in a $301 million underwriting benefit that decreased the net claims ratio by 2.2% compared with a $381 million charge in the prior year that increased the net claims ratio by 3.2%.

The $301 million beneficial risk-free rate impact on the underwriting result was largely offset by a $260 million adverse mark-to-market impact on investment income.

Net catastrophe claims (US$M)

905

6.6% of NEP

2020 688

Prior accident year claims development

Prior accident year claims development was $192[1,2] million adverse or 1.4% of net earned premium, compared with $366[2] million or 3.1% adverse in the prior year.

North America reported $148[2] million of adverse development reflecting significant strengthening in legacy excess & surplus (E&S) lines and discontinued programs. Across reserves for ongoing business, we experienced a modest overall release with increases in financial lines and property programs more than offset by favourable development in commercial retail, workers' compensation and A&H.

International reported $66[1] million of favourable development, primarily due to better than expected development in QBE Re casualty, property, UK motor, European liability and Asia which more than offset further strengthening in financial lines and QBE Re North America.

Australia Pacific reported $111 million of adverse development, reflecting significant strengthening in commercial liability as well as workers' compensation and New Zealand, partly offset by releases in CTP, LMI and credit & surety.

Prior accident year claims development (US$M)

(192)[1,2]

1 Excludes $55 million of adverse prior accident year claims development in International which is more than offset by related premium adjustments also recognised in the period.

2 Excludes $1 million (2020 $20 million) of positive prior accident year claims development pertaining to North America Crop insurance that is matched by additional premium cessions under the MPCI scheme.

Balance sheet and capital management

PCA multiple

1.75x[1]

2020 1.72x

Target PCA multiple

1.6–1.8x

Debt to total capital

24.1%[1]

2020 25.8%

Target debt to total capital

15–30%

Capital management

In March 2021, QBE redeemed $200 million of subordinated Tier 2 notes. These notes were subject to APRA's transitional arrangements and, as of 31 December 2020, only $37 million was regulatory capital qualifying. As such, the redemption had minimal impact on regulatory capital at 31 December 2021.

In September 2021, QBE undertook a GBP400 million capital qualifying Tier 2 subordinated debt issuance to prefund the intended redemption of GBP327 million of subordinated debt.

Debt to total capital was 26.9% at 31 December 2021. Allowing for the subordinated debt which is intended to be redeemed, pro forma debt to total capital improved to 24.1% from 25.8% at 31 December 2020.

QBE has $900 million of perpetual fixed rate resetting capital notes that are AT1 qualifying under APRA's capital adequacy framework. The notes are classified as equity, pay franked after tax distributions and do not impact the weighted average number of shares for earnings per share calculations (since the notes are written off in whole or in part if APRA determines QBE is, or would become, non-viable).

The after-tax distribution on QBE's AT1 capital was $50 million, while the reclassification of the 2017 notes (in July 2020) contributed to an $11 million reduction in financing and other costs during the year.

Prescribed capital amount

QBE's indicative PCA multiple increased to 1.81x at 31 December 2021 from 1.72x at 31 December 2020, reflecting:

- the $803 million full year cash profit;
- the GBP400 million subordinated Tier 2 note issue in September 2021; and
- an increase in the premium liabilities surplus due to significant premium rate increases.

These beneficial impacts were largely offset by:

- the March 2021 redemption of $200 million of subordinated notes which reduced Tier 2 capital by $37 million;
- an increase in the insurance liabilities risk charge, primarily driven by strong premium growth; and
- a higher asset risk charge reflecting the increase in reinsurance recoveries receivable, premium receivable and deferred reinsurance expense.

Allowing for the intended redemption of GBP327 million of subordinated debt, the Group's indicative pro forma PCA multiple was 1.75x, at the higher end of our 1.6–1.8x target range.

Capitalisation and capital metrics

AS AT 31 DECEMBER			2021		2020
		BENCHMARK	STATUTORY	PRO FORMA[1]	STATUTORY
Net assets	US$M		**8,882**	**8,882**	8,492
Less: intangible assets	US$M		**(2,449)**	**(2,449)**	(2,534)
Net tangible assets	US$M		**6,433**	**6,433**	5,958
Add: borrowings	US$M		**3,268**	**2,826**	2,955
Total tangible capitalisation	US$M		**9,701**	**9,259**	8,913
Debt to total capital	%	15–30	**26.9**	**24.1**	25.8
Debt to equity	%		**36.8**	**31.8**	34.8
Debt to tangible equity	%		**50.8**	**43.9**	49.6
Premium solvency[2]	%		**46.7**	**46.7**	50.6
QBE's regulatory capital base	US$M		**10,387**	**9,945**	9,348
APRA's PCA	US$M		**5,725**	**5,692**	5,434
PCA multiple		1.6–1.8x	**1.81x**	**1.75x**	1.72x

1 Pro forma adjusting for GBP327 million pre-funded debt repayment intended to be repaid.

2 The ratio of net tangible assets to net earned premium.

Net outstanding claims

At 31 December 2021, the risk margin was $1,418 million or 8.8% of the net discounted central estimate of outstanding claims compared with $1,537 million and 9.7% at 31 December 2020.

Excluding foreign exchange and the CTP reinsurance transaction, the risk margin decreased $45 million in 2021 compared with a $344 million increase in 2020.

The probability of adequacy (PoA) of net outstanding claims reduced to 91.7% from 92.5% at 31 December 2020 but remains comfortably above the midpoint of the Group's 87.5%–92.5% target range.

The reduction in risk margin as a percentage of the net discounted central estimate primarily reflects a $140 million risk margin release due to reduced COVID-19 related uncertainty, particularly with respect to business interruption, trade credit and LMI, which more than offset significant margin strain associated with strong new business growth.

Excluding foreign exchange, the risk margin increased $95 million on a management basis compared with $44 million in the prior year, reflecting especially strong new business growth.

Borrowings

At 31 December 2021, total borrowings were $3,268 million, up $313 million from $2,955 million at 31 December 2020.

The increase in borrowings reflects the GBP400 million subordinated note issue in September 2021, which more than offset the $200 million subordinated note redemption in March 2021.

Excluding the pre-funding of the intended redemption of GBP327 million of subordinated debt, pro forma borrowings are $2,826 million.

Gross interest expense on borrowings for the year was $177 million, down from $185 million in the prior year. The average annualised cash cost of borrowings at 31 December 2021 was 5.4%, down from 6.1% as at 31 December 2020, and will reduce to around 5.3% after the intended redemption of GBP327 million of subordinated debt.

At 31 December 2021, all but $6 million of the Group's borrowings continued to count towards regulatory capital.

Total borrowings[1] (US$M)

Less than one year	442
One to five years	2,288
More than five years	538

Borrowings profile

Senior debt[2]	-
Subordinated debt	100%

1 Based on first call date.
2 Senior debt at 31 December 2021 is $6 million.

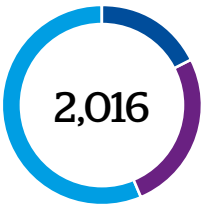
AS AT 31 DECEMBER		2021	2020
Net discounted central estimate	US$M	**16,107**	15,797
Risk margin	US$M	**1,418**	1,537
Net outstanding claims	US$M	**17,525**	17,334
Probability of adequacy	%	**91.7**	92.5
Risk margin to central estimate	%	**8.8**	9.7

Identifiable intangibles and goodwill

The carrying value of identifiable intangibles and goodwill at 31 December 2021 was $2,449 million, down from $2,534 million at 31 December 2020.

During the year, the carrying value of intangibles reduced by $85 million due to amortisation and impairment expense of $71 million and a $104 million foreign exchange impact which more than offset net additions in the period, being mainly the capitalisation of software in relation to various information technology projects.

Goodwill (US$M)



North America	358
International	524
Australia Pacific	1,134

Investment performance and strategy

Total investment income (US$M)

122

104 from 2020

Total investment return

0.4%

2020 0.9%

Fixed income Vs **Growth assets**

(0.4)% **13.5%**

2020 1.9% 2020 (4.8%)

The Group's investment portfolio remains conservatively positioned with around 94% invested in high quality fixed income securities and the remaining 6% invested in growth assets, primarily unlisted property and infrastructure assets.

Our corporate credit portfolio performed in line with general spread movements throughout the year and contributed incremental yield as expected.

The portfolio proved highly resilient from a credit event perspective with minimal exposure to ratings downgrades and certainly well below the level of ratings downgrades seen across the fixed income market more broadly.

Our decision to adopt a duration position modestly short of that required to match the Group's insurance liabilities added value as bond yields rose, benefitting pre tax profit by $41 million.

Unlisted property, infrastructure and private equity enjoyed strong returns of 13.6%, 10.8% and 15.9% respectively, with most of the private equity portfolio (excluding $50 million held for sale at year end) sold immediately prior to year-end.

The total investment return for the year was 0.4% compared with 0.9% in the prior year reflecting the increase in risk-free rates during the year. After adjusting for the risk-free rate impact on fixed income securities, the total investment return was 1.3% compared with a negative return of 0.9% in the prior year.

Closing total cash and investments was $28,967 million, up from $27,735 million at 31 December 2020. Strong operating cash flow coupled with the net increase in subordinated debt were partly offset by a $764 million foreign exchange impact.

We intend gradually introducing a modest amount of additional risk to the portfolio during 2022.

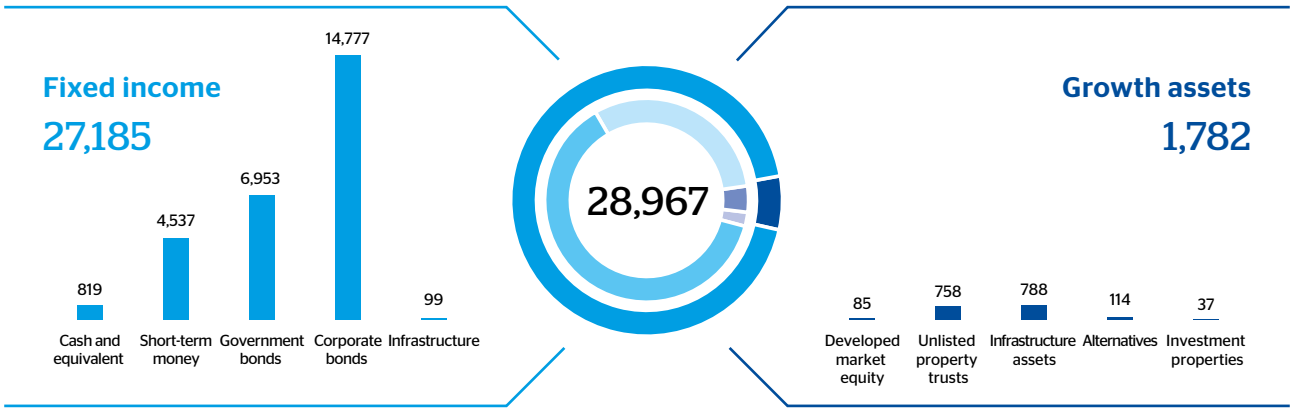
Interest bearing financial assets – S&P security grading

AS AT 31 DECEMBER	2021 %	2020 %
Rating		
AAA	**16**	12
AA	**37**	38
A	**37**	36
<A	**10**	14

Currency mix of investments

AS AT 31 DECEMBER	2021 %	2020 %
US dollar	**31**	33
Australian dollar	**27**	27
Sterling	**19**	17
Euro	**13**	14
Other	**10**	9

Total cash and investments (US$M)



	POLICY-HOLDERS' FUNDS	SHARE-HOLDERS' FUNDS
Cash and cash equivalents	547	272
Short-term money	3,030	1,507
Government bonds	4,643	2,310
Corporate bonds	9,868	4,909
Infrastructure debt	66	33

Fixed income
- Policyholders' funds
- Shareholders' funds

Growth assets
- Policyholders' funds
- Shareholders' funds

	POLICY-HOLDERS' FUNDS	SHARE-HOLDERS' FUNDS
Developed market equity	57	28
Unlisted property trusts	506	252
Infrastructure assets	526	262
Alternatives	76	38
Investment properties	25	12

Closing remarks

Continued favourable market conditions and strong business momentum underpin our confidence in the outlook; however, we remain cautious around economic uncertainty and the potential trajectory of inflation. The prospect of rising interest rates holds positive implications for earnings longer term.

Outlook focus

Maximise market opportunity

Drive targeted growth and margin improvement

Reduce volatility

Enhance portfolio balance to reduce volatility and increase risk-adjusted returns

Build further capital strength

To support our growth ambitions

Sustainability

Make a positive contribution to the economies and communities in which we operate

We are encouraged by the strong turnaround in profitability and organic growth momentum achieved in 2021, and are focused on building on this momentum in 2022 by capitalising on continued favourable market conditions to drive targeted growth and a further improvement in underwriting performance.

Achieving an appropriate risk-adjusted return on capital in North America remains our highest priority. We have several initiatives underway to further optimise and grow the portfolio in order to build a better balanced, less volatile and higher quality earnings base in the region.

We continue to focus on risk (including reserve, underwriting, catastrophe, credit and operational) at a more granular level to improve capital allocation by cell and by region, thus facilitating a more accurate assessment of premium rate adequacy and better informing our decisions on where to grow. As return on equity continues to improve, we are increasingly focused on developing the systems and culture to sustain long-term organic growth.

The further, albeit reduced level of, adverse prior accident year claims development was disappointing, particularly in North America. In a reserving context, claims inflation remains a key area of focus and, where appropriate, we have strengthened both current and prior accident year assumptions to allow for elevated inflation levels going forward. Given the uncertain inflationary backdrop, we have also taken a more cautious approach to reserving for large individual risk claims.

Notwithstanding very significant growth, the Group's regulatory capital position strengthened during the year and remains comfortably above the midpoint of our target range. The recently revised dividend policy will better support the Group's growth ambitions, facilitate the gradual re-risking of the investment book and provide flexibility to manage the dynamics of the global insurance cycle more broadly.

During 2022, we intend to gradually optimise investment returns by modestly increasing exposure to risk assets, including reintroducing enhanced fixed income assets. Our target asset allocation is designed to be resilient, enabling stable cross-cycle exposures.

Sustainability is essential to our new purpose and our ability to make a positive and impactful contribution to the environments, economies and communities in which we operate. Progress against our sustainability commitments will enhance our ability to attract and retain customers, talent and capital. Our 2022 Sustainability Scorecard includes clear sustainability goals aligned to the QBE Sustainability Framework and we remain focused on integrating sustainability into our strategy and business planning to meet our climate and broader sustainability commitments.

With premium rate increases in excess of claims inflation, coupled with ongoing expense discipline and operating leverage, we remain confident of achieving a stronger, more consistent and sustainable level of financial performance over the medium term.

Inder Singh
Group Chief Financial Officer