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17 August 2016

The Manager  
Market Announcements Office  
ASX Limited  
Level 4  
Exchange Centre  
20 Bridge Street  
SYDNEY NSW 2000

Dear Sir/Madam,

**Report on results and financial statements for the half year ended 30 June 2016**

The Directors of QBE Insurance Group Limited announce the financial results for the half year ended 30 June 2016.

The following documents are attached:

1. Appendix 4D – half year report; and
2. QBE's half year report including financial statements for the half year ended 30 June 2016.

Yours faithfully

A handwritten signature in black ink, appearing to read "Carolyn Scobie", written in a cursive style.

Carolyn Scobie  
**Company Secretary**

Attachments



## QBE Insurance Group Limited

### Appendix 4D – Half year report for the period to 30 June 2016

#### Results for announcement to the market

	UP / DOWN	% CHANGE	2016 US\$M	2015 US\$M
Revenue from ordinary activities	down	1%	<b>7,890</b>	7,928
Profit from ordinary activities after income tax attributable to equity holders of the company	down	46%	<b>265</b>	488
Net profit for the period attributable to ordinary equity holders of the company	down	46%	<b>265</b>	488

Net profit after tax for the period to 30 June 2016 was \$265 million, down from a profit of \$488 million for the same period last year.

The Group's underwriting result was a profit of \$54 million compared with a profit of \$295 million last year, reflecting a combined operating ratio of 99.0% compared with 95.3%. Net claims expense was impacted by a material reduction in risk-free rates used to discount claims liabilities (\$283 million or 5.0% of net earned premium). The combined commission and expense ratio was down compared with the same period last year (34.3% compared with 35.4%) primarily due to the benefit of expense initiatives and the disposal of our high cost base M&LS business.

Excluding the impact of lower risk-free rates, the statutory combined operating ratio would have been 94.0%, at the lower end of our target range of 94%-95% advised to the market in February 2016.

The comparative result benefited from gains of \$150 million mainly relating to the disposal of our US and Australian agency businesses.

DIVIDENDS	AMOUNT PER SECURITY (AUSTRALIAN CENTS)	FRANKED AMOUNT PER SECURITY (AUSTRALIAN CENTS)
Interim dividend	<b>21</b>	<b>10.5</b>

The Dividend Reinvestment Plan will be satisfied by the acquisition of shares on-market with no discount applicable. The Bonus Share Plan will be satisfied by the issue of new shares with no discount applicable. The unfranked part of the dividend is declared to be conduit foreign income.

The share issue price for the Dividend Reinvestment Plan and the Bonus Share Plan will be based on a volume weighted average in the 10 trading days between Tuesday 30 August 2016 and Monday 12 September 2016 (both dates inclusive).

The record date for determining shareholder entitlements to the dividend is 26 August 2016.

The last date for receipt of election notices applicable to the Bonus Share Plan and the Dividend Reinvestment Plan will be 29 August 2016.

The interim dividend will be paid on 28 September 2016.

#### Additional disclosures

Additional Appendix 4D disclosure requirements can be found in the QBE Insurance Group Limited half year report for the period to 30 June 2016 (Attachment A).

The half year report should be read in conjunction with any market or public announcements made by QBE Insurance Group Limited during the period in accordance with the continuous disclosure requirements of the *Corporations Act 2001* and the ASX Listing Rules.

The independent auditor's review report is included at page 63 of the half year report.

#### Other information

During the period, QBE Insurance Group Limited held an interest in Pacific Re Limited (30.97%) and Raheja QBE General Insurance Company (49%). The Group's aggregate share of profits of these entities is not material.





QBE Insurance Group Limited

# 2016 Half Year Report

QBE is proud of our rich history supporting rural and regional customers, agents and producers, from crop insurance in North America to farm insurance in Australia. Our strong partnerships, deep expertise and flexible coverage give customers the confidence to get on with the job and achieve their ambitions, knowing their livelihood and assets are well protected.

Made possible





**QBE has deep industry expertise in Agribusiness, supporting communities across Australia and the United States.**

In Australia, our local Elders insurance agents work with customers to provide tailored, specific insurance solutions – home & contents, farm property, liability and farm vehicles.

In the US, we partner with farmers, their agents, grain marketers and suppliers to better understand their core business. Our local experts provide local understanding of farming challenges and our reputation for outstanding customer service is reflected in coverage of more than 50 million crop acres across 46 states.

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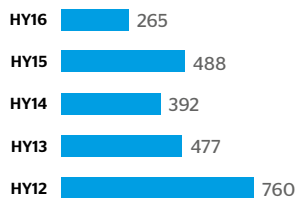
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# 2016 half year snapshot<sup>1</sup>

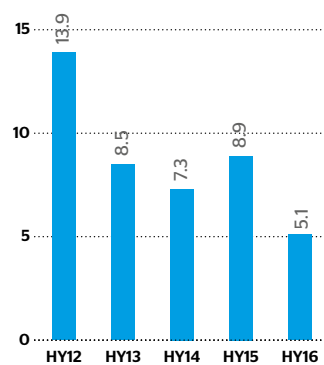
## Performance

### Net profit after income tax (US\$M)

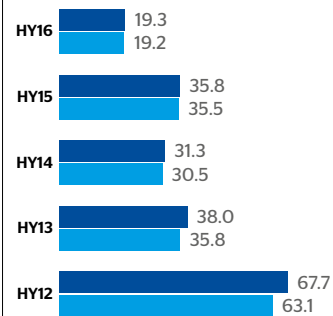


↓ 46%

### Return on average shareholders' funds (%)



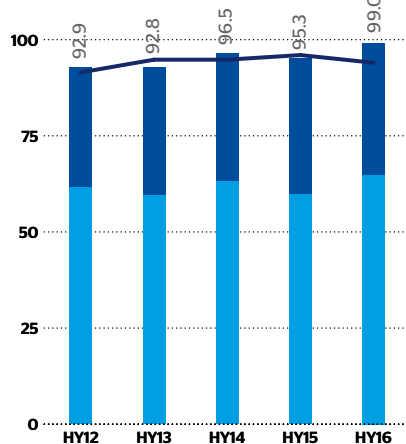
### Earnings per share (EPS) (US¢)



● Basic EPS  
● Diluted EPS

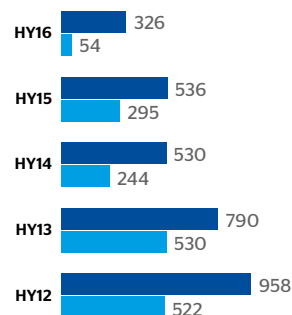
↓ 46%  
↓ 46%

### Combined operating ratio (COR) (%)



● Combined commission and expense ratio  
● Net claims ratio  
— COR excluding discount rate adjustment

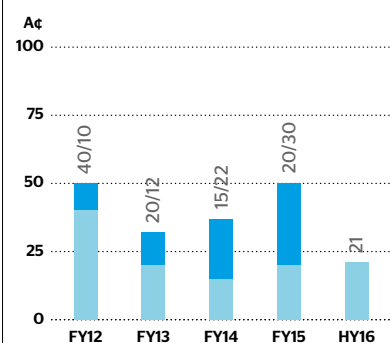
### Insurance profit and underwriting result (US\$M)



● Insurance profit  
● Underwriting result

↓ 39%  
↓ 82%

### Dividend per share (A¢)



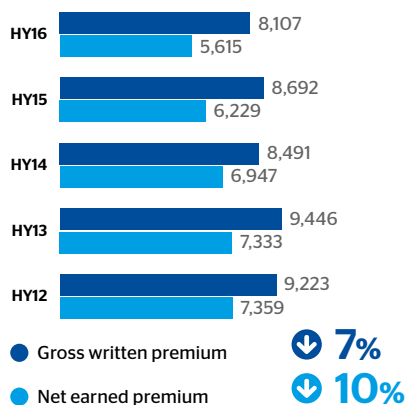
↑ 5% on 1H 2015

● Dividend per share (A¢) final  
● Dividend per share (A¢) interim

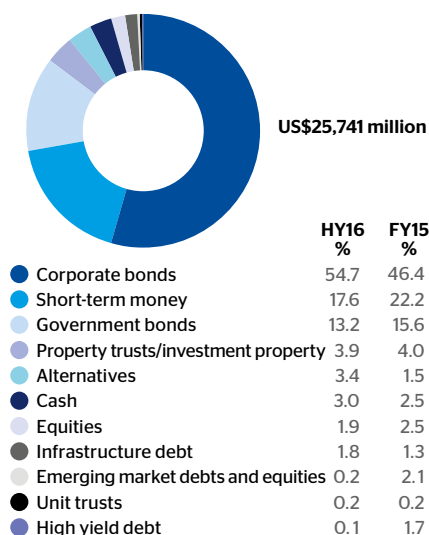
<sup>1</sup> The information in the tables above is extracted or derived from the Group's audited financial statements. The Group Chief Financial Officer's report sets out further analysis of the results to assist in comparison of the Group's performance against targets provided to the market in February 2016.

## Profile

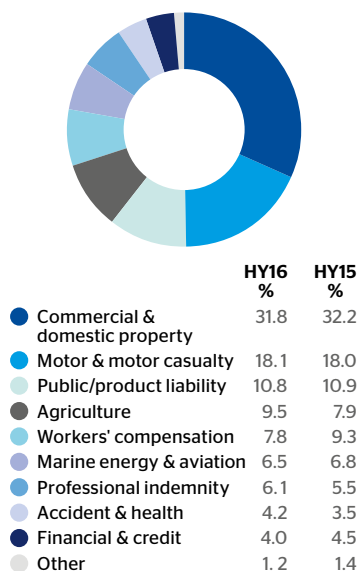
### Gross written premium and net earned premium (US\$M)



### Investments and cash at 30 June 2016



### Gross earned premium by class of business

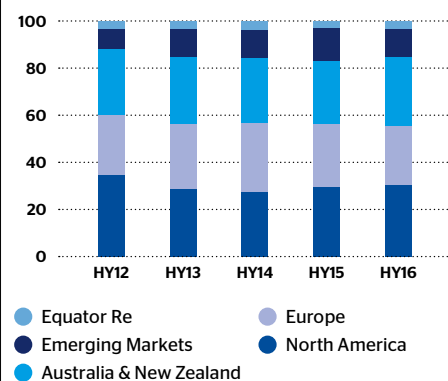


### Net earned premium by type

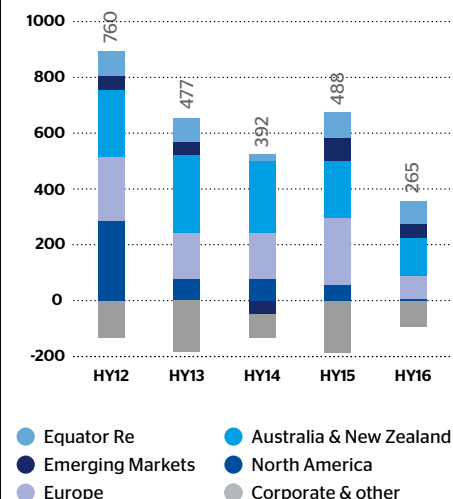
**94%**  
direct and facultative insurance

**6%**  
inward reinsurance

### Divisional analysis of net earned premium (%)



### Net profit after tax by division (US\$M)





# First half 2016 in review

In an environment where both insurance pricing and investment markets are increasingly challenging, QBE's strong and differentiated global franchise has delivered a half year result that puts us on track to deliver on our 2016 financial targets, albeit with a greater contribution from positive prior accident year claims development than originally envisaged. Cash generation remains strong and our balance sheet and expected retained earnings growth is more than capable of supporting our 3% per annum across the cycle premium growth target.

## General overview

Across all industries, tough operating conditions call for a clearly defined market position and strategy.

This is most evident in the insurance industry today, where we face headwinds caused by low interest rates and reduced insurance pricing. We started 2016 expecting premium rates to fall marginally and our experience to date suggests this assessment is valid. Meanwhile, global risk-free rates continue to trend lower – to the point that around 77% of global sovereign bond yields are now below 1% while around 40% are negative.

These conditions challenge the returns of all insurance companies and our business is not immune. As I discuss later in this report, this is particularly evident in our Australian & New Zealand Operations where cumulative pricing declines concurrent with heightened claims inflation have detracted from performance in several of our short tail classes, exacerbated by the well-publicised deterioration in the NSW compulsory third party (CTP) scheme.

Despite these challenges, we are well placed to continue to meet our underwriting targets in the short and medium term. I can say this because QBE's business has strong foundations, including our diversification by product line and geography, supported by decisive action to introduce price increases and remediate emerging issues in Australian & New Zealand Operations. These attributes and actions are coupled with a strategy and underwriting focus that is custom-made for the current operating environment.

## QBE's strategy

QBE's strategy builds upon our differentiated position as one of only around fifteen insurers that operate on a truly global basis.

This market position has not come about by accident. We have worked hard to ensure our business partners and customers have a clear understanding of who we are and what we stand for, while recent years have seen us focus on globalising QBE's operating model and improving everything we do. This activity has reached the point where QBE now does things faster, better and cheaper than ever before. We have also been through a detailed process of working out what is core to our business. What do we think we can excel at? Where should we concentrate our efforts and where should we grow? This means that the business we are in today is the business that we want to be in.

While we have been refining our operating model, we have been building out the capabilities that our customers value most highly. With more than 80% of our business being commercial and specialty insurance, we wouldn't survive without a deep understanding of the industries we partner with, coupled with a full suite of services for our customers. This extends from a high quality claims proposition to our ability to support clients in their risk management needs as well as underwriting and risk assessment.

Building on this clear market position, at an Investor Update held in our Sydney Head Office in May 2016, our leadership team introduced six themes that together form the core of our strategy:

- **Underwriting excellence** – QBE has always had strong underwriting DNA and, alongside the development of a truly global business, we have worked to institutionalise a consistent approach to underwriting across our operations. All of the initiatives undertaken since 2013 to remediate, transform and improve the quality of our business have contributed to a substantial reduction in the proportion of our business generating underwriting losses. While we still have work to do, this represents meaningful progress at a time when prices have been reducing. To ensure we continue to improve underwriting capability and discipline, we are investing in the way we manage the underwriting process, including the establishment of a Group Underwriting Committee, and have institutionalised the constant review of our underwriting standards.
- **Customer and partner-led growth** – In the current pricing environment it is critical that we are selective in the growth opportunities we pursue. Improving customer retention is a low-risk and high value-add opportunity. In 2015, we introduced strategies to improve our retention by 1% per annum, effectively increasing growth through retaining more of the business that we write, thereby enabling us to be even more selective in pursuing new business. Increased use of analytics is key to this objective as we analyse customer buying habits and the way in which we connect with them, while also more effectively capturing cross selling opportunities. Our Emerging Markets division is also a focal point for growth and the high growth economies served by this division will experience rising demand for insurance for many years to come.
- **World class talent** – Our commitment to building, developing and retaining the very best talent is already a real differentiator for QBE and will underpin our long-term success. In 2012, we set up our own Leadership Academy in partnership with Duke University. Over 2,150 of our leaders have now been through Academy programs and in May 2016 we launched the first pilot program for our Underwriting Academy. Our goal is for every QBE underwriter to be accredited by the relevant local insurance body.
- **Operational efficiency** – We are on track to achieve our previously announced 2016 expense savings of \$150 million (equating to a 1% improvement in the expense ratio), and planning for further savings in 2017 is well advanced. Our divisions have all committed to greater leverage of our global shared services centre (GSSC) in the Philippines, with a series of transitions planned for the next 18 months. The increase in scope of the GSSC, which already employs in excess of 3,000 people, will enable us to re-engineer end-to-end processes through a combination of software robotics, automation and general scale advantages which will also result in further expense savings.
- **Claims excellence** – For the first time, we have appointed a Global Head of Claims as part of a move to unify claims operations across the regions and leverage global best-practice capabilities. Our goal is to create more consistency and sharing of global standards to create efficiencies and build improved customer service. These initiatives are already delivering bottom line benefits and provide confidence in our ability to deliver targeted run-rate claims cost savings of \$200 million per annum by 2018. In particular, we have seconded some of our key European claims management talent to North America and Australia to share expertise and develop sustained excellence.
- **Data and analytics** – In recent years we have built data and analytics teams across a range of initiatives; however, we are now taking a more co-ordinated approach, establishing data and analytics as a global function, with a mandate to drive measurable performance inputs and create a culture of data driven decision making in every aspect of our business. Momentum is building, with more than 70 active projects in development or deployment. Many of these projects directly support other strategic themes, with an emphasis on customer insight and retention, underwriting and distribution as well as claims. Our global analytics team is already over 130 and we are strengthening efforts to create analytical insights that are consistent and reusable across our business.

As well as introducing these strategic themes at the May 2016 Investor Update, we clearly articulated what we expect successful strategy execution will deliver for shareholders over the next three years including:

- **Strengthened franchise** – Further improvement in QBE's market position and relationships with distribution partners and end customers, reflected in our 3% per annum across the cycle premium growth target;
- **Improved performance** – Continued improvement in our business performance, with QBE's combined operating ratio improving to around 93%;
- **Growing dividends** – Significant free cash flow generation, coupled with a payout ratio of up to 65% of full year cash profit, provides the potential for strong dividend growth; and
- **Well capitalised** – We are committed to maintaining a Standard & Poor's insurer financial strength rating of 'A+' or better which, together with continued focus on effective reinsurance protections, will maintain QBE's resilience to downside scenarios.

Of course, there has been one notable macro development subsequent to the Investor Update in the form of the United Kingdom referendum on Brexit. While the timing and mechanics for Britain's proposed exit from the European Union have not been finalised, we are hopeful the market's immediate response to the referendum outcome will be seen, with the benefit of hindsight, to have been an over-reaction.

From an operational perspective, we anticipate a modest incremental administrative cost if QBE is required to reorganise its continental European businesses to renew European Union business. There may also be a small capital impost associated with the new licensed entities.

More significant is the impact of Brexit on global confidence and therefore on global economic growth prospects and investment returns. We have already seen bond yields fall significantly in the aftermath of the referendum outcome, contributing to an adverse discount rate adjustment of \$283 million to QBE's pre-tax profit for the half year as risk-free rates used to discount net outstanding claims decreased.

Although it is too early to speculate on the longer term impact of Brexit on the prospects of our business, it is conceivable that we will see a further substantial downward step in global interest rates, which would correspondingly reduce investment returns generated by insurance companies. However, if these lower investment returns provide a catalyst for the global insurance pricing cycle to turn, or at least stabilise, this may be a net positive for QBE.

We will publicly update our medium-term targets in conjunction with the release of our 2016 final result in February 2017.

## 2016 half year result

Our 2016 interim profit was \$265 million, down 46% from \$488 million in the same period last year, reflecting the aforementioned adverse discount rate adjustment of \$283 million compared with a benefit of \$45 million in the prior period. The combined ratio increased to 99.0% from 95.3% in the prior period, again due to the decline in risk-free rates.

Excluding the impact of discount rate movements, the interim result was underpinned by a combined operating ratio of 94.0%, in line with our FY16 guidance of 94%–95%, albeit with a greater contribution from positive prior accident year claims development than originally envisaged.

It is pleasing to see that our Northern Hemisphere divisions are delivering on our plans. Richard Pryce and the team in Europe have delivered a sparkling result in challenging market conditions, recording a combined operating ratio of 88.3%, adjusted for the aforementioned discount rate movements and transactions to reinsure UK long tail liabilities.

Our North American Operations, which recently welcomed Russ Johnston as Chief Executive Officer, has received a great deal of attention in past years. We remain confident in the trajectory of this business and expect the underlying full year 2016 combined operating ratio will represent a further stepped improvement over the much-improved performance achieved by Dave Duclos and the team in 2015.

Our Emerging Markets division has a strong footprint in 22 markets, many of which we have been operating in for decades. The division is growing sensibly and continues to generate underwriting profits.

Turning to Australian & New Zealand Operations, the sound headline result reflects continued strong returns in long tail portfolios and our lenders' mortgage insurance (LMI) business. However, the result included an unacceptable deterioration in the attritional claims ratio as a result of increased NSW CTP claims frequency, coupled with premium pricing pressure, higher than normal claims inflation and increased claims frequency in our short tail portfolios. A swift and decisive response is required and will encompass a combination of price increases, tightened terms and conditions and improved risk selection. We anticipate that the actions taken will benefit our attritional claims ratio in 2017.

With immediate effect the Group Chief Financial Officer, Pat Regan, will take responsibility for the Australian & New Zealand business whilst we undertake a search for a permanent Chief Executive Officer for the division. I believe this change of leadership, along with the increased near-term focus on tight management of underwriting performance and cost control, will deliver on the division's potential in the current environment and will set us up for future success.

We have a stated objective of achieving gross written premium growth of 3% per annum across the cycle, and initially anticipated growth of around this level would be achievable in 2016. Ultimately, margin is more important to us than growth and, in a market where the macro conditions are slightly more challenging than we might have expected, particularly in Asia and Europe, our revised target is for nominal growth in 2016 adjusted for foreign exchange movements and the 2015 disposals.

## Interim dividend

Our dividend policy is designed to ensure that we reward shareholders relative to cash profit and maintain sufficient capital for future investment and growth of the business.

The Board has declared an interim 2016 dividend of 21 Australian cents per share, franked at 50%, representing a 5% increase on the 20 Australian cents declared at the same time last year.

The payout for the 2016 interim dividend is A\$288 million or 74% of cash profit, above the Board's revised 65% full year payout policy. In arriving at the interim dividend, the Board gave consideration to the unusual market conditions that gave rise to the lower risk-free rates used to discount net outstanding claims, as well as the Group's overall capital position and profitability.

Cash generation remains strong and our balance sheet and expected retained earnings growth is more than capable of supporting our 3% per annum premium growth target across the cycle.

## Looking forward

We anticipate that global pricing will remain under pressure in 2016, although we expect overall premium rate reductions will be broadly in line with 2015 experience.

We have adjusted our 2016 forecast gross written premium and net earned premium for our current view on foreign exchange rates, market conditions and, in the case of net earned premium only, the \$176 million charge incurred during the first half to reinsure UK long tail liabilities (as discussed in the Chief Financial Officer's report).

This has resulted in a minor reduction in our gross written premium<sup>1,2</sup> target range to \$13.7 billion – \$14.1 billion and our net earned premium<sup>1</sup> target range to \$11.5 billion – \$11.9 billion.

Our targeted combined operating ratio and insurance profit margin<sup>3</sup> remain unchanged at 94%–95% and 8.5%–10% respectively, excluding any impact from risk-free rates used to discount net outstanding claims but including allowance for further positive prior accident year claims development.

John Neal  
**Group Chief Executive Officer**

1 Premium targets are based on assumed average foreign exchange rates relative to the US dollar as follows: AUD 0.72; GBP 1.36; and EUR 1.10.

2 Excludes M&LS gross written premium that is 100% reinsured to National General. Nil impact on net earned premium.

3 Assumes a 2.7% net investment yield.

# Financial and operations overview

QBE's interim result demonstrates the benefit of our earnings diversity which, together with a strong capital base and growing divisional cash remittances, has allowed us to increase the 2016 interim dividend by 5% notwithstanding a very significantly adverse impact from lower risk-free rates used to discount net outstanding claims.

## General overview

As I usually do, I have commented below on three broad areas of focus:

1. Driving financial performance
2. Investment strategy and performance
3. Financial strength and capital management

### 1. Driving financial performance

We aim to run a tightly controlled business that is stable, predictable and profitable.

In this regard, there are several elements of our 2016 interim result that are pleasing. While our statutory combined operating ratio was 99.0%, adjusted for discount rate movements our 94.0% combined operating ratio was well within our 94%–95% target range, albeit with a greater contribution from positive prior accident year claims development than originally envisaged.

That said, the deterioration in Australian & New Zealand Operations' attritional claims ratio is, frankly, very disappointing.

From my perspective, the key themes emerging from the half year result were as follows:

#### (a) Four consecutive halves of positive prior accident year claims development

The Group reported \$218 million of positive prior accident year claims development – our fourth consecutive (and largest) half of positive prior accident year development. European Operations and Australian & New Zealand Operations recorded significant positive development with a small amount of net positive development across the rest of the Group.

In light of recent experience as well as our efforts in driving claims efficiencies through our claims excellence initiatives, I now think it is reasonable to expect ongoing positive prior accident year claims development of 1%–2% of net earned premium, at least in the near future.

#### (b) A further significant reduction in expenses

QBE has made an excellent start towards achieving our targeted \$300 million of expense savings by the end of 2018.

During the first half, we reduced our expense base by \$124 million which contributed to a 1.2% improvement in our expense ratio (allowing for the distorting impact of transactions to reinsure UK long tail liabilities as outlined overleaf).

#### (c) Strong result in Europe with solid progress in North America and Emerging Markets

Despite challenging market conditions, our European business again produced an outstanding result, reporting a combined operating ratio of 88.3% (excluding discount rate movements and the aforementioned reinsurance transactions). Moreover, the division reported \$119 million of positive prior accident year claims development, continuing the long history of releases from this business and highlighting the conservative approach taken to current accident year reserving.



North America's transformation program progressed under the new leadership of Russ Johnston. A much improved expense ratio was partially offset by adverse prior accident year development primarily on our commercial auto book – an industry wide issue.

While there are a number of areas within our Emerging Markets business that remain a work in progress, particularly in Latin America, it was pleasing to see continued growth and a small underwriting profit despite difficult market conditions and adverse catastrophe experience.

#### (d) Australian & New Zealand Operations' performance

Adjusted for discount rate impact, Australian & New Zealand Operations' combined operating ratio of 93.9% was in line with the Group average; however, the deterioration in the attritional claims ratio was disappointing and unacceptable.

Favourable inflation trends led to positive prior accident year claims development of \$83 million in long tail classes, but this was more than offset by a substantial deterioration in the attritional claims ratio, driven by NSW CTP, trade credit and a number of short tail lines, including householders, motor and commercial property.

This deterioration is the result of sustained competitive pricing pressure, coupled with rising repair and replacement costs, tighter economic conditions with respect to trade credit and, of course, the now well publicised increase in NSW CTP claim frequency. We will respond swiftly and firmly to restore short tail margins through price increases, tightened terms and conditions and portfolio amendments, including policy cancellation (trade credit) and non-renewal. Moreover, significant premium rate increases coupled with legislative amendments due to take effect from 1 July 2017 are expected to assist in the restoration of NSW CTP margins while maintaining premium affordability.

## 2. Investment strategy and performance

The first six months of 2016 were certainly eventful from an investment market and geopolitical standpoint.

Despite significant market volatility, we achieved a strong annualised net investment return of 3.3%, assisted by mark to market gains on sovereign and corporate bonds as global risk-free rates reached new lows. Once again, the majority of our asset classes outperformed comparable market benchmarks.

In line with our commitment over time to more closely match the duration of our investment assets with the duration of our claims liabilities, during the half we took advantage of global bond market volatility to add duration. As a consequence, the decline in sovereign yields was a significant contributor to our first half investment return being ahead of expectations.

To mitigate the impact of low bond yields, we further diversified our fixed income portfolio adding exposure in structured credit, infrastructure debt and corporate bond holdings as wider credit spreads at the start of the year provided attractive yield pickup over sovereigns.

Looking ahead, we expect recent market volatility to continue and will maintain our conservative stance enabling us to take advantage of any further market dips to enhance portfolio returns.

Our targeted full year net investment return for 2016 is now 2.7%.

## 3. Financial strength and capital management

### (a) Strong cash remittances from the operating divisions

Cash remittances from the operating divisions remained very strong at \$648 million for the half compared with \$201 million for the prior period and represent 226% of the Group cash profit. Dividend coverage (net of DRP) is very strong at 3.0x.

This is a positive start in achieving our targeted \$3 billion of cumulative cash remittances over the three years to 2018.

#### Group head office cash flows

FOR THE HALF YEAR ENDED	30 JUNE 2016 US\$M	30 JUNE 2015 US\$M
Opening head office cash balance	845	369
Total divisional dividend remittances	648	201
Interest on parent entity borrowings	(45)	(45)
Gross organic cash flow	603	156
Dividends paid (30 June 2015 net of DRP)	(312)	(187)
Net organic cash flow	291	(31)
Other (including asset sales)	(342)	278
Closing head office cash balance	794	616

### (b) A strong capital position

As illustrated at our Investor Update in May 2016, the Group's capital position is extremely strong when measured on both regulatory and, in particular, rating agency capital requirements.

As at 30 June 2016, the Group's capital position was estimated to be around 1.2x S&P's 'A' rated required capital level and is viewed by Standard & Poor's as being "well above the AA level".

## Operating and financial performance

### Summary income statement

FOR THE HALF YEAR ENDED	STATUTORY RESULT		2015 ADJUSTMENTS		ADJUSTED RESULT
	30 JUNE 2016 US\$M	30 JUNE 2015 US\$M	ARGENTINE WORKERS' COMP	HELD FOR SALE & DISPOSALS	30 JUNE 2015 US\$M
Gross written premium	8,107	8,692	135	–	8,557
Gross earned premium revenue	6,876	7,293	145	–	7,148
Net earned premium	5,615	6,229	145	–	6,084
Net claims expense	(3,637)	(3,727)	(165)	–	(3,562)
Net commission	(993)	(1,073)	(7)	–	(1,066)
Underwriting and other expenses	(931)	(1,134)	(24)	(55)	(1,055)
Underwriting result	54	295	(51)	(55)	401
Net investment income on policyholders' funds	272	241	32	–	209
Insurance profit	326	536	(19)	(55)	610
Net investment income on shareholders' funds	165	145	20	(12)	137
Financing and other costs	(125)	(127)	–	–	(127)
Gains on sale of entities	–	150	–	150	–
Amortisation and impairment of intangibles	(19)	(25)	–	–	(25)
Profit before income tax	347	679	1	83	595
Income tax expense	(80)	(189)	(1)	(50)	(138)
Profit after income tax	267	490	–	33	457
Profit attributable to non-controlling interests	(2)	(2)	–	–	(2)
Net profit after income tax	265	488	–	33	455

### Overview of the 2016 interim result

To assist in the explanation of our 2016 interim result and consistent with our basis of reporting in the prior period, the 2015 statutory profit in the table above has been adjusted to exclude the following material items:

- the sale of the Argentine workers' compensation business completed on 10 August 2015;
- the sale of the Australian and North American agency businesses and other non-material disposals during the period which gave rise to realised gains on sale of \$150 million; and
- the M&LS business which was "held for sale" at 30 June 2015, and gave rise to a \$55 million write down of deferred acquisition costs. Whilst the sale completed on 1 October 2015, the business continues to be written as an accommodation by North American Operations and is fully reinsured to the purchaser.

Unless otherwise stated, the commentary following compares the statutory result for the current half with the adjusted result for the prior period, as set out in the table above.

The Group reported a 2016 interim net profit after tax of \$265 million, down 42% from \$455 million in the prior period, reflecting a \$283 million pre-tax charge associated with lower risk-free rates used to discount net outstanding claims compared with a \$45 million benefit in the prior period.

Excluding amortisation of intangibles and other non-cash items, cash profit for the half was \$287 million, down 39% from \$471 million reported in the prior period.

Cash profit return on equity fell to 5.6% from 8.6% in the prior period, again reflecting the substantial discount rate impact.

On a constant currency basis and excluding M&LS premium in both years (HY16 \$215 million, HY15 \$263 million), gross written premium was flat reflecting growth in Emerging Markets and Australia & New Zealand, partially offset by a slight contraction in Europe and North America coupled with the ongoing competitive global premium pricing landscape.

On the same basis but also adjusting for a \$176 million charge to reinsure UK long tail liabilities as discussed overleaf, net earned premium was up 3% relative to the prior period.

The combined operating ratio increased to 99.0% from 93.4% in the prior period, due to the reduction in risk-free rates. Excluding this impact, the combined operating ratio was 94.0% compared with 94.1% in the prior period. A higher attritional claims ratio due to the competitive landscape, mix changes and short tail claims inflation in Australia was offset by a lower combined commission and expense ratio and increased positive prior accident year claims development.

The annualised net investment return on policyholders' funds increased to 3.4% from 2.7% in the prior period, contributing 4.8% to the insurance profit margin compared with 3.4% in the first half of 2015. Current year returns were supplemented by foreign exchange gains as well as mark to market gains on sovereign and corporate bonds as global risk-free rates reached new lows.

The Group reported an insurance profit of \$326 million, down 47% from \$610 million in the prior period, again due to the movement in risk-free rates which heavily impacted the underwriting result, partially offset by higher investment returns on policyholders' funds. The insurance margin fell to 5.8% from 10.0% in the prior period.

Investment income on shareholders' funds increased to \$165 million from \$137 million in the prior period, consistent with the improvement in returns on policyholders' funds.

Interest expense fell slightly to \$125 million, in line with a small reduction in Group borrowings.

The effective tax rate was stable at 23% and is broadly consistent with QBE's expected longer term underlying tax rate.

## Cash profit

FOR THE HALF YEAR ENDED	30 JUNE 2016 US\$M	30 JUNE 2015 US\$M
Cash profit before tax	378	621
Tax expense on cash profit	(89)	(148)
Profit attributable to non-controlling interests	(2)	(2)
Net cash profit after tax	287	471
Gains on sale of entities after tax	–	88
M&LS deferred acquisition cost write down after tax	–	(55)
Amortisation and impairment of intangibles after tax	(22)	(16)
Net profit after tax	265	488
Basic earnings per share – cash basis (US cents)	¢ 20.9	34.5
Cash profit return on equity	% 5.6	8.6
Dividend payout ratio (percentage of cash profit) <sup>1</sup>	% 74	42

<sup>1</sup> Dividend payout ratio is calculated as the total AUD dividend divided by cash profit converted to AUD at the average rate during the period.

## Premium income

Headline gross written premium decreased 5% during the half to \$8,107 million from \$8,557 million in the prior period, essentially reflecting the stronger US dollar.

On an average basis and compared with the first half of 2015, the Australian dollar, sterling and euro depreciated against the US dollar by 5.8%, 6.4% and 0.6% respectively, adversely impacting gross written premium by \$364 million.

On a constant currency basis and excluding M&LS premium in both years (HY16 \$215 million, HY15 \$263 million), gross written premium was flat reflecting growth in Emerging Markets and Australia & New Zealand, partially offset by a slight contraction in Europe and North America and exacerbated by the ongoing competitive global premium pricing landscape.

Group-wide premium rate reductions averaged around 1.3% during the half, in line with the prior period and the average reduction experienced across full year 2015. While pricing remains highly competitive in Europe and Asia, rate reductions are moderating in global reinsurance and showing recent signs of improvement in Australia & New Zealand. Pricing trends are slightly negative in North America.

Excluding M&LS, the North American gross written premium reduction was a modest 1%, including a 0.3% decline in average premium rates. Strong growth in Specialty and affiliated agency business was offset by further remediation in Standard Lines (particularly in commercial auto).

European Operations recorded a 1% reduction in gross written premium on a constant currency basis. This is a sound outcome in light of the competitive pricing landscape which saw average premium rate reductions of 3.0% during the period and ongoing pressures associated with the impact of lower commodity prices, especially in the oil and gas sector.

Australia & New Zealand reported gross written premium growth of 3% on a constant currency basis, including premium rate reductions averaging 0.3% during the half. Solid growth was achieved across a number of portfolios.

Emerging Markets achieved gross written premium growth of 10% on a constant currency basis, with growth in Asia Pacific and Latin America of 2% and 16% respectively. In Asia, strong growth in Indonesia, Malaysia, the Philippines, Vietnam and Papua New Guinea helped offset challenging conditions in Hong Kong and Singapore and average premium rate reductions of 3.0%. In Latin America, strong growth in Argentina and Brazil more than offset further remediation of Colombian SOAT.

During the half, European Operations completed a transaction to reinsure certain long tail claims liabilities to a third party, with a negligible impact on profit. Excluding the \$176 million reinsurance expense associated with this transaction and \$226 million of gross earned M&LS reinsurance premium, the Group's reinsurance expense ratio fell to 12.9% of gross earned premium from 14.9% in the prior period. This was due to the cancellation of some external LMI and crop reinsurance that was assumed by Equator Re, coupled with reduced aggregate exposures post the sale of M&LS.

On a constant currency basis and adjusting for the sale of M&LS (HY16 nil, HY15 \$157 million) as well as the aforementioned UK reinsurance charge, net earned premium was up 3% relative to the prior period, largely reflecting reduced reinsurance spend.

## Underwriting performance

### Key ratios – Group

FOR THE HALF YEAR ENDED	30 JUNE 2016	30 JUNE 2015	
	STATUTORY %	STATUTORY %	ADJUSTED %
Net claims ratio	<b>64.8</b>	59.8	58.6
Net commission ratio	<b>17.7</b>	17.3	17.5
Expense ratio	<b>16.5</b>	18.2	17.3
Combined operating ratio	<b>99.0</b>	95.3	93.4
Adjusted combined operating ratio <sup>1</sup>	<b>94.0</b>	96.0	94.1
Insurance profit margin	<b>5.8</b>	8.6	10.0

<sup>1</sup> Combined operating ratio adjusted to exclude the impact of changes in risk-free rates used to discount net outstanding claims.

## Divisional performance

### Contributions by region

FOR THE HALF YEAR ENDED	GROSS WRITTEN PREMIUM		NET EARNED PREMIUM		COMBINED OPERATING RATIO		INSURANCE PROFIT BEFORE INCOME TAX	
	30 JUNE 2016 US\$M	30 JUNE 2015 US\$M	30 JUNE 2016 US\$M	30 JUNE 2015 US\$M	30 JUNE 2016 %	30 JUNE 2015 %	30 JUNE 2016 US\$M	30 JUNE 2015 US\$M
North American Operations	<b>2,818</b>	3,109	<b>1,710</b>	1,832	<b>104.0</b>	100.2	<b>(26)</b>	29
European Operations	<b>2,508</b>	2,659	<b>1,385</b>	1,660	<b>98.3</b>	85.8	<b>83</b>	278
Australian & New Zealand Operations	<b>1,861</b>	1,928	<b>1,654</b>	1,668	<b>95.9</b>	90.8	<b>148</b>	247
Emerging Markets	<b>850</b>	929	<b>655</b>	741	<b>99.5</b>	99.5	<b>36</b>	34
Equator Re	<b>1,125</b>	976	<b>197</b>	182	<b>70.1</b>	68.6	<b>74</b>	87
Equator Re elimination	<b>(1,125)</b>	(976)	–	–	–	–	–	–
Corporate adjustments	<b>70</b>	(68)	<b>14</b>	1	–	–	<b>11</b>	(65)
<b>Group adjusted</b>	<b>8,107</b>	8,557	<b>5,615</b>	6,084	<b>99.0</b>	93.4	<b>326</b>	610
Held for sale and disposals	–	–	–	–	–	0.9	–	(55)
Argentine workers' comp business	–	135	–	145	–	135.2	–	(19)
<b>Group statutory</b>	<b>8,107</b>	8,692	<b>5,615</b>	6,229	<b>99.0</b>	95.3	<b>326</b>	536
Direct and facultative	<b>7,471</b>	7,871	<b>5,251</b>	5,851	<b>99.2</b>	96.0	<b>296</b>	454
Inward reinsurance	<b>636</b>	821	<b>364</b>	378	<b>96.7</b>	83.0	<b>30</b>	82
<b>Group statutory</b>	<b>8,107</b>	8,692	<b>5,615</b>	6,229	<b>99.0</b>	95.3	<b>326</b>	536

### Incurred claims

The Group's net claims ratio increased to 64.8% from 58.6% in the prior period, reflecting the significantly adverse impact of lower risk-free rates used to discount net outstanding claims and an increase in the attritional claims ratio, partially offset by increased positive prior accident year claims development.

The net claims ratio also benefited from a 1.1% impact from transactions to reinsure UK long tail liabilities which reduced net earned premium and net claims incurred by \$176 million and \$178 million respectively.

The following table provides a summary of the major components of the net claims ratio.

### Analysis of net claims ratio

FOR THE HALF YEAR ENDED	30 JUNE 2016		30 JUNE 2015	
	STATUTORY	%	STATUTORY	ADJUSTED
			%	%
Attritional claims	54.5		54.2	49.1
Large individual risk and catastrophe claims	9.8		8.9	9.1
Claims settlement costs	3.0		2.8	3.0
Claims discount	(1.3)		(6.6)	(1.9)
Net incurred central estimate claims ratio (current accident year)	66.0		59.3	59.3
Changes in undiscounted prior accident year central estimate	<sup>1</sup> (3.9)		<sup>2</sup> (1.1)	<sup>3</sup> (1.3)
Impact of UK reinsurance transaction <sup>4</sup>	(3.2)		—	—
Change in discount rates	5.0		(0.7)	(0.7)
Other (including unwind of prior year discount)	1.1		2.5	1.5
Net incurred central estimate claims ratio	65.0		60.0	58.8
Movement in risk margins	(0.2)		(0.2)	(0.2)
Net incurred claims ratio (current financial year)	64.8		59.8	58.6

1 Net of \$50 million of discount movement due to long tail classes including dust disease in Australia and our retained Argentine business, where the level of assumed claims inflation is directly linked to the discount rate.

2 Net of \$140 million of discount movement due to long tail classes including dust disease in Australia and motor third party bodily injury and workers' compensation in Argentina, where the level of assumed claims inflation is directly linked to the discount rate.

3 Net of \$12 million of discount movement due to long tail classes including dust disease in Australia and motor third party bodily injury in Argentina, where the level of assumed claims inflation is directly linked to the discount rate.

4 Represents \$178 million of discounted recoveries from the reinsurance of UK long tail liabilities.

As presented in the table below, excluding Crop and the M&LS business which was sold effective 1 October 2015, the Group's underlying attritional claims ratio deteriorated to 51.1% from 48.0% in the prior period reflecting:

- a material increase in Australia due to NSW CTP claims frequency, business mix changes (including increased NSW CTP), increased short tail claims costs (including parts and repair costs) and heightened trade credit claims frequency, which together adversely impacted the Group's attritional claims ratio by 2.5%; and
- a slight increase in the attritional claims ratio across the rest of the Group overall.

The following table provides an analysis of the year-on-year movement in the attritional claims ratio.

### Analysis of adjusted attritional claims ratio

FOR THE HALF YEAR ENDED	30 JUNE 2016		30 JUNE 2015	
	NEP US\$M	ATTRITIONAL %	NEP US\$M	ATTRITIONAL %
Rest of world	5,484	51.1	5,607	148.0
Crop insurance	307	83.1	216	85.1
M&LS <sup>2</sup>	—	—	261	39.7
UK long tail liability reinsurance premium	(176)	—	—	—
QBE Group adjusted	5,615	54.5	6,084	49.1

1 Prior year analysis included an adjustment for \$112 million of incremental group large individual risk and catastrophe (GLRC) aggregate reinsurance premium expense reflecting the purchase of the GLRC effective 1 January 2015. This adjustment is no longer relevant since both periods now include GLRC premium expense.

2 The M&LS business was sold effective 1 October 2015.



Material large individual risk and catastrophe claims reported during the half are summarised in the table below.

#### Large individual risk and catastrophe claims

FOR THE HALF YEAR ENDED 30 JUNE 2016	COST US\$M	% OF NEP
Ecuador earthquake (April)	65	1.2
Alberta wildfires (May)	53	0.9
North American wind/hail (April)	42	0.7
North American wind/hail (March)	38	0.7
Cat 701 – QLD, NSW, VIC and TAS storms (June)	29	0.5
Cyclone Winston (February)	29	0.5
North American wind/hail (May)	20	0.4
Japanese earthquake (April)	11	0.2
Other catastrophe claims including bulk IBNR	57	1.0
GLRC recoveries	(113)	(2.0)
Total catastrophe claims including bulk IBNR	231	4.1
Individual risk claims including bulk IBNR	451	8.0
GLRC recoveries	(131)	(2.3)
Total large individual risk claims including bulk IBNR	320	5.7
Total large individual risk & catastrophe claims including bulk IBNR	551	9.8

FOR THE HALF YEAR ENDED 30 JUNE 2015	COST US\$M	% OF NEP
Total catastrophe claims including bulk IBNR	313	5.1
Total large individual risk claims including bulk IBNR	239	4.0
Total large individual risk & catastrophe claims including bulk IBNR	552	9.1

The total net cost of large individual risk and catastrophe claims was stable at \$551 million compared with \$552 million in the prior period. Relative to net earned premium, the cost of large individual risk and catastrophe claims increased to 9.8% of net earned premium from 9.1% in the prior period, reflecting a 0.3% impact from the cost of the one-off transaction to reinsure UK long tail liabilities, coupled with seasonality in the calculation of GLRC recoveries.

Excluding the impact of the UK long tail liability reinsurance, the full year 2016 net cost of large individual risk and catastrophe claims is expected to be capped (under the majority of circumstances) at around 9% of net earned premium, indicating a likely improved second half of the year.

The total net cost of catastrophe claims fell to \$231 million or 4.1% of net earned premium from \$313 million or 5.1% in the prior period. Particularly benign catastrophe experience in Australia and New Zealand was partially offset by elevated catastrophe experience in Europe (QBE Re) and North America, with ongoing catastrophe activity in Emerging Markets.

In contrast, the total net cost of large individual risk claims increased to \$320 million or 5.7% of net earned premium from \$239 million or 4.0% in the prior period, reflecting heightened large risk claims activity in trade credit and property in Australia & New Zealand as well as Standard Lines in North America.

As summarised in the table below, the currency weighted average risk-free rate (excluding the Argentine peso) used to discount net outstanding claims fell from 1.62% at 31 December 2015 to 0.92% at 30 June 2016. Risk-free rates in all of the Group's major currencies fell significantly but especially sterling and euro, with euro risk-free rates now negative.

#### Movement in weighted average risk-free rates

CURRENCY		30 JUNE 2016	31 DECEMBER 2015	30 JUNE 2015	31 DECEMBER 2014
Australian dollar	%	1.77	2.37	2.43	2.46
US dollar	%	1.20	1.80	1.59	1.33
Sterling	%	0.56	1.47	1.53	1.30
Euro	%	(0.16)	0.59	0.75	0.58
Group weighted average (ex Argentine peso)	%	0.92	1.62	1.60	1.45
Estimated impact of discount rate (charge) benefit <sup>1</sup>	\$M	(283)	38	45	(325)

<sup>1</sup> Excludes movement in Argentine peso risk-free rate as the impact was explicitly offset by higher projected claims inflation.

The reduction in risk-free rates gave rise to an adverse underwriting impact of \$283 million that increased the net claims ratio by 5.0% compared with a benefit of \$45 million in the prior period which reduced the net claims ratio by 0.7%.

The result also included \$218 million of positive prior accident year claims development which benefited the claims ratio by 3.9% compared with \$79 million or 1.3% of favourable development in the prior period. This is the fourth consecutive half of positive development which has averaged \$122 million or 1.9% of net earned premium per half over that period.

The Group's overall positive prior accident year claims development of \$218 million is comprised of:

- European Operations once again reported strong positive development of \$119 million, down slightly from \$140 million in the prior period largely due to currency movements, with favourable development spread across long tail and short tail classes in the insurance divisions;
- Australian & New Zealand Operations recorded \$83 million of positive development, up from \$45 million in the prior period, due to the emergence of favourable development across a number of long tail portfolios;
- North American Operations incurred \$34 million of adverse development, up from \$16 million in the prior period, largely due to a deterioration in commercial auto claims frequency and severity consistent with industry-wide trends, which was partially offset by favourable development in Crop;
- Emerging Markets reported \$17 million of positive development compared with \$15 million in the prior period, reflecting favourable trends emerging in Argentina, Singapore and Malaysia; and
- Equator Re experienced \$34 million of releases compared with \$51 million of adverse development in the prior period.

Risk margins were 8.8% of the net central estimate of outstanding claims (FY15 8.9%) and the probability of adequacy of net outstanding claims remained constant at 89.0%.

### Commission and expenses

Excluding the impact of the UK long tail liability reinsurance, the Group's combined commission and expense ratio improved to 33.2% from 34.8% in the prior period.

On the same basis, the commission ratio improved slightly to 17.1% from 17.5% in the prior period, reflecting business mix changes in North America, additional override commissions in Europe and a small divisional business mix benefit. This was partially offset by an adverse movement in Australian & New Zealand Operations largely as a result of the sale of underwriting agencies, effective 1 April 2015.

Again excluding the impact of the UK long tail liability reinsurance, the Group's expense ratio improved significantly during the half, falling to 16.1% from 17.3% in the prior period, due to a \$124 million net reduction in operating expenses. This included a reduction in costs following the sale of the M&LS business effective 1 October 2015, much of which is reflected in the significant improvement in North America's expense ratio during the half.

Consistent with the expense reduction targets outlined at our May 2016 Investor Update, some of the additional cost efficiencies achieved during the half were reinvested in longer term expense reduction and growth initiatives.

### Income tax expense

The Group's effective tax rate was stable at 23% of pre-tax profit and is broadly consistent with QBE's expected long term underlying tax rate.

During the half, QBE paid \$121 million in corporate income tax to global tax authorities, including \$86 million in Australia. Income tax payments in Australia benefit our dividend franking account, the balance of which stood at A\$325 million as at 30 June 2016.

In order to maintain franking stability, the combination of a higher dividend payout ratio and increased profitability of non-Australian operations warrants a reduction in the franking rate to 50% for the 2016 and 2017 dividends.

### Foreign exchange

As a significant proportion of our underwriting activity is denominated in US dollars, the Group's financial statements are presented in this currency. Assets and liabilities of all our foreign operations that have a functional currency different from the Group's presentation currency are translated to US dollars at the closing balance date rates of exchange and income and expenses are translated at the cumulative average rates of exchange for the period, with the foreign exchange movements reported through the foreign currency translation reserve (component of equity).

QBE is also exposed to currency translation risk in relation to the ultimate parent entity's net investment in foreign operations (NIFO) to its functional currency of Australian dollars. QBE does not ordinarily seek to use derivatives to mitigate this risk for the following reasons:

- currency translation gains and losses generally have no cash flow;
- currency translation gains and losses are accounted for in the foreign currency translation reserve and therefore do not impact profit or loss unless related to the disposal of an entity; and
- management of translation risk needs to be balanced against the impact on capital requirements and liquidity risk.

In extended periods of extraordinary volatility, QBE may elect to utilise derivatives to mitigate currency translation risk in order to preserve capital. Brexit would be considered such an example and, consequently, the Group hedged its sterling NIFO exposures in early July.

During the first half of 2016, the Group's major currencies varied against the USD as summarised in table below.

#### Movement in the Group's major currencies relative to the USD

FOR THE HALF YEAR ENDED 30 JUNE 2016	SPOT	AVERAGE
AUD	0.75	0.73
GBP	1.33	1.43
EUR	1.11	1.12

The impact of exchange rate movements on the 2016 interim result was a pre-tax operational foreign exchange gain of \$39 million compared with a \$29 million loss in the prior period. The net movement in the foreign currency translation reserve, share capital and other reserves due to foreign currency fluctuation was a \$108 million negative impact on equity.

The table below shows the impact of foreign exchange on the 2016 interim result and balance sheet on a constant currency basis.

#### Impact of exchange rate movements

	2016 ACTUAL US\$M	2016 AT 2015 EXCHANGE RATES <sup>1</sup> US\$M	EXCHANGE RATE IMPACT	
			US\$M	%
Gross written premium	8,107	8,471	(364)	(4)
Gross earned premium	6,876	7,219	(343)	(5)
Net earned premium	5,615	5,920	(305)	(5)
Net profit after tax	265	285	(20)	(8)
Total investments and cash	25,728	26,457	(729)	(3)
Total assets	43,273	44,706	(1,433)	(3)
Gross outstanding claims provision	18,803	19,661	(858)	(5)
Total liabilities	32,889	34,022	(1,133)	(3)
Net assets	10,384	10,684	(300)	(3)

1 Income statement items are restated to 30 June 2015 average rates of exchange and balance sheet items to 31 December 2015 closing rates of exchange.

## Balance sheet

### Capital management summary

Consistent with the strength of the balance sheet, the major ratings agencies reaffirmed the Group's financial strength and issuer credit ratings, with Standard & Poor's revising the Group's outlook from "stable" to "positive" and referring to QBE Group's capital adequacy as being "well above the AA level" and our liquidity as "exceptional".

A number of capital management initiatives were undertaken during the period as discussed overleaf.

### Capital summary

AS AT	30 JUNE 2016 US\$M	31 DECEMBER 2015 US\$M
Net assets	10,384	10,560
Less: intangible assets	(3,592)	(3,604)
Net tangible assets	6,792	6,956
Add: borrowings	3,482	3,529
Total capitalisation	10,274	10,485

AS AT	30 JUNE 2016 <sup>1</sup> US\$M	31 DECEMBER 2015 <sup>2</sup> US\$M
APRA's Prescribed Capital Amount (PCA)	5,549	5,637
QBE's regulatory capital base	9,378	9,737
PCA multiple	1.69x	1.73x

1 Indicative APRA PCA multiple at 30 June 2016.

2 Prior year APRA PCA multiple has been restated to be consistent with APRA returns finalised subsequent to year end.

At 30 June 2016, the Group's indicative APRA PCA multiple was 1.69x, down from 1.73x at 31 December 2015. Excluding the impact of exchange rate movements and the overall impact of lower risk-free rates, the multiple would have been around 1.73x.

In light of the extent to which our capital position now exceeds S&P's minimum 'AA' capital requirement, we remain comfortable with our regulatory capital position at around 1.7x our PCA.

**Key financial strength ratios**

	BENCHMARK		30 JUNE 2016	31 DECEMBER 2015
Debt to equity	25% to 35%	%	33.7	33.6
Debt to tangible equity		%	51.7	51.1
PCA multiple <sup>1</sup>	1.6x to 1.8x	x	1.69	1.73
Premium solvency <sup>2</sup>		%	58.1	56.5
Probability of adequacy of outstanding claims	87.5% to 92.5%	%	89.0	89.0

<sup>1</sup> Prior year APRA PCA multiple has been restated to be consistent with APRA returns finalised subsequent to year end.

<sup>2</sup> Premium solvency ratio is calculated as the ratio of net tangible assets to net earned premium.

**Borrowings**

At 30 June 2016, the Group's borrowings stood at \$3,482 million, a reduction of \$47 million or 1.3% from \$3,529 million as at 31 December 2015, largely reflecting the impact of currency depreciation on our sterling debt.

During the half, Group Treasury established:

- a \$600 million two year committed revolving credit facility, which matures on 31 March 2018. This facility remained undrawn throughout the period; and
- a \$4 billion medium term note issuance program which allows QBE to issue senior unsecured notes, tier 2 subordinated debt securities and additional tier 1 securities.

Group Treasury was also active in the capital markets during the period executing the following transactions:

- a tender exchange for our £325 million tier 2 subordinated debt securities due 24 May 2041. £291 million was tendered and exchanged for £327 million of new tier two subordinated debt securities maturing 24 May 2042;
- notified holders of our £300 million perpetual capital securities of our intention to call these securities on their first call date. This transaction closed on the 18 July 2016. As a result of a previous Group Treasury liability management exercise, QBE already owned £292 million of these securities; and
- an intermediated tender exchange for our \$1 billion tier 2 subordinated debt securities due 24 May 2041. \$456 million was tendered and exchanged for \$524 million of new tier 2 subordinated debt securities maturing 17 June 2046.

Both the sterling tender exchange and the USD intermediated tender exchange transactions were designed to further optimise the Group's capital efficiency by reacquiring securities which had become subject to regulatory capital amortisation from 1 January 2016, replacing them with new regulatory capital qualifying tier 2 subordinated debt securities.

At 30 June 2016, QBE's ratio of borrowings to shareholders' funds was 33.7%, up marginally from 33.6% at 31 December 2015 but still within our benchmark range of 25%–35%. Debt to tangible equity was 51.7%, up marginally from 51.1% at 31 December 2015.

Interest expense for the period was \$125 million, down 2% from \$127 million for the same period last year. The weighted average annual cash cost of borrowings outstanding at the balance sheet date reduced from 6.2% at 31 December 2015 to 5.8% at 30 June 2016.

All of the debt issued during the first half of 2016 was by way of regulatory capital qualifying tier 2 subordinated debt. As a consequence, the weighting towards regulatory capital qualifying tier 2 within the Group's overall borrowing mix was unchanged at 74% at 30 June 2016. QBE's debt maturity profile has been normalised with additional duration layered into the term structure.

As a result of the sterling and USD tender exchange transactions, the amount of the Group's tier 2 subordinated debt exposed to future regulatory amortisation has been materially reduced from \$1,479 million at 1 January 2016 to \$583 million at 30 June 2016, with the annual estimated regulatory capital amortisation reducing from \$244 million to \$96 million.

During the second half of 2016, QBE's regulatory or ratings agency capital positions are not expected to be materially impacted by the residual amortisation reflecting the Group's current excess tier 2 capital position.

**Borrowings maturity<sup>1</sup>**

AS AT	30 JUNE 2016 %	31 DECEMBER 2015 %
Less than one year	9	–
One to five years	38	30
More than five years	53	70

**Borrowings profile**

AS AT	30 JUNE 2016 %	31 DECEMBER 2015 %
Subordinated debt	74	74
Senior debt	17	17
Capital securities	9	9

<sup>1</sup> Based on first call date.

Further details of borrowings are set out in note 4.1 to the financial statements.

## Insurance liabilities

The table below summarises our provisions for outstanding claims and unearned premium, separately identifying the central estimate and risk margin.

### Insurance liabilities

AS AT	30 JUNE 2016 US\$M	31 DECEMBER			
		2015 US\$M	2014 US\$M	2013 US\$M	2012 US\$M
Net outstanding claims	15,291	15,379	16,948	18,208	18,412
Unearned premium net of deferred insurance costs <sup>1</sup>	5,361	4,685	5,341	5,968	6,023
	20,652	20,064	22,289	24,176	24,435
Central estimate – outstanding claims	14,060	14,119	15,595	16,643	17,079
Central estimate – unearned premium	4,767	4,139	4,398	4,956	5,024
Risk margin – outstanding claims	1,231	1,260	1,353	1,565	1,333
Risk margin – unearned premium <sup>1</sup>	594	546	943	1,012	999
	20,652	20,064	22,289	24,176	24,435
Risk margin in excess of 75% probability of adequacy using APRA's risk weighted capital adequacy model	989	978	1,396	1,606	1,374
	%	%	%	%	%
Probability of adequacy – outstanding claims	89.0	89.0	88.7	90.7	87.5
Probability of adequacy – total insurance liabilities	91.9	91.8	94.7	95.3	93.9
Weighted average discount rate (including Argentine peso)	1.0	1.9	1.7	2.8	2.2
Weighted average term to settlement (years)	3.0	3.0	2.8	3.0	2.9

<sup>1</sup> Adjusted for deferred reinsurance expense for future business not yet written of \$186 million (2015 \$217 million).

As required by Australian Accounting Standards, insurance liabilities are discounted by applying sovereign bond rates as a proxy for risk-free interest rates and not the actual earning rate of our investments.

As at 30 June 2016, risk margins in net outstanding claims fell 2% to \$1,231 million from \$1,260 million at 31 December 2015, mainly due to the impact of foreign exchange. As the net discounted central estimate fell by a proportionally smaller 0.4% from \$14,119 million to \$14,060 million, risk margins reduced to 8.8% of the net discounted central estimate from 8.9% at 31 December 2015.

Notwithstanding the slight reduction in the margin above central estimate, the probability of adequacy was unchanged at 89.0%, reflecting a reduction in the Group's coefficient of variation (CoV) due to a higher level of short tail claims (particularly crop) as a proportion of net outstanding claims liabilities at 30 June 2016, as well as the impact of the transactions to reinsure some of our UK long tail claims liabilities.

The probability of adequacy of total insurance liabilities was 91.9% compared with 91.8% at 31 December 2015, with the level of risk margins deemed appropriate to cover the inherent uncertainty in the net discounted central estimate.

### Intangible assets

As at 30 June 2016, the carrying value of intangible assets (identifiable intangibles and goodwill) was \$3,592 million, down marginally from \$3,604 million at 31 December 2015.

During the half, the carrying value of intangibles reduced by \$12 million, primarily due to the net impact of amortisation and exchange rate movements partially offset by additions, which largely comprised the capitalisation of expenditure in relation to various information technology projects across the Group.

At 30 June 2016, QBE reviewed all material intangibles for indicators of impairment, consistent with the Group's policy and the requirements of the relevant accounting standard.

Noting the limited headroom (being the excess of recoverable value over carrying value) in respect of the 2015 year end valuation of goodwill in North American Operations, a detailed impairment test was completed. The latest impairment testing indicated that the headroom at the balance date decreased to \$79 million compared with \$196 million at 31 December 2015, predominantly as a result of the lower interest rate environment. The valuation continues to be highly sensitive to a range of assumptions, in particular, to increases in the forecast combined operating ratio used in the terminal value calculation and changes in discount rate and long-term investment return assumptions.

Details of the sensitivities associated with this valuation are included in note 1.2.2 to the financial statements.



**Reconciliation of movement in intangible assets**

AS AT	30 JUNE 2016			31 DECEMBER 2015		
	IDENTIFIABLE INTANGIBLES US\$M	GOODWILL US\$M	TOTAL US\$M	IDENTIFIABLE INTANGIBLES US\$M	GOODWILL US\$M	TOTAL US\$M
Opening balance	414	3,190	3,604	423	3,408	3,831
Disposals	(1)	–	(1)	(3)	(30)	(33)
Additions/reclassifications	53	–	53	138	6	144
Amortisation/impairment <sup>1</sup>	(31)	–	(31)	(120)	(1)	(121)
Foreign exchange	(7)	(26)	(33)	(24)	(193)	(217)
Closing balance	428	3,164	3,592	414	3,190	3,604

1 \$12 million of amortisation expense is included in underwriting expenses (full year 2015 \$26 million).

**Investment performance and strategy**

The first half of 2016 was eventful from both a market and geopolitical standpoint. Initial market volatility in January and February gave way to stability as China's economy showed signs of improved economic activity and the oil price recovered. The half concluded with Brexit which added a layer of geopolitical uncertainty to an already sub-par global economy. Bond yields declined to record lows reflecting concerns surrounding the potential impact of Brexit on the UK and European economies, coupled with a reassessment of the path of US Federal Reserve policy tightening.

QBE's investment portfolio weathered this volatility delivering an annualised return of 3.3% net of expenses.

In line with our commitment over time to more closely match the duration of our investment assets with the 3.0 year duration of our claims liabilities, we took advantage of global bond market volatility to add duration. Modified asset duration ended the half year at 1.3 years, up from 0.9 years at 31 December 2015. As a consequence, the decline in sovereign yields was a significant contributor to the our first half investment return being ahead of expectations. Realised and unrealised gains on fixed income amounted to \$154 million during the half, up from \$13 million in the prior period, including \$96 million in policyholders' funds.

Major central banks are likely to maintain extremely accommodative monetary policy for the foreseeable future keeping bond yields anchored at low levels for longer. To mitigate the impact of low bond yields we further diversified our fixed income portfolio during the half adding exposure in structured credit, infrastructure debt and corporate bond holdings as wider credit spreads at the start of the year provided attractive yield pickup over sovereigns. The credit quality of the portfolio remains conservative relative to our global peers and we will continue to monitor ratings actions post-Brexit to ensure that the individual corporate bonds we hold are consistent with our conservative strategy.

After a volatile start, growth assets settled and were confined to a relatively narrow trading range during the latter part of the half. Amid the volatility in markets and with an eye on uncertainty ahead of the Brexit referendum, we reduced growth asset exposure early in the half by lowering exposure to equities, particularly UK and emerging markets, while marginally increasing exposure to infrastructure to generate income and provide more capital stability to the portfolio. Overall, growth assets delivered a positive return for the half year and constituted 9.5% of the investment portfolio at 30 June 2016.

While portfolio returns for the first half were ahead of plan, they incorporate the benefit of the substantial fall in bond yields which are unlikely to recur in the second half and which have also resulted in a lower running yield of the fixed income book going forward. Looking ahead, we expect recent market volatility to continue and will maintain our conservative stance enabling us to take advantage of any further market dips to enhance portfolio returns.

## Total net investment income

FOR THE HALF YEAR ENDED 30 JUNE	POLICYHOLDERS' FUNDS		SHAREHOLDERS' FUNDS		TOTAL	
	2016 US\$M	2015 US\$M	2016 US\$M	2015 US\$M	2016 US\$M	2015 US\$M
Income on growth assets	6	105	13	58	19	163
Fixed interest, short-term money and cash income	243	173	153	100	396	273
Gross investment income	249	278	166	158	415	436
Investment expenses	(7)	(9)	(4)	(5)	(11)	(14)
Net investment income	242	269	162	153	404	422
Foreign exchange gain (loss)	34	(20)	5	(9)	39	(29)
Other income (expenses)	(4)	(8)	(2)	1	(6)	(7)
Net investment and other income	272	241	165	145	437	386

## Annualised gross and net investment yield

FOR THE HALF YEAR ENDED 30 JUNE	YIELD ON INVESTMENT ASSETS BACKING POLICYHOLDERS' FUNDS		YIELD ON INVESTMENT ASSETS BACKING SHAREHOLDERS' FUNDS		TOTAL	
	2016 %	2015 %	2016 %	2015 %	2016 %	2015 %
Gross investment yield <sup>1</sup>	3.1	3.1	3.2	2.9	3.2	3.0
Net investment yield <sup>2</sup>	3.0	3.0	3.1	2.9	3.1	2.9
Net investment and other income yield <sup>3</sup>	3.4	2.7	3.2	2.7	3.3	2.7

1 Gross yield is calculated with reference to gross investment income as a percentage of average investment assets backing policyholders' or shareholders' funds as appropriate.

2 Net yield is calculated with reference to net investment income before borrowing costs as a percentage of average investment assets backing policyholders' or shareholders' funds as appropriate.

3 Net investment and other income yield is calculated with reference to net investment and other income as a percentage of average investment assets backing policyholders' or shareholders' funds as appropriate.

## Total investments and cash

AS AT	INVESTMENT ASSETS BACKING POLICYHOLDERS' FUNDS		INVESTMENT ASSETS BACKING SHAREHOLDERS' FUNDS		TOTAL	
	30 JUNE 2016 US\$M	31 DECEMBER 2015 US\$M	30 JUNE 2016 US\$M	31 DECEMBER 2015 US\$M	30 JUNE 2016 US\$M	31 DECEMBER 2015 US\$M
Cash and cash equivalents	425	404	338	258	763	662
Short-term money	2,744	3,616	1,780	2,308	4,524	5,924
Government bonds	2,094	2,538	1,308	1,620	3,402	4,158
Corporate bonds	8,473	7,560	5,608	4,825	14,081	12,385
Infrastructure debt	283	212	175	136	458	348
Unit trusts	27	39	17	25	44	64
Strategic equities	—	—	121	108	121	108
Other equities	221	351	137	224	358	575
Emerging market equity	20	155	13	99	33	254
Emerging market debt	20	194	13	124	33	318
High yield debt	16	280	10	178	26	458
Alternatives	545	242	338	155	883	397
Property trusts	618	637	384	406	1,002	1,043
Investment properties	8	7	5	7	13	14
Total investments and cash	15,494	16,235	10,247	10,473	25,741	26,708

## Interest bearing financial assets

SECURITY RATING			CURRENCY MIX		MARKET VALUE OF GROWTH ASSETS		MARKET VALUE OF TOTAL INVESTMENTS AND CASH	
AS AT	30 JUNE 2016 %	31 DECEMBER 2015 %	AS AT	30 JUNE 2016 %	31 DECEMBER 2015 %	30 JUNE 2016 %	31 DECEMBER 2015 %	
S&P rating			US dollar	40	45	31	31	
AAA	13	17	Australian dollar	43	37	30	30	
AA	37	37	Sterling	8	12	20	21	
A	41	38	Euro	9	6	8	8	
<A	9	8	Other	–	–	11	10	

## Interim dividend

Our dividend policy is designed to ensure that we reward shareholders relative to cash profit and maintain sufficient capital for future investment and growth of the business.

The interim dividend for 2016 will be 21 Australian cents per share, up 5% compared with the 2015 interim dividend of 20 Australian cents per share.

The dividend will be 50% franked and is payable on 28 September 2016. The dividend reinvestment programs remain at a nil discount with demand for shares under the Dividend Reinvestment Plan to be satisfied by acquiring shares on-market.

The payout for the 2016 interim dividend is A\$288 million or 74% of cash profit calculated by converting cash profit to Australian dollars at the average rate of exchange during the period. The calculation of cash profit is shown on page 11.

In conjunction with the release of the 2015 interim result and commencing with the 2016 interim dividend, the Board announced an increase in the Group's full year payout ratio to 65% of cash profit, up from the previous maximum of 50%. The 2016 interim dividend payout ratio of 74% is above the Board's revised full year payout policy reflecting acknowledgment of the unusual market conditions that gave rise to the lower risk-free rates used to discount net outstanding claims, as well as the Group's overall capital position and profitability.

## Closing remarks

While we have made progress against our strategic objectives over the last six months, there is still room for improvement.

Our priorities for the remainder of 2016 are to:

- drive necessary actions to restore the Australian & New Zealand Operations' attritional claims ratio;
- achieve our 94%–95% 2016 combined operating ratio target (excluding the impact of changes in discount rates);
- demonstrate continued positive prior accident year claims development;
- exceed our \$150 million 2016 expense reduction target;
- deliver divisional cash remittances of >\$1 billion for 2016; and
- maintain a strong capital position consistent with S&P "AA" capital.

Pat Regan  
**Group Chief Financial Officer**

# North American Operations business review

“The progress we have made during the half in driving profitable growth in our chosen specialty and commercial lines businesses, together with the significant reduction in our acquisition cost ratio, gives us confidence in our ability to achieve our medium term target of a mid-90s combined operating ratio.”

**Russ Johnston**

Chief Executive Officer • North American Operations

Gross written premium US\$ million	Net earned premium US\$ million	Underwriting result US\$ million	Insurance profit US\$ million
<b>2,818</b>	<b>1,710</b>	<b>(68)</b>	<b>(26)</b>
↓ 9% from 2015	↓ 7% from 2015	↓ \$65M from 2015	↓ \$55M from 2015
		Combined operating ratio <sup>1</sup> <b>100.5%</b> (2015 100.6%)	Insurance profit margin <b>(1.5)%</b> (2015 1.6%)

## 2016 overview

North American Operations is a specialist insurance and reinsurance franchise focused on four key business units: Standard Lines, Specialty, Crop and Assumed Reinsurance, with the latter a component of QBE's global reinsurance business headquartered in London.

Dave Duclos announced his retirement from full time executive responsibilities at the end of the first half. Russ Johnston was appointed CEO North America Operations and has succeeded him in this role.

Premium rates softened slightly overall, resulting in an average rate reduction of 0.3% compared with flat in the prior corresponding period. As a consequence, it has become increasingly important to drive continued improvement in how we define, target, select and price risk while driving greater efficiency and improving the customer experience.

North America has established a profitable and growing Specialty business. Our Standard Lines business continues to improve, we are developing a reinsurance franchise in North America and our Crop business is performing well.

Lower corn and soybean pricing, coupled with farmers opting for higher deductibles, has impacted Crop revenues. Nevertheless, the business continues to leverage its position as a market leader, growing market share and crop conditions remain positive year to date and bode well for the harvest season.

The commercial auto class of business has remained a challenge for the second consecutive year. Increased claims costs and adverse prior accident year development have been a recurring industry challenge. We continue to focus on improved risk selection coupled with firm pricing action to improve our performance in this area.

<sup>1</sup> Combined operating ratio adjusted to exclude the impact of changes in risk-free rates used to discount net outstanding claims.

## Operating and financial performance

### Underwriting performance

North American Operations reported a combined operating ratio of 104.0% compared with 100.2% in the prior corresponding period. The underwriting result includes a charge of \$60 million or 3.5% as a result of lower risk-free rates used to discount claims liabilities compared with a small positive impact in the prior corresponding period. Excluding this charge, the combined operating ratio was 100.5% compared with 100.6% a year earlier.

The interim result was impacted by \$34 million or 2.0% of adverse prior accident year claims development compared with \$16 million or 0.9% in the prior period, mainly due to a deterioration in commercial auto claims frequency and severity trends on more recent accident years. Although this is a well-documented industry-wide issue, the vast majority of QBE's development pertained to one specific commercial auto program. Firm corrective action has been taken, including material price increases and greatly strengthened underwriting controls, to ensure this portfolio returns to profitability in 2017.

Underwriting profitability in our key segments of Crop and Specialty remains especially strong. The performance of the Crop business is trending above historical averages with signs to date pointing to a strong harvest and soft commodity prices remaining relatively stable compared with initial contract pricing. We continue to build a leading Specialty franchise and drive strong profitable organic growth. Specialty premium grew by 51% while delivering a first half combined operating ratio in the low nineties.

North American Operations' expense ratio improved markedly to 15.5% from 19.7% last year reflecting a combination of the sale of the M&LS business, further cost efficiencies and positive operating leverage as a result of profitable growth across key segments including Specialty and affiliated agencies.

### Underwriting result

FOR THE HALF YEAR ENDED 30 JUNE		2016	2015 <sup>1</sup>	2014 <sup>1</sup>	2013 <sup>1</sup>	2012 <sup>1</sup>
Gross written premium	US\$M	2,818	3,109	2,472	2,750	3,229
Gross earned premium	US\$M	2,184	2,309	2,259	2,598	3,063
Net earned premium	US\$M	1,710	1,832	1,917	2,115	2,557
Net incurred claims	US\$M	1,225	1,145	1,152	1,293	1,416
Net commission	US\$M	288	329	357	395	475
Expenses	US\$M	265	361	377	412	378
Underwriting result	US\$M	(68)	(3)	31	15	288
Net claims ratio	%	71.6	62.5	60.1	61.1	55.3
Net commission ratio	%	16.8	18.0	18.6	18.7	18.6
Expense ratio	%	15.5	19.7	19.7	19.5	14.8
Combined operating ratio	%	104.0	100.2	98.4	99.3	88.7
Adjusted combined operating ratio <sup>2</sup>	%	100.5	100.6	—	—	—
Insurance profit margin	%	(1.5)	1.6	2.9	1.8	12.7

1 Comparability of prior period data is diminished as a result of the sale of M&LS and the adoption of a significantly revised crop premium earning pattern in 2015.

2 Combined operating ratio adjusted to exclude the impact of changes in risk-free rates used to discount net outstanding claims. Management results were not reported in the first half of 2014 and prior.

### Premium income

Gross written premium fell 9% to \$2,818 million from \$3,109 million in the prior corresponding period, largely reflecting the sale of the M&LS business which completed effective 1 October 2015. Excluding the impact of M&LS business, the half-on-half decline in gross written premium was a more modest \$28 million or 1%.

Crop gross written premium reduced \$151 million or 13% compared with the first half of 2015, reflecting lower commodity prices coupled with reduced volatility pricing factors and farmers electing to take higher policy deductibles after favourable conditions in 2015. Notwithstanding lower gross written premium, policy count increased by ~2% indicating modest growth in market share consistent with the industry leading position of this business.

Specialty continued its strong growth trajectory with gross written premium up \$92 million or 51%. New business across the segment has nearly doubled over the past 12 months with a substantial amount of growth generated in management liability and professional lines as well as from the addition of several new programs to the specialty programs portfolio.

Standard Lines premium declined \$37 million or 3% driven by continued underwriting action in underperforming areas coupled with increased underwriting discipline in areas where technical rates are under pressure (particularly in property and commercial auto). Our affiliated agency business remains strong with 8% growth driven by our home builder channel.

Net earned premium fell 7% to \$1,710 million compared with \$1,832 million a year earlier. Excluding the impact of the M&LS sale, net earned premium increased \$139 million or 9%. Fuelled by growth in new business, Specialty net earned premium grew \$61 million or 41%.



## Gross earned premium by class of business

FOR THE HALF YEAR ENDED 30 JUNE	2016 %	2015 %
Commercial & domestic property	34.2	42.0
Agriculture	25.6	20.1
Motor & motor casualty	11.7	14.0
Workers' compensation	9.3	9.0
Public/product liability	7.8	7.7
Accident & health	5.3	3.8
Professional indemnity	4.1	1.7
Marine energy & aviation	1.1	1.0
Financial & credit	0.9	0.7

## Claims expense

North America Operations reported a 2016 net claims ratio of 71.6% compared with 62.5% in the first half of 2015.

The higher claims ratio includes the impact of lower risk-free rates used to discount claims liabilities which occurred mostly in the later part of the half year. This adversely impacted the interim result by \$60 million or 3.5% compared with a small benefit in the prior corresponding period.

Excluding the impact of Crop and M&LS, the attritional claims ratio increased slightly to 50.3%.

After a benign 2015, large individual risk and catastrophe claims increased to 7.2% of net earned premium compared with 5.4% in the prior corresponding period, mainly due to severe hail storms in Texas that impacted Standard Lines.

The claims ratio was also adversely impacted by \$34 million of prior accident year development, up from \$16 million in the prior period, primarily due to the commercial auto classes in Standard Lines driven by higher claims frequency and severity trends which have been broadly consistent across the industry. Adverse development in commercial auto was partially offset by favourable development for Crop.

## Commission and expenses

The combined commission and expense ratio improved significantly during the half falling to 32.3% from 37.7% last year, driven by the sale of M&LS coupled with positive leverage associated with cost reduction and net earned premium growth.

The commission ratio decreased to 16.8% from 18.0% in the prior corresponding period reflecting a net mix benefit of 0.8% largely driven by Crop, coupled with a 0.4% benefit from profit commissions driven by better than expected prior year performance for Crop. Absent business mix changes, commission rates were broadly unchanged.

The expense ratio improved materially to 15.5% from 19.7% in the prior corresponding period and included a 2.1% benefit associated with the sale of the M&LS business. The significant improvement in the underlying expense ratio largely reflects the earning of run-rate savings from actions implemented during the prior year coupled with positive leverage as a result of profitable growth across key areas including higher net earned premium in Specialty.

## Strategic agenda and other developments

A number of initiatives are currently underway as North America Operations is focused on delivering a mid-90's combined operating ratio by 2018. Our strategic agenda remains focused on the following six key priorities:

**Underwriting excellence:** Re-underwriting elements of our Standard Lines business is a key priority. Through a very targeted geographical and industry focus we are improving pricing and risk selection, and are shedding underperforming risks in commercial auto. New commercial auto business reduced in the period and we remain focused on managing the impact this class has on the North American portfolio. In personal lines we continue to focus on a homeowner led approach to the business and on being less reliant on personal auto to drive both a higher customer engagement and improve our underwriting performance. We have further refined our view of our agents and brokers using data analytics to help us manage the profitability of this part of our portfolio. While property rates continue to be under pressure, our use of robust technical pricing tools allows us to closely monitor both price adequacy and aggregation.

Our Specialty Lines portfolio is tracking in line with growth and profitability expectations. Crop has had a promising start to the year with low preventative planting claims and relatively stable soft commodity prices and our Reinsurance and Standard Lines businesses continue to improve. This all contributes to our confidence in posting an improved combined operating ratio in 2016 when compared with 2015.

**Customer and partner led growth:** The Specialty products launched over the past two and a half years have allowed us to develop an organic growth capability that we are now leveraging across the Standard Lines portfolio. We are launching an excess and surplus lines business and are building on our existing personal lines platform to give us greater diversity in our portfolio. By focusing on core personal lines, investing in a high net worth strategy and building a renters capability, we will create a highly diversified portfolio that will provide personal lines solutions to different demographic segments of the market. We refer to this as the wealth pyramid. Additionally, as part of building an effective distribution platform, three targeted regions have been established in 2016, with leadership already in place. Our value proposition is centred on the breadth of our Specialty and Standard Lines product offerings and delivering integrated "go-to-market" capabilities.

**Operational efficiency:** We must continue to build capabilities that will enable us to sustain financial results and brand value. We are streamlining processes and creating an organisation design that leverages our capabilities both in our shared services centre in the Philippines and on-shore. At the same time, we are creating a more cost effective and scalable service model through smart investments in technology and solutions-enabling business processes, allowing us to better leverage the global capabilities of the Group. This approach will deliver significant expense ratio benefits as we continue to grow premium and rebalance the portfolio towards more profitable lines.

**Claims excellence:** We appointed a new Chief Claims Officer during the half and have implemented a series of initiatives focused on reducing fraud and improving recoveries and third party management, ensuring we drive improvements in the claims ratio. A positive customer experience, process efficiency and effective technical practices are the principles underpinning our activity in this area.

**Data analytics:** During the first half we have made improvements in our analytical capabilities across customer analysis, underwriting and claims predictive analysis. We are using this capability to drive improved decision making at both the transaction and portfolio level.

**World class talent:** We continue to develop a performance-driven and results-focused culture. We appointed a new Chief Human Resources Officer during the half and have continued to capitalise on market disruption by bringing in new and talented senior leaders across our business and functions. We are also developing our in-house technical expertise with the launch of our underwriting academy.

# European Operations business review

“Our European business is well placed to operate in challenging market conditions reflecting its focus on very clear risk and price selection criteria coupled with robust claims and cost management initiatives. We are delighted to report such a strong first half result against a challenging industry and economic backdrop.”

**Richard Pryce**

Chief Executive Officer • European Operations

<b>Gross written premium</b> <b>US\$ million</b> <b>2,508</b> ↓ 6% from <sup>2</sup> 2015	<b>Net earned premium<sup>1</sup></b> <b>US\$ million</b> <b>1,561</b> ↓ 6% from <sup>2</sup> 2015	<b>Underwriting result<sup>1</sup></b> <b>US\$ million</b> <b>22</b> ↓ \$214M from 2015 <b>Combined operating ratio<sup>3</sup></b> <b>88.3% (2015 88.0%)</b>	<b>Insurance profit (loss)<sup>1</sup></b> <b>US\$ million</b> <b>81</b> ↓ \$197M from 2015 <b>Insurance profit margin</b> <b>5.2% (2015 16.7%)</b>
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## 2016 overview

Trading conditions continued to challenge many areas of our business driven by surplus capacity putting additional pressure on renewal rates. We recorded a further weighted average premium rate reduction of 3.0% during the half, slightly more than the 2.4% in our plans but still better than the 3.3% average reduction seen in the first half of 2015.

Over the last three years we have invested selectively in our customer proposition by expanding product and people capability across our geographies, which is helping us retain our profitable portfolio and selectively acquire new business. During the half, we added to our insurance and reinsurance teams in Latin America, appointed a new leader for Canada and increased our client engagement team.

Net earned premium was less than planned principally due to the completion of transactions to reinsure some of our more volatile UK long-tail claim exposures. These transactions provide protection against future adverse development in these portfolios.

The first half witnessed an increasing preoccupation with the prospect, and then more recently the effects, of the UK leaving the European Union. We have been reviewing the potential impact on European Operations for some time now and while the economic and political decisions remain uncertain, we are well positioned to implement the requisite solutions at a relatively nominal cost in the event we can no longer access the single market from the UK.

<sup>1</sup> Adjusted for transactions to reinsure UK long tail liabilities.

<sup>2</sup> Down 1% on a constant currency basis.

<sup>3</sup> Combined operating ratio adjusted to exclude the impact of changes in risk-free rates used to discount net outstanding claims.

## Operating and financial performance

### Underwriting performance

Reinsurance transactions in relation to some of our UK long tail liabilities reduced net claims incurred by \$178 million and net earned premium by \$176 million. Although broadly profit neutral, the transactions improved European Operations' first half combined operating ratio by 0.3% (with a 4.8% positive impact on the net claims ratio offset by a 4.4% adverse impact on the combined commission and expense ratio as highlighted in the table below) and reduced the level of uncertainty in the residual net discounted central estimate of outstanding claims.

In order to assist year on year comparability, the underwriting performance (including claims and expense) commentary hereafter refers to the 2016 interim result excluding the impact of these long tail liability reinsurance transactions.

The underwriting result included a \$161 million adverse impact caused by lower risk-free rates used to discount net outstanding claims compared with a \$36 million benefit in the prior corresponding period. Risk-free rates in the division's main currencies of GBP, EUR and USD fell significantly across the half, exacerbated by the uncertainty created by the Brexit referendum immediately prior to the balance date.

Excluding the discount rate impact, the combined operating ratio increased slightly to 88.3% from 88.0% in the prior period, largely reflecting a significant increase in global catastrophe activity (after an especially benign 2015) which particularly impacted QBE Re. Elsewhere, both Retail and International Markets reported improved underwriting results relative to the prior corresponding period.

The underwriting performance reflects our ongoing commitment to underwriting excellence. Underwriting discipline, which is paramount for both renewal and new business decisions, is a key component of our culture. We closely monitor the performance of every portfolio and will continue to make the requisite decisions to maintain acceptable returns.

### Underwriting result

FOR THE HALF YEAR ENDED 30 JUNE		2016	2016 <sup>1</sup> ADJUSTED	2015	2014	2013	2012
Gross written premium	US\$M	2,508	2,508	2,659	2,705	3,154	2,797
Gross earned premium	US\$M	1,930	1,930	2,112	2,471	2,469	2,290
Net earned premium	US\$M	1,385	1,561	1,660	2,003	2,003	1,863
Net incurred claims	US\$M	812	990	815	1,214	1,230	1,105
Net commission	US\$M	279	279	312	383	383	334
Expenses	US\$M	270	270	297	319	277	273
Underwriting result	US\$M	24	22	236	117	113	151
Net claims ratio	%	58.6	63.4	49.1	59.7	61.4	59.4
Net commission ratio	%	20.1	17.9	18.8	18.8	19.1	17.9
Expense ratio	%	19.5	17.3	17.9	15.7	13.8	14.6
Combined operating ratio	%	98.3	98.6	85.8	94.2	94.3	91.9
Adjusted combined operating ratio <sup>2</sup>	%	85.6	88.3	88.0	—	—	—
Insurance profit margin	%	6.0	5.2	16.7	8.9	8.4	13.6

1 Adjusted for transactions to reinsure UK long tail liabilities.

2 Combined operating ratio adjusted to exclude the impact of changes in risk-free rates used to discount net outstanding claims. Management results were not reported in the first half of 2014 and prior.

### Premium income

Headline gross written premium fell 6% to \$2,508 million from \$2,659 million in the prior corresponding period, impacted by the significantly weaker GBP (sterling denominated business accounts for around 34% of European Operations' premium income).

On a constant currency basis, gross written and net earned premium decreased by 1%.

Premium renewal rates continued to deteriorate in most products and territories, resulting in an average reduction of 3.0% across our portfolios. On a positive note, there are signs that the rate pressure for QBE Re is moderating.

In addition to market competition we are continuing to experience premium pressures due to the effects of suppressed commodities pricing especially in the oil and gas sector. In order to mitigate some of the impact of reduced global premium on our top-line, two of our key strategic priorities are aimed at broadening our distribution footprint and enhancing our customer offering. As expected, we are seeing more growth opportunities from our extended distribution in Europe and Canada and it is pleasing to see more cross-selling activity across our entire customer base.

New business volumes continue to track well despite market conditions and reflect ongoing underwriting discipline and customer focus. We are utilising more sophisticated techniques (including data analytics) to target the right new business including far more effective cross-selling strategies, especially in the Retail division.

The retention ratio is slightly behind plan and prior period at 82.8%, principally as a result of the decision not to renew one of our largest and longstanding accounts due to unacceptable terms which impacted gross written premium by \$41 million.

## Gross earned premium by class of business

FOR THE HALF YEAR ENDED 30 JUNE	2016 %	2015 %
Commercial & domestic property	25.6	27.4
Public/product liability	20.3	20.8
Marine energy & aviation	14.9	14.8
Professional indemnity	14.0	14.2
Motor & motor casualty	12.6	11.4
Workers' compensation	5.2	6.0
Other	3.9	2.5
Financial & credit	1.8	1.5
Accident & health	1.6	1.3

## Claims expense

The net claims ratio benefited from positive prior accident year claims development of \$119 million or 7.6% of net earned premium, broadly consistent with the 8.4% of development reported in the prior corresponding period. Almost all of the favourable development came from the insurance divisions and was spread across several long and short tail portfolios.

The current accident year attritional claims ratio was broadly stable and continues to benefit from disciplined underwriting and our various claims initiatives.

The overall cost of large individual risk and catastrophe claims was in line with the prior corresponding period. Pleasingly, the cost of catastrophe claims was in line with expectations despite a marked increase in global catastrophe activity over the last six months following an especially benign 2015. Catastrophe events included earthquakes in Japan and Ecuador, wildfires in Alberta as well as UK storms and flooding in Continental Europe. While the cumulative cost of large individual risk claims was less than the particularly active prior corresponding period, it was above our planning assumptions reflecting a number of large individual risk claims within the marine, energy and liability portfolios.

Claims handling costs fell relative to the prior corresponding period reflecting improved claims department efficiency.

## Commission and expenses

The net commission ratio improved to 17.9% from 18.8% in the prior corresponding period.

Importantly, we have seen an improvement in the gross commission ratio reflecting the considerable efforts by all our underwriting teams as they try to resist the demands for more commission. The quality of our customer proposition enables us to focus on value to them rather than getting embroiled in commission only discussions.

Operating expenses have fallen further as a result of the expense reduction and operational efficiency plans commenced three years ago. The expense ratio in the most recent half improved to 17.3% from 17.9% in the prior corresponding period, with further improvement expected as a result of ongoing divisional and Group expense and efficiency initiatives.

## Strategic agenda and other developments

The management actions taken combined with the longer term strategies implemented over the last three years have been entirely focused on building a business that will be successful regardless of market conditions. The current market conditions, along with macroeconomic dynamics, will continue to challenge the industry so we need to remain committed to our underwriting discipline and wider strategic agenda.

We have made good progress putting the customer at the centre of our business. However, there is much more to do as we build out product capability across our geographies which will be supported by our leading risk solutions capability.

During the remainder of 2016, we will be focused on delivering our customer value proposition for claims. We are expanding our data science capability to support our underwriting teams in making more informed decisions and we recently hired our first Head of Data Science. We are also looking to extract significantly more value from our investment in analytical capability already embedded in the claims function. We have detailed action plans to both enhance operational efficiency and reduce expenses over the next 24 months, which are particularly important in these challenging market conditions.

We will continue to invest prudently to enhance our capability and remain committed to helping our colleagues achieve their ambitions in a dynamic and enjoyable environment.

Above all else, we will focus on underwriting discipline to preserve our margins.



# Australian & New Zealand Operations business review

“Although a sound headline result reflecting continued strong returns in our long tail and LMI portfolios, the significant increase in the attritional claims ratio is disappointing. We will implement necessary price increases, tighter policy terms and improved risk selection to restore short tail margins as soon as possible.”

## Pat Regan

Group Chief Financial Officer &  
Acting Chief Executive Officer • Australian & New Zealand Operations

Gross written premium US\$ million	Net earned premium US\$ million	Underwriting result US\$ million	Insurance profit (loss) US\$ million
<b>1,861</b>	<b>1,654</b>	<b>67</b>	<b>148</b>
⬇️ 3% from <sup>1</sup> 2015	⬇️ 1% from <sup>2</sup> 2015	⬇️ \$86M from 2015	⬇️ \$99M from 2015
		Combined operating ratio <sup>3</sup> <b>93.9%</b> (2015 90.7%)	Insurance profit margin <b>8.9%</b> (2015 14.8%)

## 2016 overview

Our business in Australia and New Zealand is built on solid foundations as evidenced by the division reporting a sound 2016 interim combined operating ratio of 93.9%<sup>3</sup>, despite a significant deterioration in the attritional claims ratio. Partly offsetting the increase in the attritional claims ratio, the result benefited from positive prior accident year claims development of \$83 million or 5.0% of net earned premium and the continued consistent earnings stream generated by our Lenders' Mortgage Insurance (LMI) business.

Three factors combined to drive an unacceptable increase in our attritional claims ratio: premium pricing pressure coupled with higher than normal claims inflation has impacted our short tail business; troubling claims trends in the NSW compulsory third party (CTP) scheme; and increased claims frequency and severity in our trade credit business. Each of the above issues is actionable as discussed overleaf. A combination of repricing and Government reform is expected to restore CTP margins in due course. A strategic review of our trade credit business has seen us increase pricing, withdraw limits and restructure our portfolio through cancellation and non-renewal. A combination of premium increases, tightened terms and conditions and improved risk selection will drive the remediation required on Australian short tail lines.

<sup>1</sup> Up 3% on a constant currency basis.

<sup>2</sup> Up 6% on a constant currency basis.

<sup>3</sup> Combined operating ratio adjusted to exclude the impact of changes in risk-free rates used to discount net outstanding claims.

## Operating and financial performance

### Underwriting performance

Australian & New Zealand Operations reported a combined operating ratio of 95.9%, up from 90.8% in the prior period, with relatively benign catastrophe experience and positive prior accident year claims development more than offset by an increase in frequency and severity of large individual risk claims and a substantial increase in attritional claims.

Excluding the impact of lower risk-free rates used to discount net outstanding claims, the combined operating ratio was 93.9% compared with 90.7% in the prior period.

Business mix changes aside, the attritional claims ratio deteriorated across a number of portfolios including NSW CTP, motor (commercial and personal), householders, commercial property and trade credit. Whilst there are legislative, economic and portfolio specific factors driving the deterioration in NSW CTP and trade credit, the significant deterioration in short tail classes reflects the cumulative impact of sustained pricing pressure coupled with increased claims inflation, including higher repair and replacement costs.

We will respond swiftly and firmly to restore margins through price increases, tightened terms and conditions and portfolio adjustments, and we expect favourable legislative amendments in the NSW CTP market as already noted.

Long tail classes such as liability and professional indemnity performed well, reflecting strong underwriting controls, risk selection and favourable prior accident year claims development.

Our LMI business continues to perform strongly on the back of relatively low unemployment and record low interest rates; however, premium levels have declined since peaking in 2014 thereby reducing the relative exposure to this class of business. Moreover, we have allowed for some cyclical moderation in underwriting margins relative to the prior period.

### Underwriting result

FOR THE HALF YEAR ENDED 30 JUNE		2016	2015	2014	2013	2012
Gross written premium	US\$M	1,861	1,928	2,275	2,517	2,489
Gross earned premium	US\$M	1,871	1,913	2,192	2,406	2,366
Net earned premium	US\$M	1,654	1,668	1,916	2,106	2,041
Net incurred claims	US\$M	1,120	1,050	1,134	1,238	1,267
Net commission	US\$M	250	235	267	293	268
Expenses	US\$M	217	230	274	343	337
Underwriting result	US\$M	67	153	241	232	169
Net claims ratio	%	67.7	62.9	59.2	58.8	62.1
Net commission ratio	%	15.1	14.1	13.9	13.9	13.2
Expense ratio	%	13.1	13.8	14.3	16.3	16.5
Combined operating ratio	%	95.9	90.8	87.4	89.0	91.8
Adjusted combined operating ratio <sup>1</sup>	%	93.9	90.7	—	—	—
Insurance profit margin	%	8.9	14.8	17.2	16.4	14.5

<sup>1</sup> Combined operating ratio adjusted to exclude the impact of changes in risk-free rates used to discount net outstanding claims. Management results were not reported in the first half of 2014 and prior.

### Premium income

Gross written premium fell 3% to \$1,861 million from \$1,928 million a year earlier, reflecting the weaker Australian dollar.

On a constant currency basis, gross written premium increased 3% due to growth across a number of portfolios.

The reinsurance ratio fell to 11.6% of gross earned premium from 12.8% in the prior period, reflecting savings on our reinsurance program including cancellation of the 25% quota share on our LMI portfolio (which was assumed by Equator Re). This followed the decision to purchase catastrophe stop loss reinsurance for the 2016 and 2017 underwriting years.

Net earned premium fell by 1% to \$1,654 million from \$1,668 million in the prior period. On a constant currency basis, net earned premium grew 6% driven by the increase in written premium and reduced reinsurance spend.

Premium rate movements were slightly better than anticipated, down on average by only 0.3% across the half (down 0.1% in Australia and 2.9% in New Zealand) compared with an average rate reduction of 2.1% in the prior period. June commercial renewals have shown evidence of positive rate movements. For renewable business, retention increased to 83.4% from 83.0% in the previous year.

## Gross earned premium by class of business

FOR THE HALF YEAR ENDED 30 JUNE

	2016 %	2015 %
Commercial & domestic property	34.2	33.5
Motor & motor casualty	24.8	23.0
Financial & credit	11.3	13.4
Public/product liability	7.8	8.7
Workers' compensation	7.6	7.0
Agriculture	4.8	5.0
Accident & health	4.2	3.8
Marine energy & aviation	2.8	3.1
Professional indemnity	2.3	2.3
Life	0.1	0.2

### Claims expense

The net claims ratio increased to 67.7% from 62.9% in the prior period, arising from a combination of the substantial deterioration in the attritional claims ratio coupled with the 2.0% adverse discount rate impact, partially offset by benign catastrophe claims experience and increased prior accident year reserve releases.

The increase in the attritional claims ratio includes the impact of the now well documented deterioration in NSW CTP claims frequency, an adverse mix impact (primarily due to growth in NSW CTP), increased claims frequency in trade credit and increased claims costs across a number of our short tail portfolios.

Attritional claims ratios in our short tail portfolios – motor, householders and property – have increased as a result of price competition combined with heightened claims inflation, including the rising cost of repair and replacement. Targeted remedial action, including premium rate increases and tightened terms and conditions, has already been, and will continue to be, taken to restore margins.

In the past 12 months, compound premium rate increases of approximately 15% have been applied to the NSW CTP portfolio. A combination of this and the proposed scheme reforms are expected to restore the portfolio to an acceptable return on capital by the end of 2017 while maintaining premium affordability.

The net cost of large individual risk and catastrophe claims fell to 5.5% from 9.0% previously, reflecting more benign catastrophe experience relative to the extremely active first half of 2015.

Our long tail portfolios continue to deliver strong results and contributed to \$83 million of prior accident year claims release compared with \$45 million in the prior period.

Risk-free rates used to discount net outstanding claims declined materially to end the half significantly below 31 December 2015 levels. This resulted in a \$33 million or 2.0% adverse impact on the net claims ratio compared with a negligible impact in the prior period.

### Commission and expenses

The commission ratio increased to 15.1% from 14.1% in the prior corresponding period, reflecting the loss of commission income following the sale of the agencies in April 2015 coupled with additional costs associated with the extension of the ANZ distribution agreement.

The expense ratio improved to 13.1% from 13.8% a year earlier with further expense savings partially offset by increased investment in technology including the successful implementation of the Guidewire system for our Direct and South Australian CTP portfolios, as well as our customer experience program. The Group Shared Services Centre continues to focus on operational excellence and there are a number of ongoing initiatives designed to deliver additional efficiencies and further enhance customer service levels.

### Strategic agenda and other developments

The fundamentals of our business remain in good shape as evidenced by the continued strong performance of our long tail classes and continued positive prior accident year claims development.

Following a period of healthy premium increases in 2011 to 2013, premium pricing in Australia has lagged claims inflation across a number of lines of business. These trends worsened through the first half and demanded action.

Across our short tail classes of business (property and motor) we are seeking minimum rate increases of 5% and have increased excesses and deductibles. There are some portfolios where we have little or no option but to exit if more meaningful price rises cannot be achieved. Our market leading position in Australian commercial insurance gives us confidence that we can achieve the level of portfolio remediation required.

Our trade credit and surety portfolio has suffered as a result of the macro-economic changes in the market place, most notably in certain industry classes such as construction and retail, which has led to a significant increase in both claims frequency and severity. Accordingly, we have reduced our credit limits, amended the scope of our underwriting (notably in Asia), increased rates and restricted our capacity for the more obvious economically vulnerable industries.

All of our remediation activities are under constant review and are being tracked against a benchmark to return each and every portfolio to acceptable levels of performance and profitability (reflected in the attritional claims ratio) throughout the balance of this year and into 2017.

We recently created the new role of Chief Underwriting Officer (CUO), which will have responsibility for underwriting, product, reinsurance and accreditation, creating alignment between these strategies and ensuring we are adhering to our global and divisional underwriting standards. The Group Chief Actuarial Officer has been appointed to the role with the express responsibility of overseeing the remediation plans.

# Emerging Markets business review

“Emerging Markets achieved solid underlying growth in the first half of 2016. In delivering on our strategic agenda, we continue to focus on the business lines with the highest potential for profitable growth and where QBE’s core strengths are best utilised.”

**David Fried**

Chief Executive Officer • Emerging Markets

Gross written premium US\$ million	Net earned premium US\$ million	Underwriting result US\$ million	Insurance profit (loss) US\$ million
<b>850</b>	<b>655</b>	<b>3</b>	<b>36</b>
↓ 9% from <sup>1</sup> 2015	↓ 12% from <sup>2</sup> 2015	↓ \$1M from 2015	↑ \$2M from 2015
		Combined operating ratio <sup>3</sup> <b>99.5%</b> (2015 99.5%)	Insurance profit margin <b>5.5%</b> (2015 4.6%)

All amounts in the above table exclude Argentine workers' compensation business.

## 2016 overview

Emerging Markets achieved gross written and net earned premium growth of 10% and 7% respectively on a constant currency basis. The division maintained its combined operating ratio at 99.5% even with the impacts of Cyclone Winston in Fiji in March and April's earthquake in Ecuador. The double-digit growth was a direct result of the continued implementation of the Emerging Markets profitable growth strategy.

Economic uncertainty translated into continued currency volatility, most notably in Argentina and Brazil. The slowdown in China also had a negative impact on trade and the corresponding demand for commercial insurance cover in areas like marine. Overall, emerging market economies experienced flat or falling premium rates during the period.

Despite economic challenges, Latin America recorded gross written premium growth of 16% on a constant currency basis, with the strong growth partly attributable to a change in portfolio focus consistent with the emerging markets strategy. Several markets in Asia – notably Indonesia, Malaysia, the Philippines, Vietnam and Papua New Guinea – recorded underlying growth ranging from 7% to 32%, while the Pacific business averaged growth of 10%. This geographic diversity helped offset economic-related challenges in the larger markets of Hong Kong and Singapore.

The long-term outlook for emerging markets remains positive and will continue to drive premium growth. Favourable demographics, a growing middle class and high net worth population, further infrastructure investment and increasing intra-regional trade flows will lead to further insurance market expansion and increased market penetration.

1 Up 10% on a constant currency basis.

2 Up 7% on a constant currency basis.

3 Combined operating ratio adjusted to exclude the impact of changes in risk-free rates used to discount net outstanding claims.



## Operating and financial performance

### Underwriting performance

In the first half of 2016, reported gross written and net earned premium decreased by 9% and 12% respectively; however, on a constant currency basis gross written and net earned premium increased by 10% and 7% respectively. The lower level of net earned premium growth reflects the gradual shift in the business mix towards specialty lines requiring higher levels of reinsurance as well as increased catastrophe reinsurance costs following Cyclone Pam in 2015.

Even with material impacts from Cyclone Winston in Fiji, the earthquake in Ecuador and also a significant flood in Chile, Emerging Markets recorded a stable combined operating ratio of 99.5%, with an underwriting profit of \$3 million.

Underwriting remediation activities continued resulting in a material improvement in the attritional claims ratio in Latin America as well as lower large risk claims in Asia Pacific. In Colombia, the profitability of the SOAT portfolio improved further reflecting a strengthened governance structure and the benefits of insights provided by our increased utilisation of data analytics.

### Underwriting result

FOR THE HALF YEAR ENDED 30 JUNE		2016	2015 <sup>1</sup>	2014 <sup>1</sup>	2013 <sup>1</sup>	2012 <sup>1</sup>
Gross written premium	US\$M	850	929	896	987	635
Gross earned premium	US\$M	793	864	855	860	596
Net earned premium	US\$M	655	741	718	712	473
Net incurred claims	US\$M	359	417	432	405	251
Net commission	US\$M	152	170	173	171	116
Expenses	US\$M	141	150	130	127	84
Underwriting result	US\$M	3	4	(17)	9	22
Net claims ratio	%	54.8	56.4	60.2	56.9	53.1
Net commission ratio	%	23.2	22.9	24.1	24.0	24.5
Expense ratio	%	21.5	20.2	18.1	17.8	17.8
Combined operating ratio	%	99.5	99.5	102.4	98.7	95.3
Adjusted combined operating ratio <sup>2</sup>	%	99.5	99.5	—	—	—
Insurance profit margin	%	5.5	4.6	1.5	3.1	6.1

<sup>1</sup> Excludes Argentine workers' compensation business which was sold in 2015.

<sup>2</sup> Combined operating ratio adjusted to exclude the impact of changes in risk-free rates used to discount net outstanding claims. Management results were not reported in the first half of 2014 and prior.

### Premium income

As previously noted, Emerging Markets maintained its solid growth momentum in the first half of 2016.

Asia Pacific recorded a 1% decrease in gross written premium to \$419 million due to the stronger US dollar; however, gross written premium increased 2% on a constant currency basis. Several markets – including Indonesia, Malaysia, the Philippines, Vietnam and Papua New Guinea – enjoyed strong performances, helping to offset challenging conditions in Hong Kong and Singapore. Pricing continued to soften in Asia with premium reductions averaging 3.0% due to surplus industry capacity. Premium rates remained flat in the Pacific.

Despite the competitive environment, QBE retained its leading positions in Hong Kong (ranked 1st) and Singapore (ranked 6th) and also remained the leading general insurer in Fiji, Papua New Guinea, Solomon Islands and Vanuatu. In Hong Kong, QBE won a major multi-year contract providing workers' compensation coverage for the Mass Transit Railway's Express Rail Link project and also entered a 10-year exclusive general insurance distribution agreement with Manulife.

In Latin America, the stronger US dollar also adversely impacted headline gross written premium, which declined 15% to \$431 million. Gross written premium grew 16% on a constant currency basis, driven mainly by Argentina and Brazil which recorded top-line growth of 41% and 32% respectively. A deliberate shift in the business mix towards writing more commercial, specialty and SME risks contributed to the strong underlying growth.

In Argentina, QBE ranked first (18% market share) in cargo insurance while in Ecuador, QBE ranked first (8%) in property insurance and is also the second largest (12%) private general insurer in the country. Inter-divisional collaboration is delivering increasing benefits in Latin America with assistance from European Operations helping to secure accounts with two Colombian ports in the Bay of Cartagena, one of the largest trade hubs in the region. We further expanded affinity partnerships during the half, including 40 new accounts in Mexico and a partnership with Brazilian retailer Lebes. We also maintained our leading position in the Brazilian travel sector, where we have a market share of 43% through partnerships with travel assistance operators.

## Gross earned premium by class of business

FOR THE HALF YEAR ENDED 30 JUNE

	2016 %	2015 %
Motor & motor casualty	29.0	27.5
Commercial & domestic property	28.3	25.5
Marine energy & aviation	11.9	9.0
Workers' compensation	9.6	19.0
Accident & health	8.4	5.2
Public/product liability	5.2	5.8
Professional indemnity	2.5	3.3
Other	2.0	1.9
Agriculture	1.7	1.4
Financial & credit	1.4	1.4

### Claims expense

Pleasingly, the net claims ratio improved to 54.8% from 56.4% in the prior corresponding period, mainly reflecting a 2.6% improvement in the attritional claims ratio coupled with better large individual risk claims experience in Asia Pacific.

In March, Cyclone Winston caused tremendous devastation in Fiji, resulting in the QBE Group receiving claims totalling approximately \$29 million with a \$12 million net impact to the Asia Pacific region. Following April's earthquake in Ecuador, QBE Group received around 12,000 claims totalling approximately \$65 million, including a \$13 million net impact to Latin America. More than 90% of these claims were closed and paid by 30 June 2016. In April, flooding in the business district of Chile's capital, Santiago, resulted in a further \$6 million net claim impact.

Emerging Market's attritional claims ratio improved by 2.6% relative to the prior corresponding period, largely reflecting improvement in Latin America on the back of further remediation of Colombian SOAT coupled with business mix changes.

Prior accident year claims development was 2.6% of net earned premium compared with 2.0% in the prior period, reflecting favourable trends emerging in Argentina, Singapore and Malaysia.

### Commission and expenses

The net commission ratio increased slightly to 23.2% from 22.9% but remained stable against full year 2015 figures reflecting changes in portfolio mix (including growth in Brazilian travel insurance partially offset by further downsizing of Colombian SOAT) as part of the ongoing implementation of the profitable growth strategy.

The net underwriting expense ratio was also slightly higher at 21.5% in the first half of 2016 compared with 20.2% in the prior corresponding period. This was due to continued investment to support the long-term growth strategy – with a particular emphasis on technology and a strengthened governance framework. Inflationary pressures in Latin America (most notably in Argentina) and investment initiatives to support business development were also contributing factors. Relative to the prior period, the rate of expense growth has reduced significantly compared to 2015.

## Strategic agenda and other developments

Emerging Markets' double-digit growth aspiration remains as we continue to implement the Emerging Markets profitable growth strategy. Our focus is on four areas of business – specialty, commercial, SME and personal lines – where we see the highest potential for profitable growth and also where the QBE Group's core strengths are best utilised.

We also aspire to be the leading provider of technology-driven solutions across the SME line of business. QBE Qnect, an innovative online insurance portal, was originally introduced in Hong Kong and Singapore in 2014. With rising demand elsewhere, the platform has already been extended to Argentina and will soon be launched in Colombia. We have also introduced a global initiative to further refine the delivery of our comprehensive suite of products for SMEs.

In personal lines, we are aiming to enter more strategic partnerships in both bancassurance and affinity in order to access target customers without building our own mass retail distribution network. Through partnerships with the country's three largest travel assistance companies, QBE is now the leading travel insurance provider in Brazil. Additionally, we recently entered into a 10 year exclusive distribution partnership with Manulife in Hong Kong. This partnership serves to further complement Manulife's product offerings while also reinforcing QBE's leading market position in Hong Kong.

To achieve all of these ambitions, we continue to enhance productivity, efficiency and consistency through implementation of a single operating model across Emerging Markets that is aligned with the Group's operating model. Accordingly, some administrative, claims, human resources and finance services are being relocated to the QBE Group's Shared Services Centre (GSSC) in the Philippines.

We also continue to strengthen underwriting capabilities in our two regional centres of excellence in Singapore and Miami, with a focus on both winning and retaining profitable and high-quality business. Building on our customer-centric approach, we are also utilising technology and working with intermediaries and end-customers to mitigate potential risk exposures.

# Equator Re business review

“Equator Re plays a pivotal role in the Group’s strategy by supporting divisional growth ambitions and facilitating the optimisation of the Group’s reinsurance and capital requirements.”

**Jim Fiore**

Group Chief Reinsurance Officer & President • Equator Re

Gross written premium US\$ million	Net earned premium US\$ million	Underwriting result US\$ million	Insurance profit US\$ million
<b>1,125</b>	<b>197</b>	<b>59</b>	<b>74</b>
⬆ 15% from 2015	⬆ 8% from 2015	⬆ \$2M from 2015	⬇ \$13M from 2015
		Combined operating ratio <sup>1</sup> <b>63.5%</b> (2015 70.8%)	Insurance profit margin <b>37.6%</b> (2015 47.8%)

## 2016 overview

The first half of 2016 has seen further expansion of Equator’s role as the Group’s reinsurance solution provider. During 2015, the Group’s external excess of loss reinsurance protections were purchased on Equator’s account with Equator then providing bespoke solutions catering to the individual needs of each division. In 2016, Equator expanded this approach to include the Group’s external large risk and catastrophe aggregate contract (GLRC).

By writing the GLRC on its own account, Equator has been able to structure more tailored aggregate solutions which reflect the risk appetites, limits and retentions required by each division. In doing so, Equator has removed the potential volatility that participation in a global program would otherwise expose each division to, thereby assisting each division to better manage achievement of its business plan. Whilst this approach does not result in additional volatility to the Group, it does generate more volatility within Equator’s results. This is consistent with Equator’s pivotal role in supporting the optimisation of the Group’s capital and reinsurance needs and, in doing so, facilitating the Group strategy.

On the core catastrophe and per risk programs, Equator’s book renewed largely as expiring, with two exceptions. In Emerging Markets we were able to combine covers previously provided to Asia-Pacific and Latin America separately, generating net reinsurance savings for the division in the process. Secondly, reductions in catastrophe exposure, program restructuring and the removal of pre-paid reinstatements generated premium savings for North America.

Our proportional book continues to grow in support of North America’s Specialty business and via the participation in North America’s crop hail and MPCl quota share programs.

<sup>1</sup> Combined operating ratio adjusted to exclude the impact of changes in risk-free rates used to discount net outstanding claims.

## Operating and financial performance

### Underwriting performance

The first half of 2016 benefited from relatively benign catastrophe experience, with the Ecuador earthquake and Cyclone Winston being the only events to have impacted Equator, resulting in a combined operating ratio of 70.1%. This strong performance also reflects the changing nature of Equator's portfolio, which is increasingly exposed to aggregate claims experience rather than purely per risk excess of loss events.

The underwriting and actuarial team continue to work collaboratively with our divisional partners to assess new business opportunities and develop reinsurance solutions which enable divisions to stay relevant in their chosen markets and ensure the most effective capital utilisation globally, ultimately resulting in an optimal return for shareholders.

### Underwriting result

FOR THE HALF YEAR ENDED 30 JUNE		2016	2015	2014	2013	2012
Gross written premium	US\$M	1,125	976	607	775	796
Gross earned premium	US\$M	583	485	404	417	412
Net earned premium	US\$M	197	182	280	266	273
Net incurred claims	US\$M	116	106	267	197	246
Net commission	US\$M	18	13	5	11	9
Expenses	US\$M	4	6	4	4	4
Underwriting result	US\$M	59	57	4	54	14
Net claims ratio	%	58.9	58.2	95.4	74.0	90.2
Net commission ratio	%	9.1	7.1	1.8	4.1	3.5
Expense ratio	%	2.0	3.3	1.4	1.7	1.3
Combined operating ratio	%	70.1	68.6	98.6	79.8	95.0
Adjusted combined operating ratio <sup>1</sup>	%	63.5	70.8	—	—	—
Insurance profit margin	%	37.6	47.8	9.0	21.8	14.5

<sup>1</sup> Combined operating ratio adjusted to exclude the impact of changes in risk-free rates used to discount net outstanding claims. Management results were not reported in the first half of 2014 and prior.

### Premium income

Gross written premium of \$1,125 million is 15% higher than the prior corresponding period and reflects the ongoing evolution in the protections Equator provides to the operating divisions.

Net earned premium was \$197 million, up 8% relative to the prior corresponding period, with growth more subdued than the top line reflecting additional reinsurance costs incurred on the GLRC.

The reinsurance expense ratio increased to 66.2% of gross earned premium from 62.5% in the prior corresponding period, reflecting the assumption of 100% of the external GLRC to facilitate the provision of bespoke aggregate protection for large individual risk and catastrophe claims to each of QBE's divisions. Excluding the added cost of the GLRC, Equator's reinsurance spend was broadly in line with the prior period, with material reductions in the catastrophe excess of loss program being offset by two years of earnings on the risk excess of loss program which was first purchased by Equator in 2015.

### Claims expense

The first half of 2016 benefited from an exceptionally low claims ratio of 58.9%, in line with a similarly strong performance in the prior corresponding period; however, the factors driving the claims ratio differ materially year on year.

Both 2016 and 2015 benefited from relatively benign large individual risk and catastrophe experience, albeit 2015 was even more benign than the current year. Material claims during the first half of 2016 included the earthquake in Ecuador, Cyclone Winston in Fiji and several trade credit losses, all of which were well within allowances.

The significant growth in our pro rata book, particularly with respect to North American Specialty and Crop, has naturally driven an increase in Equator Re's attritional claims ratio to 18.8%, compared with 2.5% in the prior period.

Equator Re enjoyed \$34 million of prior accident year claims releases compared with \$51 million of adverse development in the prior period.

The underwriting result also included a \$13 million adverse impact from lower risk free rates used to discount net outstanding claims liabilities compared with a \$4 million benefit in the prior year and a \$34 million strengthening of risk margins compared with a \$15 million strengthening in the prior year.



## Commission and expenses

The combined commission and expense ratio increased slightly to 11.1% from 10.4% in the prior corresponding period.

The commission ratio increased to 9.1% from 7.1% previously due to increased proportional business which attracts higher commission than excess of loss programs, although the impact will soften somewhat as premium is earned across the remainder of 2016.

The expense ratio improved to 2.0% compared with 3.3% a year earlier, largely due to the timing of costs related to the transition of functions in 2015 and a delay in filling vacant roles in 2016. In response to our growing service offering we continue to build out our capabilities in Bermuda with a number of new positions created and filled. Whilst this additional head count has not yet impacted expenses materially, the full year budget does allow for an overall increase in operating costs beyond the first half run rate to reflect these additional resources. We expect full year expenses to be in line with business plan.

## Strategic agenda and other developments

The Group has a stated objective of growing our presence in the multinational market. During the second half of 2016, Equator Re will be central to this growth initiative; it will act as the internal reinsurance vehicle to facilitate the flow of premium, underwriting risk and cash between local servicing offices (where policies are issued) and the QBE producing office.

Equator has expanded the size and capabilities of its pricing and capital modelling team and has embarked on a project to review the capital deployed around the Group. Working with Group and the divisions, Equator will develop reinsurance solutions that reduce divisional capital requirements thus improving the fungibility and accessibility of that capital globally. Whilst this work is in its early stages, this is a focus for the second half of 2016 as we consider our 2017 product offering.

As part of a Solvency II equivalence program, the Bermudan regulatory environment is undergoing some change. We are well prepared for these changes and do not expect any significant impact from a move to an economic balance sheet.

# Divisional outlook for 2016<sup>1,2</sup>

## North American Operations

2016 target full year GWP:

**US\$4.5billion**

2016 target full year NEP:

**US\$3.5billion**

In the second half of 2016, we will continue to execute on building a true national platform. We have established field offices in three major geographies led by highly respected and recognised industry executives with the objective of managing our underwriting pipeline, cultivating and expanding trading partners and aligning resources to uncover new cross enterprise opportunities.

By executing on our claims, operations and underwriting initiatives while remaining focused on keeping our customers and employees at the centre of everything that we do, we are confident North America can improve its 2016 operating ratios. The reset of our Standard Lines business, growth of our Specialty franchise and the leverage and diversity our world class Crop and Reinsurance businesses gives us confidence we can deliver on our longer term goal of sustaining a mid-90s combined operating ratio.

## European Operations

2016 target full year GWP:

**US\$4.1billion**

2016 target full year NEP:

**US\$3.2billion**

The reduction in our full year premium in reporting currency is entirely due to the reduction in the value of sterling following the UK referendum.

We remain focused on our performance and strategic agenda whilst at the same time ensuring that we effectively manage any impact from the UK referendum. In times of uncertainty we will be strong and visible leaders for our customers and colleagues.

An example of real change in the UK is the new Insurance Act which came into force on 12 August 2016. This is the biggest change in insurance law for over a century. We have prepared well for this change and all our teams are ready and willing to help our customers.

## Australian & New Zealand Operations

2016 target full year GWP:

**US\$3.7billion**

2016 target full year NEP:

**US\$3.3billion**

We have implemented management changes which we believe are essential to return the business to the performance levels our shareholders expect.

With immediate effect the Group Chief Financial Officer, Pat Regan, will take responsibility for the Australian & New Zealand business whilst we undertake a search for a permanent Chief Executive Officer for the division.

We believe this change of leadership, along with the increased near-term focus on tight management of underwriting performance and cost control, will deliver on the division's potential in the current environment and will set us up for future success.

## Emerging Markets

2016 target full year GWP:

**US\$1.6billion**

2016 target full year NEP:

**US\$1.3billion**

The outlook remains positive despite short-term economic challenges.

In Asia Pacific, GDP is forecast to grow by around 6% this year and next. The creation of the ASEAN Economic Community and China's 'One Belt, One Road' plans should help trade and infrastructure investment, with positive implications for insurance demand.

In Latin America, GDP growth is expected to rebound to about 2% in 2017. In Argentina and Brazil, the economic and political environment is showing signs of improvement, which could have a positive impact if sustained.

We continue to develop inter-regional synergies, with the leadership team providing oversight for underwriting, distribution and claims.

I would like to thank our employees for their contribution to a very solid first half result and also our valued partners for their continued support.

## Equator Re

2016 target full year NEP:

**US\$410million**

We continue to work with the divisions to develop solutions to address their capital and exposure management needs. Given the diversified nature of Equator's portfolio, we have the capacity to offer significant protections in some of the Group's targeted growth areas without generating a corresponding increase in capital requirements. This will be our focus for the remainder of 2016 as we enter the renewal cycle.

With a largely 1 January renewal season, we do not expect to write significant volumes of business in the remainder of 2016.

Regardless of catastrophe experience, we are confident that the changes we have implemented during 2016 will deliver a strong result for our divisional partners and the Group overall.

- 1 Premium targets are based on assumed average foreign exchange rates relative to the US dollar as follows: AUD 0.72; GBP 1.36; and EUR 1.10.
- 2 Excludes M&LS gross written premium that is 100% reinsured to National General. Nil impact on net earned premium.

# Directors' Report

FOR THE HALF YEAR ENDED 30 JUNE 2016

Your directors present their report on QBE Insurance Group Limited and the entities it controlled at the end of, or during, the half year ended 30 June 2016.

## Directors

The following directors held office during the half year and up to the date of this report:

Marty Becker (Chairman)  
 Stephen Fitzgerald  
 John M Green (Deputy Chairman)  
 Margaret Leung  
 John Neal  
 Sir Brian Pomeroy  
 Patrick Regan  
 Jann Skinner  
 Rolf Tolle (appointed 11 March 2016)

## Consolidated results

FOR THE HALF YEAR ENDED	STATUTORY RESULT	
	30 JUNE 2016	30 JUNE 2015
	US\$M	US\$M
Gross written premium	8,107	8,692
Gross earned premium revenue	6,876	7,293
Net earned premium	5,615	6,229
Net claims expense	(3,637)	(3,727)
Net commission	(993)	(1,073)
Underwriting and other expenses	(931)	(1,134)
Underwriting result	54	295
Net investment income on policyholders' funds	272	241
Insurance profit	326	536
Net investment income on shareholders' funds	165	145
Financing and other costs	(125)	(127)
Gains on sale of entities	—	150
Amortisation and impairment of intangibles	(19)	(25)
Profit before income tax	347	679
Income tax expense	(80)	(189)
Profit after income tax	267	490
Net profit attributable to non-controlling interests	(2)	(2)
Net profit after income tax	265	488

## Result

Net profit after tax for the period to 30 June 2016 was \$265 million, down from a profit of \$488 million for the same period last year.

Net earned premium of \$5,615 million was down 10% compared with the same period last year. The decrease principally reflects the disposal of our Argentine workers' compensation and North American Mortgage & Lender Services (M&LS) businesses in the second half of 2015 and a higher reinsurance expense mainly due to the reinsurance of long tail liabilities in European Operations. The overall reinsurance impact was broadly profit neutral with reinsurance expense of \$176 million offset by recoveries of \$178 million.

The Group's underwriting result was a profit of \$54 million compared with a profit of \$295 million last year, reflecting a combined operating ratio of 99.0% compared with 95.3%. Net claims expense was impacted by a material reduction in risk-free rates used to discount claims liabilities (\$283 million or 5.0% of net earned premium) and the reinsurance recovery mentioned above. The combined commission and expense ratio was down compared with the same period last year (34.3% compared with 35.4%) primarily due to the benefit of expense initiatives and the disposal of our high cost base M&LS business.

Excluding the impact of lower risk-free rates used to discount claims liabilities, the statutory combined operating ratio would have been 94.0%, at the lower end of our target range of 94%-95% advised to the market in February 2016.

Net investment income was \$437 million compared with \$386 million in the same period last year, impacted by the lower interest rate environment. Fair value gains on the fixed income book due to recent market volatility, partly offset by modest fair value losses on growth assets, and foreign exchange gains benefited the result compared with the prior period.

The prior year result benefited from gains of \$150 million mainly relating to the disposal of our US and Australian agency businesses.

The tax rate was 23% of net profit, down from 28%, reflecting the mix of corporate tax rates in the countries in which QBE operates.

## Dividends

The directors are pleased to announce an interim dividend of 21 Australian cents per share for the period ended 30 June 2016 compared with 20 Australian cents per share for the period ended 30 June 2015. The interim dividend will be franked at 50%. The total dividend payout is A\$288 million compared with an interim dividend payout of A\$274 million in 2015.

Our objective is to deliver a stable and growing dividend to our shareholders. Our current dividend policy sets the full year dividend payout ratio at up to 65% of cash profit commencing with the 2016 interim dividend.

## Operating and financial review

Information on the Group's results, operations, business strategies, prospects and financial position is set out on pages 4 to 41 of this half year report.

## Outstanding claims provision

The net central estimate of outstanding claims is determined by the Group Chief Actuary after consultation with internal actuaries at 30 June and both internal and external actuaries at the 31 December balance date. The assessment takes into account the statistical analysis of past claims, allowance for claims incurred but not reported, reinsurance and other recoveries and future interest and inflation factors.

As in previous years, the directors consider that substantial risk margins are required over the actuarial central estimate to mitigate the inherent uncertainty in the central estimate. The probability of adequacy of the outstanding claims provision at 30 June 2016 was 89.0%, unchanged from 89.0% at 31 December 2015. The APRA prudential standards provide a capital credit for outstanding claims in excess of a probability of adequacy of 75%.

## Material business risks

As a global insurance and reinsurance business, QBE is subject to a substantial variety of business risks. The Board believes that effective management of these risks is critical to delivering value for QBE's stakeholders. It is QBE's policy to adopt a rigorous approach to managing risk throughout the Group. Risk management is a continuous process and an integral part of QBE's governance structure, broader business processes and, most importantly, culture.

Some of the material business risks that QBE faces include strategic risk, insurance risk, credit risk, market risk, liquidity risk and operational risk. Explanations of these risks and their mitigations are set out in more detail in note 4 to the Group's financial statements for the year ended 31 December 2015, which we recommend you to read. Further details of how QBE manages risk are set out in the Chief Risk Officer's Report in the annual report and that part of the Corporate Governance Statement in respect of ASX CGC Principle 7: Recognise and Manage Risk.

A recent and topical example of the risks facing QBE is the result of the UK referendum regarding ongoing membership of the European Union (Brexit) which saw a majority of voters in favour of leaving the European Union. QBE has been planning for this possible outcome for some time. As such, we do not anticipate any material impact on our day to day insurance operations although we will closely monitor developments in this area.

The Corporate Governance Statement is available on the QBE website at [www.qbe.com](http://www.qbe.com).

Commentary on significant judgements and estimates impacting the 30 June result and balance sheet, with particular emphasis on the limited headroom in relation to goodwill in our North American operations, is included in note 1.2 to the financial statements for the half year ended 30 June 2016.

## Events after the balance sheet date

The sterling capital securities were called on 18 July 2016. Further detail is provided in note 4.1 to the financial statements.

In response to the foreign exchange volatility created by the result of the Brexit vote, in early July 2016 the Group hedged its sterling net investment in foreign operations. See note 4.2 to the financial statements.

Other than as identified, the directors are not aware of any matter or circumstance that has arisen since 30 June 2016 that has significantly affected, or may significantly affect, the Group's operations, the results of those operations and the Group's state of affairs in future financial periods.

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## Directors' Report CONTINUED

FOR THE HALF YEAR ENDED 30 JUNE 2016

### Auditor's independence declaration

A copy of the auditor's independence declaration as required under section 307C of the *Corporations Act 2001* is set out on page 45.

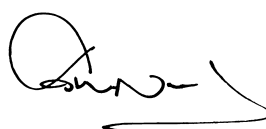
### Rounding of amounts

The company is of a kind referred to in the *ASIC Corporations (Rounding in Financial/Directors' Reports) Instrument 2016/191*. Amounts have been rounded off in the Directors' Report to the nearest million dollars or, in certain cases, to the nearest thousand dollars in accordance with that instrument.

Signed in SYDNEY on 17 August 2016 in accordance with a resolution of the directors.



WM Becker  
Director



JD Neal  
Director



# Auditor's independence declaration

FOR THE HALF YEAR ENDED 30 JUNE 2016

## Auditor's independence declaration for the half year ended 30 June 2016

As lead auditor for the review of QBE Insurance Group Limited for the half year ended 30 June 2016, I declare that to the best of my knowledge and belief, there have been:

- (a) no contraventions of the auditor independence requirements of the *Corporations Act 2001* in relation to the review; and
- (b) no contraventions of any applicable code of professional conduct in relation to the review.

This declaration is in respect of QBE Insurance Group Limited and the entities it controlled during the period.



RJ Clark  
**Partner, PricewaterhouseCoopers**

Sydney  
17 August 2016

# Consolidated statement of comprehensive income

FOR THE HALF YEAR ENDED 30 JUNE 2016

	NOTE	30 JUNE 2016 US\$M	30 JUNE 2015 US\$M
Gross written premium		8,107	8,692
Unearned premium movement		(1,231)	(1,399)
Gross earned premium revenue	2.1	6,876	7,293
Outward reinsurance premium		(1,577)	(2,484)
Deferred reinsurance premium movement		316	1,420
Outward reinsurance premium expense		(1,261)	(1,064)
Net earned premium (a)		5,615	6,229
Gross claims expense	2.2	(4,486)	(4,197)
Reinsurance and other recoveries revenue	2.2	849	470
Net claims expense (b)	2.2	(3,637)	(3,727)
Gross commission expense		(1,158)	(1,238)
Reinsurance commission revenue	2.1	165	165
Net commission (c)		(993)	(1,073)
Underwriting and other expenses (d)		(931)	(1,134)
<b>Underwriting result (a)+(b)+(c)+(d)</b>		<b>54</b>	<b>295</b>
Investment and other income – policyholders' funds	3.1	279	250
Investment expenses – policyholders' funds	3.1	(7)	(9)
<b>Insurance profit</b>		<b>326</b>	<b>536</b>
Investment and other income – shareholders' funds	3.1	169	150
Investment expenses – shareholders' funds	3.1	(4)	(5)
Financing and other costs		(125)	(127)
Gains on sale of entities		–	150
Amortisation and impairment of intangibles		(19)	(25)
Profit before income tax		347	679
Income tax expense		(80)	(189)
Profit after income tax		267	490
<b>Other comprehensive income</b>			
<i>Items that may be reclassified to profit or loss</i>			
Net movement in foreign currency translation reserve		(307)	119
Net movement in cash flow hedges		(4)	–
Income tax credit relating to these components of other comprehensive income		5	26
<i>Items that will not be reclassified to profit or loss</i>			
Losses on remeasurement of defined benefit superannuation plans		(25)	(15)
Income tax credit (expense) relating to this component of other comprehensive income		1	(1)
Other comprehensive income after income tax		(330)	129
Total comprehensive income after income tax		(63)	619
<b>Profit after income tax attributable to:</b>			
Ordinary equity holders of the company		265	488
Non-controlling interests		2	2
		267	490
<b>Total comprehensive income after income tax attributable to:</b>			
Ordinary equity holders of the company		(65)	617
Non-controlling interests		2	2
		(63)	619

	NOTE	30 JUNE 2016 US CENTS	30 JUNE 2015 US CENTS
<b>EARNINGS PER SHARE FOR PROFIT AFTER INCOME TAX ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE COMPANY</b>			
Basic earnings per share	4.5	19.3	35.8
Diluted earnings per share	4.5	19.2	35.5

The consolidated statement of comprehensive income above should be read in conjunction with the accompanying notes.

# Consolidated balance sheet

AS AT 30 JUNE 2016

	NOTE	30 JUNE 2016 US\$M	31 DECEMBER 2015 US\$M
<b>Assets</b>			
Cash and cash equivalents		763	662
Investments	3.2	24,965	26,032
Derivative financial instruments	4.2	51	33
Trade and other receivables		6,316	4,950
Current tax assets		75	46
Deferred insurance costs		2,899	2,538
Reinsurance and other recoveries on outstanding claims	2.3	3,512	3,204
Other assets		6	6
Defined benefit plan surpluses		38	44
Property, plant and equipment		247	263
Deferred tax assets		767	767
Investment properties		13	14
Investment in associates		29	13
Intangible assets		3,592	3,604
<b>Total assets</b>		<b>43,273</b>	<b>42,176</b>
<b>Liabilities</b>			
Derivative financial instruments	4.2	121	35
Trade and other payables		2,060	2,101
Current tax liabilities		81	43
Unearned premium		8,074	7,006
Outstanding claims	2.3	18,803	18,583
Provisions		81	76
Defined benefit plan deficits		90	67
Deferred tax liabilities		97	176
Borrowings	4.1	3,482	3,529
<b>Total liabilities</b>		<b>32,889</b>	<b>31,616</b>
<b>Net assets</b>		<b>10,384</b>	<b>10,560</b>
<b>Equity</b>			
Share capital	4.3	8,638	8,440
Treasury shares held in trust		(1)	–
Reserves		(1,553)	(1,248)
Retained profits		3,241	3,313
<b>Shareholders' funds</b>		<b>10,325</b>	<b>10,505</b>
Non-controlling interests		59	55
<b>Total equity</b>		<b>10,384</b>	<b>10,560</b>

The consolidated balance sheet above should be read in conjunction with the accompanying notes.

# Consolidated statement of changes in equity

FOR THE HALF YEAR ENDED 30 JUNE 2016

	SHARE CAPITAL US\$M	TREASURY SHARES HELD IN TRUST US\$M	RESERVES US\$M	RETAINED PROFITS US\$M	SHARE- HOLDERS' FUNDS US\$M	NON- CONTROLLING INTERESTS US\$M	TOTAL EQUITY US\$M
<b>2016</b>							
As at 1 January	8,440	–	(1,248)	3,313	10,505	55	10,560
Profit after income tax	–	–	–	265	265	2	267
Other comprehensive income	–	–	(306)	(24)	(330)	–	(330)
Total comprehensive income	–	–	(306)	241	(65)	2	(63)
<b>Transactions with owners in their capacity as owners</b>							
Shares acquired and held in trust	–	(38)	–	–	(38)	–	(38)
Share-based payment expense	–	–	40	–	40	–	40
Shares vested and/or released to participants	–	37	(37)	–	–	–	–
Contributions of equity, net of transaction costs and tax	1	–	–	–	1	–	1
Reclassification on disposal of owner occupied property	–	–	(4)	4	–	–	–
Dividends paid on ordinary shares	–	–	–	(317)	(317)	–	(317)
Foreign exchange movement	197	–	2	–	199	2	201
As at 30 June	8,638	(1)	(1,553)	3,241	10,325	59	10,384

	SHARE CAPITAL US\$M	TREASURY SHARES HELD IN TRUST US\$M	RESERVES US\$M	RETAINED PROFITS US\$M	SHARE- HOLDERS' FUNDS US\$M	NON- CONTROLLING INTERESTS US\$M	TOTAL EQUITY US\$M
<b>2015</b>							
As at 1 January	9,391	–	(1,405)	3,044	11,030	52	11,082
Profit after income tax	–	–	–	488	488	2	490
Other comprehensive income	–	–	145	(16)	129	–	129
Total comprehensive income	–	–	145	472	617	2	619
<b>Transactions with owners in their capacity as owners</b>							
Shares acquired and held in trust	–	(18)	–	–	(18)	–	(18)
Share-based payment expense	–	–	29	–	29	–	29
Contribution of equity from non-controlling interests	–	–	–	–	–	2	2
Shares vested and/or released to participants	–	18	(18)	–	–	–	–
Contributions of equity, net of transaction costs and tax	41	–	–	–	41	–	41
Reclassification of premium on purchase of non-controlling interests	–	–	16	(16)	–	–	–
Dividends paid on ordinary shares	–	–	–	(228)	(228)	–	(228)
Dividend reinvestment under Bonus Share Plan	–	–	–	3	3	–	3
Foreign exchange movement	(519)	–	(6)	–	(525)	–	(525)
As at 30 June	8,913	–	(1,239)	3,275	10,949	56	11,005

The consolidated statement of changes in equity above should be read in conjunction with the accompanying notes.

# Consolidated statement of cash flows

FOR THE HALF YEAR ENDED 30 JUNE 2016

	30 JUNE 2016 US\$M	30 JUNE 2015 US\$M
<b>Operating activities</b>		
Premium received	6,638	7,292
Reinsurance and other recoveries received	610	727
Outward reinsurance paid	(1,399)	(1,663)
Claims paid	(3,701)	(4,212)
Acquisition and other underwriting costs paid	(1,858)	(2,171)
Interest received	220	269
Dividends received	24	40
Other operating income	14	28
Other operating payments	(90)	(136)
Interest paid	(121)	(123)
Income taxes paid	(121)	(192)
Net cash flows from operating activities	216	(141)
<b>Investing activities</b>		
Proceeds on sale of growth assets	2,068	2,322
Payment for purchase of growth assets	(1,223)	(3,313)
Payments for foreign exchange transactions	(7)	(129)
Net (payments for purchase) proceeds on sale of interest bearing financial assets	(620)	1,197
Payment for purchase of entities (net of cash acquired)	(18)	(16)
Proceeds on disposal of entities (net of cash disposed)	11	449
Proceeds on sale of investment property	2	–
Proceeds on sale of property, plant and equipment	10	–
Payments for purchase of property, plant and equipment	(23)	(25)
Payments for purchase of software	(18)	(5)
Net cash flows from investing activities	182	480
<b>Financing activities</b>		
Capital contribution from non-controlling interests	–	2
Purchase of treasury shares	(66)	(17)
Proceeds from settlement of staff share loans	1	1
Proceeds from borrowings	4	–
Repayment of borrowings	(5)	–
Dividends paid	(289)	(184)
Net cash flows from financing activities	(355)	(198)
Net movement in cash and cash equivalents	43	141
Cash and cash equivalents at 1 January	662	852
Effect of exchange rate changes	58	(11)
Cash transferred to assets held for sale	–	(18)
Cash and cash equivalents at 30 June	763	964

The consolidated statement of cash flows above should be read in conjunction with the accompanying notes.

# Notes to the financial statements

FOR THE HALF YEAR ENDED 30 JUNE 2016

## 1. OVERVIEW

### 1.1 Basis of preparation of half year financial report

This general purpose consolidated financial report for the half year ended 30 June 2016 has been prepared in accordance with Accounting Standard AASB 134 *Interim Financial Reporting* and the *Corporations Act 2001*.

The financial report for the half year ended 30 June 2016 does not include all the notes normally included in an annual financial report. Accordingly, it is recommended that this report be read in conjunction with QBE's annual report for the financial year ended 31 December 2015 and any public announcements made by QBE Insurance Group Limited and its controlled entities (QBE or the Group).

The accounting policies adopted are consistent with those of the previous financial year and corresponding interim reporting period, except as set out below.

#### New and amended standards adopted by the Group

The Group adopted the following new or revised accounting standards which became effective for the annual reporting period commencing on 1 January 2016.

#### TITLE

AASB 2015-1	Annual improvements to Australian Accounting Standards 2012 – 2014 Cycle
AASB 2015-2	Disclosure Initiative: Amendments to AASB 101
AASB 2015-3	Amendments to Australian Accounting Standards arising from the Withdrawal of AASB 1031 Materiality
AASB 2015-5	Investment Entities: Applying the Consolidation Exception
AASB 2014-3	Accounting for Acquisitions of Interests in Joint Operations
AASB 2014-4	Clarification of Acceptable Methods of Depreciation and Amortisation
AASB 2014-9	Equity Method in Separate Financial Statements

The adoption of these new or revised standards did not materially affect the Group's accounting policies or financial statements.

#### Statement of compliance

The financial report complies with AASB 134 and, as such, is in compliance with IAS 34 *Interim Financial Reporting* as issued by the International Accounting Standards Board.

### 1.2 Significant judgements and estimates

The Group makes judgements and estimates in respect of the reported amounts of certain assets and liabilities. Noted below are the most material judgements and estimates that should be considered when reviewing the financial statements for the half year ended 30 June 2016.

#### 1.2.1 Outstanding claims provision

The determination of the amounts that the Group will ultimately pay for claims arising under insurance and reinsurance contracts involves a number of critical assumptions. Some of the uncertainties impacting these assumptions are as follows:

- changes in patterns of claims incidence, reporting and payment;
- volatility in the estimation of future costs for long tail insurance classes due to the longer period of time that elapses before claims are paid;
- the existence of complex underlying exposures, often at high attachment points;
- the incidence of catastrophic events close to the balance date;
- changes in the legal environment, including the interpretation of liability laws and the quantum of damages; and
- changing social, political and economic trends, for example price and wage inflation.

The potential impact of changes in key assumptions used in the determination of the central estimate and the probability of adequacy of the central estimate on the Group's profit or loss are summarised in note 2.3.7 to the consolidated financial statements for the year ended 31 December 2015.



### 1.2.2 Intangible assets

QBE monitors goodwill and identifiable intangible assets for indicators of impairment at each reporting date in accordance with the Group's policy, which is set out in note 7.2 to the consolidated financial statements for the year ended 31 December 2015.

At 30 June 2016, QBE has reviewed all material intangible assets for indicators of impairment and has completed detailed impairment tests where indicators of impairment were identified. No impairment charge resulted from the analysis undertaken.

A detailed impairment test was completed in respect of goodwill in QBE's North American Operations. The headroom (being the excess of recoverable value over carrying value) at the balance date reduced to \$79 million compared with \$196 million at 31 December 2015, mainly reflecting lower long-term investment return expectations (3.75% compared with 4.25% previously) as a result of post Brexit investment market volatility, partly offset by the consequent reduction in the post-tax discount rate applied (9.25% compared with 9.5% previously). The valuation continues to be highly sensitive to a range of assumptions, in particular, to increases in the forecast combined operating ratio used in the terminal value calculation and changes in discount rate and long-term investment return assumptions.

If the terminal value of the combined operating ratio was increased by 1% compared with QBE's estimate, the impairment charge would be \$246 million. If the post-tax discount rate was increased by 0.5%, the impairment charge would be \$209 million. If the long-term investment return was reduced by 0.5%, the impairment charge would be \$140 million.

### 1.2.3 Recoverability of future tax losses

In North American Operations, a deferred tax asset (DTA) of \$573 million continues to be recognised. Uncertainty continues to exist in relation to the recoverability of this DTA, which is subject to there being sufficient future taxable profits over the period of time in which the losses can be utilised. QBE has made a judgement that North American Operations will be able to generate sufficient taxable profits over the next several years, based on its future business plans. Losses expire over the next 17 years, with the majority expiring between 2030 and 2033. The uncertainty around the recognition of the DTA will be resolved in future years assuming that taxable profits are generated. Recovery of the DTA remains sensitive to changes in the forecast combined operating ratio, premium growth and investment yield assumptions as these items are the key drivers of future taxable income.

### 1.2.4 Liability adequacy test

At each balance date, the adequacy of the unearned premium liability is assessed on a net of reinsurance basis against the present value of the expected future cash flows relating to potential future claims in respect of the relevant insurance contracts, plus an additional risk margin to reflect the inherent uncertainty of the central estimate. The assessment is carried out at the operating segment level, being a portfolio of contracts subject to broadly similar risks and which are managed together as a single portfolio, with the exception of Emerging Markets where the risks are broadly similar across the Latin American and Asia Pacific geographic regions rather than across the operating segment as a whole.

# Notes to the financial statements CONTINUED

FOR THE HALF YEAR ENDED 30 JUNE 2016

## 1.3 Segment information

The Group provides segment information by operating division to assist the understanding of the Group's performance. The Group's operating segments are consistent with the basis on which information is provided to the Group Executive for measuring performance and determining the allocation of capital, being the basis upon which the Group's underwriting products and services are managed within the various markets in which QBE operates.

30 JUNE 2016	NORTH AMERICAN OPERATIONS US\$M	EUROPEAN OPERATIONS US\$M	AUSTRALIAN & NEW ZEALAND OPERATIONS US\$M	EMERGING MARKETS US\$M	EQUATOR RE US\$M	TOTAL REPORTABLE SEGMENTS US\$M	CORPORATE <sup>1</sup> US\$M	OTHER <sup>2</sup> US\$M	TOTAL US\$M
Total assets	11,887	18,378	11,927	3,591	7,463	53,246	1,145	(11,118)	43,273
Total liabilities	(10,237)	(14,029)	(8,803)	(2,782)	(5,854)	(41,705)	(2,302)	11,118	(32,889)
Net assets	1,650	4,349	3,124	809	1,609	11,541	(1,157)	–	10,384
Other non-current assets	1,822	558	1,297	166	–	3,843	9	–	3,852
Gross written premium	2,818	2,508	1,861	850	1,125	9,162	–	(1,055)	8,107
Gross earned premium revenue – external	2,136	1,913	1,865	793	–	6,707	–	169	6,876
Gross earned premium revenue – internal	48	17	6	–	583	654	–	(654)	–
Outward reinsurance premium expense	(474)	(545)	(217)	(138)	(386)	(1,760)	–	499	(1,261)
Net earned premium	1,710	1,385	1,654	655	197	5,601	–	14	5,615
Net claims expense	(1,225)	(812)	(1,120)	(359)	(116)	(3,632)	–	(5)	(3,637)
Net commission	(288)	(279)	(250)	(152)	(18)	(987)	–	(6)	(993)
Underwriting and other expenses	(265)	(270)	(217)	(141)	(4)	(897)	4	(38)	(931)
Underwriting result	(68)	24	67	3	59	85	4	(35)	54
Net investment income on policyholders' funds	42	59	81	33	15	230	–	42	272
Insurance (loss) profit	(26)	83	148	36	74	315	4	7	326
Net investment income on shareholders' funds	26	21	42	40	7	136	10	19	165
Financing and other costs	–	–	–	–	–	–	(125)	–	(125)
Amortisation and impairment of intangibles	–	–	–	–	–	–	–	(19)	(19)
Profit (loss) before income tax	–	104	190	76	81	451	(111)	7	347
Income tax credit (expense)	5	(19)	(56)	(25)	–	(95)	–	15	(80)
Profit (loss) after income tax	5	85	134	51	81	356	(111)	22	267
Net profit attributable to non-controlling interests	–	–	–	–	–	–	–	(2)	(2)
Net profit (loss) after income tax	5	85	134	51	81	356	(111)	20	265

1 The corporate segment includes non-operating holding companies and financing entities which do not form part of the Group's insurance operations.

2 "Other" includes the impact of consolidation adjustments and internal reinsurance eliminations, together with the costs associated with amortisation of intangibles which do not form part of the divisional management results.

30 JUNE 2015	NORTH AMERICAN OPERATIONS US\$M	EUROPEAN OPERATIONS US\$M	AUSTRALIAN & NEW ZEALAND OPERATIONS US\$M	EMERGING MARKETS US\$M	EQUATOR RE US\$M	TOTAL REPORTABLE SEGMENTS US\$M	CORPORATE <sup>1</sup> US\$M	OTHER <sup>2,3</sup> US\$M	TOTAL US\$M
Total assets	12,730	17,600	10,983	3,964	7,603	52,880	872	(7,651)	46,101
Total liabilities	(10,437)	(14,504)	(8,207)	(3,171)	(6,210)	(42,529)	(218)	7,651	(35,096)
Net assets	2,293	3,096	2,776	793	1,393	10,351	654	–	11,005
Other non-current assets	1,912	645	1,290	221	–	4,068	10	–	4,078
Gross written premium	3,109	2,659	1,928	1,064	976	9,736	–	(1,044)	8,692
Gross earned premium revenue – external	2,309	2,112	1,913	1,009	–	7,343	–	(50)	7,293
Gross earned premium revenue – internal	–	–	–	–	485	485	–	(485)	–
Outward reinsurance premium expense	(477)	(452)	(245)	(123)	(303)	(1,600)	–	536	(1,064)
Net earned premium	1,832	1,660	1,668	886	182	6,228	–	1	6,229
Net claims expense	(1,145)	(815)	(1,050)	(584)	(106)	(3,700)	–	(27)	(3,727)
Net commission	(329)	(312)	(235)	(178)	(13)	(1,067)	–	(6)	(1,073)
Underwriting and other expenses	(361)	(297)	(230)	(173)	(6)	(1,067)	(8)	(59)	(1,134)
Underwriting result	(3)	236	153	(49)	57	394	(8)	(91)	295
Net investment income on policyholders' funds	32	42	94	82	30	280	4	(43)	241
Insurance profit (loss)	29	278	247	33	87	674	(4)	(134)	536
Net investment income on shareholders' funds	23	16	46	86	15	186	(9)	(32)	145
Financing and other costs	–	–	–	–	–	–	(127)	–	(127)
Gains on sale of entities	–	–	–	–	–	–	150	–	150
Amortisation and impairment of intangibles	–	–	–	–	–	–	–	(25)	(25)
Profit (loss) before income tax	52	294	293	119	102	860	10	(191)	679
Income tax credit (expense)	2	(53)	(88)	(39)	(7)	(185)	(22)	18	(189)
Profit (loss) after income tax	54	241	205	80	95	675	(12)	(173)	490
Net profit attributable to non-controlling interests	–	–	–	–	–	–	–	(2)	(2)
Net profit (loss) after income tax	54	241	205	80	95	675	(12)	(175)	488

1 The corporate segment includes non-operating holding companies and financing entities which do not form part of the Group's insurance operations.

2 "Other" includes the impact of consolidation adjustments and internal reinsurance eliminations, together with the costs associated with amortisation of intangibles which do not form part of the divisional management results.

3 "Other" includes the write down of deferred acquisition costs to recoverable value resulting from the classification of the Mortgage & Lender Services business in our North American Operations as held for sale (\$55 million).

## Notes to the financial statements CONTINUED

FOR THE HALF YEAR ENDED 30 JUNE 2016

### 2. UNDERWRITING ACTIVITIES

#### 2.1 Revenue

	NOTE	30 JUNE 2016 US\$M	30 JUNE 2015 US\$M
<b>Gross earned premium revenue</b>			
Direct and facultative		6,465	6,785
Inward reinsurance		411	508
		6,876	7,293
<b>Other revenue</b>			
Reinsurance and other recoveries revenue	2.2	849	470
Reinsurance commission revenue		165	165
		7,890	7,928

#### 2.2 Net claims expense

	NOTE	30 JUNE 2016 US\$M	30 JUNE 2015 US\$M
Gross claims and related expenses		4,486	4,197
Reinsurance and other recoveries revenue	2.1	849	470
Net claims expense		3,637	3,727

##### 2.2.1 Prior accident year claims development

The result for the half year ended 30 June 2016 includes the benefit of prior accident year net undiscounted central estimate releases of \$218 million (2015 \$69 million release). Continuing positive prior accident year development in European Operations and Australian & New Zealand Operations more than offset adverse development in North American Operations, with the latter mainly reflecting industry-wide deterioration in commercial auto claims frequency and severity in more recent accident years.

#### 2.3 Outstanding claims

	NOTE	30 JUNE 2016 US\$M	31 DECEMBER 2015 US\$M
Gross discounted central estimate	2.3.1	17,572	17,323
Risk margin	2.3.3	1,231	1,260
Gross outstanding claims provision		18,803	18,583
Reinsurance and other recoveries on outstanding claims	2.3.2	(3,512)	(3,204)
Net outstanding claims provision		15,291	15,379

##### 2.3.1 Gross discounted central estimate

	NOTE	30 JUNE 2016 US\$M	31 DECEMBER 2015 US\$M
Gross undiscounted central estimate		17,795	17,925
Claims settlement costs		389	396
		18,184	18,321
Discount to present value		(612)	(998)
Gross discounted central estimate	2.3	17,572	17,323

### 2.3.2 Reinsurance and other recoveries on outstanding claims

		30 JUNE 2016 US\$M	31 DECEMBER 2015 US\$M
	NOTE		
Reinsurance and other recoveries on outstanding claims <sup>1</sup>		3,700	3,426
Discount to present value		(188)	(222)
Reinsurance and other recoveries on outstanding claims	2.3	3,512	3,204

1 Reinsurance and other recoveries on outstanding claims is shown net of a provision for impairment of \$32 million (31 December 2015 \$31 million).

### 2.3.3 Risk margin

The risk margin included in the net outstanding claims provision is 8.8% (31 December 2015 8.9%) of the net discounted central estimate. The probability of adequacy at 30 June 2016 is 89.0% (31 December 2015 89.0%) which is well above APRA's 75% benchmark.

## 3. INVESTMENTS

### 3.1 Net investment income and expenses

	30 JUNE 2016 US\$M	30 JUNE 2015 US\$M
Income on growth assets	19	163
Income on fixed interest securities, short-term money and cash	396	273
Gross investment income <sup>1</sup>	415	436
Investment expenses	(11)	(14)
Net investment income	404	422
Foreign exchange gain (loss)	39	(29)
Other expense	(6)	(7)
Net investment and other income	437	386
Investment and other income – policyholders' funds	279	250
Investment expenses – policyholders' funds	(7)	(9)
Investment and other income – shareholders' funds	169	150
Investment expenses – shareholders' funds	(4)	(5)
Net investment and other income	437	386

1 Includes net fair value gains of \$149 million (2015 \$132 million), interest income of \$242 million (2015 \$260 million) and dividend income of \$24 million (2015 \$44 million).

## Notes to the financial statements CONTINUED

FOR THE HALF YEAR ENDED 30 JUNE 2016

### 3.2 Investments

	30 JUNE 2016 US\$M	31 DECEMBER 2015 US\$M
<b>Fixed income</b>		
Short-term money	4,524	5,924
Government bonds	3,402	4,158
Corporate bonds	14,081	12,385
Infrastructure debt	458	348
Unit trusts	44	64
	<b>22,509</b>	<b>22,879</b>
<b>Growth assets</b>		
Developed market equity	479	683
Emerging market equity	33	254
Emerging market debt	33	318
High yield debt	26	458
Property trusts	1,002	1,043
Alternatives	883	397
	<b>2,456</b>	<b>3,153</b>
<b>Total investments</b>	<b>24,965</b>	<b>26,032</b>

### 3.3 Derivatives

Derivatives may be used in the investment portfolio as both a hedging tool and to alter the risk profile of the portfolio. The Group's effective exposure to investment derivatives at the balance date is set out in the table below. Derivatives used in the investment portfolio are marked to market and settled on a daily basis, and therefore have a fair value of nil.

	30 JUNE 2016 US\$M	31 DECEMBER 2015 US\$M
<b>GROSS EXPOSURE</b>		
<b>Fixed interest futures</b>		
ASX 90 day bank bills	594	760
SFE Australian 3 year bond futures	253	81
90 day sterling futures	–	(713)
<b>Equity futures</b>		
ASX SPI 200	3	104
S&P 500 E-mini	–	191

### 3.4 Fair value hierarchy

The Group's investment assets are disclosed in the table below using a fair value hierarchy which reflects the significance of inputs into the determination of their fair value.

	30 JUNE 2016				31 DECEMBER 2015			
	LEVEL 1 US\$M	LEVEL 2 US\$M	LEVEL 3 US\$M	TOTAL US\$M	LEVEL 1 US\$M	LEVEL 2 US\$M	LEVEL 3 US\$M	TOTAL US\$M
<b>Fixed income</b>								
Short-term money	948	3,569	7	4,524	861	5,062	1	5,924
Government bonds	2,301	1,099	2	3,402	2,849	1,300	9	4,158
Corporate bonds	–	14,080	1	14,081	–	12,384	1	12,385
Infrastructure debt	–	175	283	458	–	139	209	348
Unit trusts	–	44	–	44	–	64	–	64
	<b>3,249</b>	<b>18,967</b>	<b>293</b>	<b>22,509</b>	<b>3,710</b>	<b>18,949</b>	<b>220</b>	<b>22,879</b>
<b>Growth assets</b>								
Developed market equity	453	–	26	479	657	–	26	683
Emerging market equity	–	33	–	33	–	254	–	254
Emerging market debt	–	33	–	33	–	318	–	318
High yield debt	–	26	–	26	–	458	–	458
Property trusts	–	1,002	–	1,002	–	1,043	–	1,043
Alternatives	–	632	251	883	–	397	–	397
	<b>453</b>	<b>1,726</b>	<b>277</b>	<b>2,456</b>	<b>657</b>	<b>2,470</b>	<b>26</b>	<b>3,153</b>
<b>Total investments</b>	<b>3,702</b>	<b>20,693</b>	<b>570</b>	<b>24,965</b>	<b>4,367</b>	<b>21,419</b>	<b>246</b>	<b>26,032</b>



The Group's approach to measuring the fair value of investment and derivative assets is described below:

### Short-term money

Term deposits are valued at par plus accrued interest and are categorised as level 1. Other short-term money (bank bills, certificates of deposit, treasury bills and other short-term instruments) is priced using interest rates and yield curves observable at regular intervals in accordance with standard market practices.

### Government and corporate bonds

Bonds which are traded in active markets and have quoted prices from external data providers are categorised as level 1. Bonds which are not traded in active markets are priced using broker quotes, using comparable prices for similar instruments or using pricing techniques set by local regulators or exchanges.

### Infrastructure debt

Infrastructure debt prices are sourced from the investment manager who may use a combination of observable market prices or comparable market prices where available and other valuation techniques.

### Developed market equity

Listed equities traded in active markets are valued by reference to quoted bid prices. Unlisted equities are priced using QBE's share of the net assets of the entity.

### Emerging market debt, emerging market equity, high yield debt, unit trusts and unlisted property trusts

These assets are valued using quoted bid prices in active markets or current unit prices as advised by the responsible entity, trustee or equivalent of the investment management scheme.

### Alternatives

Alternatives comprise fund of funds vehicles. Fair value is based on the net asset value of the vehicle, and the responsibility for the valuation of the underlying securities lies with the external manager. In most cases, an independent administrator will be utilised by the external fund manager for pricing and valuation. A combination of observable market prices or comparable market prices (where available) and other valuation techniques may be used in the determination of fair value.

### Movements in level 3 investments

The following table provides an analysis of investment assets valued with reference to level 3 inputs.

	30 JUNE 2016 US\$M	30 JUNE 2015 US\$M
<b>LEVEL 3</b>		
At 1 January	246	186
Purchases	338	44
Disposals	(12)	(17)
Fair value losses recognised in profit or loss	(2)	–
Foreign exchange	–	(3)
At 30 June	570	210

## Notes to the financial statements CONTINUED

FOR THE HALF YEAR ENDED 30 JUNE 2016

### 4. CAPITAL STRUCTURE

#### 4.1 Borrowings

FINAL MATURITY DATE	PRINCIPAL AMOUNT	30 JUNE 2016 US\$M	31 DECEMBER 2015 US\$M
<b>Bank loans</b>			
19 September 2016	\$3 million	3	–
17 December 2016	\$1 million	1	–
		4	–
<b>Senior debt</b>			
1 May 2018	\$600 million	599	599
		599	599
<b>Subordinated debt</b>			
29 September 2040	A\$200 million	148	145
24 May 2041	\$539 million (2015 \$1,000 million)	539	1,000
24 May 2041	£34 million (2015 £325 million)	45	479
24 May 2042	£327 million	386	–
2 December 2044	\$700 million	695	695
12 November 2045	\$300 million	300	300
17 June 2046	\$524 million	455	–
		2,568	2,619
<b>Capital securities<sup>1</sup></b>			
No fixed date	£8 million	11	11
No fixed date	\$301 million	300	300
		311	311
<b>Total borrowings</b>		<b>3,482</b>	<b>3,529</b>

<sup>1</sup> The sterling capital securities were called on 18 July 2016. Details of capital securities held as investment assets and eliminated on consolidation are set out in note 5.1 of the annual report for the year ended 31 December 2015.

#### Subordinated debt due 2041

On 17 June 2016, QBE exchanged \$456 million of the \$1,000 million subordinated debt securities due 2041 for \$524 million of subordinated debt due 2046. The new subordinated debt securities have a 30 year maturity and entitle holders to receive a fixed rate coupon of 5.875% per annum until 17 June 2026. The rate will reset in 2026 and 2036 to a rate calculated by reference to the then 10 year mid-market swap rate plus a margin of 4.395%. Interest is payable semi-annually in arrears.

The securities are redeemable at the option of QBE, with the written approval of APRA, on each interest reset date or at any time in the event of certain tax and regulatory events.

The securities must be converted into a variable number of QBE ordinary shares, or written off, if APRA determines QBE to be non-viable. The number of QBE ordinary shares issued on conversion will be capped at a maximum based on 20% of the volume-weighted average price (VWAP) of QBE ordinary shares at the issue date.

On 23 June 2016, QBE repurchased a further \$5 million of these securities for cash.

#### Subordinated debt due 2041

On 19 May 2016, QBE exchanged £291 million of the subordinated debt securities due 2041 for £327 million of subordinated debt securities due 2042. The new subordinated debt securities have a 26 year maturity and entitle holders to receive a fixed rate coupon of 6.115% per annum until 24 May 2022. The rate will reset in 2022, 2027, 2032 and 2037 to a rate calculated by reference to the then five year mid-market swap rate plus a margin of 5.0%. Interest is payable semi-annually in arrears.

The securities are redeemable at the option of QBE, with the written approval of APRA, on each interest reset date or at any time in the event of certain tax and regulatory events.

The securities must be converted into a variable number of QBE ordinary shares, or written off, if APRA determines QBE to be non-viable. The number of QBE ordinary shares issued on conversion will be capped at a maximum based on 20% of the VWAP of QBE ordinary shares at the issue date.

#### 4.1.1 Fair value of borrowings

The Group's borrowings are initially measured at fair value net of transaction costs directly attributable to the transaction and are subsequently remeasured at amortised cost.

	30 JUNE 2016 US\$M	31 DECEMBER 2015 US\$M
Bank loans	4	–
Senior debt	606	601
Subordinated debt	2,849	2,813
Capital securities	320	322
	<b>3,779</b>	<b>3,736</b>

#### 4.2 Derivative financial instruments

Forward foreign exchange contracts are used as a tool to manage the Group's operational foreign exchange exposure and interest rate swaps are used to hedge exposure to interest rate movements in relation to some of the Group's borrowings. QBE does not ordinarily use derivatives to mitigate currency risk on translation to the ultimate parent's functional currency of Australian dollars; however, in periods of extraordinary volatility that are expected to persist for an extended period of time, QBE may elect to utilise derivatives to mitigate currency translation risk to preserve capital. The volatility created by the recent UK referendum decision to leave the European Union (Brexit) is an example of such volatility and, since 30 June 2016, we have therefore elected to hedge our sterling net investment in foreign operations.

	30 JUNE 2016			31 DECEMBER 2015		
	EXPOSURE US\$M	FAIR VALUE ASSET US\$M	FAIR VALUE LIABILITY US\$M	EXPOSURE US\$M	FAIR VALUE ASSET US\$M	FAIR VALUE LIABILITY US\$M
Forward foreign exchange contracts	1,825	51	117	651	33	35
Interest rate swaps	149	–	4	146	–	–

Forward foreign exchange contracts and interest rate swaps are categorised as level 1 in the fair value hierarchy.

#### 4.3 Share capital

	30 JUNE 2016		30 JUNE 2015	
	NUMBER OF SHARES MILLIONS	US\$M	NUMBER OF SHARES MILLIONS	US\$M
Issued ordinary shares, fully paid at 1 January	1,370	8,440	1,363	9,391
Shares issued under the Employee Share and Option Plan	–	1	–	–
Shares issued under dividend reinvestment plans	–	–	4	41
Foreign exchange	–	197	–	(519)
Issued ordinary shares, fully paid at 30 June	1,370	8,638	1,367	8,913
Shares notified to the Australian Securities Exchange	1,371	8,645	1,369	8,923
Less: Plan shares subject to non-recourse loans, derecognised under IFRS	(1)	(7)	(2)	(10)
Issued ordinary shares, fully paid at 30 June	1,370	8,638	1,367	8,913

## Notes to the financial statements CONTINUED

FOR THE HALF YEAR ENDED 30 JUNE 2016

### 4.4 Dividends

	2015		2014
	FINAL	INTERIM	FINAL
Dividend per share (Australian cents)	30	20	22
Franking percentage	100%	100%	100%
Franked amount per share (Australian cents)	30	20	22
Dividend payout (A\$M)	411	274	300
Payment date	14 April 2016	2 October 2015	13 April 2015

On 17 August 2016, the directors declared a 50% franked interim dividend of 21 Australian cents per share, payable on 28 September 2016. The interim dividend payout is A\$288 million (2015 A\$274 million). The record date is 26 August 2016.

The unfranked part of the dividend is declared to be conduit foreign income. For shareholders not resident in Australia, the dividend will not be subject to Australian withholding tax.

### 4.5 Earnings per share

	30 JUNE 2016 US CENTS	30 JUNE 2015 US CENTS
Basic earnings per share	19.3	35.8
Diluted earnings per share	19.2	35.5

Earnings used in calculating diluted earnings per share is the net profit after income tax attributable to ordinary equity holders of the company being \$265 million (2015 \$488 million).

#### 4.5.1 Reconciliation of weighted average number of ordinary shares used in calculating earnings per share

	30 JUNE 2016 NUMBER OF SHARES MILLIONS	30 JUNE 2015 NUMBER OF SHARES MILLIONS
Weighted average number of ordinary shares on issue	1,371	1,367
Weighted average number of non-recourse loan shares issued under the Employee Share and Option Plan (the Plan)	(1)	(2)
Weighted average number of ordinary shares used as the denominator in calculating basic earnings per share	1,370	1,365
Weighted average number of dilutive potential ordinary shares relating to shares issued under the Plan	9	10
Weighted average number of ordinary shares used as the denominator in calculating diluted earnings per share	1,379	1,375

## 5. OTHER

### 5.1 Contingent liabilities

Contingent liabilities are disclosed when the possibility of a future settlement of economic benefits is considered to be less than probable but more likely than remote. If the expected settlement of the liability is probable and quantifiable, a provision is recognised.

In the normal course of business, the Group is exposed to contingent liabilities in relation to claims litigation arising out of its insurance and reinsurance transactions and may be exposed to the possibility of contingent liabilities in relation to non-insurance litigation. There are no individually significant amounts not provided for and such transactions are not considered likely to have a material impact on the net assets of the Group.

There have been no material changes to the Group's contingent liabilities since 31 December 2015.

In the prior period, QBE announced the disposal of the Mortgage & Lender Services business in North American Operations. Whilst the purchaser assumed responsibility for all potential future litigation in relation to this business, the sale contract specifically excluded liabilities associated with class action litigation or regulatory examinations in relation to this business already underway. This business is subject to litigation and regulatory examinations in the normal course of business. We do not have sufficiently reliable information at the date of this report to assess any potential liability for such class actions or regulatory examinations.

On 9 September 2015, QBE was served with a statement of claim alleging breaches of continuous disclosure and conduct obligations in relation to profit guidance issued for the year ended 31 December 2013. QBE rejects the allegations and is defending the claim. As at the date of this report, it is not possible to produce a reliable estimate of the potential financial effect arising from the claim, if any.

### 5.2 Post balance sheet events

The sterling capital securities were called on 18 July 2016. Refer to note 4.1.

In early July 2016, the Group hedged its sterling net investment in foreign operations. Refer to note 4.2.

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## Directors' declaration

In the directors' opinion:

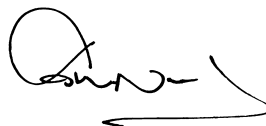
- (a) the financial statements and notes set out on pages 46 to 61 are in accordance with the *Corporations Act 2001*, including:
  - (i) complying with accounting standards, the Corporations Regulations 2001 and other mandatory professional reporting requirements; and
  - (ii) giving a true and fair view of the Group's financial position as at 30 June 2016 and of its performance for the half year ended on that date; and
- (b) there are reasonable grounds to believe that the company will be able to pay its debts as and when they become due and payable.

The directors have been given the declarations by the Group Chief Executive Officer and Group Chief Financial Officer recommended under the ASX Corporate Governance Council's *Corporate Governance Principles and Recommendations*.

Signed in SYDNEY on 17 August 2016 in accordance with a resolution of the directors.



WM Becker  
Director



JD Neal  
Director



# Independent auditor's review report

TO THE MEMBERS OF QBE INSURANCE GROUP LIMITED

## Report on the half year financial report

We have reviewed the accompanying half year financial report of QBE Insurance Group Limited (the company), which comprises the consolidated balance sheet as at 30 June 2016, the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the half year ended on that date, selected explanatory notes and the directors' declaration for QBE Insurance Group Limited (the consolidated entity). The consolidated entity comprises both the company and the entities it controlled during that half year.

## Directors' responsibility for the half year financial report

The directors of the company are responsible for the preparation of the half year financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such internal control as the directors determine is necessary to enable the preparation of the half year financial report that is free from material misstatement whether due to fraud or error.

## Auditor's responsibility

Our responsibility is to express a conclusion on the half year financial report based on our review. We conducted our review in accordance with Australian Auditing Standard on Review Engagements ASRE 2410 *Review of a Financial Report Performed by the Independent Auditor of the Entity*, in order to state whether, on the basis of the procedures described, we have become aware of any matter that makes us believe that the financial report is not in accordance with the *Corporations Act 2001* including: giving a true and fair view of the consolidated entity's financial position as at 30 June 2016 and its performance for the half year ended on that date; and complying with Accounting Standard AASB 134 *Interim Financial Reporting* and the *Corporations Regulations 2001*. As the auditor of QBE Insurance Group Limited, ASRE 2410 requires that we comply with the ethical requirements relevant to the audit of the annual financial report.

A review of a half year financial report consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with Australian Auditing Standards and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

## Independence

In conducting our review, we have complied with the independence requirements of the *Corporations Act 2001*.

## Conclusion

Based on our review, which is not an audit, we have not become aware of any matter that makes us believe that the half year financial report of QBE Insurance Group Limited is not in accordance with the *Corporations Act 2001* including:

- (a) giving a true and fair view of the consolidated entity's financial position as at 30 June 2016 and of its performance for the half year ended on that date; and
- (b) complying with Accounting Standard AASB 134 *Interim Financial Reporting* and the *Corporations Regulations 2001*.

PricewaterhouseCoopers

PricewaterhouseCoopers

RJ Clark

RJ Clark  
Partner

Sydney  
17 August 2016

SJ Hadfield

SJ Hadfield  
Partner

# Historical review

FOR THE HALF YEAR ENDED 30 JUNE 2016

		HALF YEAR ENDED 30 JUNE					YEAR ENDED 31 DECEMBER				
		2016	2015	2014	2013	2012	2015	2014	2013	2012	2011
Gross written premium	US\$M	<b>8,107</b>	8,692	8,491	9,446	9,223	15,092	16,332	17,975	18,434	18,291
Gross earned premium	US\$M	<b>6,876</b>	7,293	7,819	8,413	8,404	14,922	16,521	17,889	18,341	17,840
Net earned premium	US\$M	<b>5,615</b>	6,229	6,947	7,333	7,359	12,314	14,084	15,396	15,798	15,359
Claims ratio	%	<b>64.8</b>	59.8	63.1	59.4	61.5	60.3	63.2	64.5	66.0	68.2
Commission ratio	%	<b>17.7</b>	17.3	17.1	17.8	16.8	17.2	16.8	16.8	16.2	14.9
Expense ratio	%	<b>16.5</b>	18.2	16.3	15.6	14.6	17.3	16.1	16.5	14.9	13.7
Combined operating ratio	%	<b>99.0</b>	95.3	96.5	92.8	92.9	94.9	96.1	97.8	97.1	96.8
Investment income											
before fair value gains/losses	US\$M	<b>291</b>	262	338	367	391	541	676	691	723	948
after fair value gains/losses	US\$M	<b>437</b>	386	429	388	683	665	814	772	1,227	767
Insurance profit	US\$M	<b>326</b>	536	530	790	958	1,031	1,074	841	1,262	1,085
Insurance profit to net earned premium	%	<b>5.8</b>	8.6	7.6	10.8	13.0	8.4	7.6	5.5	8.0	7.1
Financing and other costs	US\$M	<b>125</b>	127	150	168	166	244	297	345	324	275
Operating profit (loss)											
before income tax	US\$M	<b>347</b>	679	487	585	914	953	931	(448)	941	868
after income tax and non-controlling interest	US\$M	<b>265</b>	488	392	477	760	687	742	(254)	761	704
Number of shares on issue <sup>1</sup>	millions	<b>1,370</b>	1,363	1,276	1,218	1,178	1,370	1,363	1,247	1,194	1,112
Shareholders' funds	US\$M	<b>10,325</b>	10,949	11,228	11,163	11,546	10,505	11,030	10,356	11,358	10,386
Total assets	US\$M	<b>43,273</b>	46,101	48,990	49,105	48,852	42,176	45,000	47,271	50,748	46,737
Net tangible assets per share <sup>1</sup>	US\$	<b>4.96</b>	5.31	5.29	4.59	4.56	5.07	5.32	4.75	4.49	3.93
Borrowings to shareholders' funds	%	<b>33.7</b>	32.8	38.4	42.7	37.1	33.6	32.5	44.1	43.4	45.8
Basic earnings per share <sup>1</sup>	US cents	<b>19.3</b>	35.8	31.3	38.0	67.7	50.3	57.4	(22.8)	65.1	64.9
Basic earnings per share – cash basis <sup>2</sup>	US cents	<b>20.9</b>	34.5	33.2	49.3	75.2	65.3	63.5	62.9	89.1	73.0
Diluted earnings per share	US cents	<b>19.2</b>	35.5	30.5	35.8	63.1	49.8	55.8	(22.8)	61.6	61.3
Return on average shareholders' funds	%	<b>5.1</b>	8.9	7.3	8.5	13.9	6.4	6.9	(2.3)	7.0	6.8
Dividend per share	Australian cents	<b>21</b>	20	15	20	40	50	37	32	50	87
Dividend payout	A\$M	<b>288</b>	274	192	244	473	685	492	394	593	956
Total investments and cash <sup>3</sup>	US\$M	<b>25,741</b>	27,903	31,359	29,955	28,851	26,708	28,583	30,619	31,525	28,024

<sup>1</sup> Reflects shares on an accounting basis.

<sup>2</sup> Earnings per share on a cash basis is calculated with reference to cash profit, being profit after tax adjusted for amortisation and impairment of intangibles and other non-cash items net of tax.

<sup>3</sup> Includes financial assets at fair value through profit or loss, cash and cash equivalents and investment properties.



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