

## Trends and developments

# Several external factors impact the environment in which the financial services industry operates

Despite a persistent low interest rate environment, global economic conditions developed positively, also in the countries in which NN Group is active. At the same time, regulatory, demographic and climate change require the sector to continue to adapt.

**Rapid progress in digitalisation and changing customer behaviour continue to transform the competitive landscape. Regulation and measures from industry regulators have influenced the offering of products and services.**

Combined, these factors imply that the financial services sector as a whole, as well as individual companies, needs to formulate efficient and responsible answers to challenges, in alignment with the interests of customers and other stakeholders.

### Economic and demographic changes and outlook

The positive development in global economic conditions that began in the second half of 2016 gained further momentum in 2017.

The global economy is stronger than it has been over the past decade. In advanced economies, growth momentum was broad-based, with stronger activity in the United States, Europe and Japan.

Growth in Europe, with the exception of the United Kingdom (due to Brexit), reflects continued strength in domestic demand, which was supported by monetary conditions and diminished political risk and policy uncertainty, as well as an increase in exports.

Economic growth in the Netherlands was higher in 2017 compared to other mature European countries, and is expected to remain solid in the coming years. In emerging and developing Europe (including Turkey), short-term growth was significantly above EU average growth, and growth prospects continue to be favourable for 2018. In Japan, growth was supported by accommodative fiscal and monetary policies, and by the strengthening of global demand.

In the short term, global growth forecasts are relatively balanced, with strong consumer and business confidence, including in the euro area. A disadvantage is that substantial policy uncertainty remains, reflecting, for example, difficult-to-predict developments in US regulatory and fiscal policies, the potential adoption of trade restrictions, the Brexit negotiations and geopolitical risks.

The outlook for the medium term is more subdued as demographic factors may negatively impact future growth. With fertility rates decreasing and populations ageing, the working-age population is projected to decline in the coming years, which will put pressure on pension and health care systems.

### Low interest rates and financial market stability

Market sentiment remained strong and volatility continued to be low in 2017. On the monetary policy front, the US Federal Reserve raised short-term interest rates in March, June and December. In most other advanced economies, the monetary policy stance remained broadly unchanged, with the exception of the European Central Bank's (ECB) announcement that it will halve the pace of its bond-buying asset purchase programme, starting in January 2018.

In 2017, long-term sovereign bond yields stayed broadly stable in Germany, the Netherlands and Japan, and declined by 20–30 basis points in other EU countries, as spreads relative to German yields reduced sharply after the French presidential election. Prices in equity markets have continued to increase due to strong company earnings, high consumer and business confidence, and strong macroeconomic data. As the search for yield intensifies, however, vulnerabilities and market risks increase.

Asset valuations are becoming stretched in some markets, as investors accept higher credit and liquidity risk.



## Trends and developments Continued

### Regulation

In 2017, consultations started to review part of the Solvency II regime. After many years of careful designing and planning for its implementation, it is important that customers, companies, regulators and investors have time to become familiarised with how the framework functions. It is important to provide for stable regulation and a level playing field in Europe. In early 2017, the new IFRS17 standard was published for the valuation of insurance liabilities, which is expected to be implemented in 2021. Together with the already published IFRS9 standard for asset valuation, accounting standards are now increasingly based on market value approaches.

In 2017, legislation was proposed by the Dutch Government with regard to recovery and resolution planning for insurance companies in the Netherlands. This legislative process is likely to be finalised in 2018. Also at a European level, the topic of recovery and resolution of insurance companies is given attention. Consumer-related legislation, such as the EU Insurance Distribution Directive (IDD), will help insurance firms further improve the quality and transparency of information provided to consumers. Also important is the EU General Data Protection Regulation (GDPR) that will become applicable on 25 May 2018. The GDPR will have a significant impact, as it will provide for a truly unified, high and consistent level of protection of personal data within the European Union (a.o.) introducing new rights for natural persons and obligations for organisations that process personal data. Data protection refers to the protection of personal data of individuals and is derived from the right to Privacy. Both the right to privacy and data protection are fundamental human rights. As a large financial services company, NN processes large numbers of (sensitive) personal data of our customers and employees. This places an extra responsibility on us to do our best to properly and in a timely manner comply with the GDPR.

### Competitive landscape

Digital innovations will continue to drive change across the financial services value chain, particularly in the property and casualty (P&C) market and asset management industry. This affects product development and underwriting, back-office operations and online distribution. Social, mobile, analytics and cloud technologies will become utility assets as insurers focus on smarter technologies, such as artificial intelligence, blockchain and the Internet of Things. Digitalisation also brings opportunities for financial services companies to broaden and deepen product offerings and increase partnerships with insurtech startups. The use of (big) data for analysing client propositions offers opportunities to strengthen interaction with customers and create more intuitive partnerships, as well as create better and tailor-made product solutions. Insurers and asset managers are aware this requires ensuring a proper balance between individual choices, privacy and solidarity.

### Changing pension systems

Low interest rates, digitalisation and the move to passive investment solutions continue to put pressure on the asset management industry. The outlook for life insurance and pension products differs across countries. On a global scale, life insurers have managed to restore profits allowing them to retain earnings, raise capital buffers, and adapt their business models in response to the low-yield environment. Also, insurers have been adjusting their asset mix to higher-yielding and less liquid assets. In the Netherlands, the market for (individual) life and pension products is challenging. The new Dutch government announced initial ambitions to reform the second pillar of the pension system. The Central and Eastern European (CEE) region maintains significant potential for future growth, and witnessed rising demand for life insurance products and continued growth of the insurance sector in the region.

### Uncertain geopolitical developments

In the refinement of business strategies, financial services companies should take due account of other developments, such as ambiguity around geopolitical developments, which potentially lead to uncertainties in the economy and markets. The increased frequency and severity of major weather events mean that climate change has enlarged the risks and costs of insurance. Cyber risks to business and governments are growing, as events in 2017 demonstrated, with a sizable increase in the impact and sophistication of financially motivated cyber-attacks on financial institutions. A greater reliance on technology, combined with the interconnectedness of the global financial system, means that many participants in the system could potentially be at risk.

### Being prepared to drive change

From this general assessment we can conclude that the environment in which financial services companies operate is prone to continuous change. Companies must be agile and well prepared to deal with and take advantage of the opportunities these changes bring.

## Understanding and addressing our material topics

# To earn trust and support, we maintain an open and continuous dialogue with our stakeholders

**NN considers employees, customers, shareholders, business partners and society at large (including regulators and societal organisations) to be important stakeholders. We seek their feedback on different topics in order to learn what topics they consider important.**

Identifying the most relevant developments and topics within our sector, and the potential impact they have on our company, is an ongoing process, relevant also to our annual reporting efforts. The Global Reporting Initiative's (GRI) Sustainability Standards define material aspects as those that may reasonably be considered important for influencing the decisions of stakeholders, or reflecting the organisation's economic, environmental and social impacts.

As in every year, we checked the list of trends and topics through an analysis of recent laws and regulations, external research, reporting guidelines, benchmarks and peer reports. Instead of an extensive survey amongst internal and external stakeholders, we took a different approach in 2017.

As a result of the acquisition of Delta Lloyd, the first step in our process was the integration of the 2016 materiality matrices of NN Group and Delta Lloyd. As most topics in the matrices were similar, some topics were integrated. For example, talent attraction and retention and training and development were merged into human capital development. The scores of the topics were merged based on the number of employees per organisation.

In line with the GRI Standards, the x-axis of the matrix was adjusted from 'Relevance to NN' to 'NN's impact on the topic'. This resulted in trends, such as demographic change and low interest rates, ending up in the left quartiles of the matrix. Although our impact on these trends is limited, they are truly relevant to our business and therefore described on pages 17-18 of this Annual Review.

To validate the outcome of this exercise, we organised a dialogue session with a group of 20 internal and external stakeholders. The latter included investors, regulators, NGOs and experts in the area of sustainability.

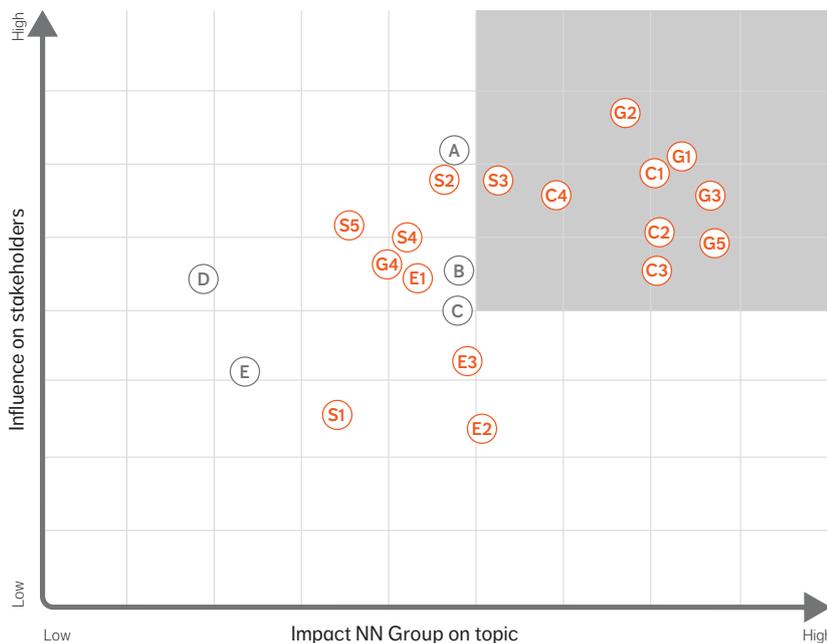
Internally, we invited representatives from different business units and relevant staff functions. During the session, all topics were discussed and rated on a scale of one to five. The process was supported by an external specialised agency to ensure it was balanced and independent.

The materiality matrix was discussed with NN Group's Management Board, and validated by the Supervisory Board. The outcome is reflected in the chart below.

The most material topics, indicated in the upper right quarter of the matrix, and NN Group's response to them are described in the next chapter of this Annual Review. Although climate change is placed outside the upper right quarter, we address climate change risks and opportunities in this chapter, and in our response to the recommendations of the Taskforce Climate-related Financial Disclosures (on pages 58-61).

-  [Read more about the trends that are relevant to our business on pages 17-18.](#)
-  [Read more about the most material topics and our response to them on pages 20-23.](#)

### Topics recognised as most material by our stakeholders



#### Customers

- C1** Customer centricity
- C2** Innovation
- C3** New technologies, digital transformation and big data
- C4** Data privacy and security

#### Good governance

- G1** Transparency
- G2** Business Ethics & Compliance
- G3** Risk management
- G4** Responsible tax practices
- G5** Financial performance

#### Employees

- E1** Diversity and inclusion
- E2** Employee engagement
- E3** Human capital development

#### Society and environment

- S1** Financial and economic empowerment
- S2** Sustainable products and services
- S3** Responsible investment
- S4** Human Rights
- S5** Climate change

#### Macro-economic trends and developments

- A** Low interest rates and stability of financial markets
- B** Regulations
- C** Pension system
- D** Demographic change
- E** Geopolitical developments

## Understanding and addressing our material topics Continued

# A number of topics, resulting from the materiality assessment and our own analysis, impact the financial services industry and our company

### Material topics

#### Customers

#### **C1 C2** Customer centricity and innovation

The fundamental need of people to protect themselves against life's uncertainties will continue to drive growth in the insurance industry over the long term. But we are living in a new world: people are increasingly independent. They expect, and are used to, financial services companies delivering 24/7, no threshold access, through any means or device. A company's business model and the way it offers products and services must support this.

Innovation and digitalisation contribute to the further optimisation of product development and distribution capabilities. At the same time, they change the competitive landscape in our industry with new, non-traditional entrants. The result is an intensified focus on customers' needs, and a need for new and improved ways to service them.

#### Opportunities and risks

Customers are willing to consider products and services that offer something different from traditional savings and pension models. They do, however, continue to demand transparency and prudent management of their investments.

Companies need to decide where they want to invest in order to engage with their customers and build an ecosystem that facilitates customer contact. By doing this correctly and efficiently, a real competitive advantage can be obtained. Continuous feedback and interaction with customers is needed to design easy-to-understand products that anticipate their future needs, and that are priced at customers' expectations. Drivers for customer satisfaction are not only price and service, but also contributing to a more sustainable society and the quality of interaction moments.

#### Our response

We want to be the intuitive partner for our customers when it comes to planning their financial futures. This can take many forms, including digitalisation, developing new products to anticipate changing customer demands and finding new ways to distribute our products.

Innovation takes place within the business units, by improving our existing offering, process and services to create a digital, personal and relevant customer experience.

For example, in the Netherlands, we have defined 'Next Best Actions'. These are relevant and personal propositions that we offer during our contact with our customers.

We use a self-learning engine to determine the most suitable recommendations, resulting in higher customer satisfaction and improved cross-sell ratios.

Cultivating the right innovation mindset is key to ensuring that we have the necessary agility to deliver truly customer-oriented solutions and shorten the time to market. Our six international innovation labs – Sparklabs – provide an out-of-office environment to foster innovative ideas and infuse innovative thinking into our company. In 2017, we had more than 120 experiments (sparks) in our innovation pipeline. When new start-up products or services become successful, we may integrate them into our regular businesses.

We also believe that innovating our customer experience is supported by connecting with relevant partners. An example is our strategic partnership with Hesapkurdu.com, the leading online loan aggregator for mortgages and consumer loans in Turkey. This partnership provides for the exclusive distribution of NN Hayat ve Emeklilik's life and pension products for a period of 15 years.

Since March 2017, we have been a key partner in the Dutch Blockchain Coalition, a public-private consortium aimed at applying blockchain technology in Dutch society.

 [Read more about our innovation efforts to create the customer experience of tomorrow on pages 35-38 of this Annual Review.](#)

## Understanding and addressing our material topics Continued

### Material topics

#### Customers Continued

##### **C3 C4** New technology and data privacy

New technologies continue to impact the digitalisation of society, which is fundamentally changing the behaviours, needs and requirements of customers. The increased availability and sharing of data enables companies to improve the way they develop and offer tailor-made and personalised products and services. The expectation is that a variety of breakthrough technologies are set to spur a fundamental transformation of the financial services industry, such as blockchain, cloud computing, the Internet of Things, telematics, drones and artificial intelligence. With this comes increased risk and exposure to cyber crime activities and unwanted privacy breaches.

##### Opportunities and risks

Financial services companies are investing in new digital platforms to facilitate connectivity and benefit from these new technologies. At the same time, they possess large amounts of payment data or personal information about their customers. Therefore security awareness and data protection are vitally important.

Attacks on financial services companies can have a major impact, such as claims and lawsuits, but also a loss of trust, driven by customers' concerns about whether their information is truly safe. A major breach can seriously impact a company's reputation and brand.

##### Our response

Protecting financial and customer data is a key component in our daily business operations. We make every effort to provide optimal security and ensure confidentiality of our customers' data and transactions. Cyber security is an integral part of our risk management strategy, both internally and externally.

We invest in information security and data privacy and have dedicated security teams, consisting of more than 100 security professionals and our Chief Information Security Officer, with support from our NN Security Operation Centre (SoC). They collaborate with Business Unit Security Officers to provide 24/7 protection for our customers and our organisation against current and emerging cyber threats. We work with well-known certification authorities. We use encryption and authentication mechanisms to secure online communication and transactions.

Through education and awareness, security strategies are implemented at all levels of the organisation. Examples are periodic instructions to all employees on how data are to be stored and managed, phishing security tests, and awareness campaigns on password protection. We constantly perform security scans and employ security guidelines which our businesses must meet to properly protect data.

We work closely with various partners such as universities, law enforcement, other financial institutions, Team High Tech Cybercrime (THTC) and the National Cyber Security Centre (NCSC) to support our own cyber security initiatives such as the Dutch Cyber Collective ([www.nederlandsocybercollectief.nl](http://www.nederlandsocybercollectief.nl)) and other business innovations.

 Read more about our how we approach new technology and data privacy in the business segment chapters on pages 28-34 of this Annual Review.

##### The EU General Data Protection Regulation (GDPR)

Ensuring proper information security and data privacy is an important element of the GDPR. The GDPR will become applicable in the European Union on 25 May 2018. It aims to give citizens more control over their personal data and will for the first time unify all data protection legislation across Europe.

Under the GDPR, customers have enhanced rights, for example, the 'right of access', meaning that we should be able to respond within a month to any customer's request for information about the why, what and which of their personal data being processed by NN.

The GDPR is in line with our 'NN statement of Living our Values', which states that we use our knowledge responsibly, keep confidential what is entrusted to us and communicate proactively and honestly. NN has processes in place to safeguard personal data, and currently our businesses are busy implementing additional measures to properly and timely comply with this regulation. A central NN GDPR programme has been installed to manage the consistency and coordination of the implementation across our European businesses. All European businesses will appoint a Data Protection Officer (DPO). Through a mandatory e-learning course, all employees will learn about the basic principles of privacy/data protection and what is expected of them.

## Understanding and addressing our material topics Continued

### Material topics

#### Good governance

##### G1 G2 Business ethics and transparency

Several factors play a role in the success of a company that are beyond the scope of customer centricity and generating good financial returns alone. Business ethics and being transparent are crucial for ensuring long-term success. Customers ask for transparent products and services that are easy to understand and also have a positive impact on society and the environment, enabling them to make the right choices. They increasingly care about how companies integrate sustainability aspects into their business and product offerings. Businesses must be committed to operating from a transparent and ethical foundation as it relates to the treatment of employees, respect to the environment, and fair market practices in terms of pricing and consumer treatment.

##### Opportunities and risks

The reputation of a business among stakeholders is paramount in determining whether a company is a reliable supplier of products or a worthwhile investment. If a company is perceived to not operate transparently or ethically, customers are less inclined to buy its products and investors to buy its stock. Consistent ethical behaviour and transparency can contribute to a positive public image.

##### Our response

Our values guide our interactions with our stakeholders, and embody responsible business conduct and corporate citizenship. They are published in our 'NN statement of Living our Values'. Additionally, the NN Code of Conduct gives more detailed guidelines for specific behaviour. Written acknowledgement of the Code has been mandatory for NN Group since the first half of 2017, and needs to be acknowledged annually by all employees. Two other standards that guide us in our activities are the 'NN Group Human Rights Statement' and the 'NN Group Environmental Statement'. Before introducing new products and services, they go through our product approval and review process (PARP). We review our product range regularly to ensure that they meet our customer, compliance, risk, capital and profitability requirements. We strive to manage all our assets, in an environmentally and socially responsible way, by integrating environmental, social and governance (ESG) aspects in our investment processes.

 Read more about our values on pages 13-16 and responsible business standards on page 26 of this Annual Review.

##### G3 Risk and capital management

NN Group's role is to support customers in building and protecting their assets and covering their risks. Our risk and capital management activities seek to keep the company safe and profitable, in the interest of our stakeholders. NN Group adapts our risk management practices to new developments to ensure the business operates in a controlled way.

 For more information, refer to the 'Core skills that enable our strategy' chapter on pages 25-27 of this Annual Review, and the 'Risk management' in our Financial Report on pages 129-158 (Note 50).

##### Dutch unit-linked products

In the Netherlands, unit-linked products have received negative public attention since the end of 2006. We have taken this criticism to heart, as our aim is to support our customers as best we can. In recent years, Dutch insurance subsidiaries of NN Group have made significant progress in reaching out to individual customers who purchased unit-linked products in the past, addressing vulnerable customer groups as a priority ('activeren').

To date, Dutch insurance subsidiaries of NN Group have reached out to 100% of customers with a unit-linked policy. We encouraged all customers to carefully assess their unit-linked products in order to enable them to address their personal situation and offered customers the option to switch to another product or make changes to their policy free of charge.

As at 31 December 2017, the portfolios of Dutch insurance subsidiaries of NN Group comprised approximately 500,000 active policies. Dutch subsidiaries of NN Group will continue to support customers with a unit-linked policy by providing aftercare. In a limited number of cases (less than 1,000), Dutch insurance subsidiaries of NN Group have settled disputes with individual customers. These are tailor-made solutions. A limited number of individual customers and several consumer protection organisations have initiated legal proceedings against Dutch insurance subsidiaries of NN Group.

 Read more on pages 117-119 of the Financial Report (Note 43).

##### G5 Financial performance

Prudent financial management is NN Group's main driver to maintain a strong balance sheet. This is key to absorbing market volatility and ensuring NN Group and our operating entities are sufficiently capitalised at all times. This is how we ensure good financial performance, keeping our customers' money safe and generating attractive returns. For 2017, our Solvency II ratio and cash capital position remained robust, at 199% and EUR 1,434 million respectively, in line with our disciplined approach to managing our capital. Our operating performance was strong, with the operating result of the ongoing business at EUR 1,586 million. Our total Assets under Management increased to EUR 246 billion.

 Read more about how we manage our balance sheet on pages 39-40 of this Annual Review, and page 37 of the Financial Report.

## Understanding and addressing our material topics Continued

### Material topics

#### Society and environment

##### S3 Climate change

Although not recognised as the most material topic by our stakeholders, we believe it is evident that climate change impacts our businesses. As one of the biggest challenges facing the world today, we can already see the effects of climate change with weather events such as windstorms, drought and sea level rise. The UN Intergovernmental Panel on Climate Change has predicted that if average global temperatures increase more than 2°C this century, these events will become more frequent and severe, posing a significant threat to livelihoods and the wellbeing of society. This underlines the need to take urgent action to meet the goals of the Paris Agreement to keep a global temperature rise this century to a maximum of 2°C, and striving for 1.5°C, above pre-industrial levels.

##### Risks and opportunities

We are exposed to climate risks primarily through our non-life insurance policies, which cover damage caused by weather events such as windstorms or hail, and through our investment holdings in companies which may be affected by tightening regulation, technological developments and changing consumer preferences. At the same time, climate change creates opportunities for the development of new products and investments that contribute to climate change solutions for ourselves and for the clients and beneficiaries on behalf of whom we invest.

##### Our response

We manage our greenhouse gas emissions to mitigate the impacts of our direct operations and are a carbon-neutral company. We further improve our understanding of climate risks to provide adequate protection for our customers through our insurance products, while managing the risks posed to our investment portfolio, and using our influence and expertise to encourage investee companies to play their part in the transition to a lower-carbon economy.

We believe that collaboration is important to tackle climate change. In 2017, we strengthened our network by joining the Institutional Investors Group on Climate Change. NN Investment Partners, our asset manager, endorsed the 'Letter from Global Investors to Governments of the G7 and G20 nations' urging them to stand by the Paris Agreement, and expanded its engagement on climate risk by joining the collaborative Climate Action 100+ initiative.

To further understand and manage the risks and opportunities of climate change, it is important that the quality and availability of climate-related financial disclosures continue to improve. NN Group therefore endorsed the recommendations of the Financial Stability Board's Task Force on Climate-related Financial Disclosures (TCFD) and made steps to integrate them in our own reporting.



For our response to the TCFD, refer to pages 58-61 of this Annual Review.

##### S3 Responsible investment

Our Responsible Investment Policy Framework sets out our vision and approach on Responsible Investment (RI), which we define as the integration of environmental, social and governance (ESG) aspects in our investment processes and ownership practices. NN Investment Partners (NN IP) formalised its commitment to Responsible Investment by signing the United Nations-supported Principles for Responsible Investment in 2008. NN IP has since made the consideration of ESG factors an integral part of its investment decisions, in the conviction that these may impact both risks and returns. For clients who want to take sustainability a step further, NN IP also offers specialised Socially Responsible Investment (SRI) strategies and tailor-made RI solutions.



For more information, please refer to the chapter on responsible investment on pages 41-44 of this Annual Review.