

**Rating Action: Moody's affirms Direct Line Insurance Group's IFRS at A1 changes outlook to negative**

---

16 January 2023

London, January 16, 2023 - Moody's Investors Service (Moody's) has today affirmed the A1 insurance financial strength rating (IFSR) on Direct Line Insurance Group's (DLG) key operating entity - U K Insurance Limited - and changed the outlook to negative from stable.

A full list of affected ratings can be found at the end of this press release.

**RATINGS RATIONALE**

**NEGATIVE OUTLOOK REFLECTS DIFFICULT TRADING CONDITIONS**

The change in outlook to negative reflects the deterioration in DLG's profitability during YE2022 combined with Moody's expectation of further earnings headwinds, which could arise from high claims inflation and difficult pricing conditions in the UK retail property and casualty (P&C) market. The negative outlook also reflects the risks that it could take the group longer than anticipated to rebuild its capital resilience, with the YE2022 Solvency II ratio now towards the bottom end of DLG's target range of 140% to 180%. Moody's views positively the actions taken by the Group to restore its balance sheet strength, but the suspension of the final YE2022 dividend, coupled with a challenging earnings outlook, could, at least temporarily, adversely impact the group's access to external market funding.

Akin to its peers, DLG reported a significant reduction in its earnings in the first half of 2022 (H1 2022), with profit before tax down 32% to £178 million. This was driven in part by the normalization of motor claims frequency from lower levels during the pandemic related lockdowns, but also by significant levels of motor claims severity inflation. More recently, the group announced that a further uptick in motor severity inflation coupled with elevated weather losses (totaling around £140 million, well above the group's £73 million budget) will result in an overall underwriting loss for YE2022, with a combined ratio (normalized for weather) in the range of 102-103%.

In addition to underwriting losses the group has also realized some investment losses related to the sale of longer duration credit and has been hit by a £45 million revaluation of its commercial property portfolio. This loss, together with the impact of volatile financial markets, has further eroded DLG's Solvency II ratio from its 152% position at H1 2022, towards the bottom end of its 140%-180% target range.

Moody's believes that the group will continue to take necessary actions to (1) rebuild its regulatory solvency ratio back up towards its operating target of 160%; and (2) restore its underwriting margins and internal capital generating capabilities.

Moody's believes DLG will strengthen its profitability in 2023, with earnings supported by pricing increases, lower technology investment spend, lower operating expense and higher investment returns on the back of rising interest rates. Nevertheless, owing to challenging conditions, the group has lowered its underwriting profit forecast for the year ahead, expecting the combined ratio to be around 97%-98% (versus the group's 93%-95% medium term combined ratio target). YE2024 onwards, as market pricing reaches a new equilibrium, the group should start to benefit from its

new tech-enabled pricing capabilities and its partnership with Motability Operations Ltd, which will expand the group's motor customer base by around 15%, whilst adding further scale to DLG's claims management service.

Moody's also expects DLG to sustainably rebuild its Solvency II ratio to around 160% over the coming 12-18 months, supported by the suspension of the final dividend and investment portfolio actions taken to reduce the group's sensitivities to financial market volatility, most notably widening credit spreads.

However, the negative outlook reflects the risk that it could take materially longer for the group to rebuild its earnings power and capital adequacy owing to the difficult trading conditions in the UK retail P&C market, to which the group is highly exposed. Heightened competition in the home market and high claims inflation and the cost-of-living crisis may result in the group sacrificing volume and market position to protect its combined ratio. Moreover, owing to the capital management actions already taken, there may be less scope for further changes to support the group's solvency ratio in a near term stress scenario.

#### RATING AFFIRMATION

The affirmation of DLG's ratings reflects the group's: (1) powerful brands and top tier position in the UK retail P&C market, together with a growing share of the UK SME commercial P&C sector; (2) a relatively conservative investment portfolio, which has been further de-risked during 2022; and (3) low financial leverage with good average earnings coverage of interest. These strengths, however, are tempered by the group's dependence on the very competitive and highly regulated UK personal motor insurance market.

Notwithstanding the significant decline in earnings during 2022, the group has a long track record of underwriting discipline, which had consistently translated into strong returns on capital, averaging 11% over the period from 2017 to 2021.

#### FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

Negative rating pressure could arise over the next 12-18 months in case: (1) DLG is not able to restore its internal capital generation capabilities and underwriting profitability to towards the group's medium-term target; (2) it becoming apparent that DLG's franchise is weakening; and/or (3) the group's Solvency II ratio remaining consistently below 160%.

Given the negative outlook, there is limited upward pressure on the ratings, but the outlook could revert to stable over the outlook horizon in case of: (1) DLG's underwriting earnings improving in line with management plans, without a meaningful loss of market share; (2) the restoration of the group's Solvency II ratio to around 160%; and (3) the group maintain its financial leverage below 25% (calculated based on IFRS4 equity).

#### LIST OF AFFECTED RATINGS

U K Insurance Limited:

..Affirmation:

Insurance financial strength rating, affirmed at A1

..Outlook Action:

Outlook changed to Negative from Stable

Direct Line Insurance Group plc:

..Affirmation:

Subordinated debt rating, affirmed at Baa1 (hyb)

Preferred Stock Non-cumulative, affirmed at Baa3 (hyb)

..Outlook Action:

Outlook changed to Negative from Stable

#### PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Property and Casualty Insurers Methodology published in August 2022 and available at <https://ratings.moodys.com/api/rmc-documents/391814>. Alternatively, please see the Rating Methodologies page on <https://ratings.moodys.com> for a copy of this methodology.

#### REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found on <https://ratings.moodys.com/rating-definitions>.

For ratings issued on a program, series, category/class of debt or security this announcement provides certain regulatory disclosures in relation to each rating of a subsequently issued bond or note of the same series, category/class of debt, security or pursuant to a program for which the ratings are derived exclusively from existing ratings in accordance with Moody's rating practices. For ratings issued on a support provider, this announcement provides certain regulatory disclosures in relation to the credit rating action on the support provider and in relation to each particular credit rating action for securities that derive their credit ratings from the support provider's credit rating. For provisional ratings, this announcement provides certain regulatory disclosures in relation to the provisional rating assigned, and in relation to a definitive rating that may be assigned subsequent to the final issuance of the debt, in each case where the transaction structure and terms have not changed prior to the assignment of the definitive rating in a manner that would have affected the rating. For further information please see the issuer/deal page for the respective issuer on <https://ratings.moodys.com>.

For any affected securities or rated entities receiving direct credit support from the primary entity(ies) of this credit rating action, and whose ratings may change as a result of this credit rating action, the associated regulatory disclosures will be those of the guarantor entity. Exceptions to this approach exist for the following disclosures, if applicable to jurisdiction: Ancillary Services, Disclosure to rated entity, Disclosure from rated entity.

The ratings have been disclosed to the rated entity or its designated agent(s) and issued with no amendment resulting from that disclosure.

These ratings are solicited. Please refer to Moody's Policy for Designating and Assigning Unsolicited Credit Ratings available on its website <https://ratings.moodys.com>.

Regulatory disclosures contained in this press release apply to the credit rating and, if applicable, the related rating outlook or rating review.

Moody's general principles for assessing environmental, social and governance (ESG) risks in our credit analysis can be found at [https://ratings.moody's.com/documents/PBC\\_1288235](https://ratings.moody's.com/documents/PBC_1288235).

The Global Scale Credit Rating on this Credit Rating Announcement was issued by one of Moody's affiliates outside the EU and is endorsed by Moody's Deutschland GmbH, An der Welle 5, Frankfurt am Main 60322, Germany, in accordance with Art.4 paragraph 3 of the Regulation (EC) No 1060/2009 on Credit Rating Agencies. Further information on the EU endorsement status and on the Moody's office that issued the credit rating is available on <https://ratings.moody's.com>.

Please see <https://ratings.moody's.com> for any updates on changes to the lead rating analyst and to the Moody's legal entity that has issued the rating.

Please see the issuer/deal page on <https://ratings.moody's.com> for additional regulatory disclosures for each credit rating.

Helena Kingsley-Tomkins  
VP-Senior Analyst  
Financial Institutions Group  
Moody's Investors Service Ltd.  
One Canada Square  
Canary Wharf  
London  
United Kingdom  
JOURNALISTS: 44 20 7772 5456  
Client Service: 44 20 7772 5454

Simon James Robin Ainsworth  
Associate Managing Director  
Financial Institutions Group  
JOURNALISTS: 44 20 7772 5456  
Client Service: 44 20 7772 5454

Releasing Office:  
Moody's Investors Service Ltd.  
One Canada Square  
Canary Wharf  
London, E14 5FA  
United Kingdom  
JOURNALISTS: 44 20 7772 5456  
Client Service: 44 20 7772 5454

**MOODY'S**  
INVESTORS SERVICE

© 2023 Moody's Corporation, Moody's Investors Service, Inc., Moody's Analytics, Inc. and/or their licensors and affiliates (collectively, "MOODY'S"). All rights reserved.

**CREDIT RATINGS ISSUED BY MOODY'S CREDIT RATINGS AFFILIATES ARE THEIR CURRENT OPINIONS OF THE RELATIVE FUTURE CREDIT RISK OF ENTITIES, CREDIT COMMITMENTS, OR DEBT OR DEBT-LIKE SECURITIES, AND MATERIALS, PRODUCTS, SERVICES AND INFORMATION PUBLISHED BY MOODY'S (COLLECTIVELY, "PUBLICATIONS") MAY INCLUDE SUCH CURRENT OPINIONS. MOODY'S DEFINES CREDIT RISK AS THE RISK THAT AN**

**ENTITY MAY NOT MEET ITS CONTRACTUAL FINANCIAL OBLIGATIONS AS THEY COME DUE AND ANY ESTIMATED FINANCIAL LOSS IN THE EVENT OF DEFAULT OR IMPAIRMENT. SEE APPLICABLE MOODY'S RATING SYMBOLS AND DEFINITIONS PUBLICATION FOR INFORMATION ON THE TYPES OF CONTRACTUAL FINANCIAL OBLIGATIONS ADDRESSED BY MOODY'S CREDIT RATINGS. CREDIT RATINGS DO NOT ADDRESS ANY OTHER RISK, INCLUDING BUT NOT LIMITED TO: LIQUIDITY RISK, MARKET VALUE RISK, OR PRICE VOLATILITY. CREDIT RATINGS, NON-CREDIT ASSESSMENTS ("ASSESSMENTS"), AND OTHER OPINIONS INCLUDED IN MOODY'S PUBLICATIONS ARE NOT STATEMENTS OF CURRENT OR HISTORICAL FACT. MOODY'S PUBLICATIONS MAY ALSO INCLUDE QUANTITATIVE MODEL-BASED ESTIMATES OF CREDIT RISK AND RELATED OPINIONS OR COMMENTARY PUBLISHED BY MOODY'S ANALYTICS, INC. AND/OR ITS AFFILIATES. MOODY'S CREDIT RATINGS, ASSESSMENTS, OTHER OPINIONS AND PUBLICATIONS DO NOT CONSTITUTE OR PROVIDE INVESTMENT OR FINANCIAL ADVICE, AND MOODY'S CREDIT RATINGS, ASSESSMENTS, OTHER OPINIONS AND PUBLICATIONS ARE NOT AND DO NOT PROVIDE RECOMMENDATIONS TO PURCHASE, SELL, OR HOLD PARTICULAR SECURITIES. MOODY'S CREDIT RATINGS, ASSESSMENTS, OTHER OPINIONS AND PUBLICATIONS DO NOT COMMENT ON THE SUITABILITY OF AN INVESTMENT FOR ANY PARTICULAR INVESTOR. MOODY'S ISSUES ITS CREDIT RATINGS, ASSESSMENTS AND OTHER OPINIONS AND PUBLISHES ITS PUBLICATIONS WITH THE EXPECTATION AND UNDERSTANDING THAT EACH INVESTOR WILL, WITH DUE CARE, MAKE ITS OWN STUDY AND EVALUATION OF EACH SECURITY THAT IS UNDER CONSIDERATION FOR PURCHASE, HOLDING, OR SALE.**

MOODY'S CREDIT RATINGS, ASSESSMENTS, OTHER OPINIONS, AND PUBLICATIONS ARE NOT INTENDED FOR USE BY RETAIL INVESTORS AND IT WOULD BE RECKLESS AND INAPPROPRIATE FOR RETAIL INVESTORS TO USE MOODY'S CREDIT RATINGS, ASSESSMENTS, OTHER OPINIONS OR PUBLICATIONS WHEN MAKING AN INVESTMENT DECISION. IF IN DOUBT YOU SHOULD CONTACT YOUR FINANCIAL OR OTHER PROFESSIONAL ADVISER.

ALL INFORMATION CONTAINED HEREIN IS PROTECTED BY LAW, INCLUDING BUT NOT LIMITED TO, COPYRIGHT LAW, AND NONE OF SUCH INFORMATION MAY BE COPIED OR OTHERWISE REPRODUCED, REPACKAGED, FURTHER TRANSMITTED, TRANSFERRED, DISSEMINATED, REDISTRIBUTED OR RESOLD, OR STORED FOR SUBSEQUENT USE FOR ANY SUCH PURPOSE, IN WHOLE OR IN PART, IN ANY FORM OR MANNER OR BY ANY MEANS WHATSOEVER, BY ANY PERSON WITHOUT MOODY'S PRIOR WRITTEN CONSENT. MOODY'S CREDIT RATINGS, ASSESSMENTS, OTHER OPINIONS AND PUBLICATIONS ARE NOT INTENDED FOR USE BY ANY PERSON AS A BENCHMARK AS THAT TERM IS DEFINED FOR REGULATORY PURPOSES AND MUST NOT BE USED IN ANY WAY THAT COULD RESULT IN THEM BEING CONSIDERED A BENCHMARK.

All information contained herein is obtained by MOODY'S from sources believed by it to be accurate and reliable. Because of the possibility of human or mechanical error as well as other factors, however, all information contained herein is provided "AS IS" without warranty of any kind. MOODY'S adopts all necessary measures so that the information it uses in assigning a credit rating is of sufficient quality and from sources MOODY'S considers to be reliable including, when appropriate, independent third-party sources. However, MOODY'S is not an auditor and cannot in every instance independently verify or validate information received in the credit rating process or in preparing its Publications.

To the extent permitted by law, MOODY'S and its directors, officers, employees, agents, representatives, licensors and suppliers disclaim liability to any person or entity for any indirect,

special, consequential, or incidental losses or damages whatsoever arising from or in connection with the information contained herein or the use of or inability to use any such information, even if MOODY'S or any of its directors, officers, employees, agents, representatives, licensors or suppliers is advised in advance of the possibility of such losses or damages, including but not limited to:

(a) any loss of present or prospective profits or (b) any loss or damage arising where the relevant financial instrument is not the subject of a particular credit rating assigned by MOODY'S.

To the extent permitted by law, MOODY'S and its directors, officers, employees, agents, representatives, licensors and suppliers disclaim liability for any direct or compensatory losses or damages caused to any person or entity, including but not limited to by any negligence (but excluding fraud, willful misconduct or any other type of liability that, for the avoidance of doubt, by law cannot be excluded) on the part of, or any contingency within or beyond the control of, MOODY'S or any of its directors, officers, employees, agents, representatives, licensors or suppliers, arising from or in connection with the information contained herein or the use of or inability to use any such information.

NO WARRANTY, EXPRESS OR IMPLIED, AS TO THE ACCURACY, TIMELINESS, COMPLETENESS, MERCHANTABILITY OR FITNESS FOR ANY PARTICULAR PURPOSE OF ANY CREDIT RATING, ASSESSMENT, OTHER OPINION OR INFORMATION IS GIVEN OR MADE BY MOODY'S IN ANY FORM OR MANNER WHATSOEVER.

Moody's Investors Service, Inc., a wholly-owned credit rating agency subsidiary of Moody's Corporation ("MCO"), hereby discloses that most issuers of debt securities (including corporate and municipal bonds, debentures, notes and commercial paper) and preferred stock rated by Moody's Investors Service, Inc. have, prior to assignment of any credit rating, agreed to pay to Moody's Investors Service, Inc. for credit ratings opinions and services rendered by it fees ranging from \$1,000 to approximately \$5,000,000. MCO and Moody's Investors Service also maintain policies and procedures to address the independence of Moody's Investors Service credit ratings and credit rating processes. Information regarding certain affiliations that may exist between directors of MCO and rated entities, and between entities who hold credit ratings from Moody's Investors Service, Inc. and have also publicly reported to the SEC an ownership interest in MCO of more than 5%, is posted annually at [www.moodys.com](http://www.moodys.com) under the heading "Investor Relations — Corporate Governance — Charter Documents - Director and Shareholder Affiliation Policy."

Additional terms for Australia only: Any publication into Australia of this document is pursuant to the Australian Financial Services License of MOODY'S affiliate, Moody's Investors Service Pty Limited ABN 61 003 399 657AFSL 336969 and/or Moody's Analytics Australia Pty Ltd ABN 94 105 136 972 AFSL 383569 (as applicable). This document is intended to be provided only to "wholesale clients" within the meaning of section 761G of the Corporations Act 2001. By continuing to access this document from within Australia, you represent to MOODY'S that you are, or are accessing the document as a representative of, a "wholesale client" and that neither you nor the entity you represent will directly or indirectly disseminate this document or its contents to "retail clients" within the meaning of section 761G of the Corporations Act 2001. MOODY'S credit rating is an opinion as to the creditworthiness of a debt obligation of the issuer, not on the equity securities of the issuer or any form of security that is available to retail investors.

Additional terms for Japan only: Moody's Japan K.K. ("MJKK") is a wholly-owned credit rating agency subsidiary of Moody's Group Japan G.K., which is wholly-owned by Moody's Overseas Holdings Inc., a wholly-owned subsidiary of MCO. Moody's SF Japan K.K. ("MSFJ") is a wholly-owned credit rating agency subsidiary of MJKK. MSFJ is not a Nationally Recognized Statistical Rating Organization ("NRSRO"). Therefore, credit ratings assigned by MSFJ are Non-NRSRO Credit Ratings. Non-NRSRO Credit Ratings are assigned by an entity that is not a NRSRO and, consequently, the rated obligation will not qualify for certain types of treatment under U.S. laws. MJKK and MSFJ are credit

rating agencies registered with the Japan Financial Services Agency and their registration numbers are FSA Commissioner (Ratings) No. 2 and 3 respectively.

MJJK or MSFJ (as applicable) hereby disclose that most issuers of debt securities (including corporate and municipal bonds, debentures, notes and commercial paper) and preferred stock rated by MJJK or MSFJ (as applicable) have, prior to assignment of any credit rating, agreed to pay to MJJK or MSFJ (as applicable) for credit ratings opinions and services rendered by it fees ranging from JPY100,000 to approximately JPY550,000,000.

MJJK and MSFJ also maintain policies and procedures to address Japanese regulatory requirements.