

DIRECT LINE GROUP ANNOUNCES Q3 UPDATE AND ITS MEDIUM-TERM STRATEGY AND NEW TARGETS

Direct Line Insurance Group plc is today announcing its Q3 trading update and medium-term strategy and new financial targets ahead of its inaugural Capital Markets Day tomorrow, 21 November, 2019.

Penny James, CEO, comments:

"I'm encouraged with the Group's performance in Q3, with motor returning to modest growth, helped by some improvement in market conditions. Although we are only halfway through Q4 the improving trends have continued.

"Looking ahead I'm excited by our potential. At the heart of our business is the passion to provide our customers with outstanding service and peace of mind, and these qualities have been the foundation of the Group's good financial returns, supported by our robust balance sheet. My new executive team and I are building a platform that combines our strengths of customer and brand with technology, and is a simpler, leaner and more agile business to deliver the real potential we see, unlocking value for shareholders.

"I believe that our strategy, supported by our five sustainability pillars of People, Customer, Society, Planet and Governance, enables us to continue to deliver benefits to all our stakeholders including attractive and sustainable shareholder returns.

"We are starting to conclude a phase of high capital expenditure aimed at bringing our technology to the forefront of the industry. We are in the process of rolling out much of this technology now, and while there remains more to do, we are pleased with the progress so far. We expect capital expenditure to begin to decline from its peak in 2019 and for all our major IT platforms to be substantially rolled out by the end of 2021.

"Assisted by the technology change, we will transform our business by working in a faster and nimbler way to deliver the potential of the Group. This includes improving our cost efficiency, enabling faster and more accurate pricing and continuing to improve customer experience. All this aims to strengthen margins on the business we write and increase our competitiveness to deliver growth.

"I am looking forward to welcoming investors and analysts to our Doncaster contact centre tomorrow to share more details on our plans, introduce you to our exceptional people and to show, first hand, the really special culture we have at Direct Line Group."

Strategic objectives

We are first and foremost a people business which aims to give our customers peace of mind. We benefit from the focus of operating in the UK only while also having scale and flexibility from providing all major retail general insurance products through different leading brands and all major distribution channels.

Today our strategic advantage is grounded in our culture of serving our customers well, through brands, distribution, deep technical expertise and excellent claims management. This combination has helped provide our customers with excellent service and shareholders with reliable and attractive cash returns.

At the same time, we have been making significant investments in our technology to help us reach and serve even more customers, more efficiently, and improve their experience further.

Today we are launching the Group's vision, purpose and six key strategic objectives to drive improvements in how we reach our customers and to deliver the skills and capabilities that are critical to win them:

Best at Direct

A direct relationship with our customers provides opportunity for profitable growth by meeting a broader set of customer needs and the foundation for future product and service innovation.

We are aiming to be the UK's leading direct insurer "by a mile" by anticipating our customers' needs and making it easy for them to buy from us.

Win on Price Comparison Websites

Price comparison websites ("PCWs") are the biggest market for new business in the UK and are a key route for profitable growth.

Our new technology enables us to deliver a step change in our pricing and trading capability, so that our PCW brands win customers from our competitors.

Extend our reach

Our new IT platforms, when combined with our experience in brands and customer service, will give us a scale platform to make it easier for us to extend our partnership reach and to participate in the consolidation of the sector.

Technical edge

We want to give our customers a great experience and create a sustainable competitive advantage for the Group by better utilising our inherent scale advantage in repair, data and claims insight and management.

To achieve this, we will use our data, scale, skill and insight across claims, pricing and underwriting to deliver valued products to customers.

Nimble and cost efficient

We are taking action to bring our cost base in line with the market to compete better, in particular through PCWs and partnerships. Alongside, we are also introducing new ways of working designed to leverage our advantages within each product and channel.

We are taking these steps to transform into an agile, cost effective business to drive efficiency and simplicity for us and our customers.

Great people

Direct Line Group is a people focused business and we are proud of the top quartile engagement of our people which is the underpin to our strong customer service.

As disruption in our market increases, we also need to become brilliant at innovation and change. We can only do this by empowering and developing the best people.

Therefore, we want to be a home for empowered people who celebrate difference and challenge the status quo to deliver for our customers.

These six strategic objectives are intrinsically supported by our focus on sustainability: People, Planet, Customers, Society and Governance. We are proud of our strong ESG ratings¹, and our culture is that we instinctively put our people first, care for our customers and act for the benefit of our community and planet. We are now putting these sustainability pillars at the heart of our strategic thinking, ensuring the sustainability lens is constantly in our thinking as we shape our business for the future.

Financial targets

Costs: We are announcing today that we aim to improve our operating expense ratio to 20% by the year ending 31 December 2023, bringing us to a sustainably competitive level. We expect to achieve this through a combination of automation and process improvement, self-service and digitalisation, lowering our cost of change and improving organisational agility.

For the year ended 31 December 2018 operating expenses were £722 million and before amortisation and depreciation were £644 million. We aim to reduce operating expenses before amortisation and depreciation by more than £50m by year ending 31 December 2021 to below £590 million, absorbing the cost of planned growth and expected inflation. We expect an increase in non-cash amortisation and depreciation charges as our technology assets are brought into use, resulting in reported operating expenses of less than £700 million, in line with our expectations for 2019.

The Group expects to incur restructuring and other one-off costs totalling approximately £60 million across the years ending 31 December 2019 and 2020. We will take further steps to reduce costs when we believe the payback on implementation is compelling.

We expect to reduce our capital expenditure as our major technology assets are brought into use, to less than £100 million from the year ending 31 December 2021 compared with £155 million for the year ended 31 December 2018 (2019 guidance: approximately £175 million).

This, and the reduction in operating expenses before amortisation and depreciation have a direct positive impact on our operational capital generation of over £100 million per annum pre-tax.

Quality of earnings: We aim to grow the current year contribution to operating profits² to more than a half by the year ending 31 December 2021 through a combination of lower costs, improved current year loss ratio and modest growth. We expect investment income yield of 2.0% in 2020 with no material gains. We are also reiterating our combined operating ratio of between 93% and 95% through the medium term³. This is supported by the benefits of our technology transformation, the major part of which we expect to complete by the end of 2021.

Capital Management

The Group reiterates its capital management policy and solvency risk appetite range of between 140% and 180% of solvency capital requirements. In normal circumstances we would not expect to need to hold in excess of 160%. In the event the Group holds surplus capital the Board will consider both special dividends and share buybacks.

At the Group's current valuation, where the regular dividend yield is materially higher than market comparators, the Board's preference is to return any surplus capital, after ordinary dividends, by way of a buyback programme.

Furthermore, we intend to use our capital and risk management expertise to fully explore and execute the opportunities available to us, including reinsurance, to optimise returns on the capital we hold.

Notes:

1. Please see our Environmental, Social and Governance page at our Group website <https://www.directlinegroup.co.uk/en/investors/esg.html>
2. Operating profit normalised for weather less prior year reserve releases.
3. Normalised for weather and before restructuring and other one-off costs.

Q3 trading update

Overall, trading since the middle of the year showed signs of improvement, and highlighted some of our key strengths, particularly in motor where our claims inflation experience remains within our 3% to 5% long-term expectation.

Trading update for the 3 months to 30 September 2019

	Q3 2019 £m	Q3 2018 £m	Change
Gross written premium			
Motor	457.8	456.4	0.3%
Home	158.6	166.7	(4.9%)
Rescue and other personal lines	117.4	113.4	3.5%
Commercial	124.2	118.0	5.3%
Total	858.0	854.5	0.4%
Of which direct own brands ¹	612.7	610.4	0.4%
	30 Sep 2019	30 Sep 2018	Change
Total in-force policies	14,837	15,183	(2.3%)
Of which direct own brands ¹	7,235	7,078	2.2%

Financial highlights

- Motor gross written premium increased by 0.3% compared to Q3 2018, a significant improvement on previous quarters and the positive trend has continued into Q4. This improvement arose principally from better new business trading, in particular from Churchill on price comparison websites, which has supported in force policy count stabilising in the quarter. Darwin² contributed to growth during the period and continued to cautiously expand within the Group's existing footprint.
- The Group continued to price for its view of motor claims inflation, maintaining pricing discipline in a market that, overall, experienced broadly flat pricing. Motor claims severity inflation remained at the upper end of long-term expectations of 3% to 5%, with frequency in 2019 continuing to improve compared to 2018.
- Home gross written premium was 4.9% lower compared to Q3 2018, driven by the run-off of partnerships. Total in-force policies were down 1.0% in the quarter.
- Home claims inflation in 2019 has benefited from favourable experience on escape of water, contributing to claims inflation to date in 2019 which is lower than the Group's expectations of the long-term average. Very early estimates for the November floods are approximately £10 million across both Home and Commercial.
- Rescue and other personal lines gross written premium increased by 3.5% compared to Q3 2018. Green Flag, the Group's direct Rescue brand, passed a landmark of over one million in force policies with gross written premiums up 15.5% compared to Q3 2018. This growth was partially offset by a reduction in packaged bank account volumes.
- Commercial gross written premium increased by 5.3%, compared to Q3 2018. This reflected growth in both Direct Line for Business, in particular in its products for small and micro enterprises and tradespeople, and in NIG and other.

For information: gross written premium for the 9 months to 30 September 2019

	9 months 2019 £m	9 months 2018 £m	Change
Gross written premium			
Motor	1,258.3	1,296.2	(2.9%)
Home	441.9	457.4	(3.4%)
Rescue and other personal lines	333.9	323.3	3.3%
Commercial	399.1	387.9	2.9%
Total	2,433.2	2,464.8	(1.3%)
Of which direct own brands ¹	1,684.9	1,709.4	(1.4%)

Notes:

1. Direct own brands include in-force policies for Home and Motor under the Direct Line, Churchill, Darwin and Privilege brands, Rescue policies under the Green Flag brand and Commercial policies under the Direct Line for Business brand.
2. Darwin is a new brand aimed at price comparison website customers.

Forward-looking statements disclaimer

Certain information contained in this document, including any information as to the Group's strategy, plans or future financial or operating performance, constitutes "forward-looking statements". These forward-looking statements may be identified by the use of forward-looking terminology, including the terms "aims", "ambition", "anticipates", "aspire", "believes", "continue", "could", "estimates", "expects", "guidance", "intends", "may", "mission", "outlook", "over the medium term", "plans", "predicts", "projects", "propositions", "seeks", "should", "strategy", "targets" or "will" or, in each case, their negative or other variations or comparable terminology, or by discussions of or references to strategy, plans, objectives, goals, future years, future events or intentions. These forward-looking statements include all matters that are not historical facts. They appear in several places throughout this document and include statements regarding the intentions, beliefs or current expectations of the Directors concerning, among other things: the Group's results of operations, financial condition, prospects, growth, strategies and the industry in which the Group operates. Examples of forward-looking statements include financial targets and guidance which are contained in this document specifically with respect to the return on tangible equity, solvency capital ratio, the Group's combined operating ratio, prior-year reserve releases, cost reduction, reductions in expense and commission ratios, investment income yield, new technology implementation, net realised and unrealised gains and risk appetite range. By their nature, all forward-looking statements involve risk and uncertainties because they relate to events and depend on circumstances that may or may not occur in the future or are beyond the Group's control.

Forward-looking statements are not guaranteeing future performance. The Group's actual results of operations, financial condition and the development of the business sector in which the Group operates may differ materially from those suggested by the forward-looking statements contained in this document, for example directly or indirectly as a result of, but not limited to, United Kingdom ("UK") domestic and global economic business conditions, the outcome of the UK general election on 12 December 2019 and the views and policies of any government following such election, the outcome of discussions within the UK parliament and discussions between the UK and the European Union ("EU") regarding a withdrawal agreement and/or the manner and terms on which, if any, the UK leaves the EU (usually called "Brexit") and the terms in due course of any future trading relationship between the UK and the EU, market-related risks such as fluctuations in interest rates and exchange rates, the policies and actions of and changes to the approaches by regulatory authorities (including (without limitation) changes arising out of the FCA market study on general insurance pricing practices and/or changes related to capital and solvency requirements or the Ogden discount rate or rates), the impact of competition, currency changes, inflation and deflation, the timing impact and other uncertainties of future acquisitions, disposals, joint ventures or combinations within relevant industries, as well as the impact of tax and other legislation and other regulation in the jurisdictions in which the Group and its affiliates operate. In addition, even if the Group's actual results of operations, financial condition and the development of the business sector in which the Group operates are consistent with the forward-looking statements contained in this document, those results or developments may not be indicative of results or developments in subsequent periods.

The forward-looking statements contained in this document reflect knowledge and information available as of the date of preparation of this document. The Group and the Directors expressly disclaim any obligations or undertaking to update or revise publicly any forward-looking statements, whether because of new information, future events or otherwise, unless required to do so by applicable law or regulation. Nothing in this document should be construed as a profit forecast.

Neither the content of Direct Line Group's website nor the content of any other website accessible from hyperlinks on the Group's website is incorporated into, or forms part of, this document.

Corporate information

Direct Line Insurance Group plc is a public limited company registered in England & Wales, number 02280426. The address of the registered office is Churchill Court, Westmoreland Road, Bromley BR1 1DP.

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