Direct Line Group

3 March 2020

DIRECT LINE INSURANCE GROUP PLC

PRELIMINARY RESULTS FOR THE YEAR ENDED 31 DECEMBER 2019

RESILIENT BUSINESS MODEL DRIVES GOOD RESULTS; LAUNCHING A SHARE BUYBACK

PENNY JAMES, CEO OF DIRECT LINE GROUP, COMMENTED

"We have delivered a good set of results, and continued to improve the quality, while navigating a difficult motor market and delivering significant change in the business. Our cost reductions and model of disciplined underwriting helped maintain a combined operating ratio of 92.2%, supported by all our product lines. This helped deliver 2.9% growth in our final dividend to 14.4 pence and I'm pleased to announce the launch of a share buyback of up to £150 million which we expect to complete by the end of July 2020.

"The motor insurance market began to show signs of improvement in the second half of 2019, helping us return to growth while our other major markets were competitive, with pricing largely keeping pace with inflationary cost pressures.

"At our Capital Markets Day in November, my new executive team and I updated you on our operational progress and set out the next stage of the Group's strategy, one aimed at making insurance personal, inclusive and a force for good. We have maintained our momentum for example by adding Darwin to another price comparison website, increasing functionality on our new Motor IT platform and adding Tradesperson and Van to our Direct Line for Business platform.

"We remain on track to achieve the operational and financial targets we outlined at our Capital Markets Day and are excited about our delivery plan for 2020."

Results summary

	FY 2019 £m	FY 2018[1,2] £m restated	Change
In-force policies (thousands)	**14,789**	15,073	(1.9%)
Of which: direct own brands[3] (thousands)	**7,290**	7,188	1.4%
Gross written premium	**3,203.1**	3,211.9	(0.3%)
Of which: direct own brands[3]	**2,227.8**	2,228.9	0.0%
Operating profit[4]	**546.9**	606.4	(9.8%)
Combined operating ratio[4,5]	**92.2%**	91.6%	(0.6pts)
Profit before tax	**509.7**	580.5	(12.2%)
Return on tangible equity[4]	**20.8%**	21.6%	(0.8pts)
Dividend per share – interim (pence)[6]	**7.2**	7.0	2.9%
– final (pence)[6]	**14.4**	14.0	2.9%
– special (pence)	**–**	8.3	–
	31 Dec 2019	31 Dec 2018	Change
Solvency capital ratio post-dividends and share buyback[7]	**165%**	170%	(5pts)

Financial highlights

- Grew direct own brand in-force policies by 1.4% with strong growth in Green Flag and Commercial direct own brands. Total in-force policies were lower as partnership volumes reduced.
- Total Group gross written premium was broadly steady as underwriting discipline resulted in fewer Motor and Home policies and lower premiums which was largely offset by growth in Green Flag and Commercial direct own brands.
- Operating expenses before restructuring and one-off costs of £693.7 million (2018 restated: £718.2 million) were in line with target of less than £700 million. Restructuring and one-off costs were £11.2 million (2018: £nil).
- Combined operating ratio was 92.2%. Adjusting for normal weather and changes to the Ogden discount rate, the combined operating ratio of 93.5% (2018 restated: 93.3%) was towards the lower end of the Group's medium-term target range of 93% to 95%. The current-year Motor loss ratio was broadly stable.
- Profit before tax was down 12.2% to £509.7 million (2018 restated: £580.5 million). The impact of benign weather in 2019 was more than offset by lower reserve releases, in part Ogden discount rate-related, non-repeat of investment and property gains and restructuring and one-off costs in 2019.
- Proposed final ordinary dividend of 14.4 pence, an increase of 2.9% on 2018. Announcing a £150 million share buyback and awarding our people £500 of free shares each.
- Strong capital position with a solvency capital ratio of 165% after proposed capital distributions (2018: 170%).

Strategic and operational highlights

- Launched our new purpose, vision and strategic objectives at our Capital Markets Day in November 2019.
- New Motor Insurance platform launched for Privilege new business across all distribution channels including price comparison websites ("**PCWs**").
- Launched Darwin, our new PCW proposition, on two aggregators.
- Launched our new travel system and migrated our RBS and NatWest customers onto the new platform which provides an end-to-end digital solution for over 1.6 million customers.
- Continued to transform Green Flag, which passed the one million customer milestone.
- NIG continued to focus on profit improvement through risk selection and mobilisation of new quote tools leading to increased pricing sophistication and improved efficiency.
- Direct Line for Business has continued to roll-out products on its new digital platform, most recently for Tradesperson and Van.

For further information, please contact

ANDY BROADFIELD
DIRECTOR OF INVESTOR RELATIONS AND CAPITAL

Tel: +44 (0)1651 831022

LISA TREMBLE
GROUP CORPORATE AFFAIRS AND SUSTAINABILITY DIRECTOR

Tel: +44 (0)1651 834211

PAUL SMITH
DIRECTOR OF INVESTOR RELATIONS DESIGNATE

Tel: +44 (0)1651 831756

Notes:

1. Results for the year ended 31 December 2018 have been restated to reflect the fully retrospective adoption of IFRS 16 'Leases'. See note 23 to the consolidated financial statements.
2. In-force policies, including direct own brands, as at 31 December 2018 have been restated to include 41,000 policies omitted from previously reported amounts.
3. 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 under the Direct Line for Business and Churchill brands.
4. See glossary on pages 47 to 49 for definitions and appendix A – Alternative performance measures on pages 50 to 53 for reconciliation to financial statement line items.
5. A reduction in the ratio represents an improvement as a proportion of net earned premium, while an increase in the ratio represents a deterioration. See glossary pages 47 to 49 for definitions.
6. The Group's dividend policy includes an expectation that generally one-third of the regular annual dividend will be paid in the third quarter as an interim dividend and two-thirds will be paid as a final dividend in the second quarter of the following year.
7. Estimates based on the Group's Solvency II partial internal model.

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 strategy, plans, objectives, goals, 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, percentage targets for current-year contribution to operating profit, prior-year reserve releases, cost reduction, reductions in expense and commission ratios, investment income yield, net realised and unrealised gains, capital expenditure 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 and/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 discussions between the UK and the European Union ("EU") regarding the terms, following Brexit, of any future trading and other relationships between the UK and the EU;
- the terms of future trading and other relationships between the UK and other countries following Brexit;
- market-related risks such as fluctuations in interest rates and exchange rates;
- the policies and actions of regulatory authorities (including 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, partnership arrangements, joint ventures or combinations within relevant industries; and
- 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 constitutes or 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.

Financial summary

	FY 2019 £m	FY 2018[1,2] £m restated	Change
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Gross written premium	**3,203.1**	3,211.9	(0.3%)
Of which: direct own brands	**2,227.8**	2,228.9	0.0%
Net earned premium	**2,984.9**	3,089.5	(3.4%)
Underwriting profit	**232.1**	259.8	(10.7%)
Instalment and other operating income	**180.2**	192.0	(6.1%)
Investment return	**134.6**	154.6	(12.9%)
Operating profit	**546.9**	606.4	(9.8%)
Restructuring and one-off costs	**(11.2)**	–	–
Operating profit after restructuring and one-off costs	**535.7**	606.4	(11.7%)
Finance costs	**(26.0)**	(25.9)	(0.4%)
Profit before tax	**509.7**	580.5	(12.2)%
Tax	**(89.8)**	(108.5)	17.2%
Profit after tax	**419.9**	472.0	(11.0)%
Key metrics			
Current-year attritional loss ratio[3,4]	**71.6%**	72.6%	1.0pts
Loss ratio[3,4]	**61.9%**	61.9%	0.0pts
Commission ratio[3,4]	**7.1%**	6.5%	(0.6pts)
Expense ratio[3,4]	**23.2%**	23.2%	0.0pts
Combined operating ratio[3,4]	**92.2%**	91.6%	(0.6pts)
Return on tangible equity[4]	**20.8%**	21.6%	(0.8pts)
Investment income yield[4]	**2.4%**	2.5%	(0.1pts)
Net investment income yield[4]	**2.1%**	2.0%	0.1pts
Investment return yield[4]	**2.2%**	2.4%	(0.2pts)
Basic earnings per share (pence)	**29.5**	33.3	(11.4%)
Diluted earnings per share (pence)	**29.2**	32.9	(11.2%)
Return on equity	**15.5%**	17.3%	(1.8pts)
Dividend per share – interim (pence)	**7.2**	7.0	2.9%
– final (pence)	**14.4**	14.0	2.9%
– total ordinary (pence)	**21.6**	21.0	2.9%
– special (pence)	**–**	8.3	–
	31 Dec 2019	31 Dec 2018[1] restated	Change
Net asset value per share (pence)	**193.4**	187.5	3.1%
Tangible net asset value per share (pence)	**142.0**	145.9	(2.7%)
Solvency capital ratio post-dividends[5]	**165%**	170%	(5pts)

Notes:

1. Results for the year ended 31 December 2018 have been restated to reflect the fully retrospective adoption of IFRS 16 'Leases'. See note 23 to the consolidated financial statements.
2. In-force policies, including direct own brands, as at 31 December 2018 have been restated to include 41,000 policies omitted from previously reported amounts.
3. A reduction in the ratio represents an improvement as a proportion of net earned premium, while an increase in the ratio represents a deterioration. See glossary on pages 47 to 49 for definitions.
4. See glossary on pages 47 to 49 for definitions and appendix A – Alternative performance measures on pages 50 to 53 for reconciliation to financial statement line items.
5. See note 7 on page 2, reported after proposed dividends.

CEO REVIEW

Direct Line Group has amazing people, a passion for great customer service and leading brands. It is especially exciting to be part of a business that is putting in place a transformation programme that is firmly focused on laying the foundations for our future success. There have been many highlights this year, and I am thrilled that in the midst of significant business change, a highly competitive market and an evolving regulatory backdrop, we have delivered another good set of financial results, with improved quality, demonstrating our discipline and the value of our business model. Overall, I'm pleased with our progress against the strategic and financial targets we set out at our Capital Markets Day in November.

Business performance

In 2019, we delivered £546.9 million of operating profit, a combined operating ratio of 92.2% and a return on tangible equity of 20.8%.

Direct own brands in-force policies grew by 1.4% to 7.3 million (2018 restated: 7.2 million) as Green Flag and Commercial direct own brands continued their strong growth, offset by lower volumes in Motor and Home. Total in-force policies were 1.9% lower than 2018 primarily due to lower Travel policies as lower packaged bank account volumes reduced and lower Motor and Home partner volumes reflecting previously announced partner exits.

Gross written premium was 0.3% lower than in 2018 (2019: £3,203.1 million, 2018: £3,211.9 million). The impact of lower average premiums in Motor and Home and lower partnership volumes were almost fully offset by strong growth in Green Flag and Commercial direct own brands. The second half of 2019 saw gross written premium increase by 3.4% compared to the first half of 2019 (H1 2019: £1,575.1 million; H2 2019: £1,628.0 million) as performance across Motor and Home direct own brands improved.

The current-year attritional loss ratio improved by 1.0 percentage point (2019: 71.6%, 2018 restated: 72.6%) with Home, Rescue and other personal lines and Commercial all improving and Motor remaining broadly steady. This demonstrates the benefits of our focus on underwriting discipline and claims management in a competitive market.

Claims related to large weather events totalled £6 million in 2019 compared with £75 million in 2018 and expectations of £65 million for both years. The results also include a £16.9 million charge arising from the change in the Ogden discount rate to minus 0.25%, from the assumed rate of 0% in the first half of 2019 (2018: release of £54.8 million).

We made good progress on costs in 2019, reducing operating expenses before restructuring and one-off costs by £24.5 million to £693.7 million. We aim to reduce operating expenses, excluding amortisation and depreciation charges, by £50 million from 2018 to 2021, and in 2019 we achieved £11 million of this target and aim to achieve the remaining £39m over the next two years. Lower operating expenses helped to maintain the expense ratio at 23.2% (2018 restated: 23.2%). Of the estimated £60 million restructuring and one-off costs announced at our Capital Markets Day, that we expect over 2019 and 2020, we incurred £11.2 million in 2019 (2018: £nil).

Overall, the combined operating ratio was 92.2%. When normalised for weather and Ogden discount rate changes the ratio was 93.5%[1] (2018 restated: 93.3%), towards the lower end of our 93% to 95% medium term target range.

Profit before tax was down 12.2% to £509.7 million (2018 restated: £580.5 million). The impact of benign weather in 2019 was more than offset by lower reserve releases, in part Ogden discount rate-related, non-repeat of investment and property gains and restructuring and one-off costs in 2019.

We made further progress to improve the quality of our earnings; the current-year contribution to operating profit, normalised for weather and Ogden discount rate changes, increased by three percentage points to 39%[1], as the Group was more than able to offset lower investment gains and the £9.6 million one-off gain from the sale of our Bristol office in 2018. We continue to target the proportion from current-year to be more than 50% by the end of 2021.

Return on tangible equity was 20.8%, ahead of our 15% hurdle.

Motor – Disciplined underwriting and low claims frequency

In Motor we continued to focus on maintaining target loss ratios in a highly competitive market and achieved a broadly stable current-year loss ratio of 81.2% (2018 restated: 81.4%) reflecting our underwriting discipline and supported by lower than expected claims frequency.

Motor in-force policies and gross written premium were lower than 2018, as we sought to preserve margins. First half trading was particularly challenging; however, we were able to return to growth in the second half of 2019, with gross written premium increasing 2.4% compared to the second half of 2018 and up 4.7% in Q4 2019 compared to Q4 2018.

Motor delivered an operating profit of £302.6 million (2018 restated: £418.1 million) and a combined operating ratio of 94.8% (2018 restated: 88.6%). The 2019 result includes a £15.9 million charge arising from the change in the Ogden discount rate to minus 0.25%, from an assumed rate of 0%, compared to a £50.6 million release in 2018.

Prior-year reserve releases (including the effects from the change in the Ogden discount rate) were 6.0 percentage points lower and continued to reduce as expected, reflecting the Group's lower risk profile due to a number of years of increased reinsurance protection.

Our claims severity experience was consistent through 2019 with underlying inflation at the upper end of our long-term expectations of 3% to 5%. Claims frequency was lower as a result of improvements to risk mix, counter-fraud initiatives and benign weather. Looking ahead, we continue to expect underlying claims inflation to be between 3% and 5%.

Home – Good underwriting and claims performance

The Home result reflects the actions we've taken on pricing and underwriting in recent years and benign weather in 2019.

Home own brand in-force policies were 1.3% lower reflecting lower new business volumes as we increased new business prices ahead of the market, while retention remained strong.

Home delivered an operating profit of £150.6 million (2018 restated: £83.9 million) and a combined operating ratio of 80.3% (2018 restated: 93.5%). Normalised for weather, the combined operating ratio was 86.9%[1], 4.7 percentage points better than 2018, reflecting favourable claims experience following a number of actions we've taken, particularly to moderate escape of water inflation, and also lower attritional weather losses.

Rescue and other personal lines – Reshaping for future growth

This division comprises Rescue, including our challenger brand Green Flag, as well as other personal lines products – Pet, Travel, Creditor and our mid-to-high-net-worth business, UK Select.

Rescue and other personal lines gross written premium grew by 3.1% to £436.0 million supported by increases across most product lines, while in-force policies were 2.6% lower primarily due to lower packaged bank account volumes.

Offsetting this reduction, Green Flag direct delivered double-digit growth for the third successive year, growing in-force policies by 13.7% to over 1 million and gross written premium by 13.5% to £79.0 million.

Rescue grew operating profit by 12.2% to £45.1 million (2018 restated: £40.2 million) and reported a combined operating ratio of 81.5% (2018 restated: 85.0%) as results benefited from benign weather and lower costs.

Operating profit for Rescue and other personal lines of £39.1 million was £4.9 million lower than 2018 as the improved performance in the Rescue division was more than offset by lower prior-year reserve releases in other personal lines.

Commercial – Investing for growth and margin improvement

Within Commercial we have two main businesses, NIG and other and Commercial direct own brands. Commercial direct own brands include Direct Line for Business and commercial products sold under the Churchill brand primarily on PCWs.

Overall, Commercial delivered £54.6 million of operating profit (2018 restated: £60.4 million) and a combined operating ratio of 95.7% (2018 restated: 95.4%). Lower prior-year reserve releases were partially offset by improved current-year claims performance. Large weather claims totalled £3.0 million (2018: £10.0 million).

Commercial direct own brands grew in-force polices by 5.2% to 541,000 customers as the Group continued to roll-out its new digital platform targeting small and micro businesses. Gross written premium was 8.3% higher than 2018.

NIG and other grew gross written premium by 1.7% to £379.5 million while in-force policies were broadly stable, reflecting focus on improving technical pricing to support profitability.

Note:

1. See glossary on pages 47 to 49 for definitions and appendix A – Alternative performance measures on pages 50 to 53 for reconciliation.

Strategic update

A strategy to transform our business

The Group aims to create a world where insurance is personal, inclusive and a force for good. We'll do this by helping people carry on with their lives, giving them peace of mind, now and in the future. Because that's how we believe we will secure long-term sustainability in the changing world ahead.

Our six strategic objectives set out a clear path for us to realise our potential. The first three aim to ensure that our products are easy to use and available everywhere:

- Best at direct: to be the UK's leading direct player because we anticipate our customers' needs and develop services and products they want to buy.
- Win on PCWs: to deliver a step change in our pricing and trading capability so that our leading PCW brands win customers from our competitors.
- Extend our reach: to utilise our investments to win more customers through acquisitions and partnerships.

The second three are underlying skills which are designed to help us deliver great value and an excellent customer experience:

- Technical edge: to use our data, scale, skill and insight across claims, pricing and underwriting to deliver value to customers.
- Nimble and cost efficient: to transform into an agile, cost effective business to drive efficiency and simplicity for us and our customers.
- Great people: a home for empowered people who celebrate difference and challenge the status quo to deliver for our customers.

Core strengths that are hard to replicate

As a UK focused company, we have the ability to be a deep specialist in a market unlike any other in the world, while the range of channels and products gives us real diversification and scale that many of our peers do not have. This lets us pivot as dynamics shift in the market and this flexibility has supported our track record of delivering good returns.

Across the business, we have a number of real strengths. First and foremost, we are a people business, which means we really care and have a passion to serve our customers. Secondly, we have a strong balance sheet with further opportunities to improve its effectiveness. And thirdly we successfully combine strong brands and rich data because we are a direct player and have leading claims skills supported, for example, by our own accident repair centres. This combination is hard to replicate and we believe this provides a platform for real long-term value.

Investing in technology and new ways of working

While these core strengths persist today, we recognise that to succeed in the future we need to continue to change and we are on an ambitious transformation journey to increase the competitiveness of our business.

Like many data driven consumer markets, ours is digitising fast and our success will be predicated on combining great customer-focused brands with a strong technology foundation. Our journey has three overlapping phases, with each of our different parts of the business moving through these phases at a different pace.

The first has been building the key technology blocks, which is characterised by high investment expenditure. The run costs are being managed alongside careful expenditure on organisational change and on existing systems that are set to be phased out.

That technology is beginning to land and although there is still much to do in this ambitious and complex programme, we are now moving into the second phase: our business transformation. From this phase, we plan to improve our cost position by reducing double run-costs and improving efficiency. We also aim to further increase the accuracy and speed of our pricing and underwriting; improve our competitiveness and responsiveness to change; and enhance our customer experience.

Through increased competitiveness and by increasingly adopting more agile working practices, particularly in the areas of our business that are at the forefront of delivering change, we believe we can realise the incredible potential of our business to innovate faster and grow. This is the third phase of our transformation.

Progress against strategic objectives and 2020 priorities

Across every part of this business, there is a great deal of potential that we believe we can unlock and that's the journey we are on. We've made significant progress against our objectives to date outlined in the table below.

Objective	Why	Progress to date
Best at direct	A direct relationship with our customers provides an opportunity for growth by meeting a broader set of customer needs, and the foundation for future product and service innovation.	– Direct Line achieved best ever Customer Net Promoter Score – Green Flag passed 1 million policies milestone – Direct Line for Business: new Tradesperson and Van propositions launched
Win on PCWs	PCWs will continue to be the biggest market for new business and therefore our primary route for growth opportunities.	– Privilege Motor live on new Motor platform and available on four PCWs – Re-launched Churchill brand to increase the appeal of the brand across the PCW channel – Darwin Motor launched on two PCWs
Extend our reach	Our new customer platforms make it easier for us to onboard new books of business. We will use this to explore inorganic growth opportunities through partnerships and acquisitions.	– New Travel platform rolled out to NatWest customers – Grew three year Home proposition with RBS – New partnerships with car share start-up 'YouMeCar' and Starling Bank.
Technical edge	We aim to create a great experience for our customers and embed a sustainable competitive advantage by leveraging our strengths in repair, data and claims insight and management.	– Deployment of new risk pricing models, new rating factors and more sophisticated interactions in Motor – Extended owned repair network to 21 sites – Enhanced Escape of Water related underwriting initiatives in Home
Nimble and cost efficient	We aim to bring our cost base in line with the market to compete better, in particular through PCWs and partnerships. We will introduce new ways of working to exploit our advantages within each product and channel.	– Delivered 2019 cost target; below £700m – Embedded agile ways of working across a number of areas including Rescue and Direct Line for Business
Great people	As disruption in our market increases, we need to become brilliant at innovation and change. We can only do this by empowering and developing the best people.	– Women in Finance: 30% target achieved – First cohort of graduates completed their three year training programme – Empowering diversity; neurodiversity, BAME, disability and carers

Our 2020 priorities are all aligned to these six strategic objectives and in the first half of 2020 we will focus on continuing the development and roll-out of our technology change. Our plans include moving towards launching Direct Line and Churchill motor new business onto our new platform, launching Darwin on two more PCWs, rolling out a new claims system for Green Flag and building Contractors into NIG's new Commercial Combined product. At the same time we are completing the re-engineering of our technology platform to support these new systems and enhance productivity.

We are also heavily focused on improving efficiency in order to meet our cost targets. Last week we launched a consultation in our head office areas which aims to improve our speed of delivery at a lower cost by implementing more agile principles including moving to multi-disciplinary teams and away from working in functional silos. We are also looking to rationalise our site footprint over the next two years.

Whilst landing technology change and improving efficiency are key objectives in 2020, we are also continuing to drive our brand health with exciting plans for Direct Line and continuing to position Churchill as a PCW-first brand. These plans are all designed with fantastic customer experience and propositions at their heart.

Supporting our activities and central to the long-term sustainability of the business , we have deeply embedded and fundamental principles:

- Our values sit at the very heart of our everyday behaviours. They were created ground up and represent in full technicolour our identity.
- Our sustainability pillars bring environmental, social and governance factors into the heart of our strategic thinking, whether that's our customers, our people, our society, our planet, or the importance of strong governance – they all play central roles in delivering our business in a sustainable way.

External factors

Regulation

We have continued to operate within a highly dynamic and evolving regulatory landscape, influenced by the views and initiatives from several parties, including the UK Government, the FCA and the PRA. During 2019, both the FCA and the PRA have been focused on Brexit preparations, amongst other activities.

A main FCA focus has continued to be on pricing practices generally, including its Market Study on General Insurance Pricing Practices. For some time we have been actively taking steps regarding pricing, as well as working with the ABI and holding proactive discussions with the FCA on potential remedies. We are supportive of the FCA Market Study, the outcomes of which are due for publication in June 2020. The FCA has also been focused on firms' culture and governance, operational resilience, management of regulatory change, the general insurance distribution chain, vulnerable customers, affordability as it relates to consumer credit, complaint handling and the appropriate establishment of customers' demands and needs as per the requirements under the Insurance Distribution Directive.

The PRA has continued to focus generally on the pillars of its financial risk framework, namely reserving, pricing, reinsurance and investments, as well as operational resilience, cyber underwriting risk and the financial risks arising from climate change.

Climate change

We are committed to playing our part in helping the UK become a sustainable, low carbon economy. We intend to set a challenging target to be carbon neutral as a business and aim to be compliant with the Taskforce on Climate-related Financial Disclosures by the end of 2020. This year our objective was to ensure that our investments in investment-grade bonds were tilted more towards companies with better environmental, social and governance ("**ESG**") credentials and we were delighted that the relevant portfolios had an average ESG rating of 'A'. This represents 87% of the credit investments in the portfolio and 62% of our total investment portfolio. We also recycled 98% of our total waste and since 2014 have sourced 100% of our electricity from renewable sources. In order to achieve our goal of long-term sustainability it is important that we give back more to the planet than we take out.

Brexit

We prepared for the possibility of a disruptive Brexit. As is well known, following the Government winning a significant House of Commons majority in the December 2019 general election, the UK left the EU on 31 January ("**Brexit**") with "a deal", so that essentially there have been no substantive changes in practice to the trading and other arrangements between the UK and the EU, at least during the "implementation period" which is due to last until 31 December 2020, unless extended. Nonetheless, the terms, if any, of any future trading relationship between the UK and the EU, and between the UK and other key countries, are not yet known and there remains uncertainty and at least the possibility of a disruptive end to the implementation period.

Although we are predominantly a UK business, we do, for example, have exposure to financial markets and import goods and services to fulfil insurance claims. We have been monitoring events carefully and have proactively taken steps to mitigate the likely impact on the Group to the extent we consider it to be appropriate and proportionate to do so, given the considerable uncertainties; however, in the event of a disruptive end to the implementation period the Group would not be immune.

Consumer trends

New products, new routes to market and technology, particularly in cars, are emerging. In response we are preparing for a shift in the risk pool and an increase in the importance of data and analytics. Our new brand Darwin is using new pricing technology for motor customers who purchase via the PCW channel and our new motor insurance platform is being rolled out to make customer journeys easier. In our accident repair centres we are preparing for the future by investing in specialist equipment to repair cars with advanced driver-assistance systems ("**ADAS**") technology, as well as supporting FiveAI's recent trial of autonomous vehicles and partnering with Europe's largest car-subscription service Drover.

UK storms and Coronavirus

The recent storms Ciara and Dennis in February have shown how important it is to be with the right insurer and we are proud with how we supported our customers during these difficult times. We estimate that the claims costs of these storms will be in the region of £35 million, net of Flood Re recoveries, across our Home and Commercial businesses compared to an expected annual weather cost of around £64 million. It is too early to assess any additional claims from Storm Jorge. In addition, the Coronavirus outbreak (specifically the disease COVID-19) has the potential to impact the 2020 result of our Travel business. We have Travel reinsurance protection to mitigate the cost of an event over a 28 day period to £1 million up to a limit of £10 million. The full coverage, if utilised, can be reinstated once on the same terms. Currently, incurred claims are around £1 million. Like all businesses, we are subject to the consequences of disruption to financial markets and global supply chains which, over time, could impact the performance of our investments and the cost and speed of fulfilling customers' claims.

Dividend and capital management

The Group's solvency capital ratio as at 31 December 2019, prior to the proposed dividend and share buyback was 191%. This resulted from good capital generation from the business, supported by higher unrealised mark to market gains on the Group's available-for-sale investments, as credit spreads narrowed. This strong capital generation allowed us to continue to invest high levels of capital expenditure to support the Group's strategic objectives.

The Board has recommended a final dividend of 14.4 pence per share (2018: 14.0 pence), an increase of 0.4 pence per share (2.9%).

The Board has also approved a share buyback of up to £150 million which it expects to complete by the end of July 2020 After taking into account these dividends and share buybacks, the solvency capital ratio was 165% as at 31 December 2019. This reflects the Board's continued confidence in the Group's capital position and the sustainability of its earnings. In normal circumstances, the Board expects the Group to operate around the middle of its solvency capital ratio risk appetite range of 140% to 180%.

Outlook

The Group targets a combined operating ratio of 93% to 95% for 2020 and over the medium term, normalised for weather. By the end of 2021, the Group aims to increase the annual proportionate contribution from current-year operating profit to more than half of the Group's total operating profit.

The targeted improvement in current-year underwriting profitability is supported by the significant investment the Group is making in building future capability. This investment aims to improve the current-year loss ratio by delivering additional pricing sophistication and supporting multiple initiatives to combat fraud. In addition, the Group is targeting improved efficiency through self-service and digitalisation and a reduction in operating expenses[1] by £50 million between 2018 and 2021 and we aim to improve our operating expense ratio to 20% by 2023. We reiterate our ongoing target of achieving at least a 15% return on tangible equity per annum.

Our fundamental strengths as a business continue to bring benefits and I'm proud that our transformation programme gives us the opportunity to further enhance the ability of the Group to offer value for customers and shareholders.

PENNY JAMES

CHIEF EXECUTIVE OFFICER

Note:

1. Excluding amortisation, depreciation and restructuring and one-off costs.

FINANCE REVIEW

Performance

Operating profit[1]

	FY 2019 £m	FY 2018[2] £m restated
Underwriting profit	**232.1**	259.8
Instalment and other operating income	**180.2**	192.0
Investment return	**134.6**	154.6
Total operating profit	**546.9**	606.4
Of which:		
Current-year operating profit[1]	**252.4**	202.0
Prior-year reserve releases	**294.5**	404.4

Notes:

1. See glossary on pages 47 to 49 for definitions and appendix A – Alternative performance measures on pages 50 to 53 for reconciliation to financial statement line items.
2. Results for the period ended 31 December 2018 have been restated to reflect the fully retrospective adoption of IFRS 16 'Leases'. See note 23 to the consolidated financial statements.

Underwriting profit decreased to £232.1 million (2018 restated: £259.8 million) as lower prior-year reserve releases of £294.5 million, including the effects of changes to the Ogden discount rate detailed below, were partially offset by lower operating expenses and reduced weather-related claims of £6 million (2018: £75 million weather-related claims).

The combined operating ratio was 92.2% (2018 restated: 91.6%). The current-year attritional loss ratio improved by 1.0 percentage point to 71.6% (2018 restated: 72.6%). Home, Rescue and other personal lines and Commercial all improved, and Motor remained broadly steady. The loss ratio relating to major weather events improved by 2.2 percentage points to 0.2%, partially offset by a 0.6 percentage point increase in the commission ratio. The expense ratio was stable as lower expenses were offset by a reduction in earned premium. Overall, the current-year combined operating ratio improved by 2.6 percentage points to 102.1%.

Instalment and other operating income decreased to £180.2 million (2018: £192.0 million), due primarily to the non-repeat of a £9.6 million property gain in 2018. Other income, including from our in-house accident repair network, remained broadly stable.

Investment return decreased to £134.6 million (2018: £154.6 million) as a result of a reduction in assets under management reducing investment income, the non-repeat of £13 million of fair value adjustments in 2018 and a reduction in realised gains.

Operating profit decreased by £59.5 million to £546.9 million (2018 restated: £606.4 million) as a result of reductions in underwriting profit, instalment and other operating income and investment return. Current-year operating profit, as a proportion of total operating profit, improved, making progress towards the Group's target of achieving more than half of the Group's annual operating profit from current-year earnings by the end of 2021.

Effect of Ogden discount rate changes on claims reserves net of reinsurance

			FY 2019			FY 2018
	Motor £m	Commercial £m	Total £m	Motor £m	Commercial £m	Total £m
Prior-year	**15.9**	**1.0**	**16.9**	(47.9)	(3.5)	(51.4)
Current-year	**–**	**–**	–	(2.7)	(0.7)	(3.4)
Total claims reserve increase / (decrease)	**15.9**	**1.0**	**16.9**	(50.6)	(4.2)	(54.8)

The Civil Liability Act 2018 introduced a new framework for setting the personal injury Ogden discount rate, requiring the Government to reset the Ogden discount rate by reference to low risk rather than very low or zero risk investments. Following a Government review, as dictated by the terms of the Civil Liability Act 2018, on 15 July 2019 the Lord Chancellor announced a new Ogden discount rate of minus 0.25% to take effect from 5 August 2019. Compared to an assumed Ogden discount rate of 0% this resulted in a £16.9 million increase in reserves split across the Motor and Commercial segments. In 2018, following the granting of royal assent for the Act in December 2018, the Group reviewed the Ogden discount rate for reserves for large bodily injury claims and selected an assumed rate of 0% for reserving purposes as at 31 December 2018. This resulted in a reserves release of £54.8 million in 2018.

In-force policies and gross written premium

In-force policies (thousands)

At	31 Dec 2019[1]	30 Sep 2019[1]	30 Jun 2019[1,2]	31 Mar 2019[1,2]	31 Dec 2018[1,2]
Direct own brands	**3,921**	3,910	3,909	3,948	3,950
Partnerships	**122**	127	133	138	144
Motor	**4,043**	4,037	4,042	4,086	4,094
Direct own brands	**1,765**	1,769	1,786	1,791	1,789
Partnerships	**829**	836	844	852	862
Home	**2,594**	2,605	2,630	2,643	2,651
Rescue	**3,450**	3,470	3,479	3,503	3,532
Travel	**3,648**	3,675	3,686	3,696	3,759
Pet	**157**	158	158	157	156
Other personal lines	**122**	123	123	124	126
Rescue and other personal lines	**7,377**	7,426	7,446	7,480	7,573
Of which: Green Flag direct	**1,063**	1,039	999	966	935
Direct own brands	**541**	535	531	521	514
NIG and other	**234**	234	233	234	241
Commercial	**775**	769	764	755	755
Total in-force policies	**14,789**	14,837	14,882	14,964	15,073
Of which: direct own brands	**7,290**	7,253	7,225	7,226	7,188

Notes:

1. Commercial direct own brands include Direct Line for Business and commercial products sold under the Churchill brand; the Churchill in-force policies were previously reported within NIG and other. Prior periods have been re-presented accordingly.
2. In-force policies, including direct own brands have been restated to include Green Flag direct policies omitted from previously reported amounts. (31 December 2018: 41,000 additional policies; 31 March 2019: 44,000 additional policies; 30 June 2019: 52,000 additional policies).

Total in-force policies reduced to 14.8 million (31 December 2018: 15.1 million), primarily due to lower volumes in policies attached to packaged bank accounts, small reductions in Motor and Home own brands, and reductions in Home partnerships as Prudential and Sainsbury's partnerships are closed to new business. Own brands in-force policies grew to 7.3 million (2018 restated: 7.2 million), with growth in Green Flag and Commercial direct own brands partly offsetting the overall reduction.

Gross written premium

	H2 2019[1] £m	H2 2018[1] £m	FY 2019[1] £m	FY 2018[1] £m
Direct own brands	**820.1**	801.5	**1,591.7**	1,608.8
Partnerships	**31.0**	29.9	**59.9**	62.4
Motor	**851.1**	831.4	**1,651.6**	1,671.2
Direct own brands	**214.0**	218.2	**407.7**	412.6
Partnerships	**89.3**	98.0	**178.9**	194.3
Home	**303.3**	316.2	**586.6**	606.9
Rescue	**84.6**	83.3	**167.5**	163.4
Travel	**75.1**	70.7	**151.3**	143.9
Pet	**36.4**	36.5	**72.6**	72.4
Other personal lines	**23.4**	22.4	**44.6**	43.1
Rescue and other personal lines	**219.5**	212.9	**436.0**	422.8
Of which: Green Flag direct	**41.0**	36.3	**79.0**	69.6
Direct own brands	**75.8**	71.2	**149.4**	137.9
NIG and other	**178.3**	169.9	**379.5**	373.1
Commercial	**254.1**	241.1	**528.9**	511.0
Total gross written premium	**1,628.0**	1,601.6	**3,203.1**	3,211.9
Of which: direct own brands	**1,150.9**	1,127.2	**2,227.8**	2,228.9

Note:

1. Commercial direct own brands include Direct Line for Business and commercial products sold under the Churchill brand that were previously reported within NIG and other. Prior periods have been re-presented accordingly.

Gross written premium of £3,203.1 million (2018: £3,211.9 million) reduced slightly by 0.3% as modest declines in Motor and Home were partially offset by increases in Commercial and Rescue and other personal lines. Direct own brands gross written premium of £2,227.8 million (2018: £2,228.9 million) was broadly steady.

Motor

Motor in-force policies reduced by 1.2% to 4.0 million with gross written premium also reducing by 1.2% to £1,651.6 million as the Group continued to focus on maintaining target loss ratios in a highly competitive market.

Own brands in-force policies reduced slightly by 0.7%. Strong new business growth was achieved in Churchill following the brand's re-launch in October and a strengthened proposition for the PCW channel. Retention reduced slightly, but remained strong across direct own brands and partnerships.

A number of pricing initiatives have helped to support new business competitiveness. Motor risk-adjusted prices increased by 3.1% in 2019 while targeted changes to the risk mix reduced average premiums by 3.7%. This led to Motor average premium[1] falling slightly in 2019.

Home

In-force policies for Home's own brands reduced by 1.3% in 2019 to 1.8 million policies due to a reduction in new business volumes. Partnership volumes reduced by 3.8%, Prudential and Sainsbury's partnerships are closed to new business and continued to run off in line with expectations.

Gross written premium was 3.3% lower than 2018, predominantly due to a reduction in partnership volume, as Prudential and Sainsburys continued to run off. Own brands gross written premium reduced by 1.2% primarily due to lower renewal premiums. Retention continued to be strong.

Home own brand risk-adjusted prices increased by 2.0% driven by new business, while pricing actions improved risk mix by 2.7% giving a small reduction in average premium[2] of 0.7%.

Rescue and other personal lines

Rescue and other personal lines in-force policies reduced by 2.6% to 7.4 million. However, gross written premium increased by 3.1% to £436.0 million compared with 2018 as lower premium packaged bank account volume was replaced with higher premium own brand policies.

Green Flag Rescue continued to grow its higher average premium direct business during 2019, increasing in-force policies by 13.7% to 1.1 million. Gross written premium increased by 13.5% to £79.0 million.

In-force policies for the Group's linked Rescue channel, where cover can be purchased with a Group Motor policy, reduced to 857,000, driven by the end of the Churchill "Free Rescue" campaign in July 2018. Rescue partnerships in-force policies reduced by 4.2%, where margins tend to be lower than for direct business, driven primarily by a reduction in packaged bank account volumes.

Total Other personal lines (comprising Travel, Pet and other) in-force policies reduced by 2.8% to 3.9 million primarily due to lower packaged bank account volumes in Travel. Pet in-force policies grew in 2019, reversing a period of lower volumes, and insurance packages tailored for UK Select Home and Motor customers saw strong growth in the year.

Gross written premium for total Other personal lines increased by 3.5%.

Commercial

Commercial in-force policies increased by 2.6% compared with 2018 to 775,000, reflecting strong growth in Commercial direct own brands with NIG and other broadly stable.

Commercial direct own brands grew in-force policies by 5.2% as it continued to grow in its traditionally well performing areas of Van and Landlord, together with strong growth across the small and micro business products on its new platform. Gross written premium increased by 8.3% to £149.4 million with increases across all product lines.

NIG and other in-force policies numbers were 2.9% lower and gross written premium grew by 1.7% to £379.5 million. This reflected NIG's focus on underwriting discipline and underwriting margins.

Notes:

1. Average incepted written premium excluding IPT for Motor own brands (excluding Darwin and Privilege policies underwritten on the Group's new IT platform) for year end 31 December 2019.
2. Average incepted written premium excluding IPT for Home own brands for year end 31 December 2019.

Underwriting profit and combined operating ratio

	FY 2019	FY 2018[1] restated
Underwriting profit (£ million)	**232.1**	259.8
Loss ratio	**61.9%**	61.9%
Commission ratio	**7.1%**	6.5%
Expense ratio	**23.2%**	23.2%
Combined operating ratio	**92.2%**	91.6%

Note:

1. Results for the period ended 31 December 2018 have been restated to reflect the fully retrospective adoption of IFRS 16 'Leases'. See note 23 to the consolidated financial statements.

The Group's combined operating ratio of 92.2% (2018 restated: 91.6%) increased by 0.6 percentage points primarily due to an increase in the commission ratio. Weather-related claims reduced in 2019 and there was no repeat of the weather-event related claims experienced in the first half of 2018. The resulting improvements to the Home loss ratio were largely offset by increases in the Motor loss ratio as the contribution from prior-year reserve releases reduced. Normalised for weather and the Ogden discount rate change, the combined operating ratio was approximately 93.5%[1], towards the lower end of the Group's medium-term target range of 93% to 95%. This includes a 0.6 percentage point impact from the Ogden discount rate change in July 2019.

The loss ratio was stable at 61.9% (2018 restated: 61.9%) as a number of factors offset each other. The current-year attritional loss ratio improved by 1.0 percentage point as the Group benefited from benign weather and this was offset by lower prior-year reserve releases in part due to Ogden discount rate changes.

The commission ratio has increased primarily as a result of increased profit-share payments and volume related payments to PCWs.

The expense ratio has remained steady at 23.2% as lower costs were fully offset by lower earned premium. Operating expenses excluding restructuring and one-off costs fell by £24.5 million to £693.7 million in 2019, with reductions across all major cost categories except for insurance levies.

Note:

1. See glossary on pages 47 to 49 for definitions and appendix A – Alternative performance measures on pages 50 to 53 for reconciliation.

Ratio analysis by division

	Notes	Motor £m	Home £m	Rescue and other personal lines £m	Commercial £m	Total Group £m
For the year ended 31 December 2019						
Net earned premium	3	**1,507.7**	**573.6**	**425.2**	**478.4**	**2,984.9**
Net insurance claims	3	**1,043.3**	**268.4**	**284.4**	**251.5**	**1,847.6**
Prior-year reserve releases	20	**180.5**	**41.4**	**7.6**	**65.0**	**294.5**
Major weather events		**n/a**	**(3.0)**	**n/a**	**(3.0)**	**(6.0)**
Attritional net insurance claims		**1,223.8**	**306.8**	**292.0**	**313.5**	**2,136.1**
Loss ratio – current-year attritional		**81.2%**	**53.5%**	**68.7%**	**65.6%**	**71.6%**
Loss ratio – prior-year reserve releases		**(11.9%)**	**(7.2%)**	**(1.8%)**	**(13.6%)**	**(9.9%)**
Loss ratio – major weather events[1]		**n/a**	**0.5%**	**n/a**	**0.7%**	**0.2%**
Loss ratio – reported	3	**69.3%**	**46.8%**	**66.9%**	**52.7%**	**61.9%**
Commission ratio	3	**2.6%**	**9.7%**	**6.4%**	**18.5%**	**7.1%**
Expense ratio	3	**22.9%**	**23.8%**	**22.1%**	**24.5%**	**23.2%**
Combined operating ratio	3	**94.8%**	**80.3%**	**95.4%**	**95.7%**	**92.2%**
Current-year combined operating ratio		**106.6%**	**87.6%**	**97.2%**	**109.2%**	**102.1%**
For the year ended 31 December 2018[2] (restated)						
Net earned premium	3	1,541.8	667.8	414.7	465.2	3,089.5
Net insurance claims	3	979.3	413.3	277.2	241.3	1,911.1
Prior-year reserve releases	20	276.3	32.6	16.1	79.4	404.4
Major weather events		n/a	(65.0)	n/a	(10.0)	(75.0)
Attritional net insurance claims		1,255.6	380.9	293.3	310.7	2,240.5
Loss ratio – current-year attritional		81.4%	57.0%	70.7%	66.8%	72.6%
Loss ratio – prior-year reserve releases		(17.9%)	(4.9%)	(3.9%)	(17.1%)	(13.1%)
Loss ratio – major weather events[1]		n/a	9.7%	n/a	2.1%	2.4%
Loss ratio – reported	3	63.5%	61.8%	66.8%	51.8%	61.9%
Commission ratio	3	2.0%	9.4%	4.6%	18.9%	6.5%
Expense ratio	3	23.1%	22.3%	23.6%	24.7%	23.2%
Combined operating ratio	3	88.6%	93.5%	95.0%	95.4%	91.6%
Current-year combined operating ratio		106.5%	98.4%	98.8%	112.5%	104.7%

Notes:

1. Home and Commercial claims for major weather events, including inland and coastal flooding and storms.
2. Results for the period ended 31 December 2018 have been restated to reflect the fully retrospective adoption of IFRS 16 'Leases'. See note 23 to the consolidated financial statements.

The movement in the current-year attritional loss ratio is an indicator of underlying accident year performance as it excludes prior-year reserve releases and claims costs from major weather events. The Group's current-year attritional loss ratio of 71.6% improved by 1.0 percentage point compared to 2018, demonstrating good progress on the Group's target to improve current-year underwriting profitability. This was primarily due to improvements in escape of water claims in Home and small improvements across other divisions.

Prior-year reserve releases continued to be significant at £294.5 million (2018: £404.4 million), equivalent to 9.9% of net earned premium (2018: 13.1%) and were concentrated towards more recent accident years. In 2019, prior-year reserves increased by £16.9 million in relation to a change in the Ogden discount rate to minus 0.25% (2018: £54.8 million reserve release). Assuming current claims trends continue, prior-year reserve releases are expected to continue to reduce further in future years, although they are expected to remain a significant contribution to profits.

The Group's current-year combined operating ratio improved by 2.6 percentage points to 102.1% (2018 restated: 104.7%) as a 2.2 percentage point improvement in claims due to major weather events and a 1.0 percentage point improvement to the current-year attritional loss ratios were partially offset by a 0.6 percentage point increase in the commission ratio.

Motor

The current-year attritional loss ratio in Motor improved by 0.2 percentage points to 81.2% (2018: 81.4%). Claims severity experience was consistent through 2019 with underlying inflation at the upper end of the Group's long-term expectations of 3% to 5%. Frequency was lower as a result of improvements to risk mix, counter fraud initiatives as well as benign weather.

In total, prior-year reserve releases were £95.8 million lower year on year at £180.5 million and included an increase in reserves of £15.9 million as a result of the change in the Ogden discount rate to minus 0.25% from an assumed rate of 0% (2018: £47.9 million release). Bodily injury claims reserves continued to develop favourably.

Motor's reported combined operating ratio increased by 6.2 percentage points to 94.8% (2018 restated: 88.6%). Small improvements in the current-year attritional loss and expense ratios were offset by a 0.6 percentage point increase in the commission ratio, primarily due to increased volume related commission payments to PCWs, and a 6.0 percentage point reduction in prior-year reserve releases.

Home

The current-year attritional loss ratio, excluding major weather event claims, improved by 3.5 percentage points to 53.5%, reflecting improvements to escape of water claims, disciplined underwriting and benign weather. Home's 2019 experience was better than its long-term expectation of claims inflation which, excluding the impact of major weather events, remained at 3% to 5%.

The commission ratio of 9.7% was 0.3 percentage points higher compared to 2018 due to higher prior-year reserve releases and benign weather resulting in higher profit share payments to partners.

Home's combined operating ratio improved by 13.2 percentage points to 80.3% (2018 restated: 93.5%). This was driven primarily by a 9.2 percentage point improvement in claims relating to severe weather events, as 2019 had relatively benign weather and a 2.3 percentage point increase in prior-year releases due to favourable development on escape of water claims. Normalised for weather, the combined operating ratio was 4.7 percentage points better than 2018 at 86.9%[1] (2018 restated: 91.6%).

Rescue and other personal lines

The combined operating ratio for Rescue and other personal lines increased slightly by 0.4 percentage points to 95.4% (2018 restated: 95.0%) as a 1.5 percentage point improvement to the expense ratio was more than offset by an increase to the commission ratio. The loss ratio was broadly stable year-on-year.

Rescue's combined operating ratio of 81.5% was 3.5 percentage points better than 2018's ratio of 85.0%, as it benefited from lower claims frequency due to mild weather, the mix effects of own brand growth and lower expenses following front-line efficiency savings. Other personal lines combined operating ratio increased by 3.7 percentage points to 102.0%, due to lower prior-year reserve releases in UK Select and Travel, alongside additional headwinds in UK Select from higher large loss severity.

In addition, the Coronavirus outbreak (specifically the disease COVID-19) has the potential to impact the 2020 result of our Travel business. We have currently incurred claims of around £1 million, the majority for customer trips to regions where the Foreign & Commonwealth Office ("**FCO**") advise against all but essential travel. We ask customers to seek refunds or amendments to their trip from their travel provider in line with FCO guidance. We have Travel reinsurance protection to mitigate the cost of an event over a 28 day period to £1 million up to a limit of £10 million. The full coverage, if utilised, can be reinstated once on the same terms.

Commercial

The current-year attritional loss ratio in Commercial improved by 1.3 percentage points to 65.6% as risk selection remained the priority. Prior-year reserve releases were £14.4 million lower at £65.0 million. This was primarily due to lower general liability reserve releases on older accident years. 2019's result included a £1.0 million strengthening of prior-year reserves as a result of the change in the Ogden discount rate to minus 0.25% from an assumed rate of 0% (2018: £3.5 million release).

The combined operating ratio for Commercial increased slightly by 0.3 percentage points to 95.7% (2018 restated: 95.4%) as an improvement in the current-year attritional loss ratio of 1.3 percentage points and a reduction in claims related to severe weather were offset by the reduction in prior-year reserve releases.

Note:

1. See glossary on pages 47 to 49 for definitions and appendix A – Alternative performance measures on pages 50 to 53 for reconciliation.

Operating expenses before restructuring and one-off costs

	Note	**FY 2019 £m**	FY 2018[1] £m restated
Staff costs[2]		**261.5**	269.9
IT and other operating expenses[2,3]		**158.0**	167.6
Marketing	9	**113.9**	121.2
Insurance levies[4]	9	**81.5**	67.6
Depreciation and amortisation[5,6]	9	**78.8**	91.9
Total operating expenses before restructuring and one-off costs		**693.7**	718.2

Notes:

1. Results for the year ended 31 December 2018 have been restated to reflect the fully retrospective adoption of IFRS 16 'Leases', see note 23.
2. Staff costs and other operating expenses attributable to claims handling activities are allocated to the cost of insurance claims.
3. IT and other operating expenses include professional fees and property costs.
4. Insurance levies were previously reported in other operating expenses. Comparative data for the year ended 31 December 2018 has been re-presented accordingly.
5. Amortisation and impairment of other intangible assets includes a £1.3 million impairment charge for year ended 31 December 2019 (2018: £1.5 million), which relates to capitalised software development costs for ongoing IT projects primarily relating to development of new systems.
6. Includes depreciation on right-of-use assets of £14.2 million (31 December 2018: £14.1 million).

Operating expenses before restructuring and one-off costs reduced by £24.5 million to £693.7 million (2018 restated: £718.2 million), meeting the Group's 2019 target of reducing operating expenses to under £700 million. This resulted in an unchanged expense ratio of 23.2% (2018 restated: 23.2%). The Group saw reductions in all major cost categories with the exception of insurance levies, where there have been increases in both the Motor Insurers' Bureau and the Financial Services Compensation Scheme levies.

The Group has continued to invest in its technology transformation and other operational efficiency improvements. The core areas of focus include self-service and digitalisation, process improvement and automation, as well as reducing costs through targeted procurement activity.

Instalment and other operating income

	Note	**FY 2019 £m**	FY 2018 £m
Instalment income		**114.0**	119.9
Other operating income:			
Revenue from vehicle recovery and repair services[1]	6	**28.3**	25.1
Vehicle replacement referral income	6	**19.1**	17.2
Legal services income	6	**11.3**	11.2
Other income[2,3]	6	**7.5**	18.6
Other operating income	6	**66.2**	72.1
Total instalment and other operating income		**180.2**	192.0

Notes:

1. Revenue from vehicle recovery and repair services include salvage income previously reported in other income. Comparative data for the year ended 31 December 2018 has been re-presented accordingly.
2. Other income includes mainly fee income from insurance intermediary services.
3. In 2018 other income included a £9.6 million gain on the sale of a property.

Instalment and other operating income decreased by £11.8 million, primarily as a result of the non-repeat of a £9.6 million property gain in 2018.

Investment return

	Note	**FY 2019 £m**	FY 2018 £m
Investment income		**146.4**	159.2
Hedging to a sterling floating rate basis		**(22.1)**	(30.8)
Net investment income		**124.3**	128.4
Net realised and unrealised gains excluding hedging		**10.3**	26.2
Total investment return	5	**134.6**	154.6

Investment yields

	FY 2019	FY 2018
Investment income yield[1]	**2.4%**	2.5%
Net investment income yield[1]	**2.1%**	2.0%
Investment return yield[1]	**2.2%**	2.4%

Note:

1. See glossary on pages 47 to 49 for definitions and appendix A – Alternative performance measures on pages 50 to 53 for reconciliation to financial statement line items.

Total investment return decreased by £20.0 million to £134.6 million (2018: £154.6 million). This was due to a reduction in investment income, primarily as a result of lower assets under management, and a reduction in realised and unrealised gains excluding hedging, which was predominantly driven by investment property revaluations (2019: (£6.2) million, 2018: £12.7 million).

The investment income yield for 2019 reduced to 2.4% (2018: 2.5%). The net investment income yield was higher at 2.1% (2018: 2.0%) as a result of decreased hedging costs. In 2020, the Group expects a net investment income yield around 2.0%.

The Group's investment strategy aims to deliver several objectives, which are summarised below:

- to ensure there is sufficient liquidity available within the investment portfolio to meet stressed liquidity scenarios;
- to match periodic payment orders ("**PPO**") and non-PPO liabilities in an optimal manner; and
- to deliver a suitable risk-adjusted investment return commensurate with the Group's risk appetite.

Investment holdings

At 31 December	2019 £m	2018 £m
Investment-grade credit[1]	**3,676.8**	3,606.6
High yield	**390.8**	393.9
Investment-grade private placements	**104.0**	101.0
Credit	**4,171.6**	4,101.5
Sovereign	**99.8**	156.9
Total debt securities	**4,271.4**	4,258.4
Infrastructure debt	**278.1**	289.6
Commercial real estate loans	**205.7**	201.6
Cash and cash equivalents[2]	**896.3**	1,092.4
Investment property	**291.7**	322.1
Total investment holdings	**5,943.2**	6,164.1

Notes:

1. Asset allocation at 31 December 2019 includes investment portfolio derivatives, which have been included and have a mark-to-market asset value of £81.8 million included in investment grade credit (31 December 2018 mark-to-market asset value of £11.8 million). This excludes non-investment derivatives that have been used to hedge interest on subordinated debt and operational cash flows.
2. Net of bank overdrafts: includes cash at bank and in hand and money market funds.

At 31 December 2019, total investment holdings of £5,943.2 million were 3.6% lower than at the start of the year primarily reflecting the cash paid in 2019 for dividends partially offset by an increase in fair value of debt securities. Total debt securities were £4,271.4 million (31 December 2018: £4,258.4 million), of which 2.8% were rated as 'AAA' and a further 58.6% were rated as 'AA' or 'A'. The average duration at 31 December 2019 of total debt securities was 2.5 years (31 December 2018: 2.5 years).

At 31 December 2019, total unrealised gains, net of tax, on available-for-sale ("**AFS**") investments were £47.5 million (31 December 2018: £36.8 million unrealised losses).

Reconciliation of operating profit

	Note	FY 2019 £m	FY 2018[1] £m restated
Motor	3	**302.6**	418.1
Home	3	**150.6**	83.9
Rescue and other personal lines	3	**39.1**	44.0
Commercial	3	**54.6**	60.4
Operating profit	3	**546.9**	606.4
Restructuring and one-off costs		**(11.2)**	–
Operating profit after restructuring and one-off costs		**535.7**	–
Finance costs	10	**(26.0)**	(25.9)
Profit before tax	3	**509.7**	580.5
Tax		**(89.8)**	(108.5)
Profit for the year attributable to the owners of the Company		**419.9**	472.0

Note:

1. Results for the period ended 31 December 2018 have been restated to reflect the fully retrospective adoption of IFRS 16 'Leases'. See note 23 to the consolidated financial statements.

Operating profit by segment

All divisions contributed to profit in 2019, demonstrating the diversity of the Group's multi-product, multi-brand and multi-channel portfolio. Motor operating profit reduced primarily due to the effects on prior-year reserve releases of Ogden discount rate changes in both 2018 and 2019. Home operating profit improved primarily due to underwriting actions, claims indemnity initiatives and benign weather. Rescue operating profit of £45.1 million (2018 restated: £40.2 million) is included in the Rescue and other personal lines result.

Restructuring and one-off costs

In order to support its cost reduction targets, the Group announced approximately £60 million of restructuring and one-off costs across 2019 and 2020 at its Capital Markets Day in November. The Group incurred £11.2 million of restructuring and one-off costs in 2019 with the remainder expected to be incurred in 2020.

Finance costs

Finance costs were broadly steady at £26.0 million (2018 restated: £25.9 million) and include finance costs which were incurred on the Group's leased assets following the fully retrospective adoption of IFRS 16 'Leases' on 1 January 2019.

Effective corporation tax rate

The effective tax rate for 2019 was 17.6% (2018: 18.7%), which was lower than the standard UK corporation tax rate of 19.0% (2018: 19.0%) driven primarily by an increase in respect of prior-year over provisions, tax relief for the Tier 1 coupon payments offset by a reduction in disallowable expenses.

Profit for the year and return on tangible equity[1,2]

Profit for the year was £419.9 million (2018 restated: £472.0 million) in line with the reduction in operating profit.

Return on tangible equity decreased to 20.8% (2018 restated: 21.6%) due primarily to a £46.9 million decrease in adjusted[2] profit after tax to £408.5 million (2018 restated: £455.4 million). Profit after tax in 2019 was adjusted for restructuring and one-off costs. Profit after tax in both 2019 and 2018 was adjusted for coupon payments in respect of Tier 1 notes.

Notes:

1. Results for the period ended 31 December 2018 have been restated to reflect the fully retrospective adoption of IFRS 16 'Leases'. See note 23 to the consolidated financial statements.
2. See glossary on pages 47 to 49 for definitions and appendix A – Alternative performance measures on pages 50 to 53 for reconciliation to financial statement line items.

Earnings per share[1]

Basic earnings per share decreased by 11.4% to 29.5 pence (2018 restated: 33.3 pence). Diluted earnings per share decreased by 11.2% to 29.2 pence (2018 restated: 32.9 pence) mainly reflecting the reduction in profit after tax.

Note:

1. Results for the period ended 31 December 2018 have been restated to reflect the fully retrospective adoption of IFRS 16 'Leases'. See note 23 to the consolidated financial statements.

Net asset value

At 31 December	Note	**2019 £m**	2018[1] £m restated
Net assets[2]	13	**2,643.6**	2,558.2
Goodwill and other intangible assets	13	**(702.5)**	(566.8)
Tangible net assets	13	**1,941.1**	1,991.4
Closing number of Ordinary Shares (millions)	13	**1,366.6**	1,364.6
Net asset value per share (pence)	13	**193.4**	187.5
Tangible net asset value per share (pence)	13	**142.0**	145.9

Notes:

1. Results for the period ended 31 December 2018 have been restated to reflect the fully retrospective adoption of IFRS 16 'Leases'. See note 23 to the consolidated financial statements.
2. See glossary on pages 47 to 49 for definitions and appendix A – Alternative performance measures on pages 50 to 53 for reconciliation to financial statement line items.

Net assets at 31 December 2019 increased to £2,643.6 million (31 December 2018 restated: £2,558.2 million) and tangible net assets decreased to £1,941.1 million (31 December 2018 restated: £1,991.4 million) reflecting the 2019 retained profit and, increases in available-for-sale reserves. This was offset by additional expenditure on intangible assets as the Group continued to invest in the business.

Balance sheet management

Capital management and dividend policy

The Group aims to manage its capital efficiently and generate long-term sustainable value for shareholders, while balancing operational, regulatory, rating agency and policyholder requirements.

The Group aims to grow its regular dividend in line with business growth.

Where the Board believes that the Group has capital which is expected to be surplus to the Group's requirements for a prolonged period, it would intend to return any surplus to shareholders. In normal circumstances, the Board expects that a solvency capital ratio around the middle of its risk appetite range of 140% to 180% of the Group's solvency capital requirement ("**SCR**") would be appropriate and it will therefore take this into account when considering the potential for special distributions.

In the normal course of events the Board will consider whether or not it is appropriate to distribute any surplus capital to shareholders once a year, alongside the full year results.

The Group expects that one-third of the annual dividend will generally be paid in the third quarter as an interim dividend, and two-thirds will be paid as a final dividend in the second quarter of the following year. The Board may revise the dividend policy from time to time. The Company may consider a special dividend and/or a repurchase of its own shares to distribute surplus capital to shareholders.

The Board has recommended a final dividend of 14.4 pence per share (2018: 14.0 pence), an increase of 0.4 pence per share (2.9%). The Board has also approved a share buyback of up to £150 million which it expects to complete by the end of July 2020. This reflects the Board's continued confidence in the Group's capital position and the sustainability of its earnings. In normal circumstances, the Board expects the Group to operate around the middle of its solvency capital ratio risk appetite range of 140% to 180%.

The final dividend will be paid on 21 May 2020 to shareholders on the register on 14 April 2020. The ex-dividend date will be 9 April 2020.

Capital analysis

The Group is regulated under Solvency II requirements by the PRA on both a Group basis and for the Group's principal underwriter, U K Insurance Limited. In its results, the Group has estimated its Solvency II own funds, SCR and solvency capital ratio as at 31 December 2019.

Capital position

At 31 December 2019, the Group held a Solvency II capital surplus of £0.85 billion above its regulatory capital requirements, which was equivalent to an estimated solvency capital ratio of 165%, post the capital distributions of the proposed final dividend and share buyback.

The Group's SCR and solvency capital ratio are as follows:

At 31 December	**2019**	2018
Solvency capital requirement (£ billion)	**1.32**	1.26
Capital surplus above solvency capital requirement (£ billion)	**0.85**	0.89
Solvency capital ratio post-capital distributions	**165%**	170%

Movement in capital surplus

	2019 £bn	2018 £bn
Capital surplus at 1 January	**0.89**	0.91
Capital generation excluding market movements	**0.60**	0.47
Market movements	**0.06**	(0.06)
Capital generation	**0.66**	0.41
Change in solvency capital requirement	**(0.06)**	0.13
Surplus generation	**0.60**	0.54
Capital expenditure	**(0.19)**	(0.15)
Management capital action		–
Capital distribution – ordinary dividends[1]	**(0.30)**	(0.30)
Capital distribution – special dividends[1]	**–**	(0.11)
Capital distribution – share buyback	**(0.15)**	–
Net surplus movement	**(0.04)**	(0.02)
Capital surplus at 31 December	**0.85**	0.89

Notes:

1. Foreseeable dividends included above are adjusted to exclude the expected dividend waivers in relation to shares held by the employee share trusts, which are held to meet obligations arising on the various share option awards.

In 2019, the Group generated £0.66 billion of Solvency II capital offset by £0.19 billion of capital expenditure and capital distribution of £0.45 billion for the 2019 dividend and share buyback. The increased capital expenditure reflects the significant investment the Group is making in building future capability including the development of the next generation core personal lines IT systems. In 2020, the level of expenditure is expected to be approximately £150 million. Thereafter, expenditure levels are expected to reduce to around £100 million from 2021.

Change in solvency capital requirement

	2019 £bn
Solvency capital requirement at 1 January	**1.26**
Model and parameter changes	**(0.07)**
Exposure changes	**0.13**
Solvency capital requirement at 31 December	**1.32**

The Group's SCR has increased by £0.06 billion in the year. Model and parameter changes reduced the SCR by £0.07 billion. Exposure changes, as a result of restructuring costs, Solvency II technical provisions movements and volume and mix changes of assets under management, led to an increase in the SCR of £0.13 billion.

Scenario and sensitivity analysis

The following table shows the impact on the Group's estimated solvency capital ratio in the event of the following scenarios as at 31 December 2019. The impact on the Group's solvency capital ratio arises from movements in both the Group's solvency capital requirement and own funds.

Scenario	Impact on solvency capital ratio	
	31 Dec 2019	31 Dec 2018
Motor small bodily injury deterioration equivalent to accident years 2008 and 2009	**(7pts)**	(7pts)
One-off catastrophe loss equivalent to the 1990 storm	**(9pts)**	(8pts)
One-off catastrophe loss based on extensive flooding of the River Thames	**(9pts)**	(8pts)
Change in reserving basis for PPOs to use a real discount rate of minus 1%[1]	**(8pts)**	(10pts)
100bps increase in credit spreads[2]	**(9pts)**	(11pts)
100bps decrease in interest rates with no change in the PPO real discount rate	**1pt**	(1pt)

Notes:

1. The PPO real discount rate used is an actuarial judgement which is reviewed annually based on the economic outlook for wage inflation relative to the EIOPA discount rate curve.
2. Only includes the impact on AFS assets (excludes illiquid assets such as infrastructure debt) and assumes no change to the SCR.

Own funds

The following table splits the Group's own funds by tier on a Solvency II basis.

At 31 December	**2019 £bn**	2018 £bn
Tier 1 capital before foreseeable capital distributions	**1.80**	1.76
Foreseeable capital distributions	**(0.35)**	(0.31)
Tier 1 capital – unrestricted	**1.45**	1.45
Tier 1 capital – restricted	**0.37**	0.35
Tier 1 capital	**1.82**	1.80
Tier 2 capital – subordinated debt	**0.26**	0.26
Tier 3 capital – deferred tax	**0.09**	0.09
Total own funds	**2.17**	2.15

During 2019, the Group's own funds increased from £2.15 billion to £2.17 billion. Tier 1 capital after foreseeable capital distributions represents 84% of own funds and 138% of the estimated SCR. Tier 2 capital relates solely to the Group's £0.26 billion subordinated debt. The amount of Tier 2 and Tier 3 capital permitted under the Solvency II regulations is 50% of the Group's SCR and of Tier 3 alone is less than 15%. Therefore, the Group currently has no ineligible capital. The maximum amount of Restricted Tier 1 capital permitted as a proportion of total Tier 1 capital under the Solvency II regulations is 20%. Restricted Tier 1 capital relates solely to the Tier 1 notes issued in 2017.

Reconciliation of IFRS shareholders' equity to Solvency II own funds

At 31 December	**2019 £bn**	2018 £bn
Total shareholders' equity	**2.64**	2.56
IFRS 16 'Leases' adjustment to remove restated equity movement[1]	**–**	0.01
Goodwill and intangible assets	**(0.70)**	(0.57)
Change in valuation of technical provisions	**(0.06)**	(0.15)
Other asset and liability adjustments	**(0.08)**	(0.09)
Foreseeable capital distributions	**(0.35)**	(0.31)
Tier 1 capital – unrestricted	**1.45**	1.45
Tier 1 capital – restricted	**0.37**	0.35
Tier 1 capital	**1.82**	1.80
Tier 2 capital – subordinated debt	**0.26**	0.26
Tier 3 capital – deferred tax	**0.09**	0.09
Total own funds	**2.17**	2.15

Note

1. No adjustment has been made for IFRS 16 'Leases' in 2018 on a Solvency II basis.

Leverage

The Group's financial leverage decreased by 0.6 percentage points and continued to remain conservative at 18.6% (2018 restated: 19.2%). The decrease was primarily due to the increase in shareholders' equity as a result of improvements to the valuation of the Group's AFS investments.

At 31 December	2019 £m	2018[1] £m restated
Shareholders' equity	**2,643.6**	2,558.2
Tier 1 notes	**346.5**	346.5
Financial debt – subordinated debt	**259.0**	259.5
Total capital employed	**3,249.1**	3,164.2
Financial-leverage ratio[2]	**18.6%**	19.2%

Notes:

1. Results for the period ended 31 December 2018 have been restated to reflect the fully retrospective adoption of IFRS 16 'Leases'. See note 23 to the consolidated financial statements.
2. Total IFRS financial debt and Tier 1 notes as a percentage of total IFRS capital employed.

Credit ratings

Moody's Investors Service provide insurance financial-strength ratings for U K Insurance Limited, the Group's principal underwriter. Moody's rate U K Insurance Limited as 'A1' for insurance financial strength (strong) with a stable outlook.

Reserving

The Group makes provision for the full cost of outstanding claims from its general insurance business at the balance sheet date, including claims estimated to have been incurred but not yet reported at that date and claims handling costs. The Group considers the class of business, the length of time to notify a claim, the validity of the claim against a policy, and the claim value. Claims reserves could settle across a range of outcomes, and settlement certainty increases over time. However, for bodily injury claims the uncertainty is greater due to the length of time taken to settle these claims. The possibility of annuity payments for injured parties also increases this uncertainty.

The Group seeks to adopt a conservative approach to assessing liabilities, as evidenced by the favourable development of historical claims reserves. Reserves are based on management's best estimate, which includes a prudence margin that exceeds the internal actuarial best estimate. This margin is set by reference to various actuarial scenario assessments and reserve distribution percentiles. It also considers other short and long-term risks not reflected in the actuarial inputs, as well as management's view on the uncertainties in relation to the actuarial best estimate.

The most common method of settling bodily injury claims is by a lump sum. When this includes an element of indemnity for recurring costs, such as loss of earnings or ongoing medical care, the settlement calculations apply the statutory discount rate (known as the Ogden discount rate) to reflect the fact that payment is made on a one-off basis rather than periodically over time. The Ogden discount rate changed from 2.5% to minus 0.75% in 2017 in England, Wales and Scotland, reflecting the low interest rate environment, and case law holding that claimants were entitled to invest purely in zero risk investments, i.e. index-linked gilts. The Civil Liability Act 2018 changed the law in two ways: firstly, by requiring the Government to review the Ogden discount rate at least every five years, and secondly to do so by reference to low risk rather than very low or zero risk investments.

At year-end 2018, the Group decided that it was likely that the Ogden discount rate would change in 2019 and selected an estimate of 0% to value its lump sum bodily injury reserves. When the Ogden discount rate review process subsequently concluded in July 2019, the discount rate increased from minus 0.75% to minus 0.25% for England and Wales. The Ogden discount rate is a devolved matter in Scotland and Northern Ireland and it has remained at minus 0.75% in Scotland, and at 2.5% in Northern Ireland.

The Group reserves its large bodily injury claims at the relevant discount rate for each jurisdiction, with the overwhelming majority now reserved at minus 0.25% as most will be settled under the law in England and Wales. The Ogden discount rate will be reviewed again at the latest in 2024. There has been an ongoing reduction in large bodily injury exposures as a result of continued positive prior-year development of claims reserves, and a higher proportion of reserves being covered by reinsurance as a result of the decision to opt for a lower reinsurance attachment point from 2014 onwards.

If the claimant prefers, large bodily injury claims can be settled using a periodical payment order (PPO). This is an alternative way to provide an indemnity for recurring costs, making regular payments, usually for the rest of the claimant's life. These claims are reserved for using an internal discount rate, which is progressively unwound over time. As it is likely to take time to establish whether a claimant will prefer a PPO or a lump sum, until a settlement method is agreed, the Group makes assumptions about the likelihood that claimants will opt for a PPO. This is known as the PPO propensity. In line with the Group's experience, and the negative Ogden discount rate, the assumed PPO propensity has reduced in 2019.

The Group's prior-year reserve releases were £294.5 million (2018: £404.4 million) with good experience in large and small bodily injury claims being a key contributor.

Looking forward, the Group expects to continue setting its initial management best estimate conservatively. Assuming current claims trends continue, the contribution from prior-year reserve releases will reduce over time, although it is expected to remain significant.

Claims reserves net of reinsurance

At 31 December	2019 £m	2018 £m
Motor	**1,799.1**	1,946.4
Home	**266.3**	323.8
Rescue and other personal lines	**88.5**	89.1
Commercial	**516.1**	541.4
Total	**2,670.0**	2,900.7

Sensitivity analysis – the discount rate used in relation to PPOs and changes in the assumed Ogden discount rate

The table below provides a sensitivity analysis of the potential net impact of a change in a single factor (the internal discount rate used for PPOs and separately the Ogden discount rate) with all other assumptions left unchanged. Other potential risks beyond the ones described could have additional financial impacts on the Group.

	Increase / (decrease) in profit before tax[1,2]	
At 31 December	2019 £m	2018 £m
PPOs[3]		
Impact of an increase in the discount rate used in the calculation of present values of 100 basis points	**48.5**	50.7
Impact of a decrease in the discount rate used in the calculation of present values of 100 basis points	**(66.5)**	(70.1)
Ogden discount rate[4]		
Impact of the Group reserving at a discount rate of 0.75% compared to minus 0.25% (2018: 1% compared to 0%)	**53.3**	56.2
Impact of the Group reserving at a discount rate of minus 1.25% compared to minus 0.25% (2018: minus 1% compared to 0%)	**(75.0)**	(76.3)

Notes:

1. These sensitivities are net of reinsurance and exclude the impact of taxation.
2. These sensitivities reflect one-off impacts at 31 December and should not be interpreted as predictions.
3. The sensitivities relating to an increase or decrease in the internal discount rate used for PPOs illustrate a movement in the time value of money from the assumed level of 0% for reserving. The PPO sensitivity has been calculated as the direct impact of the change in the internal discount rate with all other factors remaining unchanged.
4. Ogden discount rate sensitivity has been calculated as the direct impact of a permanent change in the discount rate in England and Wales with all other factors remaining unchanged. The Group will consider the statutory discount rate when setting its reserves but not necessarily provide on this basis, as was the case at the year ended 31 December 2018. This is intended to ensure that reserves are appropriate for current and potential future developments.

The PPO sensitivity above is calculated on the basis of a change in the internal discount rate used for the actuarial best estimate ("**ABE**") reserves as at 31 December 2019. It does not take into account any second order impacts such as changes in PPO propensity or reinsurance bad debt assumptions.

Tax management

The Board recognises that the Group has an important responsibility to manage its tax position effectively. The Board has delegated day-to-day management of taxes to the Chief Financial Officer and oversight is provided by the Audit Committee.

These arrangements are intended to ensure that the Group: complies with applicable laws and regulations; meets its obligations as a contributor and a collector of taxes on behalf of the tax authorities; and manages its tax affairs efficiently, claiming reliefs and other incentives where appropriate.

Tax authorities

The Group has open and cooperative relationships with the tax authorities with whom it deals in the countries where the Group operates, namely the UK, the Republic of Ireland, South Africa and India.

Tax policy and governance

The Group's tax policy has been reviewed and approved by the Audit Committee in 2019. The Group Tax team supports the Chief Financial Officer in ensuring the policy is adhered to at an operational level.

For more information please see our published Group Tax policy on the Group's website at https://www.directlinegroup.co.uk/en/who-we-are/governance/other-policies.html

Total tax contribution

The Group's direct and indirect tax contribution to the UK Exchequer is significantly higher than the UK corporation tax that the Group pays on its profits. The Group collects taxes relating to employees and customers on behalf of the UK Exchequer and other national governments. It also incurs a significant amount of irrecoverable value added tax relating to overheads and claims. Taxes borne and collected in other tax jurisdictions have not been included in this note as the amounts are minimal in the context of the wider UK Group.

During 2019 the sum of taxes either paid or collected across the Group was £956.6 million. The composition of this between the various taxes borne and collected by the Group is shown below.

Total taxes borne

At 31 December	2019 £m
Current-year corporation tax charge	101.9
Irrecoverable value added tax incurred on overheads	102.8
Irrecoverable value added tax embedded within claims spend	193.8
Employer's national insurance contributions	39.2
Other taxes	8.4
Total	**446.1**

Total taxes collected

At 31 December	2019 £m
Insurance premium tax	398.9
Value added tax	13.2
Employee's pay as you earn and national insurance contributions	98.4
Total	**510.5**

Principal risks and uncertainties

We carefully assess the principal risks facing us. Principal risks are defined as having a residual risk impact of £40 million or more on a 1-in-200 years basis, taking into account customer, financial and reputational impacts.

Principal risks	Management and mitigation examples
Insurance risk is the risk of loss due to fluctuations in the timings, amount, frequency and severity of an insured event relative to the expectations at the time of underwriting. Key drivers of the outlook for insurance risk across our business plan include reserving, underwriting, distribution, pricing and reinsurance risks.	This year, motor market premium inflation has not matched expectations of claims inflation, which has led to a slowdown in customer shopping behaviour and a reduction in new business. Increases in vehicle technology are also beginning to cause an increase in claims inflation. In response we are developing our ability to distinguish this trend between vehicles to more accurately price risk. We've also launched Darwin using machine learning rating models with the aim of growing market share in areas where we have lower penetration. Changes to the Ogden discount rate have led to uncertainty in pricing and reserving. To help mitigate this, underwriting guidelines are set for all transacted business and pricing is refined by analysing comprehensive data. We invest in enhanced external data to analyse and mitigate our exposures and we set our reserves using the latest internal and external data and trends. The continued political uncertainty (including post-Brexit) could also have an impact on claims inflation and market behaviour (for example, recession affects customer behaviour) and we continue to monitor this closely. Finally, climate change presents a risk of more frequent extreme events and key risk indicators are in place to monitor related risks across Home and Motor.
Market risk is the risk of loss resulting from fluctuations in the level and in the volatility of market prices of assets, liabilities and financial instruments. Key drivers of market risk are the sensitivity of the values of our assets and investments to changes in credit spreads, and our exposure to losses as a result of changes in interest rate term structure or volatility.	Concerns about the impacts of Brexit remain, and continuing US-China tensions could impact equity and credit markets within the global economy and lead to credit spread increases. To address this, we have an investment strategy which is approved by the Board and includes limiting exposure to individual asset classes and the amount of illiquid investments we hold. We also use risk reduction techniques such as hedging foreign currency exposures with forward contracts.
Operational risk is the risk of loss due to inadequate or failed internal processes or systems, human error or from external events. The principal risks within this category are Cyber, Operational Resilience, Partnership Contractual Obligations, Change, Outsourcing and Technology & Infrastructure risks.	Operational risks can arise within all areas of the business and can become manifest through inadequate or failed internal processes or systems, human error or from external events. The key drivers for us include people, data, cyber, technology and infrastructure, resilience, partnership contractual obligations, change, and outsourcing and suppliers. Our approach is proactively to manage our operational risks to mitigate potential customer detriment, regulatory or legal censure, financial and reputational impacts. We have in place appropriate operational processes and systems, including prevention and detection measures. These include processes which seek to ensure we can absorb and/or adapt to internal or external occurrences that could disrupt business operations. We are continuing to work to improve performance of our IT systems while focusing on developing future systems capability. With significant strategic investment in train we are actively strengthening our change implementation controls to further mitigate potential impacts related to data management, IT systems stability, cyber security, and the wider internal control environment during transition. We have a mature process in place designed to enable us to maintain the right number of capable and engaged people, supported by activities that cultivate a positive culture through robust employment practices. Alongside this, we operate a robust procurement and supply chain framework for the sourcing, appointment and ongoing management of the Group's suppliers and outsource providers. Our risk management framework is designed to enable us to capture risk information in a complete and consistent way, including proactive trend analysis, root cause analysis and read across to enable early warnings and a 'learning' risk environment.

Principal risks and uncertainties continued

Principal risks	Management and mitigation examples
Regulatory and conduct risk describes the risks arising out of breaches of and/or changes to regulation, law, regulatory policy or interpretation, or to supervisory expectations or approach, that have an adverse operational and financial impact as a result of reputational damage, regulatory or legal censure, fines or prosecutions, and any other type of non-budgeted operational risk losses, associated with our conduct and activities.	We maintain a constructive and open relationship with our regulators and have a culture of delivering on our commitments to our customers. The issue of pricing practices within the general insurance market continues to be a focus of the FCA and it's an issue to which we have devoted a lot of attention. Our conduct risk management framework is designed to deliver fair outcomes to customers and minimise our risk exposure supported by a set of conduct pricing principles to enable the fair pricing of business across our book, and we continue to develop our approach to seek to anticipate developments and ensure that we can continue to provide good outcomes for our customers. Finally, we carry out planned risk-based monitoring of customer processes as well as more targeted thematic reviews to help us manage the risk of unfair customer outcomes.
Credit risk is the risk of loss resulting from defaults in obligations due and/or changes in credit standing of either issuers of securities, counterparties or any debtors to which the Group is exposed.	To manage credit risk, we set credit limits for each counterparty and actively monitor credit exposures. In addition, we only purchase reinsurance from reinsurers with at least A- rating and, for liabilities with a relatively long period of time to settlement, this rating is at least A+. Finally, we also have well defined criteria to determine which customers are offered and granted credit.
Strategic risk is the risk of direct or indirect adverse effects resulting from strategies not being optimally chosen, implemented or adapted to changing conditions.	Strategic risk is influenced by external developments such as Brexit and motor market conditions. To manage our risks, we have taken the following steps: – we agree, monitor and manage performance against the Board-approved plan and targets; – the Board leads an annual strategy and five-year planning process which considers our performance, competitor positioning and strategic opportunities; – as part of the timetable for the Strategic Plan, the Risk Function carries out a risk review of the Plan which is documented in the Group's Own Risk and Solvency Assessment and presented to the Board; and – we identify and manage emerging risks using established governance processes and forums.

Potential effects of Brexit

The UK left the EU ('Brexit') on 31 January 2020. At the date of this report there remains uncertainty as to when the implementation period will end (it is due to end on 31 December 2020 but could yet be extended, albeit requiring a change to the law) and as to what, if any, trading agreement may or may not be agreed between the UK and EU to take effect subsequent to the implementation period. There is also uncertainty as to what trading agreements may or may not be agreed with key non-EU countries to supersede such arrangements previously subject to EU trade agreements. Accordingly, there remains uncertainty as to the effect of Brexit on the Group.

If there is a smooth end to the implementation period with an agreed future trading agreement between the UK and the EU (and other key countries), and accordingly without significant disruption to the UK economy and to business generally, then any adverse impact on the Group (if any) would also not be expected to be significant. If, however, trade discussions (or the failure of them) were to lead to significant disruption then the impact on the Group could correspondingly also be disruptive and potentially material.

Internal review

Following the EU referendum result in 2016, the Group established a Brexit Working Group comprising representatives from across the Group. It was identified that there was a risk that the UK could enter a prolonged period of reduced growth due to Brexit, potentially reducing insurance sales and the value of our investment portfolio. Whilst our operations are based mainly in the UK, Brexit-related issues which could impact adversely on the Group could include: changes to the value of sterling which impact claims and non-claims supplier costs; inflation; impacts on credit spreads which in turn could impact on the Group's investments and capital; recession; recruitment and retention of people; impacts on the speed of delivery and cost of goods and services required by the business including for fulfilling insurance claims made by customers, for example because of delays at borders caused by increased border regulations and by additional costs caused by increased tariffs and devaluation of sterling; availability of reinsurers authorised to write business in the UK; data transfers; the removal of the European Health Insurance Card ("**EHIC**") leading to greater reliance on travel insurance; travel disruption; increased use of Green Cards (internationally recognised certificates that act as proof of insurance, including in the EU); potential changes to direct and indirect tax; and the regulatory impact on our capital position.

Possible implications
The Group has proactively considered a variety of possible implications of a disruptive end to existing trading and other arrangements between the UK and the EU, including of a financial and operational nature; for example:

The Group's investment portfolio
The impact on the Group's investment portfolio and in particular credit spreads related to its debt securities and therefore Group solvency: A sensitivity analysis relating to credit spreads is provided in these preliminary results and in the Group's Annual Report & Accounts. The Group has also considered Brexit impacts in its Investment Committee, and further information is provided on the work of the Investment Committee in the Group's Annual Report & Accounts. A disruptive end to previous arrangements between the UK and EU could impact adversely on the Group's investments and therefore capital and the solvency capital coverage ratio and the appropriateness of paying dividends.

Procurement and supply chain
In particular as part of the Group's ability to deal with claims made under insurance policies, the Group needs to acquire a wide range of goods and services. A significant amount and spread of goods, for example such as car parts, are sourced from within the EU. The Group has been in discussion with principal suppliers who took steps to increase stocks within the UK in the event of a potential 'hard' Brexit leading to disruption at borders. However, in the event of a lack of appropriate trading arrangements with the EU (and other countries) following the implementation period and for example in the event of the imposition of tariffs and quotas, the Group's ability to deal with claims in its normal ordinary course of business manner could be adversely impacted and there could be delays and extra costs.

The Republic of Ireland
The Group has a small amount of business in the Republic of Ireland, servicing a small Irish part of a UK partner's wider business. The Group had obtained approval in principle from the Central Bank of Ireland for the establishment of a formal third country branch in the Republic of Ireland, in order to be able to continue with this business post a 'hard' no-deal Brexit, should that have become necessary. It remains to be seen whether similar arrangements will be needed at the end of the implementation period.

Crisis management
The Group has also been focusing on Brexit from a potential crisis management perspective, with the objective of maintaining operational resilience in the event of a disruptive Brexit and with a view to being able to react better to events as they unfold, including during and following the implementation period.

Emerging risks
We define emerging risks as newly developing risks that are often difficult to quantify but may materially affect our business. Emerging risks are usually highly uncertain risks which are external to the Group and we take a proactive approach to the emerging risk management processes, with the objective of enabling us to:

- identify, manage and monitor a broad range of potential emerging risks; and
- mitigate the impact of emerging risks which could impact the delivery of the Plan.

We record each emerging risk within an Emerging Risk Register.

During 2019, the Risk function has worked with subject matter experts from the business to enhance the quality and detail of emerging risk updates. Each risk is owned by a member of the Executive with subject matter experts in the Risk function providing challenge and oversight; and emerging risks are monitored by the Risk Management Committee, Board Risk Committee and Board.

The emerging risk process is supplemented by deep dives on selected emerging risks which are reported to the Board Risk Committee for review and challenge.

Climate change
We recognise that climate change potentially poses material long-term financial risks to the business and is receiving increased scrutiny from regulators and investors. Climate change can be divided into three categories: physical, transition, and liability risks, all of which can manifest themselves through a range of existing risks within the material risk register, including insurance, market, operational, strategic and reputational risks.

Physical risks
Physical risks are the direct risks which arise from weather-related events, including the potential to affect both the frequency and severity of natural catastrophes and other weather-related events in the UK. These are not only financial risks but also risks arising from the operational impacts of weather events; for example, vacating an office due to flooding, as happened to the Group in 2015.

Transitional risks
Transitional risks arise because efforts to mitigate climate change are driving a transition towards a lower-carbon economy, which creates risks and opportunities.

For example:

- Whilst insuring electric vehicles does not fundamentally change the business model, electric vehicles have their own unique risk profile, and pose different challenges to motor underwriters, accident repair centres, and to rescue products.
- Increased operating costs due to the potential increase in carbon costs and regulatory requirements are also likely to impact all participants in the industry. The Group monitors its own impact on the climate and has an established environmental management programme.
- Our business depends on the strength of its brands and its reputation with customers and distributors. As consumers become more aware and educated about climate change and environmental issues, research shows that they are putting their faith in brands that take their corporate responsibility seriously.

Liability risks
Liability risks arise when parties, who have suffered losses from climate change, seek to recover from those they believe may have been responsible. There is some potential exposure to liability risk through commercial liability insurance. There are two types of coverage that may have an elevated exposure to climate liability risk: insurance against the risks due to pollution on agricultural insurance policies, and professional indemnity covers. We have reinsured both of these risks.

In addition to the above risks, the impacts of potential physical, transition and liability risks arising in the wider economy can also have an indirect impact on the investment portfolio through their influence on the value of assets. Our largest asset portfolios are focused on corporate bonds. During 2018, we approved a significant new investment initiative which incorporates a greater focus on indices weighted by environmental, social and governance factors, which tilt the composition of the portfolio towards higher holdings and weightings of issuers with strong environmental, social and governance scores.

The risks and impacts of climate change are wide ranging. The Group is focusing increasingly on climate change, with related risk management activity including the monitoring of climate change through the Emerging Risk process, the formation of a Climate Change working group, and commencing the implementation of the recommendations of the Financial Stability Board's Taskforce on Climate-related Financial Disclosures.

Technological developments change consumer needs for insurance
In the near term, we expect data to emerge as a key area of innovation, as insurers learn to access and use new sources of customer data to improve their understanding of risk and improve customer journeys. We expect a greater focus on transparency and fairness, and developments in new car technology, particularly automated driving and electric vehicles, are likely to be a new area for us to understand and compete in. We also expect PCWs to use digital technology and data to continue to build their role with customers. These changes could significantly affect the size and nature of the insurance market and the role of insurers. Our strategy is designed to help us transform our business and deliver insurance our customers want and need in the future.

Changes to traditional insurance business models
In the longer term (5 years+) potential disruption, from the likes of major online retail organisations which have previously not been active in the insurance market, and powerful new data sharing technologies, such as Open Banking and application programming interfaces ("**APIs**"), may create new and significant routes to market. We expect to see the lines between direct and intermediated distribution channels blend and blur – requiring new approaches to access the market. Our partnerships with Starling Bank, Tesla, and RBS and NatWest are helping us to develop new capabilities and provide new routes to market. Also connected technology and new ownership models may create demand for new types of insurance products to meet more specific needs, potentially combined with other services.

While the extent and timing of these changes are uncertain, our new strategy has been designed to help us respond to these and other market changes so that we can win in our chosen markets.

CONSOLIDATED INCOME STATEMENT

For the year ended 31 December 2019

	Notes	**2019 £m**	2018[1] £m restated
Gross earned premium	4	**3,202.6**	3,306.7
Reinsurance premium	4	**(217.7)**	(217.2)
Net earned premium	4	**2,984.9**	3,089.5
Investment return	5	**134.6**	154.6
Instalment income		**114.0**	119.9
Other operating income	6	**66.2**	72.1
Total income		**3,299.7**	3,436.1
Insurance claims	7	**(1,917.3)**	(1,966.2)
Insurance claims recoverable from reinsurers	7	**69.7**	55.1
Net insurance claims	7	**(1,847.6)**	(1,911.1)
Commission expenses	8	**(211.5)**	(200.4)
Operating expenses (including restructuring and one-off costs)	9	**(704.9)**	(718.2)
Total expenses		**(916.4)**	(918.6)
Finance costs	10	**(26.0)**	(25.9)
Profit before tax		**509.7**	580.5
Tax charge		**(89.8)**	(108.5)
Profit for the year attributable to owners of the Company		**419.9**	472.0
Earnings per share:			
Basic (pence)	12	**29.5**	33.3
Diluted (pence)	12	**29.2**	32.9

Note:

1. Results for the year ended 31 December 2018 have been restated to reflect the fully retrospective adoption of IFRS 16 'Leases', see note 23.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2019

	2019 £m	2018[1] £m restated
Profit for the year	**419.9**	472.0
Other comprehensive income		
Items that will not be reclassified subsequently to the income statement:		
Actuarial (loss) / gain on defined benefit pension scheme	**(7.3)**	2.7
Tax relating to item that will not be reclassified	**1.3**	(0.4)
	(6.0)	2.3
Items that may be reclassified subsequently to the income statement:		
Cash flow hedges	**(0.7)**	0.5
Fair value gain / (loss) on AFS investments	**118.1**	(121.4)
Less: realised net gains on AFS investments included in the income statement	**(16.5)**	(19.5)
Tax relating to items that may be reclassified	**(17.3)**	23.9
	83.6	(116.5)
Other comprehensive income / (loss) for the year net of tax	**77.6**	(114.2)
Total comprehensive income for the year attributable to owners of the Company	**497.5**	357.8

Note:

1. Results for the year ended 31 December 2018 have been restated to reflect the fully retrospective adoption of IFRS 16 ‘Leases’, see note 23.

CONSOLIDATED BALANCE SHEET

As at 31 December 2019

	Notes	2019 £m	31 December 2018[1] £m restated	1 January 2018[1] £m restated
Assets				
Goodwill and other intangible assets		**702.5**	566.8	471.1
Property, plant and equipment		**143.4**	156.2	174.4
Right-of-use assets		**149.2**	153.4	157.9
Investment property		**291.7**	322.1	309.3
Reinsurance assets	14	**1,251.3**	1,208.7	1,178.5
Deferred acquisition costs		**176.2**	170.4	185.0
Insurance and other receivables		**846.5**	875.9	981.2
Prepayments, accrued income and other assets		**120.2**	124.5	143.0
Derivative financial instruments		**121.5**	48.2	84.4
Retirement benefit asset		**9.7**	17.0	14.4
Financial investments	15	**4,673.4**	4,737.8	5,040.4
Cash and cash equivalents	16	**948.6**	1,154.4	1,358.6
Assets held for sale		**–**	–	4.2
Total assets		**9,434.2**	9,535.4	10,102.4
Equity				
Shareholders' equity		**2,643.6**	2,558.2	2,701.9
Tier 1 notes	18	**346.5**	346.5	346.5
Total equity		**2,990.1**	2,904.7	3,048.4
Liabilities				
Subordinated liabilities	19	**259.0**	259.5	264.7
Insurance liabilities	20	**3,819.6**	4,005.9	4,225.7
Unearned premium reserve	21	**1,506.0**	1,505.5	1,600.3
Borrowings	16	**52.3**	62.0	54.1
Derivative financial instruments		**30.5**	25.9	12.0
Provisions[2]		**74.3**	72.8	74.2
Trade and other payables, including insurance payables		**478.1**	481.3	583.8
Lease liabilities		**164.4**	167.3	170.1
Deferred tax liabilities		**9.6**	4.5	28.4
Current tax liabilities		**50.3**	46.0	40.7
Total liabilities		**6,444.1**	6,630.7	7,054.0
Total equity and liabilities		**9,434.2**	9,535.4	10,102.4

Notes:

1. The balance sheet as at 1 January 2018 and 31 December 2018 have been restated to reflect the fully retrospective adoption of IFRS 16 'Leases', see note 23.
2. Presentational amendments included 'Provisions' previously presented within 'Trade and other payables, including insurance payables' are now presented separately on the consolidated balance sheet. This amendment has been made to provide additional analysis of these balances and is in accordance with international accounting standards.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2019

	Share capital (note 17) £m	Employee trust shares £m	Capital reserves £m	Available-for-sale revaluation reserve £m	Foreign exchange translation reserve £m	Retained earnings £m	Shareholders' equity £m	Tier 1 notes (note 18) £m	Total equity £m
Balance at 1 January 2018 (audited)	150.0	(34.1)	1,450.0	80.2	0.3	1,068.7	2,715.1	346.5	3,061.6
First application of IFRS 16[1]	–	–	–	–	–	(13.2)	(13.2)	–	(13.2)
Balance at 1 January 2018 (restated)	150.0	(34.1)	1,450.0	80.2	0.3	1,055.5	2,701.9	346.5	3,048.4
Profit for the year	–	–	–	–	–	472.0	472.0	–	472.0
Other comprehensive loss	–	–	–	(117.0)	0.5	2.3	(114.2)	–	(114.2)
Dividends and appropriations paid (note 11)	–	–	–	–	–	(503.8)	(503.8)	–	(503.8)
Shares acquired by employee trusts	–	(19.5)	–	–	–	–	(19.5)	–	(19.5)
Credit to equity for equity-settled share-based payments	–	–	–	–	–	21.0	21.0	–	21.0
Shares distributed by employee trusts	–	18.4	–	–	–	(18.4)	–	–	–
Tax on share-based payments	–	–	–	–	–	0.8	0.8	–	0.8
Balance at 31 December 2018 (restated)	150.0	(35.2)	1,450.0	(36.8)	0.8	1,029.4	2,558.2	346.5	2,904.7
Profit for the year	**–**	**–**	**–**	**–**	**–**	**419.9**	**419.9**	**–**	**419.9**
Other comprehensive income	**–**	**–**	**–**	**84.3**	**(0.7)**	**(6.0)**	**77.6**	**–**	**77.6**
Dividends and appropriations paid (note 11)	**–**	**–**	**–**	**–**	**–**	**(420.7)**	**(420.7)**	**–**	**(420.7)**
Shares acquired by employee trusts	**–**	**(10.4)**	**–**	**–**	**–**	**–**	**(10.4)**	**–**	**(10.4)**
Credit to equity for equity-settled share-based payments	**–**	**–**	**–**	**–**	**–**	**18.4**	**18.4**	**–**	**18.4**
Shares distributed by employee trusts	**–**	**15.4**	**–**	**–**	**–**	**(15.4)**	**–**	**–**	**–**
Tax on share-based payments	**–**	**–**	**–**	**–**	**–**	**0.6**	**0.6**	**–**	**0.6**
Balance at 31 December 2019	**150.0**	**(30.2)**	**1,450.0**	**47.5**	**0.1**	**1,026.2**	**2,643.6**	**346.5**	**2,990.1**

Note:

1. Results for the year ended 31 December 2018 have been restated to reflect the fully retrospective adoption of IFRS 16 'Leases', see note 23.

CONSOLIDATED CASH FLOW STATEMENT

For the year ended 31 December 2019

	Notes	2019 £m	2018[1] £m restated
Net cash generated from operating activities before investment of insurance assets		**88.2**	23.5
Cash generated from investment of insurance assets		**373.9**	468.1
Net cash generated from operating activities		**462.1**	491.6
Cash flows used in investing activities			
Purchases of goodwill and other intangible assets		**(175.7)**	(142.4)
Purchases of property, plant and equipment		**(11.9)**	(13.3)
Proceeds on disposals of assets held for sale		**–**	13.8
Proceeds on disposal of property, plant and equipment		**–**	0.1
Net cash used in investing activities		**(187.6)**	(141.8)
Cash flows used in financing activities			
Dividends and appropriations paid	11	**(420.7)**	(503.8)
Finance costs (including lease interest)		**(26.4)**	(26.1)
Principal element of lease payments		**(13.1)**	(12.5)
Purchase of employee trust shares		**(10.4)**	(19.5)
Net cash used in financing activities		**(470.6)**	(561.9)
Net decrease in cash and cash equivalents		**(196.1)**	(212.1)
Cash and cash equivalents at the beginning of the year	16	**1,092.4**	1,304.5
Cash and cash equivalents at the end of the year	16	**896.3**	1,092.4

Note:

1. Results for the year ended 31 December 2018 have been restated to reflect the fully retrospective adoption of IFRS 16 'Leases', see note 23.

1. Accounting policies

Basis of preparation

The financial information included in this preliminary announcement has been prepared in accordance with the recognition and measurement criteria of International Financial Reporting Standards ("**IFRS**") as endorsed by the EU. However, this announcement does not itself contain sufficient information to comply with IFRS. The financial information set out in this preliminary results announcement does not constitute the statutory accounts for the year ended 31 December 2019. The financial information is derived from the statutory accounts, which comply with IFRS, within the Group's Annual Report & Accounts 2019. These accounts were signed on 2 March 2020 and are expected to be published in March 2020 and delivered to the Registrar of Companies following the Annual General Meeting to be held on 14 May 2020. The independent Auditor's report on the Group accounts for the year ended 31 December 2019 was signed on 2 March 2020, is unqualified, does not draw attention to any matters by way of emphasis and does not include a statement under S498(2) or (3) of the Companies Act 2006. This audit opinion excludes disclosures surrounding capital adequacy calculated under the Solvency II regime as these are outside of the audit scope.

Going concern

The Directors are satisfied that the Group has sufficient resources to continue in operation for the foreseeable future, a period of not less than 12 months from the date of this report. Accordingly, they continue to adopt the going concern basis in preparing the consolidated financial statements.

Adoption of new and revised standards

The Group has adopted IFRS 16 'Leases' for the first time in 2019. IFRS 16 replaces IAS 17 'Leases' and sets out the principles for recognition, measurement and disclosure of lease arrangements entered into by the Group. For all contractual arrangements where the Group is a lessee, it is required to account for these leases under a single on-balance sheet model with exemptions available for low value and short-term leases. The Group recognises a lease liability measured at the present value of future lease payments from the commencement of all lease arrangements which were previously classified as 'operating leases' under IAS 17. A further assessment was performed to ensure all leases had been recognised. These lease payments are discounted using the lessees' incremental borrowing rate at the commencement of the lease unless the interest rate implicit in the lease is readily determinable. A corresponding right-of-use asset is recognised on the balance sheet. Lease payments are allocated between the liability and finance cost, and the right-of-use asset is depreciated on a straight-line basis over the lease term.

IFRS 16 'Leases' has been adopted on a fully retrospective basis and therefore, in accordance with IAS 8 'Accounting Policies, Changes in Accounting Estimates and Errors', prior periods have been restated. The opening equity and prior period impacts of IFRS 16 on the primary financial statements are presented in note 23 to the consolidated financial statements. An assessment was undertaken to determine whether adoption of IFRS 16 included any material new accounting judgements or identifying any sources of estimation uncertainty. The Group concluded that there were none.

In September 2019, the IASB issued 'Interest Rate Benchmark Reform – Amendments to IFRS 9, IAS 39 and IFRS 7' which although not mandatory for the Group until 2020, has been adopted in 2019. The amendments modify some specific hedge accounting requirements to provide relief from the potential effects of the uncertainty caused by the IBOR reform. In addition, it requires companies to disclose additional information about their hedging relationships which are directly affected by these uncertainties. By adopting these amendments early, the Group is able to continue applying hedge accounting to some of its benchmark interest rate exposure as the amendments permit the continuation of hedge accounting where in future the hedged benchmark interest rate may no longer be separately available.

Accounting developments

New IFRS standards and amendments that are issued, but not yet effective for the 31 December 2019 reporting period and have not been early adopted by the Group are disclosed below. The Group intends to adopt these standards, if applicable, when they become effective, except for Amendments to IFRS 9 'Financial Instruments', as explained below.

In July 2014, the IASB issued the final version of IFRS 9 'Financial Instruments' which replaces IAS 39 'Financial Instruments: Recognition and Measurement' and all previous versions of IFRS 9; it was endorsed by the EU in 2016. IFRS 9 addresses the classification, measurement and derecognition of financial assets and financial liabilities, introduces new rules for hedge accounting and a new impairment model for financial assets; it is effective for annual periods beginning on or after 1 January 2018, however adoption by the Group has been deferred as described below.

In September 2016, the IASB issued 'Amendments to IFRS 4: Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts' to address issues arising from the different effective dates of IFRS 9 and IFRS 17. Amendments to IFRS 4 was endorsed by the EU in November 2017.

The Group conducted a high-level assessment of the three aspects of IFRS 9 and based on current information, the impact of applying the expected loss model for the first time is currently immaterial. The Group does not expect any other significant impact on its financial statements. The Group satisfies the exemption criteria within Amendments to IFRS 4 and has decided to defer the application of IFRS 9 until the International Accounting Standards Board effective date of the new insurance contracts standard IFRS 17 on 1 January 2021, which is expected to be delayed for at least another year. The Group will continue applying the temporary exemption from applying IFRS 9 as introduced by Amendments to IFRS 4.

Accounting developments continued

IFRS 17 'Insurance Contracts' was issued by the IASB in May 2017 to replace IFRS 4 'Insurance Contracts'. IFRS 17 is currently effective for reporting periods beginning on or after 1 January 2021, however it is expected to be delayed until 1 January 2022 following the IASB's 'Amendments to IFRS 17' exposure draft published in June 2019. Comparative figures are required. IFRS 17 is a comprehensive new accounting standard for all insurance contracts covering recognition and measurement, presentation and disclosure. The overall objective of IFRS 17 is to provide an accounting model for insurance contracts that is more useful and consistent for insurers and to replace the requirements of IFRS 4 that allowed insurers to apply grandfathering of previous local accounting policies.

The core of IFRS 17 is the general model, supplemented by an optional simplified premium allocation approach which is permitted for the liability for the remaining coverage for short duration contracts. The general model measures insurance contracts using the building blocks of: discounted probability weighted cash flows; an explicit risk adjustment; and a contractual service margin representing the unearned profit of the contract which is recognised as revenue over the coverage period.

An assessment on the impact of IFRS 17 on the Group's financial statements remains in progress. The Group expects to be able to apply the simplified premium allocation approach to most of its insurance and reinsurance contracts. IFRS 17 is yet to be endorsed by the EU.

2. Critical accounting judgements and key sources of estimation uncertainty

Full details of critical accounting judgements and key sources of estimation uncertainty used in applying the Group's accounting policies are outlined on pages 144 to 145 of the Annual Reports & Accounts 2018. There have been no significant changes to the principles or assumptions of these critical accounting judgements and key sources of estimation uncertainty during the year ended 31 December 2019, with the exception that the classification of the fair value hierarchy and goodwill and intangible assets impairment testing are no longer considered by the Group to include material accounting judgements or sources of estimation uncertainty.

3. Segmental analysis

The table below analyses the Group's revenue and results by reportable segment for the year ended 31 December 2019.

	Motor £m	Home £m	Rescue and other personal lines £m	Commercial £m	**Total Group £m**
Gross written premium	1,651.6	586.6	436.0	528.9	**3,203.1**
Gross earned premium	1,653.2	598.8	427.4	523.2	**3,202.6**
Reinsurance premium	(145.5)	(25.2)	(2.2)	(44.8)	**(217.7)**
Net earned premium	1,507.7	573.6	425.2	478.4	**2,984.9**
Investment return	88.6	16.7	5.6	23.7	**134.6**
Instalment income	83.8	20.5	2.8	6.9	**114.0**
Other operating income	51.3	0.6	11.1	3.2	**66.2**
Total income	1,731.4	611.4	444.7	512.2	**3,299.7**
Insurance claims	(1,086.8)	(276.2)	(285.2)	(269.1)	**(1,917.3)**
Insurance claims recoverable from reinsurers	43.5	7.8	0.8	17.6	**69.7**
Net insurance claims	(1,043.3)	(268.4)	(284.4)	(251.5)	**(1,847.6)**
Commission expenses	(39.9)	(55.7)	(27.2)	(88.7)	**(211.5)**
Operating expenses	(345.6)	(136.7)	(94.0)	(117.4)	**(693.7)**
Total expenses	(385.5)	(192.4)	(121.2)	(206.1)	**(905.2)**
Operating profit	**302.6**	**150.6**	**39.1**	**54.6**	**546.9**
Restructuring and one-off costs					**(11.2)**
Operating profit after restructuring and one-off costs					**535.7**
Finance costs					**(26.0)**
Profit before tax					**509.7**

	Motor	Home	Rescue and other personal lines	Commercial	Total Group
Underwriting profit	**78.9**	**112.8**	**19.6**	**20.8**	**232.1**
Loss ratio	69.3%	46.8%	66.9%	52.7%	**61.9%**
Commission ratio	2.6%	9.7%	6.4%	18.5%	**7.1%**
Expense ratio	22.9%	23.8%	22.1%	24.5%	**23.2%**
Combined operating ratio	**94.8%**	**80.3%**	**95.4%**	**95.7%**	**92.2%**

3. Segmental analysis continued

The table below analyses the Group's revenue and results by reportable segment for the year ended 31 December 2018[1] (restated).

	Motor £m	Home £m	Rescue and other personal lines £m	Commercial £m	Total Group £m
Gross written premium	1,671.2	606.9	422.8	511.0	3,211.9
Gross earned premium	1,684.3	698.0	416.6	507.8	3,306.7
Reinsurance premium	(142.5)	(30.2)	(1.9)	(42.6)	(217.2)
Net earned premium	1,541.8	667.8	414.7	465.2	3,089.5
Investment return	105.9	15.9	5.2	27.6	154.6
Instalment income	89.2	21.9	2.5	6.3	119.9
Other operating income	48.3	2.7	15.8	5.3	72.1
Total income	1,785.2	708.3	438.2	504.4	3,436.1
Insurance claims	(1,026.0)	(421.0)	(277.1)	(242.1)	(1,966.2)
Insurance claims recoverable from / (payable to) reinsurers	46.7	7.7	(0.1)	0.8	55.1
Net insurance claims	(979.3)	(413.3)	(277.2)	(241.3)	(1,911.1)
Commission expenses	(30.9)	(62.6)	(19.0)	(87.9)	(200.4)
Operating expenses	(356.9)	(148.5)	(98.0)	(114.8)	(718.2)
Total expenses	(387.8)	(211.1)	(117.0)	(202.7)	(918.6)
Operating profit	418.1	83.9	44.0	60.4	606.4
Restructuring and one-off costs					–
Operating profit after restructuring and one-off costs					606.4
Finance costs					(25.9)
Profit before tax					580.5

	Motor	Home	Rescue and other personal lines	Commercial	Total Group
Underwriting profit	174.7	43.4	20.5	21.2	259.8
Loss ratio	63.5%	61.8%	66.8%	51.8%	61.9%
Commission ratio	2.0%	9.4%	4.6%	18.9%	6.5%
Expense ratio	23.1%	22.3%	23.6%	24.7%	23.2%
Combined operating ratio	88.6%	93.5%	95.0%	95.4%	91.6%

Note:

1. Results for the year ended 31 December 2018 have been restated to reflect the fully retrospective adoption of IFRS 16 'Leases', see note 23.

4. Net earned premium

	2019 £m	2018 £m
Gross earned premium:		
Gross written premium	**3,203.1**	3,211.9
Movement in unearned premium reserve	**(0.5)**	94.8
	3,202.6	3,306.7
Reinsurance premium paid and payable:		
Premium payable	**(215.9)**	(223.5)
Movement in reinsurance unearned premium reserve	**(1.8)**	6.3
	(217.7)	(217.2)
Total	**2,984.9**	3,089.5

5. Investment return

	2019 £m	2018 £m
Investment income:		
Interest income from debt securities	**108.4**	124.0
Interest income from cash and cash equivalents	**7.9**	6.2
Interest income from infrastructure debt	**7.0**	6.9
Interest income from commercial real estate loans	**6.9**	6.2
Interest income	**130.2**	143.3
Rental income from investment property	**16.2**	15.9
	146.4	159.2
Net realised gains / (losses):		
AFS debt securities	**16.5**	19.5
Derivatives	**(9.5)**	(32.2)
Investment property	**(0.7)**	–
	6.3	(12.7)
Net unrealised (losses) / gains:		
Impairment of loans and receivables	**–**	(6.0)
Derivatives	**(12.6)**	1.4
Investment property	**(5.5)**	12.7
	(18.1)	8.1
Total	**134.6**	154.6

The table below analyses the realised and unrealised gains and losses on derivative instruments included in investment return.

	Realised 2019 £m	Unrealised 2019 £m	Realised 2018 £m	Unrealised 2018 £m
Derivative (losses) / gains:				
Foreign exchange forward contracts[1]	**(56.8)**	**103.4**	(102.6)	(41.3)
Associated foreign exchange risk	**53.4**	**(123.8)**	72.6	41.3
Net losses on foreign exchange forward contracts	**(3.4)**	**(20.4)**	(30.0)	–
Interest rate swaps[1]	**(16.8)**	**(33.6)**	22.1	(1.8)
Associated interest rate risk on hedged items	**10.7**	**41.4**	(24.3)	3.2
Net (losses) / gains on interest rate derivatives	**(6.1)**	**7.8**	(2.2)	1.4
Total	**(9.5)**	**(12.6)**	(32.2)	1.4

Note:

1. Foreign exchange forward contracts are measured at fair value through profit and loss and interest rate swaps are designated as hedging instruments.

6. Other operating income

	2019 £m	2018 £m
Revenue from vehicle recovery and repair services[1]	**28.3**	25.1
Vehicle replacement referral income	**19.1**	17.2
Legal services income	**11.3**	11.2
Other income[2,3]	**7.5**	18.6
Total	**66.2**	72.1

Notes:
1. Revenue from vehicle recovery and repair services include salvage income previously reported in other income. Comparative data for the year ended 31 December 2018 has been re-presented accordingly.
2. Other income includes mainly fee income from insurance intermediary services.
3. In 2018 other income included a £9.6 million gain on the sale of a property in Bristol.

7. Net insurance claims

	Gross	Reinsurance	Net	Gross	Reinsurance	Net
	2019 £m	2019 £m	2019 £m	2018[1] £m restated	2018 £m	2018[1] £m restated
Current accident year claims paid	**1,232.9**	**(0.2)**	**1,232.7**	1,307.8	(0.2)	1,307.6
Prior accident year claims paid	**870.7**	**(25.1)**	**845.6**	878.2	(30.9)	847.3
Decrease in insurance liabilities	**(186.3)**	**(44.4)**	**(230.7)**	(219.8)	(24.0)	(243.8)
Total	**1,917.3**	**(69.7)**	**1,847.6**	1,966.2	(55.1)	1,911.1

Claims handling expenses[2] for the year ended 31 December 2019 of £202.9 million (2018[1] restated: £192.2 million) have been included in the claims figures above.

Notes:
1. Results for the year ended 31 December 2018 have been restated to reflect the fully retrospective adoption of IFRS 16 'Leases', see note 23.
2. Includes costs in respect of low value leases of £0.3 million (31 December 2018 £0.3 million).

8. Commission expenses

	2019 £m	2018 £m
Commission expenses	**171.2**	188.5
Expenses incurred under profit participations	**40.3**	11.9
Total	**211.5**	200.4

9. Operating expenses

	2019 £m	2018[1] £m restated
Staff costs[2,3]	**267.3**	269.9
IT and other operating expenses[2,3,4]	**163.4**	167.6
Marketing	**113.9**	121.2
Insurance levies[5]	**81.5**	67.6
Depreciation and amortisation[6,7]	**78.8**	91.9
Total operating expenses (including restructuring and one-off costs)	**704.9**	718.2
Of which restructuring and one-off costs	**11.2**	–
Total excluding restructuring and one-off costs	**693.7**	718.2

Notes:
1. Results for the year ended 31 December 2018 have been restated to reflect the fully retrospective adoption of IFRS 16 'Leases', see note 23.
2. Restructuring and one-off costs of £11.2 million are included as follows: staff costs (£ 5.8 million) and other operating expenses (£5.4 million).
3. Staff costs and other operating expenses attributable to claims handling activities are allocated to the cost of insurance claims.
4. IT and other operating expenses include professional fees and property costs.
5. Insurance levies were previously reported in other operating expenses. Comparative data for the year 31 December 2018 has been re-presented accordingly.
6. Amortisation and impairment of other intangible assets includes a £1.3 million impairment charge for year ended 31 December 2019 (2018: £1.5 million), which relates to capitalised software development costs for ongoing IT projects primarily relating to development of new systems.
7. Includes depreciation on right-of-use assets of £14.2 million (31 December 2018: £14.1 million).

9. Operating expenses continued

The table below analyses the number of people employed by the Group's operations.

	At 31 December		Average for the year	
	2019	2018	**2019**	2018
Insurance operations	**7,963**	8,583	**8,388**	8,569
Repair centre operations	**1,444**	1,368	**1,384**	1,326
Support	**1,355**	1,278	**1,350**	1,266
Total	**10,762**	11,229	**11,122**	11,161

The aggregate remuneration of those employed by the Group's operations comprised:

	2019 £m	2018 £m
Wages and salaries[1]	**387.2**	380.9
Social security costs	**41.9**	41.2
Pension costs[1]	**25.5**	22.7
Share-based payments	**18.4**	21.0
Total	**473.0**	465.8

Notes:

1. For the year ended 31 December 2018, an amount of £6.0 million has been reclassified from pension costs to wages and salaries.

10. Finance costs

	2019 £m	2018[1] £m restated
Interest expense on subordinated liabilities	**23.1**	23.1
Net interest received on designated hedging instrument[2]	**(3.4)**	(3.8)
Unrealised losses on designated hedging instrument[2]	**0.1**	5.0
Unrealised (gains) on associated interest rate risk on hedged item[2]	**(0.8)**	(5.6)
Amortisation of arrangement costs and discount on issue of subordinated liabilities	**0.3**	0.4
Interest expense on lease liabilities	**6.7**	6.8
Total	**26.0**	25.9

Notes:

1. Results for the year ended 31 December 2018 have been restated to reflect the fully retrospective adoption of IFRS 16 'Leases', see note 23.
2. As described in note 19, on 27 April 2012 the Group issued subordinated guaranteed dated notes with a nominal value of £500 million at a fixed rate of 9.25%. On the same date, the Group also entered into a 10-year designated hedging instrument to exchange the fixed rate of interest on the notes for a floating rate of 3-month LIBOR plus a spread of 706 basis points, which increased to 707 basis points with effect from 29 July 2013. On 8 December 2017, the Group redeemed £250 million nominal value of the notes.

11. Dividends and appropriations

	2019 £m	2018 £m
Amounts recognised as distributions to equity holders in the period:		
2018 final dividend of 14.0 pence per share paid on 16 May 2019	**191.8**	–
2017 final dividend of 13.6 pence per share paid on 17 May 2018	–	186.1
2019 first interim dividend of 7.2 pence per share paid on 6 September 2019	**98.6**	–
2018 first interim dividend of 7.0 pence per share paid on 7 September 2018	–	95.8
2018 special dividend of 8.3 pence per share paid on 16 May 2019	**113.7**	–
2017 special dividend of 15.0 pence per share paid on 17 May 2018	–	205.3
	404.1	487.2
Coupon payments in respect of Tier 1 notes[1]	**16.6**	16.6
	420.7	503.8
Proposed dividends:		
2019 final dividend of 14.4 pence per share	**198.0**	–
2018 final dividend of 14.0 pence per share	–	192.5
2018 special dividend of 8.3 pence per share	–	114.1

Note:

1. Coupon payments on the Tier 1 notes issued in December 2017 are treated as an appropriation of retained profits and, accordingly, are accounted for when paid.

The proposed final dividend for 2019 have not been included as a liability in these financial statements.

The Board has also approved a share buyback of up to £150 million which it expects to complete by the end of July 2020.

The trustees of the employee share trusts waived their entitlement to dividends on shares held to meet obligations arising on the Long-Term Incentive Plan, Deferred Annual Incentive Plan and Restrictive Share Plan awards, which reduced the total dividends paid for the year ended 31 December 2019 by £1.5 million (2018: £2.4 million).

12. Earnings per share

Earnings per share is calculated by dividing earnings attributable to the owners of the Company less coupon payments in respect of Tier 1 notes by the weighted average number of Ordinary Shares during the year.

Basic

Basic earnings per share is calculated by dividing the earnings attributable to the owners of the Company less coupon payments in respect of Tier 1 notes by the weighted average number of Ordinary Shares during the period, excluding Ordinary Shares held as employee trust shares.

	2019 £m	2018[1] £m restated
Earnings attributable to owners of the Company	**419.9**	472.0
Coupon payments in respect of Tier 1 notes	**(16.6)**	(16.6)
Profit for the calculation of earnings per share	**403.3**	455.4
Weighted average number of Ordinary Shares (millions)	**1,367.2**	1,366.5
Basic earnings per share (pence)	**29.5**	33.3

12. Earnings per share continued

Diluted

Diluted earnings per share is calculated by dividing the earnings attributable to the owners of the Company less coupon payments in respect of Tier 1 notes by the weighted average number of Ordinary Shares during the period adjusted for the dilutive potential Ordinary Shares. The Company has share options and contingently issuable shares as categories of dilutive potential Ordinary Shares.

	2019 £m	2018[1] £m restated
Earnings attributable to owners of the Company	**419.9**	472.0
Coupon payments in respect of Tier 1 notes	**(16.6)**	(16.6)
Profit for the calculation of earnings per share	**403.3**	455.4
Weighted average number of Ordinary Shares (millions)	**1,367.2**	1,366.5
Effect of dilutive potential of share options and contingently issuable shares (millions)	**15.3**	15.8
Weighted average number of Ordinary Shares for the purpose of diluted earnings per share (millions)	**1,382.5**	1,382.3
Diluted earnings per share (pence)	**29.2**	32.9

Note:

1. Results for the year ended 31 December 2018 have been restated to reflect the fully retrospective adoption of IFRS 16 'Leases', see note 23.

13. Net assets per share and return on equity

Net asset value per share is calculated as total shareholders' equity (which excludes Tier 1 notes) divided by the number of Ordinary Shares at the end of the period excluding shares held by employee share trusts.

Tangible net asset value per share is calculated as total shareholders' equity less goodwill and other intangible assets divided by the number of Ordinary Shares at the end of the period excluding shares held by employee share trusts.

The table below analyses net asset and tangible net asset value per share.

At 31 December	2019 £m	2018[1] £m restated
Net assets	**2,643.6**	2,558.2
Goodwill and other intangible assets[2]	**(702.5)**	(566.8)
Tangible net assets	**1,941.1**	1,991.4
Number of Ordinary Shares (millions)	**1,375.0**	1,375.0
Shares held by employee share trusts (millions)	**(8.4)**	(10.4)
Closing number of Ordinary Shares (millions)	**1,366.6**	1,364.6
Net asset value per share (pence)	**193.4**	187.5
Tangible net asset value per share (pence)	**142.0**	145.9

Notes:

1. Results for the year ended 31 December 2018 have been restated to reflect the fully retrospective adoption of IFRS 16 'Leases', see note 23.
2. Goodwill has arisen on acquisition by the Group of subsidiary companies and on acquisition of new accident repair centres. Intangible assets are primarily comprised of software development costs.

Return on equity

The table below details the calculation of return on equity.

	2019 £m	2018[1] £m restated
Earnings attributable to owners of the Company	**419.9**	472.0
Coupon payments in respect of Tier 1 notes	**(16.6)**	(16.6)
Profit for the calculation of return on equity	**403.3**	455.4
Opening shareholders' equity	**2,558.2**	2,701.9
Closing shareholders' equity	**2,643.6**	2,558.2
Average shareholders' equity	**2,600.9**	2,630.1
Return on equity	**15.5%**	17.3%

Note:

1. Results for the year ended 31 December 2018 have been restated to reflect the fully retrospective adoption of IFRS 16 'Leases', see note 23.

14. Reinsurance assets

	Notes	2019 £m	2018 £m
Reinsurers' share of general insurance liabilities		**1,190.1**	1,159.9
Impairment provision[1]		**(40.5)**	(54.7)
Total excluding reinsurers' unearned premium reserves		**1,149.6**	1,105.2
Reinsurers' unearned premium reserve		**101.7**	103.5
Total		**1,251.3**	1,208.7

Note:

1. Impairment provision relates to reinsurance debtors, allowing for the risk that reinsurance assets may not be collected, or where the reinsurer's credit rating has been significantly downgraded and may have difficulty in meeting its obligations.

15. Financial investments

	2019 £m	2018 £m
AFS debt securities		
Corporate	**3,925.6**	3,916.0
Supranational	**31.3**	43.2
Local government	**29.2**	29.5
Sovereign	**99.5**	156.9
Total	**4,085.6**	4,145.6
Held to maturity debt securities		
Corporate	**104.0**	101.0
Total debt securities	**4,189.6**	4,246.6
Total debt securities		
Fixed interest rate[1]	**4,166.5**	4,211.1
Floating interest rate	**23.1**	35.5
Total	**4,189.6**	4,246.6
Loans and receivables		
Infrastructure debt	**278.1**	289.6
Commercial real estate loans	**205.7**	201.6
Total	**4,673.4**	4,737.8

Note:

1. The Group swaps a fixed interest rate for a floating rate of interest on its US Dollar and Euro and a small amount of its sterling corporate debt securities by entering into interest rate derivatives. The hedged amount at 31 December 2019 was £955.8 million (2018: £1,206.1 million).

16. Cash and cash equivalents and borrowings

	2019 £m	2018 £m
Cash at bank and in hand	**223.1**	157.4
Short-term deposits with credit institutions[1]	**725.5**	997.0
Cash and cash equivalents	**948.6**	1,154.4
Bank overdrafts[2]	**(52.3)**	(62.0)
Cash and bank overdrafts[3]	**896.3**	1,092.4

Notes:

1. This represents money market funds.
2. Bank overdrafts represent short-term timing differences between transactions posted in the records of the Group and transactions flowing through the accounts at the bank.
3. Cash and bank overdrafts disclosure note is included for the purposes of the consolidated cash flow statement.

The effective interest rate on short-term deposits with credit institutions for the year ended 31 December 2019 was 0.79% (2018: 0.58%) and average maturity was 10 days (2018: 10 days).

17. Share capital

	2019 Number millions	2018 Number millions	2019 £m	2018 £m
Issued and fully paid: equity shares				
Ordinary Shares of $10^{10}/_{11}$ pence each[1]	1,375	1,375	150.0	150.0

Note:

1. The shares have full voting dividend and capital distribution rights (including wind up) attached to them; these do not confer any rights of redemption.

Employee trust shares

The Group satisfies share-based payments under the Group's share plans primarily through shares purchased in the market and held by employee share trusts.

At 31 December 2019, 8,445,670 Ordinary Shares (2018: 10,432,376 Ordinary Shares) were owned by the employee share trusts with a cost of £30.2 million (2018: £35.2 million). These Ordinary Shares are carried at cost and at 31 December 2019 had a market value of £26.4 million (2018: £33.2 million).

18. Tier 1 notes

	2019 £m	2018 £m
Tier 1 notes	346.5	346.5

On 7 December 2017, the Group issued £350 million of fixed rate perpetual Tier 1 notes with a coupon rate of 4.75% per annum.

The Group has an optional redemption date of 7 December 2027. If the notes are not repaid on that date, a fixed rate of interest per annum will be reset. The notes are direct, unsecured and subordinated obligations of the issuer ranking pari passu and without any preference amongst themselves.

The Tier 1 notes are treated as a separate category within equity and the coupon payments are recognised outside of the profit after tax result and directly in shareholders' equity.

The Group has the option to cancel the coupon payment; this becomes mandatory if the Solvency Condition[1] is not met at the time of or following coupon payment, non-compliance with the SCR, non-compliance with the minimum capital requirement, where the Group has insufficient distributable reserves or where the relevant regulator requires the coupon payment to be cancelled.

Note:

1. All payments shall be conditional upon the Group being solvent at the time of payment and immediately after payment. The Issuer will be solvent if (i) it is able to pay its debts owed to senior creditors as they fall due and (ii) its assets exceed its liabilities.

19. Subordinated liabilities

	2019 £m	2018 £m
Subordinated guaranteed dated notes	259.0	259.5

The subordinated guaranteed dated notes with a nominal value of £500 million were issued on 27 April 2012 at a fixed rate of 9.25%. On the same date, the Group also entered into a 10-year designated hedging instrument to exchange the fixed rate of interest for a floating rate of 3-month LIBOR plus a spread of 706 basis points which was credit value adjusted to 707 basis points with effect from 29 July 2013.

On 8 December 2017, the Group repurchased £250 million nominal value of the subordinated guaranteed dated notes for a purchase price of £330.1 million including accrued interest of £2.7 million and associated transaction costs of £0.6 million.

The remaining notes, with a nominal value of £250 million, have a redemption date of 27 April 2042 with the option to repay the notes on 27 April 2022. If the notes are not repaid on that date, the rate of interest will be reset at a rate of the 6-month LIBOR plus 7.91%.

The Group has the option, in certain circumstances, to defer interest payments on the notes but to date has not exercised this right.

The notes are unsecured, subordinated obligations of the Group, and rank pari passu without any preference among themselves. In the event of a winding-up or of bankruptcy, they are to be repaid only after the claims of all other senior creditors have been met.

20. Insurance liabilities

	2019 £m	2018 £m
Insurance liabilities	**3,819.6**	4,005.9

Gross insurance liabilities

Accident year	2010 £m	2011 £m	2012 £m	2013 £m	2014 £m	2015 £m	2016 £m	2017 £m	2018 £m	2019 £m	Total £m
Estimate of ultimate gross claims costs:											
At end of accident year	3,941.7	2,698.1	2,372.7	2,184.0	2,094.5	2,118.1	2,157.7	2,217.3	2,300.1	2,110.4	
One year later	(117.1)	(99.3)	(163.3)	(117.6)	20.7	(30.0)	(86.7)	(116.2)	(62.3)		
Two years later	(99.1)	(94.6)	(118.9)	(153.0)	(38.4)	(143.5)	(53.3)	(103.1)			
Three years later	(50.3)	(89.3)	(49.3)	(21.0)	(144.9)	(62.4)	(82.8)				
Four years later	(105.5)	(60.9)	(9.9)	(102.1)	(50.2)	(22.9)					
Five years later	(57.7)	(21.2)	(79.2)	(50.8)	(51.6)						
Six years later	(25.9)	(60.3)	(36.2)	(27.4)							
Seven years later	(50.0)	(25.1)	(23.8)								
Eight years later	(17.6)	(27.9)									
Nine years later	(17.8)										
Current estimate of cumulative claims	3,400.7	2,219.5	1,892.1	1,712.1	1,830.1	1,859.3	1,934.9	1,998.0	2,237.8	2,110.4	
Cumulative payments to date	(3,327.6)	(2,179.5)	(1,870.8)	(1,674.9)	(1,648.1)	(1,610.1)	(1,621.3)	(1,577.8)	(1,631.1)	(1,086.6)	
Gross liability recognised in balance sheet	**73.1**	**40.0**	**21.3**	**37.2**	**182.0**	**249.2**	**313.6**	**420.2**	**606.7**	**1,023.8**	**2,967.1**
2009 and prior											**774.3**
Claims handling provision											**78.2**
Total											**3,819.6**

Net insurance liabilities

Accident year	2010 £m	2011 £m	2012 £m	2013 £m	2014 £m	2015 £m	2016 £m	2017 £m	2018 £m	2019 £m	Total £m
Estimate of ultimate net claims costs:											
At end of accident year	3,902.0	2,644.4	2,271.8	2,093.9	1,971.0	1,926.7	1,922.2	2,016.9	2,125.9	1,941.2	
One year later	(125.2)	(131.5)	(146.7)	(123.6)	(29.7)	(67.0)	(18.9)	(79.7)	(41.4)		
Two years later	(120.4)	(82.1)	(107.8)	(134.4)	(42.0)	(77.8)	(38.2)	(65.3)			
Three years later	(44.0)	(76.5)	(35.6)	(27.8)	(100.7)	(30.4)	(43.7)				
Four years later	(93.6)	(48.7)	(11.6)	(64.3)	(41.3)	(24.1)					
Five years later	(52.3)	(37.3)	(54.2)	(38.9)	(52.5)						
Six years later	(43.9)	(37.0)	(30.4)	(17.7)							
Seven years later	(24.8)	(20.4)	(14.6)								
Eight years later	(17.4)	(23.0)									
Nine years later	(17.1)										
Current estimate of cumulative claims	3,363.3	2,187.9	1,870.9	1,687.2	1,704.8	1,727.4	1,821.4	1,871.9	2,084.5	1,941.2	
Cumulative payments to date	(3,312.2)	(2,155.9)	(1,853.2)	(1,656.3)	(1,629.9)	(1,599.6)	(1,619.5)	(1,572.0)	(1,630.2)	(1,086.4)	
Net liability recognised in balance sheet	**51.1**	**32.0**	**17.7**	**30.9**	**74.9**	**127.8**	**201.9**	**299.9**	**454.3**	**854.8**	**2,145.3**
2009 and prior											**446.5**
Claims handling provision											**78.2**
Total											**2,670.0**

20. Insurance liabilities continued

Movements in gross and net insurance liabilities

	Gross £m	Reinsurance £m	Net £m
Claims reported	3,003.7	(742.5)	2,261.2
Incurred but not reported	1,142.7	(338.7)	804.0
Claims handling provision	79.3	–	79.3
At 1 January 2018	4,225.7	(1,081.2)	3,144.5
Cash paid for claims settled in the year[1] (restated)	(2,186.0)	31.1	(2,154.9)
Increase / (decrease) in liabilities:			
Arising from current-year claims[1] (restated)	2,489.7	(174.2)	2,315.5
Arising from prior-year claims	(523.5)	119.1	(404.4)
At 31 December 2018	4,005.9	(1,105.2)	2,900.7
Claims reported	3,001.0	(809.8)	2,191.2
Incurred but not reported	924.9	(295.4)	629.5
Claims handling provision	80.0	–	80.0
At 31 December 2018	4,005.9	(1,105.2)	2,900.7
Cash paid for claims settled in the year	**(2,103.6)**	**25.3**	**(2,078.3)**
Increase / (decrease) in liabilities:			
Arising from current-year claims	**2,311.3**	**(169.2)**	**2,142.1**
Arising from prior-year claims	**(394.0)**	**99.5**	**(294.5)**
At 31 December 2019	**3,819.6**	**(1,149.6)**	**2,670.0**
Claims reported	**2,916.0**	**(829.3)**	**2,086.7**
Incurred but not reported	**825.4**	**(320.3)**	**505.1**
Claims handling provision	**78.2**	**–**	**78.2**
At 31 December 2019	**3,819.6**	**(1,149.6)**	**2,670.0**

Notes:

1. Results for the year ended 31 December 2018 have been restated to reflect the fully retrospective adoption of IFRS 16 'Leases', see note 23.
2. Included within the incurred but not reported claims provision as at 31 December 2018 was a £55 million net provision decrease (£175 million gross provision decrease) for an assumed change in the Ogden discount rate from minus 0.75% to 0%.

Movement in prior-year net insurance liabilities by operating segment

	2019 £m	2018 £m
Motor	**(180.5)**	(276.3)
Home	**(41.4)**	(32.6)
Rescue and other personal lines	**(7.6)**	(16.1)
Commercial	**(65.0)**	(79.4)
Total	**(294.5)**	(404.4)

21. Unearned premium reserve

Movement in unearned premium reserve

	Gross £m	Reinsurance £m	Net £m
At 1 January 2018	1,600.3	(97.3)	1,503.0
Written in the period	3,211.9	(223.4)	2,988.5
Earned in the period	(3,306.7)	217.2	(3,089.5)
At 31 December 2018	1,505.5	(103.5)	1,402.0
Written in the period	**3,203.1**	**(215.9)**	**2,987.2**
Earned in the period	**(3,202.6)**	**217.7**	**(2,984.9)**
At 31 December 2019	**1,506.0**	**(101.7)**	**1,404.3**

22. Related parties

Transactions between the Group's subsidiary undertakings, which are related parties, have been eliminated on consolidation and accordingly are not disclosed.

Full details of the Group's related party transactions for the year ended 31 December 2018 are included on page 181 of the Annual Report & Accounts 2018.

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

Statutory accounts information
The Annual Report & Accounts 2018 were signed on 4 March 2019 and were delivered to the Registrar of Companies following the Annual General Meeting held on 9 May 2019. The Annual Report & Accounts 2018 is available at: https://www.directlinegroup.co.uk/content/dam/dlg/corporate/images-and-documents/investors/results-and-reports/2019/2019.03.20_Direct-Line-Group_Annual-Report-and-Accounts-2018.pdf.downloadasset.pdf

23. First-time adoption of IFRS 16

The Group adopted IFRS 16 for the first time on 1 January 2019 as explained in note 1 to the consolidated financial statements. As a result, lease liabilities in respect of property, motor vehicles and IT equipment are now recognised on the balance sheet, along with corresponding right-of-use assets. The impact of the adoption of the new standard on the income statement has been to replace rental expenses with a depreciation charge and a finance cost in respect of the leased assets. An element of the depreciation charge is attributed to claims handling expenses, which are included in claims costs.

The following tables reconcile the restated comparative financial statements to amounts previously presented under IAS 17:

Impact on the consolidated income statement for the year ended 31 December 2018

	31 December 2018 £m	IFRS 16 first-time adoption £m	**31 December 2018 £m restated**
Total income	**3,436.1**	**–**	**3,436.1**
Insurance claims[1]	(1,966.9)	0.7	(1,966.2)
Insurance claims recoverable from reinsurers	55.1	–	55.1
Net insurance claims	**(1,911.8)**	**0.7**	**(1,911.1)**
Commission expenses	(200.4)	–	(200.4)
Operating expenses[2]	(722.2)	4.0	(718.2)
Total expenses	**(922.6)**	**4.0**	**(918.6)**
Operating profit	**601.7**	**4.7**	**606.4**
Finance costs[3]	(19.1)	(6.8)	(25.9)
Profit before tax	**582.6**	**(2.1)**	**580.5**
Tax charge	(108.9)	0.4	(108.5)
Profit for the period attributable to owners of the Company	**473.7**	**(1.7)**	**472.0**
Earnings per share:			
Basic (pence)	**33.5**	**(0.2)**	**33.3**
Diluted (pence)	**33.1**	**(0.2)**	**32.9**

Notes:
1. In prior periods, the internal cost reallocation model reflected a portion of rental expenses relating to claims handling expense in insurance claims. Under IFRS 16 rental expenses were replaced with a lower depreciation charge in operating expenses, reducing the costs recharged to claims handling after reallocations. The prior period has been restated in respect of this to improve comparability with the current period.
2. Net operating expense impact of replacing rental expenses with a depreciation charge on right-of-use assets.
3. Interest expense recognised on unwinding of discounted lease liabilities.

Impact on the consolidated statement of comprehensive income for the year ended 31 December 2018

	31 December 2018 £m	IFRS 16 first-time adoption £m	**31 December 2018 £m restated**
Profit for the period	**473.7**	**(1.7)**	**472.0**
Other comprehensive loss net of tax	**(114.2)**	**–**	**(114.2)**
Total comprehensive income for the period attributable to owners of the Company	**359.5**	**(1.7)**	**357.8**

23. First-time adoption of IFRS 16 continued

Impact on the consolidated balance sheet as at 1 January 2018

	1 January 2018 £m	IFRS 16 first-time adoption £m	**1 January 2018 £m restated**
Assets			
Right-of-use assets	–	157.9	157.9
Deferred acquisition costs	185.4	(0.4)	185.0
Prepayments, accrued income and other assets	146.2	(3.2)	143.0
Equity			
Shareholders' equity	2,715.1	(13.2)	2,701.9
Liabilities			
Deferred tax	31.1	(2.7)	28.4
Lease liabilities	–	170.1	170.1

Impact on the consolidated balance sheet as at 31 December 2018

	31 December 2018 £m	IFRS 16 first-time adoption £m	**31 December 2018 £m restated**
Assets			
Right-of-use assets	–	153.4	153.4
Deferred acquisition costs	171.0	(0.6)	170.4
Prepayments, accrued income and other assets	128.0	(3.5)	124.5
Equity			
Shareholders' equity	2,573.1	(14.9)	2,558.2
Liabilities			
Deferred tax	7.6	(3.1)	4.5
Lease liabilities	–	167.3	167.3

Impact on the consolidated cash flow statement year ended 31 December 2018

	31 December 2018 £m	IFRS 16 first-time adoption £m	**31 December 2018 £m restated**
Net cash generated from operating activities before investment of insurance assets	4.2	19.3	23.5
Cash flows used in financing activities			
Finance costs	(19.3)	(6.8)	(26.1)
Principal elements of lease payments	–	(12.5)	(12.5)

GLOSSARY

Term	Definition and explanation
Actuarial best estimate ("ABE")	The probability-weighted average of all future claims and cost scenarios. It is calculated using historical data, actuarial methods and judgement. A best estimate of reserves will therefore normally include no margin for optimism or, conversely, caution.
Assets under management ("AUM")	This represents all assets management or administered by or on behalf of the Group, including those assets managed by third parties.
Available-for-sale ("AFS") investment	Available-for-sale investments are non-derivative financial assets that designated as such, or are not classified as loans and receivables, held to maturity, or financial assets at fair value through profit or loss.
Average written premium	The total written premium at inception divided by the number of policies.
Capital	The funds invested in the Group, including funds invested by shareholders and Tier 1 notes. In addition, subordinated loan capital in the Group's balance sheet is classified as Tier 2 capital for Solvency II purposes.
Claims frequency	The number of claims divided by the number of policies per year.
Claims handling provision (provision for losses and loss-adjustment expense)	Funds the Group sets aside to meet the estimated cost of settling claims and related expenses that the Group considers it will ultimately need to pay.
Combined operating ratio	The sum of the loss, commission and expense ratios. The ratio measures the amount of claims costs, commission and operating expenses, compared to net earned premium generated. A ratio of less than 100% indicates profitable underwriting. **Normalised combined operating ratio** adjusts loss and commission ratios for weather and changes to the Ogden discount rate. (See page 50 alternative performance measures.)
Commission expenses	Payments to brokers, partners and PCWs for generating business.
Commission ratio	The ratio of commission expense divided by net earned premium. (See page 50 alternative performance measures.)
Company	Direct Line Insurance Group plc (the "**Company**").
Current-year attritional loss ratio	The loss ratio for the current accident year, excluding the movement of claims reserves relating to previous accident years and claims relating to major weather events.(See page 50 alternative performance measures.)
Current-year combined operating ratio	This is calculated using the combined operating ratio less movement in prior-year reserves. (See page 50 alternative performance measures.)
Current-year normalised operating profit	This is calculated using the normalised operating profit adjusted for prior-year reserve movements. (See page 50 alternative performance measures.)
Direct own brands	Direct own brands include Home and Motor under the Direct Line, Churchill, Darwin and Privilege brands, Rescue under the Green Flag brand and Commercial under the Direct Line for Business and Churchill brands.
Earnings per share	The amount of the Group's profit after deduction of the Tier 1 coupon payments allocated to each Ordinary Share of the Company.
Expense ratio	The ratio of operating expenses divided by net earned premium. (See page 50 alternative performance measures.)
Finance costs	The cost of servicing the Group's external borrowings and includes the interest on ROU assets.
Financial Conduct Authority ("FCA")	The independent body responsible for regulating the UK's financial services industry.
Financial leverage ratio	Tier 1 notes and financial debt (subordinated guaranteed dated notes) as a percentage of total capital employed.
Gross written premium	The total premiums from contracts that were accepted during the period.
Group	Direct Line Insurance Group plc and its subsidiaries ("**Direct Line Group**" or the "**Group**").
Incremental borrowing rate ("IBR")	The rate of interest that a lessee would have to pay to borrow over a similar term and security, the funds necessary to obtain an asset of a similar value to the right-of-use asset in a similar economic environment.
Incurred but not reported ("IBNR")	Funds set aside to meet the cost of claims for accidents that have occurred, but have not yet been reported to the Group. This includes an element of uplift on the value of claims reported.
In-force policies	The number of policies on a given date that are active and against which the Group will pay, following a valid insurance claim.
Insurance liabilities	This comprises insurance claims reserves and claims handling provision, which the Group maintains to meet current and future claims.

Term	Definition and explanation
International Accounting Standards Board ("IASB")	A not-for-profit public interest organisation that is overseen by a monitoring board of public authorities. It develops IFRS standards that aim to make worldwide markets transparent, accountable and efficient.
Investment income yield	The income earned from the investment portfolio, recognised through the income statement during the period divided by the average assets under management ("**AUM**"). This excludes unrealised and realised gains and losses, impairments, and fair value adjustments. The average AUM derives from the period's opening and closing balances for the total Group. (See page 50 alternative performance measures.)
Investment return	The investment return earned from the investment portfolio, including unrealised and realised gains and losses, impairments and fair value adjustments.
Investment return yield	The investment return divided by the average AUM. The average AUM derives from the period's opening and closing balances. (See page 50 alternative performance measures.)
Loss ratio	Net insurance claims divided by net earned premium. (See page 50 alternative performance measures.)
Management's best estimate	These reserves are based on management's best estimate, which includes a prudence margin that exceeds the internal ABE.
Net asset value	The difference between the Group's total assets and total liabilities, calculated by subtracting total liabilities (including Tier 1 notes) from total assets.
Net earned premium	The element of gross earned premium less reinsurance premium ceded for the period where insurance cover has already been provided.
Net insurance claims	The cost of claims incurred in the period less any claims costs recovered under reinsurance contracts. It includes claims payments and movements in claims reserves.
Net investment income yield	This is calculated in the same way as investment income yield but includes the cost of hedging. (See page 50 alternative performance measures.)
Ogden discount rate	The discount rate set by the Lord Chancellor and used by courts to calculate lump sum awards in bodily injury cases.
Operating expenses	These are the expenses relating to business activities excluding restructuring and one-off costs. (See page 50 alternative performance measures.)
Operating profit	The pre-tax profit that the Group's activities generate, including insurance and investment activity, but excluding finance costs, restructuring and one-off costs. **Normalised operating profit** is operating profit adjusted for weather and changes to the Ogden discount rate. (See page 51 alternative performance measures.)
Periodic payment order ("PPO")	These are claims payments as awarded under the Courts Act 2003. PPOs are used to settle some large personal injury claims. They generally provide a lump-sum award plus inflation-linked annual payments to claimants who require long-term care.
Prudential Regulation Authority ("PRA")	The PRA is a part of the Bank of England. It is responsible for regulating and supervising insurers and financial institutions in the UK.
Reinsurance	Contractual arrangements where the Group transfers part or all of the accepted insurance risk to another insurer.
Reserves	Funds that have been set aside to meet outstanding insurance claims and IBNR claims.
Restructuring costs	These are costs incurred in respect of the business activities where the Group has a constructive obligation to restructure its activities.
Return on equity	This is calculated by dividing the profit attributable to the owners of the Company after deduction of the Tier 1 coupon payments by average shareholders' equity for the period.
Return on tangible equity ("RoTE")	This is adjusted profit after tax divided by the Group's average shareholders' equity less goodwill and other intangible assets. Profit after tax is adjusted to exclude restructuring and one-off costs and to include the Tier 1 coupon payments. It is stated after charging tax using the UK standard rate of 19% and for 2018 it is stated after charging tax using the effective income tax rate of 18.7%. (See page 51 alternative performance measures.)
Right of use ("ROU") asset	A lessee's right to use an asset over the life of a lease, calculated as the initial amount of the lease liability, plus any lease payments made to the lessor before the lease commencement date, plus any initial direct costs incurred, minus any lease incentives received.
Solvency II	The capital adequacy regime for the European insurance industry, which became effective on 1 January 2016. It establishes capital requirements and risk management standards. It comprises three pillars: Pillar I, which sets out capital requirements for an insurer; Pillar II, which focuses on systems of governance; and Pillar III, which deals with disclosure requirements.
Solvency capital ratio	The ratio of Solvency II own funds to the solvency capital requirement.

Term	Definition and explanation
Tangible equity	This shows the equity excluding Tier 1 notes and intangible assets for comparability with companies who have not acquired businesses or capitalised intangible assets. (See page 51 alternative performance measures.)
Tangible net assets per share	This shows the equity excluding Tier 1 notes and intangible assets for comparability with companies who have not acquired businesses or capitalised intangible assets. (See page 51 alternative performance measures.)
Underwriting result profit / (loss)	The profit or loss from operational activities, excluding investment return and other operating income. It is calculated as net earned premium less net insurance claims and total expenses, excluding restructing and other one-off costs.

APPENDIX A – ALTERNATIVE PERFORMANCE MEASURES

The Group has identified Alternative Performance Measures ("**APMs**") in accordance with the European Securities and Markets Authority's published Guidelines. The Group uses APMs to improve comparability of information between reporting periods and reporting segments, by adjusting for either uncontrollable or one-off costs which impact the IFRS measures, to aid the user of the Annual Report in understanding the activity taking place across the Group. These APMs are contained within the main narrative sections of this document, outside of the financial statements and notes, and may not necessarily have standardised meanings for ease of comparability across peer organisations.

Further information is presented below, defined in the glossary and reconciled to the most directly reconcilable line items in the financial statements and notes. Note 3 on page 34 of the consolidated financial statements presents a reconciliation of the Group's business activities on a segmental basis to the consolidated income statement. All note references in the table below are to the notes to the consolidated financial statements on pages 33 to 46.

Group APM	Closest equivalent IFRS measure	Definition and / or reconciliation	Rationale for APM
Combined operating ratio	Profit before tax	Combined operating ratio is defined in the glossary on page 47 and is reconciled in note 3 on page 34.	This is a measure of underwriting profitability and excludes non-insurance income, whereby a ratio of less than 100% represents an underwriting profit and a ratio of more than 100% represents an underwriting loss.
Commission ratio	Commission expense	Commission ratio is defined in the glossary on page 47 and is reconciled in note 3 on page 34.	Expresses commission expense, in relation to net earned premium.
Current-year attritional loss ratio	Net insurance claims	Current-year attritional loss ratio is defined in the glossary on page 47 and is reconciled to the loss ratio (discussed below) on page 14.	Expresses claims performance in the current accident year in relation to net earned premium.
Current-year combined operating ratio	Profit before tax	Current-year combined operating ratio is defined in the glossary on page 47 and is reconciled on page 14.	This is a measure of underwriting profitability, excluding the effect of prior-year reserve movements.
Current-year normalised operating profit ratio	Profit before tax	Current-year normalised operating profit ratio is defined in the glossary on page 47 and reconciled on page 52.	Expresses a relationship between current-year normalised operating profit and normalised operating profit.
Expense ratio	Total expenses	Expense ratio is defined in the glossary on page 47 and is reconciled in note 3 on page 34.	Expresses underwriting and policy expenses in relation to net earned premium.
Investment income yield	Investment income	Investment income yield is defined in the glossary on page 48 and is reconciled on page 51.	Expresses a relationship between the investment income and the associated opening and closing assets adjusted for portfolio hedging instruments.
Investment return yield	Investment return	Investment return yield is defined in the glossary on page 48 and is reconciled on page 51.	Expresses a relationship between the investment return and the associated opening and closing assets net of any associated liabilities.
Loss ratio	Net insurance claims	Loss ratio is defined in the glossary on page 48 and is reconciled in note 3 on page 34.	Expresses claims performance in relation to net earned premium.
Net investment income yield	Investment income	Net investment income yield is defined in the glossary on page 48 and is reconciled on page 51.	Expresses a relationship between the investment income and the associated opening and closing assets adjusted for portfolio hedging instruments.
Normalised combined operating ratio	Profit before tax	Combined operating ratio is defined in the glossary on page 47 and reconciled on page 52.	This is a measure of underwriting profitability, excluding the effects of weather, Ogden discount rate changes and restructuring and one-off costs and excluding non-insurance income, whereby a ratio of less than 100% represents an underwriting profit and a ratio of more than 100% represents an underwriting loss.
Operating expenses	Total expenses	Operating expenses are defined in the glossary on page 48 and reconciled in note 3 on page 34.	This shows the expenses relating to business activities excluding restructuring and one-off costs.

Group APM	Closest equivalent IFRS measure	Definition and / or reconciliation	Rationale for APM
Operating profit	Profit before tax	Operating profit is defined in the glossary on page 48 less restructuring and one-off costs and reconciled in note 3 on page 34.	This shows the underlying performance (before tax and excludes finance costs and restructuring and one-off costs) of the business activities.
Return on tangible equity	Return on equity	Return on tangible equity is defined in the glossary on page 48 and is reconciled on page 53.	This shows performance against a measure of equity that is more easily comparable to that of other companies.
Tangible equity	Equity	Tangible equity is defined in the glossary on page 49 and is reconciled on page 53.	This shows the equity excluding Tier 1 notes and intangible assets for comparability with companies who have not acquired businesses or capitalised intangible assets.
Tangible net assets per share	Net assets per share	Tangible net assets per share is defined in the glossary on page 49 and is reconciled in note 13.	This shows the equity excluding Tier 1 notes and intangible assets per share for comparability with companies who have not acquired businesses or capitalised intangible assets.
Underwriting profit	Profit before tax	Underwriting profit is defined in the glossary on page 49 and is reconciled in note 3 on page 34.	This shows underwriting performance calculated as net earned premium less net claims and operating expenses, excluding restructuring and one-off costs.

Investment income and return yields[1]

	Notes[2]	2019 £m	2018 £m
Investment income	5	**146.4**	159.2
Hedging to a sterling floating rate basis[3]	5	**(22.1)**	(30.8)
Net investment income		**124.3**	128.4
Net realised and unrealised gains excluding hedging		**10.3**	26.2
Investment return	5	**134.6**	154.6
Opening investment property		**322.1**	309.3
Opening financial investments		**4,737.8**	5,040.4
Opening cash and cash equivalents		**1,154.4**	1,358.6
Opening borrowings		**(62.0)**	(54.1)
Opening derivatives asset[4]		**11.8**	55.1
Opening investment holdings		**6,164.1**	6,709.3
Closing investment property		**291.7**	322.1
Closing financial investments	15	**4,673.4**	4,737.8
Closing cash and cash equivalents	16	**948.6**	1,154.4
Closing borrowings	16	**(52.3)**	(62.0)
Closing derivatives asset[4]		**81.8**	11.8
Closing investment holdings		**5,943.2**	6,164.1
Average investment holdings		**6,053.7**	6,436.7
Investment income yield		**2.4%**	2.5%
Net investment income yield		**2.1%**	2.0%
Investment return yield		**2.2%**	2.4%

Notes:

1. See glossary on page 48 for definitions.
2. See notes to the consolidated financial statements.
3. Includes net realised and unrealised gains / (losses) of derivatives in relation to AUM.
4. See footnote 1 on page 17 (Investment holdings).

Normalised combined operating ratio[1]

	Home 2019	Home 2018[2] (restated)	Commercial 2019	Commercial 2018[2] (restated)	Total 2019	Total 2018[2] (restated)
Loss ratio	**46.8%**	61.8%	**52.7%**	51.8%	**61.9%**	61.9%
Commission ratio	**9.7%**	9.4%	**18.5%**	18.9%	**7.1%**	6.5%
Expense ratio	**23.8%**	22.3%	**24.5%**	24.7%	**23.2%**	23.2%
Combined operating ratio	**80.3%**	93.5%	**95.7%**	95.4%	**92.2%**	91.6%
Effect of weather						
Loss ratio	**7.2%**	(2.1%)	**3.7%**	2.3%	**2.0%**	(0.1%)
Commission ratio	**(0.6%)**	0.2%	**–**	–	**(0.1%)**	0.0%
Combined operating ratio normalised for weather	**86.9%**	91.6%	**99.4%**	97.7%	**94.1%**	91.5%
Effect of Ogden discount rate						
Loss ratio	**–**	–	**(0.2%)**	0.8%	**(0.6%)**	1.8%
Combined operating ratio normalised for weather and Ogden discount rate	**86.9%**	91.6%	**99.2%**	98.5%	**93.5%**	93.3%

Notes:

1. See glossary on page 47 for definition.
2. Results for the year ended 31 December 2018 have been restated to reflect the fully retrospective adoption of IFRS 16 'Leases', see note 23 on pages 45 and 46.

Normalised operating profit[1]

	Total 2019 £m	Total 2018[2] £m (restated)
Operating profit	**546.9**	606.4
Effect of:		
Ogden discount rate	**16.9**	(54.8)
Normalised weather – claims	**(59.0)**	3.3
Normalised weather – profit share	**3.7**	(1.2)
Normalised operating profit	**508.5**	553.7
Prior-year adjustments		
Prior-year reserve movement	**294.5**	404.4
Ogden discount rate	**16.9**	(51.4)
Prior-year normalised operating profit	**311.4**	353.0
Current-year normalised operating profit	**197.1**	200.7
Current-year normalised operating profit ratio	**39%**	36%

Note:

1. See glossary on page 48 for definition.
2. Results for the year ended 31 December 2018 have been restated to reflect the fully retrospective adoption of IFRS 16 'Leases', see note 23 on pages 45 and 46.

Operating expenses[1]

	Note[2]	2019 £m	2018[3] £m (restated)
Operating expenses (including restructuring and one-off costs)	9	**704.9**	718.2
Less restructuring and one-off costs		**(11.2)**	–
Operating expenses		**693.7**	718.2

Note:

1. See glossary on page 48 for definition.
2. See notes to the consolidated financial statements.
3. Results for the year ended 31 December 2018 have been restated to reflect the fully retrospective adoption of IFRS 16 'Leases', see note 23 on pages 45 and 46.

Return on tangible equity[1]

	2019 £m	2018[2] £m restated
Profit before tax	**509.7**	580.5
Add back: restructuring and one-off costs	**11.2**	–
Coupon payments in respect of Tier 1 notes	**(16.6)**	(16.6)
Adjusted profit before tax	**504.3**	563.9
Tax charge	**–**	(108.5)
Tax charge (using the 2019 UK standard tax rate of 19%)	**(95.8)**	–
Adjusted profit after tax	**408.5**	455.4
Opening shareholders' equity	**2,558.2**	2,701.9
Opening goodwill and other intangible assets	**(566.8)**	(471.1)
Opening shareholders' tangible equity	**1,991.4**	2,230.8
Closing shareholders' equity	**2,643.6**	2,558.2
Closing goodwill and other intangible assets	**(702.5)**	(566.8)
Closing shareholders' tangible equity	**1,941.1**	1,991.4
Average shareholders' tangible equity[3]	**1,966.3**	2,111.1
Return on tangible equity	**20.8%**	21.6%

Notes:

1. See glossary on page 48 for definition.
2. Results for the year ended 31 December 2018 have been restated to reflect the fully retrospective adoption of IFRS 16 'Leases', see note 23 on pages 45 and 46.
3. Mean average of opening and closing balances.

ADDITIONAL INFORMATION

We confirm that to the best of our knowledge:

1. the financial statements within the Annual Report & Accounts, from which the financial information within these Preliminary Results have been extracted, are prepared in accordance with International Financial Reporting Standards as adopted by the European Union and give a true and fair view of the assets, liabilities, financial position and profit or loss of the Group and the undertakings included in the consolidation taken as a whole; and

2. the management report within these Preliminary Results includes a fair review of the development and performance of the business and the position of the Group, and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties faced by the Group.

Signed on behalf of the Board

PENNY JAMES
CHIEF EXECUTIVE OFFICER

2 March 2020

TIM HARRIS
CHIEF FINANCIAL OFFICER

2 March 2020

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