6 May 2020

DIRECT LINE INSURANCE GROUP PLC
TRADING UPDATE FOR Q1 2020[1] AND COVID-19 UPDATE

PENNY JAMES, CEO OF DIRECT LINE GROUP, COMMENTED

"In these difficult times our focus has been to support our customers, protect our people and do what we can to help the communities we serve. I am grateful to the team for their fantastic response which enabled us to move quickly to home working for almost all our people, except a limited number who are repairing cars for those with essential travel needs. We expect to incur £70 million across a range of measures to offer additional value to our customers with particular focus for those in financial difficulty, to give our people job security and to work with local authorities and charities to target funding towards those supporting the most vulnerable.

"We are a strong business with a clear strategy and operational momentum. We've traded well during Q1 and continue to make progress on our strategic transformation. Our solvency position is strong, partly as a result of the difficult decision to cancel our final dividend for 2019 and also because of our resilient business model. Acknowledging the importance of dividends to shareholders we will review our dividend position alongside our half year results and on an ongoing basis once it is possible to have a better understanding of the impact of Covid-19."

Trading summary

	Q1 2020 £m	Q1 2019[2] £m	Change
Gross written premium			
Motor	**410.9**	386.9	6.2%
Home	**137.8**	141.2	(2.4%)
Rescue and other personal lines	**108.3**	105.4	2.8%
Of which Green Flag direct	**19.7**	17.7	11.3%
Commercial	**132.6**	120.4	10.1%
Total	**789.6**	753.9	4.7%
Of which direct own brands[3]	**551.9**	522.5	5.6%
	31 Mar 2020	31 Dec 2019	Change
In-force policies	**14,696**	14,789	(0.6%)
Of which direct own brands[3]	**7,344**	7,290	0.7%

Q1 2020 trading and Covid-19 summary

- Gross written premium in Q1 2020 increased by 4.7% compared with Q1 2019, with own brands growth of 5.6%. This was driven by a positive Motor performance, up 6.2%, alongside continued growth in Green Flag of 11.3% and Commercial of 10.1%.
- During these difficult times we are committed to doing the right thing for our customers, people and society. We expect to incur around £70 million of cost in implementing a range of measures to provide peace of mind to our stakeholders. This includes supporting customers in financial difficulty, pausing all redundancies until at least the autumn and providing all NHS workers with free breakdown services.
- Assuming the Foreign and Commonwealth Office (FCO) travel restrictions remain in place until the end of September we estimate the impact of Covid-19 disruption to our Travel business will be approximately £44 million. After estimated reinsurance recoveries of around £18.5 million, we expect the net impact to be approximately £25 million in excess of the normal level of claims.
- In Motor, Covid-19 restrictions have led to a reduction in claims notifications of approximately 70% during April, with average severity expected to increase as average repair durations lengthen and credit hire costs increase. We will continue to track these trends closely as we start to exit from the most severe lockdown restrictions.
- We successfully moved all office-based colleagues to remote working. Our repair centres are still open, operating with much reduced staffing to repair cars for those with essential travel needs such as key workers.
- We also maintained our focus on the transformation agenda, with Darwin going live on Confused.com, the launch of Van and Tradesperson on the Direct Line for Business (DL4B) platform and the start of roll-out for a new Rescue claims system.
- Our estimated solvency capital ratio at 31 March 2020 was 174% increasing to an estimated 177% on 1 May 2020, towards the top of our 140% to 180% risk appetite range. In recognition of the regulatory guidance and heightened uncertainty in the macroeconomic environment, on 8 April the Board announced that it would no longer be recommending the final dividend for the year ended 31 December 2019. We intend to review the dividend position alongside the half year results and then on an ongoing basis once it is possible to have a better understanding of the impacts of Covid-19.
- Subject to uncertainties arising from Covid-19, we reiterate our targets of achieving a combined operating ratio in the range of 93% to 95% normalised for weather in 2020, improving our operating expense ratio to 20% by 2023 and our long-term target of achieving at least a 15% return on tangible equity per annum.

Business Update

Covid-19 response

- Our focus for the last few weeks has been on supporting our customers and protecting our people while making a difference in the wider community and we've implemented initiatives across the business at an expected cost of in the region of £70 million.

Customers:

- Recognising that our customers' individual circumstances have changed we are offering greater flexibility to provide additional value during this period. For example, we are refunding premiums to motor customers who wish to reduce their annual mileage or cancel foreign use and refunding travel customers with multi-trip policies on a pro-rata basis.
- We are also providing additional measures for those in financial difficulty by waiving cancellation fees if people have lost their job or seen reduced hours and offering payment deferrals.
- In recognition of the commitment of all NHS workers, we are providing free Green Flag rescue cover. In addition, for our NHS customers we are offering free home emergencies cover and personal protection cover together with a fast track claims system.
- Green Flag continues to help customers with essential travel needs to stay mobile, refunding premiums to customers reducing their cover in line with reduced driving habits as well as free cancellations due to financial hardship.
- Our network of 22 owned accident repair centres continues to repair cars to help those providing essential services to the country such as key workers, or those reliant on their car to buy food or seek medical assistance.
- We have also increased the period we offer full cover on commercial premises that are unoccupied due to the lockdown, from 20/30 days to 90 days.

People:

- We quickly moved to home working, including frontline colleagues, guaranteeing colleagues their usual pay regardless of whether their specific working practices changed whilst working from home. All roles are to be protected through to the autumn.
- We are not accessing the UK Government furlough or other support schemes.

Society:

- We have implemented a range of measures to support our local communities.
- Colleagues have been given the flexibility to volunteer for the NHS and support their Covid-19 community support groups.
- We have committed £7.1 million to charity, including £3.5 million to a DLG community fund which has been established to support vulnerable people in the communities in which we are based.
- We are supporting suppliers through accelerating payments and in Rescue directly supporting small-to-medium sized enterprises (SME) roadside assistance firms.

Motor

- Motor gross written premiums grew by 6.2% compared with Q1 2019 as the positive trading conditions in H2 2019 continued. In-force policies were stable compared to the end of 2019, supported by strong retention. Claims inflation was in line within our 3% to 5% long-term expectations.
- Following the implementation of Covid-19 restrictions, Motor trading has seen fewer new business customers in the market following a slowdown in car transactions and the temporary suspension of phone sales from 25 March until 16 April to support operational resilience. Retention has remained strong.
- We have experienced a reduction in Motor claims notifications of around 70% in April compared to the same period in 2019. This reduction in claims costs is expected to be partially offset by increased claims severity as average repair durations lengthen and credit hire costs increase.
- We will continue to track these trends closely as we start to exit from the most severe lockdown restrictions and we are already seeing a modest increase in miles driven in early May compared to April.

Home

- Home gross written premium was 2.4% lower than Q1 2019, while own brands premium was broadly stable, and partnership premium lower due to the continued run-off of some accounts. Home continued to see improvement in escape of water (EoW) claims following the actions taken some time ago. Claims associated with storms Ciara and Dennis are estimated at £18 million net of Flood Re recoveries.
- Since the implementation of Covid-19 restrictions, Home has experienced lower new business volumes due to reduced customer shopping for policies alongside the temporary suspension of phone sales from 25 March until 16 April to support operational resilience. This has been partially offset by improved retention. While it is too early to estimate the impact of Covid-19 on Home claims, we have seen an initial reduction in claims frequency although it is not clear whether this reduction, at least in part, is genuine or due to delays in claims reporting.

Rescue

- Rescue and other personal lines increased premiums by 2.8% driven by the strong growth in Green Flag of 11.3%.
- Following the Covid-19 restrictions, Rescue has experienced a material reduction in new business volumes due to less customer shopping alongside the suspension of phone sales from 27 March until 9 April to support operational resilience. Rescue has seen a reduction in claims notifications of around 40% but has also begun to see an increase in call outs in early May compared to April.

Travel

- Assuming the Foreign and Commonwealth Office (FCO) travel restrictions remain in place until the end of September, we estimate the net impact on Travel from the Covid-19 disruption will be approximately £25 million in excess of the normal level of claims.
- These estimates assume customers will continue to seek refunds or redress from airlines, tour operators and credit card providers where possible.

Commercial

- Commercial grew premiums by 10.1%, reflecting strong growth across Direct Line for Business (DL4B), Churchill for Business and NIG. Weather losses from storms Ciara and Dennis are estimated at £13 million.
- We provide Business Interruption (BI) cover to our SME customers across NIG and DL4B. Our standard business interruption policy wordings, on which over 99.5% of policies are written, provide cover only for certain specified diseases and do not provide cover for losses due to the Covid-19 pandemic.
- For those policies not on our standard wordings, we estimate claims costs of approximately £10 million.

Investments

- Our investment portfolio remains high quality and well diversified. Widening of credit spreads has impacted our available-for-sale (AFS) asset valuations. As at 31 March 2020 the AFS reserve was £(138) million net of tax, having moved in line with disclosed sensitivities. Since the end of Q1 2020, credit spreads have tightened and at 1 May 2020 the AFS reserve was approximately £(55) million, net of tax.
- At 31 March 2020 we held £3,814 million of debt securities with £3,436 million of these investment grade quality. The residual £378 million of debt securities were high yield debt securities with a benchmark duration of 2.5 years, less than 10% of which are exposed to sectors most impacted by Covid-19[4].
- Our liquidity remains strong with around 19% of our investment portfolio at 31 March 2020 held in cash and cash equivalents.
- Falling interest rates mean that we now expect net investment income yield to be approximately 1.8% in 2020, compared with 2.0% expected at 2019 year-end.

Capital

- Notwithstanding our strong capital position, in recognition of the regulatory guidance and heightened uncertainty in the macroeconomic environment, on 8 April the Board announced that it would no longer be recommending the final dividend for the year ended 31 December 2019.
- The Board reiterates that it will review this position alongside the half year results and on an ongoing basis once it is possible to have a better understanding of the impacts of Covid-19.
- Our estimated solvency capital ratio at 31 March 2020 was 174%, increasing to an estimated 177% on 1 May 2020, towards the top of our 140% to 180% risk appetite range.

Transformation update

- We remain as focused as ever on our technology transformation. Whilst inevitably there has been some slow down in delivery as internal and supplier resources have been reprioritised onto Covid-19 related activity and have been adjusting to home working, we continue to make good progress against the 2020 plans set out at the full year 2019 results.
- DL4B has rolled out Van and Tradesperson products on its new platform, Darwin has gone live on Confused.com, Green Flag has begun to deploy its new fully automated claims system while we have continued to make progress towards the roll out of Churchill and Direct Line on the new Motor platform.

Executive remuneration

- Given the continuing uncertainty resulting from Covid-19, the Group has agreed that Executive Directors will not be considered for any bonus for 2020 until dividends for ordinary shareholders resume. In addition, Penny James has chosen to donate her 2020 salary increase to the charity Fareshare.

Outlook

- Our business remains strong and we remain focused on our transformation and cost reduction plans as key drivers for our future commercial success.
- For 2020, we reiterate our target of a combined operating ratio of 93% to 95% normalised for weather and anticipate our restructuring costs of £60m over 2019 and 2020 will be incurred in full as we strive to maximise the opportunity for operational efficiencies.
- We remain focused on a targeted combined operating ratio of 93% to 95% normalised for weather in 2021 and over the medium term, and on improving the current-year contribution to operating profit to at least 50% by 2021, but acknowledge these will inevitably depend on the duration and uncertainties of the Covid-19 pandemic, and the pace of economic recovery and consequential impact on customer behaviour.
- We expect some impact to the timing of our cost saving programme due to the actions we are taking in the face of Covid-19, including limited delays in the delivery of certain programmes, so we may not achieve the target of reducing operating expenses by £50 million by 2021.
- Notwithstanding these challenges, we remain focused on the strategic and operational transformation of the business, including our target of improving our operating expense ratio to 20% by 2023. We also reiterate our target of achieving at least a 15% return on tangible equity per annum over the long term.
- We continue to closely monitor the impacts and uncertainties arising out of the Covid-19 pandemic and will update further with our 2020 half year results.

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Notes:

1. Direct Line Group's Trading Update relates to the three months ended 31 March 2020 and contains information to the date of publication.
2. 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.
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. High yield debt securities by sector: energy (1.7%), automotive (1.0%), restaurants (0.7%), retailers (1.5%), leisure (1.6%), transportation services (1.3%), airlines (0%), lodging (0%).

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 direct and indirect impacts and implications of the coronavirus Covid-19 on the economy, nationally and internationally, and on the Group, its operations and prospects;
- 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 and bodies (including changes related to capital and solvency requirements or the Ogden discount rate or rates or in response to the Covid-19 pandemic and its impact on the economy and customers);
- 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 and of court, arbitration, regulatory or ombudsman decisions (including in connection with Covid-19) in the jurisdictions in which the Group and its affiliates operate.

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