

Delivering sustainable returns



In 2018, the Group delivered profit before tax of £582.6 million (2017: £539.0 million). The Group's diversified product and channel portfolio, disciplined underwriting and our engaged employees have helped us to achieve this commendable result.

Governance highlights

Leadership

Your Board seeks to ensure that decisions are of the highest standard. It challenges strategic proposals, performance delivery and management responsibilities.

 See page 66


Effectiveness

The effectiveness of your Board's and its Committees' performance is considered annually in an effectiveness review.

 See page 70

Accountability

Your Board provides shareholders with an assessment of the Group's position and prospects. We monitor and review the effectiveness of the Group's risk management and internal control systems.

 See page 74

Remuneration

Your Remuneration Committee ensures a close correlation between creating value for shareholders, and remunerating Executive Directors and senior executives appropriately.

 See pages 75 and 88

Relations with shareholders and stakeholders

Your Board maintains strong relationships and regular interaction with shareholders. Their continued support for the strategic aims is important. Your Board also has regard to the interests of other stakeholders.

 See pages 66 and 75

CEO succession

Following a rigorous search process, the Group was delighted to announce, on 26 February 2019, that Penny James, Chief Financial Officer (“CFO”) had been selected to succeed Paul Geddes as Chief Executive Officer (“CEO”) with effect from the conclusion of the Annual General Meeting (“AGM”) on 9 May 2019. Paul will step down as a member of the Board and will leave the Group at the end of July 2019.

Penny joined the Board on 1 November 2017 and succeeded John Reizenstein as CFO on 1 March 2018. Penny’s deep understanding of our sector, combined with outstanding leadership skills, financial and risk expertise and deep strategic thinking, gives the Board confidence that Penny is ideally suited to leading the delivery of the Group’s short-term strategic imperatives, including technological and business transformation, and the development of the next stage of our strategy.

This year marks the 10th anniversary of Paul’s appointment as CEO. In that time Paul has made a huge contribution to the Group and the Company is deeply indebted to him for his strong leadership. During his tenure, Paul has been leading the management team which successfully separated the business from the Royal Bank of Scotland Group, floated it on the London Stock Exchange and turned it into a successful FTSE 100 company. The Board thanks Paul for his enormous contribution and wishes him well for the future.

Strategy

The Group aims to make insurance much easier and better value for our customers. The Board supports and challenges the Group’s management to develop and execute a strategy which is aligned to this aim. Our strategy looks to position us as a multi-brand, multi-product and multi-channel business, to enable us to meet our customers’ needs now and in the future, regardless of their channel preference.

Supporting this strategy is a substantial and ongoing change and investment agenda. We look to continue to invest in our direct offering, as we believe it enables us to deliver the best value for our customers and our shareholders, through our differentiated brands and propositions and simple customer journeys. Our investments in technology and digitisation are intended to improve competitiveness, agility and efficiency. This also supports our ambition to grow our profitable share of the price comparison websites market, particularly by moving us towards best-in-class pricing. By leveraging our manufacturing strengths and investments in digital capabilities, we are continuing to support our aim of winning new partnerships.

Dividends and capital management

The Group’s solvency capital ratio prior to all proposed dividends was 194%, resulting from good capital generation from the business and lower capital requirements due in part to increasing the level of reinsurance purchased by the Group in recent years. This was partially offset by higher unrealised mark

to market losses due to credit spread widening and continued capital expenditure as the Group invests with the aim of improving its capabilities and efficiency.

The Group aims to grow the dividend in line with business growth. Accordingly, the Board has recommended a final dividend of 14.0 pence per share (2017: 13.6 pence), an increase of 0.4 pence per share. If approved, the total regular dividend of 21.0 pence per share will represent 2.9% growth on 2017’s regular dividend (20.4 pence per share). This reflects the Board’s continued confidence in the Group’s earnings and the progress the business continued to make.

The Board also resolved to pay a special interim dividend of 8.3 pence per share. After both dividends, the solvency capital ratio will be 170% as at 31 December 2018¹.

The Board has taken into account the high level of political and economic uncertainty, including in relation to the UK’s exit from the EU (“Brexit”) and considers it appropriate for the time being to maintain a prudent solvency capital ratio towards the upper end of the solvency capital ratio risk appetite range of 140% to 180%. The Board will keep this position under review as it monitors developments in the political and economic environment. In normal circumstances, the Board expects the Group to operate around the middle of its solvency capital ratio risk appetite range.

Brexit

Brexit, when the UK is due to leave the EU, is scheduled to take place on 29 March 2019. Although the Group is predominantly a UK business, it does, for example, have exposure to financial markets and it imports goods and services in order to fulfil insurance claims, including from the EU. The Group has been monitoring events carefully and 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 Brexit the Group will not be immune. We have more information on this in the Risk section, on page 48.

ESG practices

The Board subscribes to the principle that a business model that is sustainable in the long term will be better able to drive value for its shareholders and other stakeholders, contributing to the development of a sustainable economy. The Group has strong values and is customer focused to ensure it is continuing to meet customer needs. The Board is proud of the high level engagement of its people, whose wellbeing is one of the pillars in our approach to ESG, reflected in our support for Mind and the Scottish Association for Mental Health as well as numerous wellbeing initiatives across the Group. Our investment portfolio has started to be weighted towards ‘green bonds’ and investments which attract higher ESG ratings. Each of our UK offices seeks to act constructively with the local community and we encourage our people to allocate at least a day each year out of their working lives to support charitable or community initiatives. Our people donated nearly 4,800 hours of company time to volunteer within their communities during 2018.

Note:

1. Further information can be found on page 32.

Linking remuneration to performance

We remain committed to ensuring that executive pay is aligned with the Company's strategy of targeting sustainable shareholder and customer value. This is primarily achieved by the Annual Incentive Plan ("AIP") and Long Term Incentive Plan ("LTIP") being aligned to performance measures shareholders consider important. This is underpinned by the delivery of a significant proportion of remuneration through shares and shareholding requirements.

The Group achieved a return on tangible equity ("RoTE") of 21.5% for 2018. A decrease of 16.5% (2017: an increase of 3.3%) in the share price over the year to 318.7 pence (2017: 381.7 pence) at 31 December 2018, together with dividend payments, provided a total shareholder return ("TSR") of minus 7.7% for the year (2017: 8.1%). This compares favourably to the FTSE 350 which had an overall return of minus 9.5% at 31 December 2018 as financial markets reacted to global trade tensions and Brexit. Over the past five years, shareholders have received a TSR of 87% compared to the FTSE 350 (excluding investment trusts) of 22%. The Group has continued to deliver good results each year, which has enabled the Board to declare cumulative dividends, including special dividends, equivalent to approximately 106% of the Initial Public Offering ("IPO") share price. More information on the Group's remuneration policy and share awards are disclosed in the Directors' remuneration report on pages 88 – 117.

IT infrastructure

The Board continues to provide oversight of the ambitious programme of activity to upgrade and better integrate the major IT systems within the Group's technology infrastructure, aimed at improving the Group's digital offering, customer experience and operational efficiency. Good progress has been made in this area and 2019 is set to be an important year for the Group in terms of the delivery of the new platform.

Customer, culture and conduct

Meeting the needs of our customers is central to the Group's strategy and sustainability. The Board recognises that opportunities will arise to improve further the services offered to customers, and along with its investment in IT capability to improve the efficiency and effectiveness of the business, it has also encouraged a range of customer experience initiatives which are designed to deliver increased levels of customer satisfaction.

The Group maintains active relationships with its insurance regulators through constructive dialogue. The Board promotes an open and collaborative culture, and provides oversight of the Group's conduct with customers. It oversees the Group's culture and the conduct policy, which aims to ensure that fair customer outcomes are achieved and that employees behave with integrity. The Group also has an Employee Code of Conduct which sets out standards to which our employees are required to adhere.

Board and Committee membership changes

Further to the announcement of the new CEO you will recall from my statement last year that John Reizenstein and Andrew Palmer stepped down from the Board at the conclusion of the AGM in May 2018.

Three Non-Executive Directors ("NEDs") joined the Board in 2018: Mark Gregory and Gregor Stewart were appointed on 1 March; and Fiona McBain joined us on 1 September. The Board is already benefiting from their skills and experiences.

Clare Thompson, independent NED, has decided to step down from the Board at the conclusion of the 2019 AGM. Having served as a Director since 2012, Clare has made an immense contribution to the Group. Her experience and wisdom have been invaluable in helping the Board and senior management to deliver excellent results for shareholders and customers. She leaves the Board with our thanks and best wishes for the future.

The Chairs of three Board Committees also changed during 2018. Gregor and Mark were appointed as Chair of the Audit Committee and Investment Committee respectively replacing Andrew Palmer. Danuta Gray also replaced Clare Thompson as Chair of the Remuneration Committee.

I would like to thank each member of the Board for their significant contribution, commitment and service, and look forward to working with them in 2019 as the Group continues to strive to build on its success to date.

Employees

The Group's employees are fundamental to the Group's success and sustainability and to ensuring a high level of service to our customers. I would like to thank each of them for their hard work, initiative and commitment to our mission. Their positive energy, embodiment of the Group's values and unwavering dedication to our customers have helped our businesses progress over the successful years since the IPO, and have put us in a strong position for the future.



MICHAEL N BIGGS
CHAIRMAN