Half Year Report for Direct Line Insurance Group plc
Results for the first half of 2014

1 August 2014

Direct Line Group's Half Year Report relates to the six months ended 30 June 2014 and contains information to the date of publication.

Financial highlights

- Gross written premium for ongoing operations[1] decreased by 5.1% in the first half of 2014 reflecting disciplined underwriting in competitive markets. Motor prices reduced on average by 2% during the second quarter compared with the same period in 2013
- Operating profit from ongoing operations[1] of £249.1 million for the first half of 2014, down 13.1% (first half 2013: £286.6 million) reflecting higher weather claims and lower prior-year reserve releases of £218.0 million (first half 2013: £239.2 million); total Group profit before tax of £225.1 million up 7.8% (first half 2013: £208.8 million)
- Combined operating ratio[2] for ongoing operations[1] of 96.6% for the first half of 2014, an increase of 2.0 percentage points (first half 2013: 94.6%) reflecting higher weather claims. Current-year attritional loss ratio of 71.8% (first half 2013: 73.8%)
- Return on tangible equity[3] from ongoing operations[1] of 15.8% for the first half of 2014 (first half 2013: 17.3%)
- Interim dividend per share of 4.4 pence representing growth of 4.8% over 2013 interim dividend, and a special interim dividend per share of 10.0 pence taking total interim dividends to 14.4 pence per share

Strategic and operational highlights

- Improvement in personal lines trading capability through new smartphone and tablet optimised websites for Motor, delivery of a number of pricing projects and implementation of further claims initiatives
- Development of telematics with launch of self-install proposition in Motor and extension to Commercial
- On track to achieve total cost base[4] target of approximately £1,000 million in 2014 with 5.4% reduction in the first half of 2014 to £496.0 million (first half 2013: £524.1 million). Restructuring and other one-off costs reduced by approximately 60% compared with the first half in 2013
- Strategic review of International, with potential disposal being explored
- Reiterate 2014 aim to achieve a combined operating ratio in the range of 95% to 97% for ongoing operations, assuming a normal level of weather claims

Paul Geddes, CEO of Direct Line Group, commented

"We delivered good results in the first half of 2014, despite major weather events and competitive markets, by maintaining our disciplined underwriting approach and from the continued delivery of our strategic initiatives. This continued performance and our strong capital position have enabled us to declare a special interim dividend of 10 pence per share as well as increase the regular interim dividend by 5%.

"Our performance has also allowed us to continue to invest in the future of our business, to enhance our product propositions and improve our customer experience. We have rolled out self-install telematics boxes, which will enable us to reward better driving, and we've made it easier to buy our Motor products on smartphones and tablets."

Notes:
See page 2

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Notes:

1. Ongoing operations include Direct Line Group's (the "**Group**") ongoing segments: Motor, Home, Rescue and other personal lines, Commercial and International. It excludes the Run-off segment and Restructuring and other one-off costs.
2. Combined operating ratio ("**COR**") is the sum of the loss, commission and expense ratios. The ratio is a measure of the amount of claims costs, commission and expenses compared to net earned premium generated.
3. Return on tangible equity ("**RoTE**") is annualised adjusted profit after tax from ongoing operations divided by the Group's average tangible shareholders' equity. Profit after tax is adjusted to exclude the Run-off segment and Restructuring and other one-off costs and is stated after charging tax (using the UK standard tax rate of 21.5%; 2013: 23.25%).
4. Operating expenses and claims handling expenses from ongoing operations, excluding the Run-off segment and Restructuring and other one-off costs.

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", "anticipates", "believes", "continue", "could", "estimates", "expects", "guidance", "intends", "may", "outlook", "plans", "predicts", "projects", "seeks", "should", "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 a number of 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: return on tangible equity, the Group's combined operating ratio, the combined operating ratio for the Group's Commercial division, and cost savings. By their nature, all forward-looking statements involve risk and uncertainties because they relate to events and depend on circumstances that may or may not occur in the future or are beyond the Group's control.

Forward-looking statements are not guarantees of 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, UK domestic and global economic business conditions, 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), the impact of competition, currency changes, inflation and deflation, the timing impact and other uncertainties of future acquisitions, disposals, joint ventures or combinations within relevant industries, as well as the impact of tax and other legislation and other regulation in the jurisdictions in which the Group and its affiliates operate. In addition, even if the Group's actual results of operations, financial condition and the development of the business sector in which the Group operates are consistent with the forward-looking statements contained in this document, those results or developments may not be indicative of results or developments in subsequent periods.

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

Financial summary

	H1 2014 £m	H1 2013 £m
Ongoing operations[1]:		
Gross written premium	**1,874.8**	1,975.9
Net earned premium	**1,674.4**	1,772.3
Underwriting profit	**56.4**	95.9
Instalment and other operating income	**76.2**	93.2
Investment return	**116.5**	97.5
Operating profit – ongoing operations	**249.1**	286.6
Run-off segment	**20.4**	10.6
Restructuring and other one-off costs	**(28.0)**	(69.9)
Operating profit	**241.5**	227.3
Finance costs	**(18.7)**	(18.5)
Gain on disposal of subsidiary	**2.3**	-
Profit before tax	**225.1**	208.8
Tax	**(49.5)**	(57.0)
Profit after tax	**175.6**	151.8
Of which ongoing operations[2]	**180.9**	205.8
Key metrics – ongoing operations[1]		
Loss ratio	**62.6%**	60.3%
Commission ratio	**11.5%**	11.3%
Expense ratio	**22.5%**	23.0%
Combined operating ratio	**96.6%**	94.6%
Earnings per share – adjusted[3] (pence)	**12.0**	13.7
Return on tangible equity[4] (annualised)	**15.8%**	17.3%
Key metrics – total Group		
Investment income yield	**2.3%**	2.0%
Investment return	**2.8%**	2.3%
Earnings per share – basic and diluted (pence)	**11.7**	10.1
Return on equity (annualised)	**12.6%**	10.8%

		As at	
	30 Jun 2014	31 Dec 2013	30 Jun 2013
Net asset value per share (pence)	**187.0**	186.6	186.9
Tangible net asset per share (pence)	**153.5**	153.2	156.6

Notes:
1. See note 1 on page 2
2. See note 1 on page 2, adjusted for finance costs and stated after charging tax (using the standard tax rate of 21.5%; 2013: 23.25%)
3. Adjusted earnings per share (diluted) excludes the Run-off segment and Restructuring and other one-off costs (using UK standard tax rate)
4. See note 3 on page 2

Business update

Overview

Direct Line Group (the "**Group**") continued to make progress in the first half of 2014 on its strategic priorities and towards its financial targets, while maintaining its disciplined approach to underwriting in a competitive marketplace.

Ongoing operating profit fell by 13.1% to £249.1 million (first half 2013: £286.6 million) as a result of major weather claims and lower prior-year reserve releases in the first half of 2014 with the COR for ongoing operations increasing by 2.0 percentage points to 96.6% (first half 2013: 94.6%). This reduction in underwriting profit together with lower instalment and other income was partially offset by a higher investment return.

Total Group profit before tax was £225.1 million (first half 2013: £208.8 million) an increase of 7.8%. This benefited from lower Restructuring and other one-off costs of £28.0 million (first half 2013: £69.9 million) and increased profit from the Run-off segment of £20.4 million (first half 2013: £10.6 million).

On a segmental basis, operating profit improved in Motor, Rescue and other personal lines and Commercial. The operating profit fell in the Home division due to claims from UK major weather events relating to the flooding in January and February 2014 of approximately £64 million (first half 2013: nil). The International operating profit was broadly stable in local currency terms.

During the first half of 2014, the Group has continued to make good progress in advancing its principal strategic priorities. The key developments were:

Distribution – In April, the Group launched its self-install telematics proposition in the UK following a successful pilot. This supports the Group's strategic aim of being a leading operator in developing the telematics market and enables it to offer telematics to a broader range of customers. Take-up remains strong for Direct Line new policies with one in five under 25 year olds electing for telematics, with take-up increasing to more than 50% for new business sales to under 21 year olds over the phone. In addition, the roll out of new smartphone and tablet optimised customer websites for Motor is now complete. The number of customers starting a quote and completing a sale on the new websites has increased significantly by 18%. The Group continues to invest in improving its systems to enhance the customer experience.

Pricing – The Group continued to progress its 30 projects in pricing this year and is approximately half-way through delivering these initiatives. These initiatives cover both Motor and Home pricing and span technical pricing, margin pricing and initiatives to reduce application fraud. These improved capabilities build on the large data assets of the Group and target improved performance, especially in the price comparison website ("**PCW**") channel. In addition, the Group continued to improve its pricing sophistication for renewing telematics policies and announced an equity investment in The Floow, the supplier of smartphone applications and telematics data analytics for the Direct Line DrivePlus telematics product range.

Claims – Initiatives included the roll out of a new service to enable faster visits to customers and the capture of evidence via smartphones for Home claims assessment. The Group is also looking at initiatives to enable customers to provide video and photographic evidence directly to help the assessment of claims. In March, DLG Legal Services started providing legal help and advice following an accident or dispute to the Group's Motor and Home customers, broadening the range of services directly offered to the Group's customers.

Costs – The Group continued to progress its initiatives in relation to business transformation and cost savings, particularly in the head office functions. These initiatives have improved efficiency and are aimed at reducing complexity. In addition, the Group continued to roll out its new data centres in conjunction with Capgemini and new voice and desktop tools as part of the IT migration from Royal Bank of Scotland Group ("**RBS Group**") infrastructure. The total cost base for the first half of 2014 was 5.4% lower than the first half of 2013 as the benefits from these initiatives began to emerge. Restructuring and other one-off costs also fell to £28.0 million (first half 2013: £69.9 million) as up-front costs associated with the Group's cost savings programmes reduced.

Commercial and International – Within Commercial, the division continued to benefit from previous investment with eTrade gross written premium up 13.0% and Direct Line for Business gross written premium (excluding Commercial Van) up 13.7%. The commercial van market, similar to the UK motor market, was highly competitive in the first half of 2014. Additional digital functionality has been added to the Direct Line for Business customer websites during the period and further eTrade initiatives are planned. A new Churchill Van product for small and medium-sized enterprise customers was launched, which allows Churchill to extend its distribution to PCWs. Furthermore, the Commercial division is piloting telematics propositions with Direct Line for Business and NIG customers. The COR, normalised for weather and large losses, in the first half of 2014 was approximately 101% placing the division on track to meet its 2014 target of less than 100%.

The International division has implemented a number of new initiatives which aim to speed up the customer quote process and make use of newly available industry data to reduce fraud. Alongside this, the division has continued to optimise its PCW distribution channel strategy and has launched a new web-only brand and proposition. Gross written premium for Germany in local currency increased by 13.3%, reflecting the expansion of the Group's share of business incepting on 1 January 2014 and the continued growth of business during the rest of the period. To improve efficiency and reduce costs, the number of operational sites in Italy is planned to be consolidated and a new customer contact centre launched.

During the first half of 2014 the Group initiated a strategic review of its International division, comprising its Italian and German operations. While the review confirmed the International division's strong market positions and the potential of the direct channel to grow in these markets, the Group decided to explore a potential disposal of these operations. Discussions are taking place with a number of parties, but at this stage there is no certainty that a disposal will occur.

UK motor and home trading

The UK motor and home markets were highly competitive during the first half of 2014 with further market premium deflation across the period. In the motor market, the second quarter of 2014 did see a period of relative stabilisation following significant market price reductions in the first quarter; however, it is too early to say whether this stabilisation marks an inflection point in the market or will be followed by further market price reductions. In the home market, the Group continued its focus on maintaining its underwriting discipline in an increasingly competitive market.

In the Motor division, gross written premium for the first half of 2014 fell by 9.0%, in comparison to the same period last year, as the Group balanced underwriting margins and volumes and only reduced prices where claims data was supportive.

Motor – effect on premium income of changes in price and risk mix[1]

Change versus same quarter in previous year	**Q2 2014**	Q1 2014	Q4 2013	Q3 2013
Change in price	**-2%**	-4%	-4%	-5%
Change in risk mix	**-2%**	-2%	-3%	-2%

Overall the Group reduced Motor prices on average by 2% during the second quarter of 2014 compared with the second quarter of 2013. This reduction was supported by positive claims trends and technical pricing initiatives. Claims trends benefited from the Group's claims transformation programme, but also recognised the positive effect of recent legal reforms.

Overall in-force policies for Motor fell by 0.7% in the second quarter and by 3.6% over the last year. Risk mix reduced by 2% in the second quarter of the year, broadly consistent with the movement over the previous three quarters.

In Home, gross written premium reduced by 5.0% while in-force policies were 3.4% lower in the first half of 2014 reflecting an increasingly competitive market. The Group continued to invest in claims transformation and pricing programmes.

Note:
1. The price and risk mix changes reflect the estimated movement based on risk models used in that period.

Regulatory update
The Group has continued to operate within a highly dynamic and evolving regulatory landscape, particularly in the UK motor insurance market where a number of reviews and initiatives have been announced by the UK Government, the Ministry of Justice ("**MoJ**"), the Financial Conduct Authority ("**FCA**"), and the Competition and Markets Authority (previously the Competition Commission).

During the first half, the FCA published its review of add-on products as well as its business plan for 2014 and 2015. Furthermore, the Competition and Markets Authority released its provisional report on the private motor insurance market. The Group will continue to support proportionate reforms which result in a level playing field across the industry.

Dividends and capital management
The Board has declared an interim dividend for Direct Line Insurance Group plc (the "**Company**") for 2014 of £66.0 million which is 4.4 pence per share, representing an increase of 4.8% on the interim dividend for 2013 and is in line with its policy to increase dividends annually in real terms.

The Board has also declared a special interim dividend of 10.0 pence per share amounting to £150.0 million. This return of capital is consistent with the Group's policy to distribute excess capital. Both the regular and special interim dividends will be paid on 12 September 2014 to shareholders on the register on 15 August 2014. The ex dividend date will be 13 August 2014.

After adjusting for the regular and special interim dividends, the Group's capital position remains strong at 30 June 2014 with an estimated risk-based capital coverage ratio of 148.8% (31 December 2013: 148.7%).

The Board constantly reviews the level of capital held by the Group and currently believes that it is appropriate to maintain capital at the upper end of its target risk-based capital coverage range of 125% to 150%. This assessment has been made after taking into account a number of factors including the route to Solvency II implementation, continued competitive market conditions and the Group's ongoing investments in its transformation plan. The Board will continue to review this position.

Outlook
For 2014, the Group reiterates its previously announced aim to achieve a combined operating ratio in the range of 95% to 97% for ongoing operations, assuming a normal level of claims from weather events, and a combined operating ratio of less than 100% for its Commercial division, assuming a normal level of claims from weather-related events and large losses.

The Group continues to target a total cost base[1] of approximately £1,000 million in 2014.

Note:
1. See note 4 on page 2

Finance review

During the first half of 2014 the Group continued to make good progress in line with its financial target of a 15% return on tangible equity ("**RoTE**").

Operating profit – ongoing operations

	H1 2014 £m	H1 2013 £m
Underwriting profit	**56.4**	95.9
Instalment and other operating income	**76.2**	93.2
Investment return	**116.5**	97.5
Operating profit	**249.1**	286.6

Overall operating profit from ongoing operations of £249.1 million represented a reduction of 13.1% on the first half of 2013 (£286.6 million). The reduction in the underwriting result was driven by claims from major weather events relative to the benign weather experienced in the same period in 2013 and lower prior-year reserve releases. The impact of the weather events was offset in part by a lower cost base, reflecting the ongoing focus on cost control and operating efficiency. Improvements in the attritional loss ratio performance reflect investment in pricing capability and focus on underwriting discipline. Reserve releases from ongoing operations of £218.0 million were lower than the first half of 2013 (£239.2 million). A higher investment return broadly offset the impacts of lower instalment and other operating income, which was partly attributable to the sale of Tracker.

In-force policies – ongoing operations (thousands)

As at	**30 Jun 2014**	31 Mar 2014	31 Dec 2013	30 Jun 2013
Motor	**3,692**	3,717	3,762	3,829
Home	**3,593**	3,666	3,719	3,753
Rescue and other personal lines	**8,153**	8,446	8,801	9,014
Commercial	**600**	592	583	561
International	**1,671**	1,670	1,610	1,586
Total	**17,709**	18,091	18,475	18,743

In-force policies for ongoing operations decreased by 4.1% during the first half of 2014 to 17.7 million (31 December 2013: 18.5 million). The fall related primarily to Rescue and other personal lines, partially offset by International and Commercial. The Rescue and other personal lines reduction derived mainly from travel policies connected to the sale of packaged building society and bank accounts.

The fall in Motor and Home in-force policies of 1.9% and 3.4% respectively during the first half of 2014 reflected the Group's continuing focus on maintaining its underwriting discipline in a competitive marketplace. International growth arose from Germany reflecting the expansion of the Group's share of business renewing on 1 January 2014. In-force policy growth in Commercial arose mainly from Direct Line for Business with positive effects from Landlord and Tradesman products, partially offset by Van where the Group has not followed market premium rate reductions.

Gross written premium – ongoing operations

	Q2 2014 £m	Q2 2013 £m	**H1 2014 £m**	H1 2013 £m
Motor	**338.5**	367.3	**665.4**	731.4
Home	**216.8**	226.9	**437.3**	460.4
Rescue and other personal lines	**93.3**	100.1	**181.2**	193.2
Commercial	**144.1**	137.1	**262.1**	250.7
International	**132.8**	138.9	**328.8**	340.2
Total	**925.5**	970.3	**1,874.8**	1,975.9

Gross written premium of £1,874.8 million decreased by 5.1% compared with the same period in the prior year (first half 2013: £1,975.9 million) and at constant currency fell by 4.6%. This reflects the impact of an ongoing competitive market, particularly in UK motor and home, together with the Group's continued focus on maintaining its underwriting discipline, partially offset by growth in the Commercial business.

Premium rates for Motor were lower during the first half of 2014 compared with the first half of 2013. This reduction was supported by positive claims trends and technical pricing initiatives. Claims trends benefited from the Group's claims transformation programme and also recognised the positive effect of legal reforms. Risk mix reduced during the first half of 2014.

In Home, gross written premium reduced by 5.0% in the first half of 2014 reflecting the Group's continuing focus on maintaining its underwriting discipline in an increasingly competitive market. The Group continued to invest in pricing programmes and claims transformation.

Rescue and other personal lines gross written premium decreased by 6.2% compared with the same period in the prior year. The reduction was due to the sale of the Group's Life business in November 2013 (first half 2013: £15.5 million). Excluding this, gross written premium was up 2.0% reflecting growth in Rescue.

Gross written premium increased by 4.5% in Commercial in the first half of 2013 compared with the first half of 2013. This increase arose mainly from eTrade products and Direct Line for Business, however the commercial van market, similar to the UK motor market, was highly competitive and the Group has maintained its underwriting discipline despite market premium rate reductions.

International gross written premium of £328.8 million was 3.4% lower than the previous period mainly due to the effect of foreign currency movements. Gross written premium for International in local currency terms fell marginally by 0.5%, as competitive markets in Italy were offset by the expansion of Germany's share of business incepting on 1 January 2014. Gross written premium for Germany in local currency increased by 13.3%.

In total, gross written premiums of £925.5 million in the second quarter fell by 4.6% compared to 2013 (second quarter 2013: £970.3 million).

Underwriting profit – ongoing operations

	H1 2014 £m	H1 2013 £m
Underwriting profit	**56.4**	95.9
Loss ratio	**62.6%**	60.3%
Commission ratio	**11.5%**	11.3%
Expense ratio	**22.5%**	23.0%
Combined operating ratio	**96.6%**	94.6%

The Group's COR for ongoing operations increased by 2.0 percentage points to 96.6% (first half 2013: 94.6%), resulting in a reduction in underwriting profit for ongoing operations to £56.4 million (first half 2013: £95.9 million).

The increase in COR was primarily the result of a 2.3 percentage point increase in the loss ratio, largely due to the claims from major weather events in the first half. Significant reserve releases of £218.0 million for the first half of 2014 were lower than the same period in 2013 (£239.2 million). These were experienced as a result of consistently conservative reserving, management actions taken to improve the risk profile of the book and initiatives relating to claims. In the first half of 2014, the Home division incurred approximately £64 million of claims from major weather events (first half 2013: nil). The Commercial division incurred approximately £16 million of claims from major weather events in the first half of 2014 (first half 2013: nil).

Current year attritional loss ratio – ongoing operations

	H1 2014	H1 2013
Reported loss ratio	**62.6%**	60.3%
Prior year reserve releases	**13.0%**	13.5%
Major weather events – Home[1]	**(3.8%)**	0.0%
Current year attritional loss ratio	**71.8%**	73.8%

The Group views the improvement in the current-year attritional loss ratio as a good indicator of underlying improvements and sustainability of ongoing performance as it excludes prior-year reserve movements and impact of major weather events in the Home division.

Overall, the current-year attritional loss ratio improved by 2.0 percentage points to 71.8% in the first half of 2014, despite competitive market conditions and increased weather-related claims in Commercial. The current-year attritional loss ratio reflected recognition of management actions to improve the risk profile of the book, offset by the impact of recent premium deflation.

Prior year reserve releases – ongoing operations[2]

	H1 2014 £m	H1 2013 £m
Motor	**149.0**	148.6
Home	**33.1**	37.0
Rescue and other personal lines	**6.6**	0.4
Commercial	**23.8**	31.9
International	**5.5**	21.3
Total	**218.0**	239.2

Overall prior-year reserve releases from ongoing operations of £218.0 million were lower than the first half of 2013 (£239.2 million) and equivalent to 13.0% of net earned premium (first half 2013: 13.5% of net earned premium).

Commission and expense ratios – ongoing operations

The commission ratio increased by 0.2 percentage points to 11.5% (first half 2013: 11.3%), mainly due to increased partnership and PCW business in International, partially offset by reduced profit share payments in Home due to higher weather claims.

The expense ratio improved by 0.5 percentage points to 22.5% (first half 2013: 23.0%), reflecting the benefits of cost reduction initiatives; these benefits were partially offset by the effect of lower net earned premium on the ratio.

Notes:
1. Home claims from major weather events, including inland and coastal flooding and storms.
2. This excludes the Run-off segment reserve releases £19.4 million (first half 2013: £4.0 million).

Segmental analysis

Combined operating ratio – ongoing operations

	Reported basis	
	H1 2014	H1 2013
Motor	**93.6%**	95.8%
Home	**97.8%**	86.3%
Rescue and other personal lines	**90.9%**	92.2%
Commercial	**104.6%**	105.3%
International	**101.3%**	99.9%
Total	**96.6%**	94.6%

Current year attritional loss ratio by division – ongoing operations

	Current year attritional	
	H1 2014	H1 2013
Motor	**87.2%**	87.1%
Home	**49.6%**	51.7%
Rescue and other personal lines	**61.4%**	60.6%
Commercial	**73.3%**	74.9%
International	**79.4%**	86.6%
Current year attritional loss ratio	**71.8%**	73.8%

On a segmental basis, the COR improved in Motor, Commercial and Rescue and other personal lines compared with the first half of 2013. The Home COR increased principally due to claims from major weather events in the first half of 2014. The International COR increased modestly principally due to a lower contribution from prior-year reserve releases.

In Motor, the 2.2 percentage points improvement in COR largely reflects similar levels of releases of reserves from prior years, against a lower net earned premium. The reserve releases of £149.0 million in the first half of 2014 were driven primarily by favourable bodily injury and property damage experience for recent accident years. The current-year attritional loss ratio was in line with the first half of 2013, which reflected recognition of management actions to improve the risk profile of the book, offset by the impact of recent premium deflation.

The Home COR increased to 97.8% in the first half of 2014 from 86.3% in the first half of 2013. The increase was driven by claims from major weather events in January and February. In the first half of 2014, claims from major weather events totalled approximately £64 million compared with nil in the first half of 2013. The current-year attritional loss ratio improved by 2.1 percentage points reflecting benefits from pricing and claims initiatives, albeit in competitive markets.

The COR for Rescue and other personal lines improved to 90.9% (first half 2013: 92.2%). The improvement was mainly as a result of higher reserve releases related to underlying improvements in Travel performance. The Rescue COR improved by 3.3 percentage points to 78.2% (first half 2013: 81.5%).

The Commercial division improved its COR to 104.6% from 105.3% principally as a result of significant improvements in underlying underwriting performance and a lower commission and expense ratio. This was despite higher weather-related claims in the first half of 2014. The current-year attritional loss ratio improved by 1.6 percentage points demonstrating the positive effect of recent management actions. The division continues to experience significant reserve releases, albeit not at the levels experienced in the first half of 2013. Excluding the impact of weather-related claims and large losses above normal levels, the COR would have been approximately 101%.

The International COR in the first half of 2014 increased to 101.3% from 99.9% in the first half of 2013. The increase was mainly due to lower reserve releases, which decreased to £5.5 million (first half 2013: £21.3 million). The 7.2 percentage point improvement in the current-year attritional loss ratio to 79.4% reflects a decrease in claims frequency in Italy, while in Germany the first half of 2013 was affected by claims from severe hailstorms.

Operating expenses and cost base – ongoing operations

	H1 2014 £m	H1 2013 £m
Staff costs	**141.2**	170.9
Marketing	**74.1**	102.1
Depreciation	**9.9**	10.9
Amortisation and impairment of other intangible assets	**31.6**	17.1
Other operating expenses	**119.6**	107.5
Total operating expenses	**376.4**	408.5
Claims handling expenses	**119.6**	115.6
Total cost base	**496.0**	524.1
Expense ratio	**22.5%**	23.0%
Claims handling ratio	**7.1%**	6.5%

The expense ratio improved by 0.5 percentage points to 22.5% due to a reduction in operating expenses compared with the first half of 2013, partially offset by the impact of lower net earned premium.

Ongoing operating expenses of £376.4 million were reduced by 7.9% from the prior period (first half 2013: £408.5 million). The reduction was principally due to the benefits from the Group's cost savings plan and tight cost control. The Group continues to pay RBS Group for transitional IT infrastructure, the costs of which are included within other operating expenses.

The Group is targeting a total cost base[1] of approximately £1,000 million in 2014 and the total cost base in the first half 2014 of £496.0 million continued to show good progress towards this target.

Instalment and other operating income – ongoing operations

	H1 2014 £m	H1 2013 £m
Instalment income	**52.6**	60.0
Other operating income:		
Solicitors' referral fee income	**0.6**	6.1
Vehicle replacement referral income	**7.6**	8.1
Revenue from vehicle recovery and repair services[2]	**9.0**	15.5
Fee income from insurance intermediary services	**1.0**	0.9
Other income	**5.4**	2.6
Total other operating income	**23.6**	33.2
Total	**76.2**	93.2

Instalment and other operating income from ongoing operations reduced by 18.2% from the first half of 2013. This was primarily as a result of reduced instalment income, lower revenues from vehicle recovery following the sale of the Tracker business and the cessation of solicitors' referral fee income in England and Wales from 1 April 2013.

Instalment income, representing interest charged on insurance premiums paid by instalments, of £52.6 million reduced by £7.4 million compared with the prior period (first half 2013: £60.0 million) as a result of fewer in-force policies in Motor and Home.

In February 2014, the Group sold its stolen vehicle recovery business, Tracker. In the first half of 2014, the Group recognised other operating income from Tracker of £1.4 million (first half 2013: £8.7 million) which was included in the above.

Notes:
1. See note 4 on page 2
2. Vehicle recovery includes post-accident and pay on use recovery and vehicle tracking. Repair services constitute the provision of non-insurance related services.

Investment return – ongoing operations

	Q2 2014 £m	Q2 2013 £m	H1 2014 £m	H1 2013 £m
Investment income	**46.7**	43.3	**93.2**	83.4
Net realised and unrealised gains	**6.9**	13.8	**23.3**	14.1
Total investment return	**53.6**	57.1	**116.5**	97.5

The total investment return increased to £116.5 million (first half 2013: £97.5 million) due to an increase in both investment income and net realised and unrealised gains. Investment income was £93.2 million, an 11.8% increase on the first half of 2013, as a result of changes in asset mix to diversify the portfolio and improve returns, which were partially offset by a lower average investment asset base. Gains were mainly due to revaluations of the property portfolio.

Investment yields – total Group

	Q2 2014	Q2 2013	H1 2014	H1 2013
Investment income yield[1]	**2.3%**	2.0%	**2.3%**	2.0%
Investment return[2]	**2.6%**	2.7%	**2.8%**	2.3%

The annualised investment income yield for the Group for the first half of 2014 was 2.3% compared to 2.0% for the first half of 2013. This reflects the increased allocation to UK commercial property, securitised credit and 'BBB' corporate debt securities.

Investment holdings – total Group

As at	30 Jun 2014 £m	31 Mar 2014 £m	31 Dec 2013 £m	30 Jun 2013 £m
Corporate debt securities	**4,920.0**	4,792.7	4,915.8	4,795.5
Supranational[3]	**339.4**	360.9	365.7	463.8
Local government[3]	**175.3**	188.2	134.5	278.7
Credit	**5,434.7**	5,341.8	5,416.0	5,538.0
Securitised credit	**468.5**	417.2	229.8	38.4
Sovereign[3]	**1,139.0**	1,207.9	1,399.5	1,654.0
Total debt securities	**7,042.2**	6,966.9	7,045.3	7,230.4
Cash and cash equivalents	**925.0**	1,283.7	1,288.9	1,444.2
Investment property	**259.7**	228.6	223.4	186.9
Total Group[4]	**8,226.9**	8,479.2	8,557.6	8,861.5

Total debt securities are £7,042.2 million (31 December 2013: £7,045.3 million), of which 16.0% are rated as 'AAA' and a further 67.1% are rated as 'AA' or 'A'. Corporate, supranational and local government debt securities account for 66.1% of the portfolio.

The total value of the investment portfolio at 30 June 2014 was £8,227.0 million, 3.9% lower than at 31 December 2013. Assets under management provide adequate access to liquidity, with 11.2% of the funds held in cash and cash equivalents. Unrealised gains (net of deferred tax) increased by £20.4 million in the first half of 2014 taking the revaluation reserve to £79.2 million as at 30 June 2014.

Following an asset and liability management study, the Group will start to diversify the investment portfolio further during 2014 with investments in infrastructure debt and short-dated high yield debt. Furthermore, the allocation to securitised credit increased by £238.7 million in the first half of 2014.

Notes:
1. Investment income yield excludes net gains and is shown on an annualised basis.
2. Investment return includes net gains and is shown on an annualised basis.
3. Asset allocation at 30 June 2014 includes investment portfolio derivatives, which have been netted and have a mark-to-market value of £29.4 million, split £21.5 million in corporate debt securities, £0.3 million in supranational, £0.5 million in local government, £7.0 million in securitised credit and £0.1 million in sovereign (31 March 2014: corporate debt securities £6.9 million, local government £0.1 million, securitised credit £0.1 million negative and sovereign £0.2 million; 31 December 2013: corporate debt securities £37.7 million and securitised credit £2.1 million; and 30 June 2013: corporate debt securities £14.2 million)
4. Net of bank overdrafts and including term deposits with financial institutions with maturities in excess of three months.

Investment property holdings shown as at 30 June 2014 comprised 23 properties. The primary sector exposures are standard retail and retail warehouses, representing 35.5% and 21.0% of the property holdings respectively.

Operating profit – ongoing operations

	H1 2014 £m	H1 2013 £m
Motor[1]	**164.3**	157.0
Home	**34.8**	86.7
Rescue and other personal lines[2]	**25.8**	21.9
Commercial	**10.8**	7.0
International	**13.4**	14.0
Total	**249.1**	286.6

Overall operating profit reduced by 13.1% as a result of claims from major weather events in the Home division and overall lower prior-year reserve releases offset by improvement in the attritional performance and investment returns. Motor, Rescue and other personal lines and Commercial experienced improvement in operating profit, with International broadly stable.

Operating profit, profit before tax and profit after tax

	H1 2014 £m	H1 2013 £m
Operating profit – ongoing operations	**249.1**	286.6
Run-off segment[2]	**20.4**	10.6
Restructuring and other one-off costs	**(28.0)**	(69.9)
Operating profit	**241.5**	227.3
Finance costs	**(18.7)**	(18.5)
Gain on disposal of subsidiary	**2.3**	-
Profit before tax	**225.1**	208.8
Tax	**(49.5)**	(57.0)
Profit after tax	**175.6**	151.8

Run-off
The Run-off segment made a profit of £20.4 million in the first half of 2014 compared with a profit of £10.6 million in the first half of 2013. Similar to the ongoing operations, the Run-off segment benefited from positive prior-year reserve releases from the recognition of improved claims experience, in particular in relation to bodily injury claims. Going forward, it is currently expected that the Run-off segment will contribute positively to operating profit, albeit at a lower level than in 2013.

Restructuring and other one-off costs
Restructuring and other one-off costs for the first half of 2014 fell to £28.0 million (first half 2013: £69.9 million) as a result of the non-repeat of costs associated with separation and divestment from RBS Group. Expenditure in the first half of 2014 includes £25.3 million relating to IT migration and £2.7 million relating to the Group's cost saving initiatives. The Group continues to expect that Restructuring and other one-off costs in 2014 will be approximately £80 million.

Finance costs
Finance costs, which primarily reflect interest on the £500 million of long-term subordinated debt issued in April 2012, increased slightly to £18.7 million (first half 2013: £18.5 million).

Gain on disposal of subsidiary
The gain on disposal of £2.3 million substantially relates to the sale of the Group’s stolen vehicle recovery business, Tracker.

Notes:
1. Up to the date of sale, the operating loss from the Tracker business was £0.4 million (first half 2013: £1.6 million).
2. The Life business, which contributed £3.4 million to the Rescue and other personal lines and £0.6 million to the Run-off operating profit in the first half of 2013, was sold in November 2013.

Taxation
The effective tax rate for the first half of 2014 was 22.0% (first half 2013: 27.3%) aligning closely with the standard UK corporation tax rate of 21.5% (first half 2012: 23.25%). In the first half of 2014, the higher effective tax rate was driven primarily by disallowable expenses and earnings from the International operations which were subject to higher corporation tax rates, offset by the remeasurement of deferred tax asset, non-taxable disposal of a subsidiary and adjustments to provisions in respect of prior-year tax.

Profit and return on tangible equity
Profit for the first half of 2014 year amounted to £175.6 million (first half 2013: £151.8 million), an increase of 15.7% on the first half of 2013.

Annualised RoTE from ongoing operations decreased to 15.8% (first half 2013: 17.3%).

Earnings per share
Basic and diluted earnings per share of 11.7 pence increased 15.8% (first half 2013: 10.1 pence), reflecting reduced Restructuring and other one-off costs partially offset by claims from major weather events and lower prior-year reserve releases in the first half.

Diluted adjusted basic earnings per share, which excludes the Run-off segment and Restructuring and other one-off costs, decreased by 12.4% to 12.0 pence (first half 2013: 13.7 pence).

Net asset value

As at	30 Jun 2014 £m	30 Jun 2013 £m	31 Dec 2013 £m (audited)
Net assets	**2,795.4**	2,792.8	2,790.0
Goodwill and other intangible assets	**(499.7)**	(451.8)	(500.1)
Tangible net assets	**2,295.7**	2,341.0	2,289.9
Net asset value per share (pence)	**187.0**	186.9	186.6
Tangible net asset value per share (pence)	**153.5**	156.6	153.2

The net asset value at 30 June 2014 was £2,795.4 million (31 December 2013: £2,790.0 million) with tangible net asset value of £2,295.7 million (31 December 2013: £2,289.9 million). This equates to 187.0 pence and 153.5 pence per share respectively at 30 June 2014 (31 December 2013: 186.6 pence and 153.2 pence, respectively).

The marginal increase in net asset value and tangible net asset value principally reflects profit for the period, partially offset by the payment of final and second special interim dividends for 2013.

Dividends
The Board has declared a regular interim dividend for the Company for 2014 of £66.0 million representing 4.4 pence per share, an increase of 4.8% on the regular interim dividend for 2013 (4.2 pence per share).

The Board has also declared a special interim dividend for the Company of 10.0 pence per share amounting to £150.0 million. Both the regular and special interim dividends will be paid on 12 September 2014 to shareholders on the register on 15 August 2014. The ex dividend date will be 13 August 2014.

Capital position and leverage[1]

The Group is well capitalised with key capital metrics within the Group's risk appetite and significantly above regulatory minima.

As at	30 Jun 2014 £m	31 Dec 2013 £m
Shareholders' equity	**2,795.4**	2,790.0
Goodwill and other intangible assets	**(499.7)**	(500.1)
Regulatory tier 1 adjustments	**(31.3)**	6.2
Total Tier 1 capital	**2,264.4**	2,296.1
Lower Tier 2 capital[2]	**496.8**	496.9
Other regulatory adjustments	**(29.7)**	(28.9)
Total regulatory capital	**2,731.5**	2,764.1
Insurance Group Directive ("IGD")		
IGD required capital[3]	**876.1**	947.9
IGD excess solvency	**1,855.4**	1,816.2
IGD coverage ratio	**311.8%**	291.6%
Risk-based capital coverage ratio (adjusted for the regular and special interim dividends)[4]	**148.8%**	148.7%

At 30 June 2014, the Group had an estimated risk-based capital coverage ratio of 148.8% after deducting the regular interim and special dividends (31 December 2013: 148.7%). On an IGD basis, the coverage ratio is 311.8% (31 December 2013: 291.6%).

During the first half of 2014, the Group completed the new Individual Capital Adequacy Standards Plus ("**ICAS+**") process with the Prudential Regulation Authority to determine the regulatory capital requirement for its principal UK-based underwriter U K Insurance Limited ("**UKI**").

The table below sets out the Group's financial leverage:

As at	30 Jun 2014 £m	31 Dec 2013 £m
Shareholders' equity	**2,795.4**	2,790.0
Subordinated dated notes	**494.8**	486.6
Total capital employed	**3,290.2**	3,276.6
Financial leverage ratio[5]	**15.0%**	14.9%

Credit ratings

Standard & Poor's and Moody's Investors Service provide insurance financial strength ratings. UKI is rated 'A' (strong) with a stable outlook by Standard & Poor's and 'A2' (good) with a stable outlook by Moody's.

Notes:
1. Figures and ratios for the first half of 2014 include unaudited profits on a regulated basis.
2. Includes that element of the subordinated dated notes applicable for regulatory capital purposes.
3. Based on the IGD for the Group.
4. The risk-based capital coverage ratio has been adjusted for proposed and/or declared dividends.
5. Total financial debt as a percentage of total capital employed.

Principal risks and uncertainties

The Directors consider that the principal risks and uncertainties explained in detail on pages 25 and 26 of the Annual Report & Accounts 2013 continue to reflect the principal risks and uncertainties of the Group.

A summary of each of the Group's principal risks and uncertainties is provided below:

- **Strategic risk**
  The external environment could put at risk our ability to meet our strategic objectives through the five key strategic priorities of distribution, pricing, claims, costs and Commercial and International.

- **Insurance risk: Underwriting and pricing risk**
  We are subject to the risk that inappropriate business could be written (or not specifically excluded) and inappropriate prices charged.

  Underwriting risk includes catastrophe risk arising from losses due to unpredictable natural and man-made events affecting multiple covered risks, particularly given the concentration of our Home business in the UK.

- **Insurance risk: Reserving risk**
  Due to the uncertain nature and timing of the risks to which we are exposed, we cannot precisely determine the amounts that we will ultimately pay to meet the liabilities covered by the insurance policies written.

  Reserving risk is our biggest risk, generated by our large Motor portfolio. Reserving risk is heightened in the case of periodic payment orders ("**PPOs**") because of their long-term nature.

  Reserving generates both upside and downside risk, with the potential for outcomes to be adverse or to be in our favour.

- **Operational risk**
  We potentially face the risks of direct or indirect losses resulting from inadequate or failed internal processes or fraudulent claims; from systems and people; or from external events.

  In particular we have IT systems risk, including that we are highly dependent on the use of RBS Group's information technology, software, data and service providers.

  Migrating IT systems away from RBS Group introduces different operational risks; there is increased likelihood of system failure at the point that functions are moved onto new infrastructure. Further, if the migration fails to stay on schedule, we will incur charges for remaining on RBS Group IT infrastructure.

  IT migration and other change initiatives also introduce people risk, as management may be distracted away from day-to-day activities.

  Operational risk includes cyber risk, the risks relating to the use of computers, other IT and the storage of data.

  Within this category, we also consider the risk of the Group not recruiting and retaining suitable talent. This risk is particularly important during the Group's current period of change.

- **Market risk**
  We are subject to the risk that, as a result of market movements, we may be exposed to fluctuations in the value of our assets or the income from our assets.

  For the Group this includes: interest rate risk, spread risk, currency risk and property risk.

- **Counterparty risk**
  We partner with many suppliers and the failure of any of these to perform their financial obligations in a timely manner could result in a financial loss.

  Our principal area of counterparty risk is our use of reinsurance against underwriting risk, sometimes called reinsurance risk or reinsurer default risk.

- **Regulatory risk**
  Regulatory risk arises if changes in law and regulations are not identified or understood, or are inappropriately and incorrectly interpreted or adopted.

  In particular, Solvency II regulations are currently being introduced. Some Solvency II requirements are still uncertain and subject to the outcome of discussion between UK and European regulators. This and other similar uncertainties increase our level of risk.

  Regulatory risk also includes the risk that business practices are not efficiently modified following a regulatory change. Further, there is a risk that current legal or regulatory requirements are not complied with.

- **Conduct risk**
  We are subject to the risk of failing to deliver the appropriate treatment for our customers throughout all stages of the customer journey and the risk that our people fail to behave with integrity.

  This includes the risk that our organisational culture is not appropriate, with a failure to communicate the correct tone from the top.

- **Brand and reputational risk**
  We are dependent on the strength of our brands, our reputation with customers and distributors in the sale of products and services. We have entered into various strategic partnerships that are important to the marketing, sale and distribution of our products.

Evolving risks
Risks can emerge and evolve over time, often as a result of changes in the environment in which we operate. Set out below are examples of current significant evolving risks that may influence the Group's future performance in this and future financial years and cause results to differ materially from expected and historical results.

Bodily injury claims costs
Bodily injury claim costs are a key source of uncertainty with several regulatory, legal and market pressures facing the Group, including:

- underlying trends in bodily injury claims frequency and average cost per claim inflation
- the results of the MoJ consultation into the discount rate used to value certain types of bodily injury claim awards
- the propensity for large injury claims to settle as PPOs, and the inflation and longevity assumptions used to value PPOs
- the impact on claims costs of the MoJ consultation and Transport Committee investigation into whiplash injuries

Regulatory environment
The UK general insurance market is subject to several regulatory reviews and potential areas of focus which are sources of uncertainty including:

- the Competition and Markets Authority's investigation into aspects of the private motor insurance market
- the FCA's market study of general insurance add-on products
- the FCA's thematic review of complaints, claims handling and the PCW market
- how the FCA embeds its new Customer Credit regulation responsibilities and its consultation on a credit cap applicable from January 2015
- the impacts of Flood Re and the proposed levy on home insurance premiums

There is also uncertainty around the way in which the FCA may apply the principles underpinning behavioural economics to the insurance industry and the impact that this has on our business.

The EU is currently developing new EU Data Protection Regulations which will replace the UK Data Protection Act. This may impact our ability to use and benefit from our stored data. Specifically, restrictions or bans on profiling may impact our ability to identify the most appropriate products or solutions for our customers.

Business transformation and project delivery
The Group is carrying out initiatives to improve its operational efficiency as part of the implementation of its business transformation plan.

There is a strategic risk of the potential failure to execute the plan, or that the expected benefits of the plan may not be achieved on time or to the extent targeted.

There is also a potential for upside risk should initiatives provide benefits that are greater than those planned, or if the expected benefits are felt by the business sooner than planned.

Uncertainties include the potential changes in the market around the use of PCWs, changes in customer behaviour and the increasing use of telematics.

Emerging risks
Risks can emerge over the long term as a result of significant changes in the environment including technology, weather patterns and socio-economic behaviours. Examples of these risks would include driverless cars, new types of competitor entering the market and climate change.

Condensed consolidated income statement

For the six months ended 30 June 2014

	Notes	**6 months 2014 £m**	6 months 2013 £m	Full year 2013 £m (audited)
Gross earned premium	5	**1,860.5**	1,960.9	3,896.3
Reinsurance premium ceded	5	**(186.4)**	(187.3)	(373.0)
Net earned premium	5	**1,674.1**	1,773.6	3,523.3
Investment return	6	**118.8**	105.4	221.1
Instalment income		**52.6**	60.0	117.8
Other operating income	7	**23.6**	33.2	62.4
Total income		**1,869.1**	1,972.2	3,924.6
Insurance claims	8	**(1,177.3)**	(1,148.3)	(2,334.8)
Insurance claims recoverable from reinsurers	8	**147.3**	83.1	180.5
Net insurance claims	8	**(1,030.0)**	(1,065.2)	(2,154.3)
Commission expenses	9	**(192.6)**	(200.3)	(392.4)
Operating expenses	10	**(405.0)**	(479.4)	(928.3)
Total expenses		**(597.6)**	(679.7)	(1,320.7)
Operating profit		**241.5**	227.3	449.6
Finance costs	11	**(18.7)**	(18.5)	(37.7)
Gain on disposal of subsidiary		**2.3**	-	12.0
Profit before tax		**225.1**	208.8	423.9
Tax charge	12	**(49.5)**	(57.0)	(111.1)
Profit for the period attributable to owners of the Company		**175.6**	151.8	312.8
Earnings per share:				
Basic (pence)	14	**11.7**	10.1	20.9
Diluted (pence)	14	**11.7**	10.1	20.8

Condensed consolidated statement of comprehensive income

For the six months ended 30 June 2014

	6 months 2014 £m	6 months 2013 £m	Full year 2013 £m (audited)
Profit for the period	**175.6**	151.8	312.8
Other comprehensive income / (loss)			
Items that will not be reclassified subsequently to profit or loss:			
Actuarial gain / (loss) on defined benefit pension scheme	**-**	0.6	(6.9)
Tax relating to items not reclassified	**-**	-	1.5
	-	0.6	(5.4)
Items that may be reclassified subsequently to profit or loss:			
Exchange differences on translation of foreign operations	**(8.2)**	(1.0)	(4.9)
Fair value gain / (loss) on available-for-sale investments	**39.5**	(71.3)	(108.2)
Less: realised net gains on available-for-sale investments included in income statement	**(14.0)**	(13.1)	(25.7)
Tax relating to items that may be reclassified	**(5.1)**	18.1	33.9
	12.2	(67.3)	(104.9)
Other comprehensive income / (loss) for the period net of tax	**12.2**	(66.7)	(110.3)
Total comprehensive income for the period attributable to owners of the Company	**187.8**	85.1	202.5

Condensed consolidated balance sheet

As at 30 June 2014

	Notes	30 Jun 2014 £m	31 Dec 2013 £m (audited)
Assets			
Goodwill and other intangible assets		**499.7**	500.1
Property, plant and equipment		**144.8**	102.3
Investment property		**259.7**	223.4
Reinsurance assets	17	**1,050.5**	1,011.0
Deferred tax assets		**15.0**	19.3
Current tax assets		**0.7**	1.3
Deferred acquisition costs		**324.7**	321.5
Insurance and other receivables		**1,104.6**	1,122.0
Prepayments, accrued income and other assets		**97.5**	95.7
Derivative financial instruments		**37.5**	40.7
Financial investments	15	**7,166.9**	7,441.2
Cash and cash equivalents	16	**846.7**	908.3
Assets held for sale		**4.1**	1.0
Total assets		**11,552.4**	11,787.8
Equity		**2,795.4**	2,790.0
Liabilities			
Subordinated liabilities		**494.8**	486.6
Insurance liabilities	17	**5,549.2**	5,757.4
Unearned premium reserve	17	**1,817.9**	1,818.7
Retirement benefit obligations		**2.0**	2.0
Borrowings	16	**75.8**	55.1
Derivative financial instruments		**17.5**	19.3
Trade and other payables including insurance payables		**740.0**	818.3
Deferred tax liabilities		**20.7**	19.3
Current tax liabilities		**39.1**	21.1
Total liabilities		**8,757.0**	8,997.8
Total equity and liabilities		**11,552.4**	11,787.8

Condensed consolidated statement of changes in equity

For the six months ended 30 June 2014

	Total Shareholders equity £m
Balance as at 1 January 2014	**2,790.0**
Profit for the period	**175.6**
Other comprehensive income	**12.2**
Dividends	**(185.6)**
Credit to equity for equity-settled share-based payments	**3.0**
Deferred tax on share-based payments	**0.2**
Balance as at 30 June 2014	**2,795.4**
Balance as at 1 January 2013	2,831.6
Profit for the period	151.8
Other comprehensive loss	(66.7)
Dividends	(120.0)
Shares acquired by employee trusts	(5.6)
Credit to equity for equity-settled share-based payments	1.7
Balance as at 30 June 2013	2,792.8
Balance as at 1 January 2013	2,831.6
Profit for the period	312.8
Other comprehensive loss	(110.3)
Dividends	(242.7)
Shares acquired by employee trusts	(5.7)
Credit to equity for equity-settled share-based payments	4.1
Deferred tax on share-based payments	0.2
Balance as at 31 December 2013	2,790.0

Condensed consolidated cash flow statement

For the six months ended 30 June 2014

	Note	**6 months 2014 £m**	6 months 2013 £m	Full year 2013 £m (audited)
Net cash used by operating activities before investment of insurance assets		**(191.2)**	(138.7)	(307.0)
Cash generated from investment of insurance assets		**412.1**	74.1	433.0
Net cash generated from / (used by) operating activities		**220.9**	(64.6)	126.0
Cash flows from investing activities				
Purchases of property, plant and equipment		**(53.3)**	(14.8)	(39.1)
Purchases of intangible assets		**(32.2)**	(47.3)	(115.5)
Purchases of assets held for sale		**(12.7)**	-	-
Net cash flows from disposal of subsidiary		**1.7**	-	18.8
Cash flows from net investment hedges		**-**	(12.4)	(9.5)
Net cash used by investing activities		**(96.5)**	(74.5)	(145.3)
Cash flows from financing activities				
Dividends paid		**(185.6)**	(120.0)	(242.7)
Repayment of subordinated liabilities		**-**	(258.5)	(258.5)
Finance costs		**(18.9)**	(18.9)	(37.8)
Purchase of employee trust shares		**-**	(5.6)	(5.7)
Net cash used by financing activities		**(204.5)**	(403.0)	(544.7)
Net decrease in cash and cash equivalents		**(80.1)**	(542.1)	(564.0)
Cash and cash equivalents at the beginning of the year		**853.2**	1,417.5	1,417.5
Effect of foreign exchange rate changes		**(2.2)**	3.8	(0.3)
Cash and cash equivalents at the end of the period	16	**770.9**	879.2	853.2

Notes to the condensed consolidated financial statements

Corporate information

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

1. General information

The financial information for the year ended 31 December 2013 and included in the condensed consolidated financial statements does not constitute statutory accounts as defined in S434 of the Companies Act 2006, but has been abridged from the statutory accounts for that year which have been delivered to the Registrar of Companies. The independent auditor's report on the Group accounts for the year ended 31 December 2013 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.

2. Accounting policies

Basis of preparation

The annual financial statements of the Group are prepared in accordance with International Financial Reporting Standards as adopted by the European Union. The condensed consolidated financial statements included in this Interim Report have been prepared in accordance with International Accounting Standard 34 'Interim Financial Reporting' as adopted by the European Union.

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 condensed consolidated financial statements.

Accounting policies and accounting developments

The following developments in accounting standards have been implemented by the Group during the period:

In December 2011, the IASB amended IAS 32 'Financial Instruments: Presentation' for the section dealing with offsetting a financial asset and a financial liability. Effective for annual periods beginning on or after 1 January 2014, to be applied retrospectively, this amendment has had no effect on the Group.

Otherwise, the same accounting policies, presentation and methods of computation are followed in the condensed consolidated financial statements as applied in the Group's latest annual audited financial statements.

3. Critical accounting estimates and judgements

The Annual Report & Accounts 2013 provides full details of critical accounting estimates and judgements used in the application of the Group's accounting policies on pages 120 to 123. There have been no significant changes to the principles or assumptions of these critical accounting estimates and judgements during the period.

Notes to the condensed financial statements continued

4. Segmental analysis

There have been no significant changes to the Group's reportable segments as set out on pages 136 to 137 of the Annual Report & Accounts 2013.

The table below shows the Group's revenue and results by reportable segment for the six months ended 30 June 2014:

	Motor[1] £m	Home £m	Rescue and other personal lines £m	Commercial £m	International £m	Total ongoing £m	Run-off £m	Total Group £m
Gross written premium	665.4	437.3	181.2	262.1	328.8	**1,874.8**	(0.3)	**1,874.5**
Gross earned premium	689.8	463.0	184.2	238.8	285.0	**1,860.8**	(0.3)	**1,860.5**
Reinsurance premium ceded	(31.8)	(23.0)	(0.7)	(16.0)	(114.9)	**(186.4)**	-	**(186.4)**
Net earned premium	658.0	440.0	183.5	222.8	170.1	**1,674.4**	(0.3)	**1,674.1**
Investment return	71.3	12.7	3.1	17.0	12.4	**116.5**	2.3	**118.8**
Instalment income	34.7	11.9	0.7	2.7	2.6	**52.6**	-	**52.6**
Other operating income	15.9	0.3	5.3	1.4	0.7	**23.6**	-	**23.6**
Total income	779.9	464.9	192.6	243.9	185.8	**1,867.1**	2.0	**1,869.1**
Insurance claims	(475.8)	(249.8)	(106.2)	(143.1)	(216.4)	**(1,191.3)**	14.0	**(1,177.3)**
Insurance claims recoverable from reinsurers	50.8	0.8	0.2	3.6	86.9	**142.3**	5.0	**147.3**
Net insurance claims	(425.0)	(249.0)	(106.0)	(139.5)	(129.5)	**(1,049.0)**	19.0	**(1,030.0)**
Commission expenses	(16.7)	(92.0)	(14.5)	(41.3)	(28.1)	**(192.6)**	-	**(192.6)**
Operating expenses	(173.9)	(89.1)	(46.3)	(52.3)	(14.8)	**(376.4)**	(0.6)	**(377.0)**
Total expenses	(190.6)	(181.1)	(60.8)	(93.6)	(42.9)	**(569.0)**	(0.6)	**(569.6)**
Operating profit before restructuring and other one-off costs	**164.3**	**34.8**	**25.8**	**10.8**	**13.4**	**249.1**	**20.4**	**269.5**
Restructuring and other one-off costs								**(28.0)**
Operating profit								**241.5**
Finance costs								**(18.7)**
Gain on disposal of subsidiary								**2.3**
Profit before tax								**225.1**
Underwriting profit / (loss)	**42.4**	**9.9**	**16.7**	**(10.3)**	**(2.3)**	**56.4**		
Loss ratio	64.6%	56.6%	57.8%	62.6%	76.1%	**62.6%**		
Commission ratio	2.6%	20.9%	7.9%	18.5%	16.5%	**11.5%**		
Expense ratio	26.4%	20.3%	25.2%	23.5%	8.7%	**22.5%**		
Combined operating ratio	**93.6%**	**97.8%**	**90.9%**	**104.6%**	**101.3%**	**96.6%**		

Note:
1. The Group's revenue and results for the period ended 30 June 2014 relating to the Tracker business, which was disposed of on 5 February 2014, were recorded in the Motor segment (other operating income: £1.4 million and operating loss: £0.4 million).

Notes to the condensed financial statements continued

4. Segmental analysis continued

The table below shows the Group's revenue and results by reportable segment for the six months ended 30 June 2013:

	Motor[2] £m	Home £m	Rescue and other personal lines[1] £m	Commercial £m	International £m	Total ongoing £m	Run-off[1] £m	Total Group £m
Gross written premium	731.4	460.4	193.2	250.7	340.2	1,975.9	4.3	1,980.2
Gross earned premium	765.3	477.8	192.1	234.1	287.4	1,956.7	4.2	1,960.9
Reinsurance premium ceded	(26.8)	(25.2)	(9.5)	(18.1)	(104.8)	(184.4)	(2.9)	(187.3)
Net earned premium	738.5	452.6	182.6	216.0	182.6	1,772.3	1.3	1,773.6
Investment return	58.8	12.0	2.9	13.7	10.1	97.5	7.9	105.4
Instalment income	39.8	12.6	0.6	3.4	3.6	60.0	-	60.0
Other operating income	27.3	0.3	4.1	1.3	0.2	33.2	-	33.2
Total income	864.4	477.5	190.2	234.4	196.5	1,963.0	9.2	1,972.2
Insurance claims	(505.4)	(183.6)	(120.4)	(133.9)	(217.8)	(1,161.1)	12.8	(1,148.3)
Insurance claims recoverable from reinsurers	11.1	(13.3)	10.2	4.0	80.9	92.9	(9.8)	83.1
Net insurance claims	(494.3)	(196.9)	(110.2)	(129.9)	(136.9)	(1,068.2)	3.0	(1,065.2)
Commission expenses	(18.9)	(98.7)	(11.2)	(45.7)	(25.2)	(199.7)	(0.6)	(200.3)
Operating expenses	(194.2)	(95.2)	(46.9)	(51.8)	(20.4)	(408.5)	(1.0)	(409.5)
Total expenses	(213.1)	(193.9)	(58.1)	(97.5)	(45.6)	(608.2)	(1.6)	(609.8)
Operating profit before restructuring and other one-off costs	157.0	86.7	21.9	7.0	14.0	286.6	10.6	297.2
Restructuring and other one-off costs								(69.9)
Operating profit								227.3
Finance costs								(18.5)
Profit before tax								208.8
Underwriting profit / (loss)	31.1	61.8	14.3	(11.4)	0.1	95.9		
Loss ratio	66.9%	43.5%	60.4%	60.1%	74.9%	60.3%		
Commission ratio	2.6%	21.8%	6.1%	21.2%	13.8%	11.3%		
Expense ratio	26.3%	21.0%	25.7%	24.0%	11.2%	23.0%		
Combined operating ratio	95.8%	86.3%	92.2%	105.3%	99.9%	94.6%		

Note:
1. The Group's revenue and results for the period ended 30 June 2013 relating to the Life business, which was disposed of on 28 November 2013, were recorded in two segments: Rescue and other personal lines (net earned premium: £6.6 million, net insurance claims: £1.2 million and operating profit: £3.4 million) and Run-off (net earned premium: £1.6 million, net insurance claims: £0.3 million and operating profit: £0.6 million).
2. The Group's revenue and results for the period ended 30 June 2013 relating to the Tracker business, which was disposed of on 5 February 2014, were recorded in the Motor segment (other operating income: £8.7 million and operating loss: £1.6 million).

Notes to the condensed financial statements continued

4. Segmental analysis continued

The table below shows the Group's revenue and results by reportable segment for the year ended 31 December 2013 (audited):

	Motor[2] £m	Home £m	Rescue and other personal lines[1] £m	Commercial £m	International £m	Total ongoing £m	Run-off[1] £m	Total Group £m
Gross written premium	1,421.1	943.1	383.4	474.5	604.5	3,826.6	7.9	3,834.5
Gross earned premium	1,498.4	958.9	383.1	468.7	579.3	3,888.4	7.9	3,896.3
Reinsurance premium ceded	(53.6)	(50.0)	(17.3)	(34.1)	(212.8)	(367.8)	(5.2)	(373.0)
Net earned premium	1,444.8	908.9	365.8	434.6	366.5	3,520.6	2.7	3,523.3
Investment return	122.8	24.1	8.2	29.6	23.4	208.1	13.0	221.1
Instalment income	78.3	25.2	1.3	6.2	6.8	117.8	-	117.8
Other operating income	48.5	0.7	9.1	3.3	0.8	62.4	-	62.4
Total income	1,694.4	958.9	384.4	473.7	397.5	3,908.9	15.7	3,924.6
Insurance claims	(978.3)	(476.7)	(240.0)	(274.8)	(453.0)	(2,422.8)	88.0	(2,334.8)
Insurance claims recoverable from reinsurers	38.1	(13.7)	20.2	4.2	169.6	218.4	(37.9)	180.5
Net insurance claims	(940.2)	(490.4)	(219.8)	(270.6)	(283.4)	(2,204.4)	50.1	(2,154.3)
Commission expenses	(36.3)	(177.9)	(27.3)	(92.2)	(57.9)	(391.6)	(0.8)	(392.4)
Operating expenses	(370.2)	(184.4)	(90.8)	(101.4)	(39.6)	(786.4)	(1.4)	(787.8)
Total expenses	(406.5)	(362.3)	(118.1)	(193.6)	(97.5)	(1,178.0)	(2.2)	(1,180.2)
Operating profit before restructuring and other one-off costs	347.7	106.2	46.5	9.5	16.6	526.5	63.6	590.1
Restructuring and other one-off costs								(140.5)
Operating profit								449.6
Finance costs								(37.7)
Gain on disposal of subsidiary								12.0
Profit before tax								423.9
Underwriting profit / (loss)	98.1	56.2	27.9	(29.6)	(14.4)	138.2		
Loss ratio	65.1%	53.9%	60.1%	62.3%	77.3%	62.6%		
Commission ratio	2.5%	19.6%	7.5%	21.2%	15.8%	11.2%		
Expense ratio	25.6%	20.3%	24.8%	23.3%	10.8%	22.3%		
Combined operating ratio	93.2%	93.8%	92.4%	106.8%	103.9%	96.1%		

Note:
1. The Group's revenue and results for the year ended 2013 relating to the Life business, which was disposed of on 28 November 2013, were recorded in two segments: Rescue and other personal lines (net earned premium: £11.8 million, net insurance claims: £1.8 million and operating profit: £6.4 million) and Run-off (net earned premium: £2.8 million, net insurance claims: £0.7 million and operating profit: £1.2 million).
2. The Group's revenue and results for the year ended 2013 relating to the Tracker business, which was disposed of on 5 February 2014, were recorded in the Motor segment (other operating income: £18.4 million and operating loss: £1.4 million).

Notes to the condensed financial statements continued

5. Net earned premium

	6 months 2014 £m	6 months 2013 £m	Full year 2013 £m (audited)
Gross earned premium:			
Gross written premium	**1,874.5**	1,980.2	3,834.5
Movement in unearned premium reserve	**(14.0)**	(19.3)	61.8
	1,860.5	1,960.9	3,896.3
Reinsurance premium ceded:			
Premium payable	**(172.5)**	(191.2)	(368.0)
Movement in reinsurance unearned premium reserve	**(13.9)**	3.9	(5.0)
	(186.4)	(187.3)	(373.0)
Total	**1,674.1**	1,773.6	3,523.3

6. Investment return

	6 months 2014 £m	6 months 2013 £m	Full year 2013 £m (audited)
Investment income:			
Interest income on available-for-sale debt securities	**85.0**	82.9	169.9
Cash and cash equivalent interest income	**2.6**	4.0	7.3
Rental income from investment property	**7.5**	4.4	11.4
	95.1	91.3	188.6
Net realised gains / (losses):			
Available-for-sale debt securities	**14.0**	13.1	25.7
Derivatives	**16.4**	(52.2)	21.5
	30.4	(39.1)	47.2
Net unrealised (losses) / gains:			
Impairments of available-for-sale debt securities[1]	**1.3**	-	-
Derivatives	**(20.2)**	54.0	(22.2)
Investment property	**12.2**	(0.8)	7.5
	(6.7)	53.2	(14.7)
Total	**118.8**	105.4	221.1

Note:
1. The impairment reversal relates to an available-for-sale debt security originally impaired in 2011.

The tables below analyse the realised and unrealised derivatives included in investment return.

	6 months 2014		6 months 2013	
	Realised £m	**Unrealised £m**	Realised £m	Unrealised £m
Derivative gains / (losses)				
Foreign exchange forward contracts	**44.1**	**6.5**	(61.7)	(12.6)
Associated foreign exchange risk	**(16.2)**	**(31.5)**	7.0	68.4
Net gains / (losses) on foreign exchange forward contracts	**27.9**	**(25.0)**	(54.7)	55.8
Interest rate derivatives	**(9.7)**	**(16.7)**	20.5	(1.8)
Associated interest rate risk	**(1.8)**	**21.5**	(18.0)	-
Net (losses) / gains on interest rate derivatives	**(11.5)**	**4.8**	2.5	(1.8)
Total	**16.4**	**(20.2)**	(52.2)	54.0

6. Investment return continued

	Full year 2013 (audited)	
	Realised £m	Unrealised £m
Derivative gains / (losses)		
Foreign exchange forward contracts	21.2	12.0
Associated foreign exchange risk	2.0	(33.3)
Net gains / (losses) on foreign exchange forward contracts	23.2	(21.3)
Interest rate derivatives	(0.8)	19.6
Associated interest rate risk	(0.9)	(20.5)
Net (losses) / gains on interest rate derivatives	(1.7)	(0.9)
Total	21.5	(22.2)

7. Other operating income

	6 months 2014 £m	6 months 2013 £m	Full year 2013 £m (audited)
Solicitors' referral fee income[1]	**0.6**	6.1	6.9
Vehicle replacement referral income	**7.6**	8.1	15.7
Revenue from vehicle recovery and repair services	**9.0**	15.5	31.8
Fee income from insurance intermediary services	**1.0**	0.9	1.7
Other income	**5.4**	2.6	6.3
Total	**23.6**	33.2	62.4

Note:
1. Following changes to Legal Aid, Sentencing and Punishment of Offenders Act 2012 the payment of referral fees in personal injury cases were prohibited with effect from 1 April 2013 in England and Wales.

8. Net insurance claims

		6 months 2014	
	Gross £m	**Reinsurance £m**	**Net £m**
Current accident year claims paid	**491.5**	**(42.4)**	**449.1**
Prior accident years claims paid	**870.1**	**(43.6)**	**826.5**
Movement in insurance liabilities	**(184.3)**	**(61.3)**	**(245.6)**
Total	**1,177.3**	**(147.3)**	**1,030.0**

		6 months 2013	
	Gross £m	Reinsurance £m	Net £m
Current accident year claims paid	487.2	(34.9)	452.3
Prior accident years claims paid	993.7	(49.9)	943.8
Movement in insurance liabilities	(332.6)	1.7	(330.9)
Total	1,148.3	(83.1)	1,065.2

		Full year 2013 (audited)	
	Gross £m	Reinsurance £m	Net £m
Current accident year claims paid	1,306.2	(90.5)	1,215.7
Prior accident years' claims paid	1,566.6	(75.8)	1,490.8
Movement in insurance liabilities	(538.0)	(14.2)	(552.2)
Total	2,334.8	(180.5)	2,154.3

Notes to the condensed financial statements continued

8. Net insurance claims continued

Claims handling expenses for the six months ended 30 June 2014 of £121.2 million (six months ended 30 June 2013: £114.5 million and year ended 31 December 2013: £246.8 million) have been included in the claims figures above.

9. Commission expenses

	6 months 2014 £m	6 months 2013 £m	Full year 2013 £m (audited)
Commission expenses	**158.3**	162.7	333.3
Expenses incurred under profit participations	**34.3**	37.6	59.1
Total	**192.6**	200.3	392.4

10. Operating expenses

	6 months 2014 £m	6 months 2013 £m	Full year 2013 £m (audited)
Staff costs	**155.1**	220.0	395.3
Marketing	**74.1**	102.1	184.2
Depreciation	**9.9**	10.9	21.0
Amortisation and impairment of other intangible assets	**31.6**	17.1	37.2
Other operating expenses	**134.3**	129.3	290.6
Total	**405.0**	479.4	928.3

Staff costs attributable to claims handling activities are allocated to the cost of insurance claims.

The table below analyses restructuring and other one-off costs included in operating expenses:

	6 months 2014 £m	6 months 2013 £m	Full year 2013 £m (audited)
Staff costs	**13.6**	48.7	57.9
Other operating expenses	**14.4**	21.2	82.6
Total	**28.0**	69.9	140.5

11. Finance costs

	6 months 2014 £m	6 months 2013 £m	Full year 2013 £m (audited)
Interest expense on subordinated dated notes[1]	**18.7**	18.5	37.7

Note:
1. On 27 April 2012, the Group issued subordinated 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 hedge to exchange the fixed rate of interest on the subordinated loan notes for a floating rate of three-month LIBOR plus a spread of 706 basis points which increased to 707 basis points with effect from 29 July 2013.

Notes to the condensed financial statements continued

12. Tax charge

	6 months 2014 £m	6 months 2013 £m	Full year 2013 £m (audited)
Current taxation:			
Charge for the period	**49.0**	48.9	102.5
(Over) / under provision in respect of prior period	**(1.0)**	2.7	1.8
	48.0	51.6	104.3
Deferred taxation:			
Charge for the period	**4.7**	4.5	1.6
(Over) / under provision in respect of prior period	**(3.2)**	0.9	5.2
	1.5	5.4	6.8
Current taxation	**48.0**	51.6	104.3
Deferred taxation	**1.5**	5.4	6.8
Tax charge for the period	**49.5**	57.0	111.1

13. Dividends

Amounts recognised as distributions to equity holders in the period:	**Pence per share**	**6 months 2014 £m**	Pence per share	6 months 2013 £m	Pence per share	Full year 2013 £m (audited)
Final dividend paid in the period[1]	**8.4**	**125.7**	8.0	120.0	8.0	120.0
Interim dividend paid in the period	**-**	**-**	-	-	4.2	62.8
Special interim dividend paid in the period[2]	**4.0**	**59.9**	-	-	4.0	59.9
Total		**185.6**		120.0		242.7

Notes:
1 The final dividend for the year ended 31 December 2013 was paid on 15 May 2014 (31 December 2012: 11 June 2013)
2 There have been two special dividends paid since 1 January 2013, the first paid on 31 December 2013 and the second paid on 15 May 2014.

Notes to the condensed financial statements continued

14. Earnings and net assets per share, return on equity

Earnings per share is calculated by dividing earnings attributable to the owners of the Company by the weighted average number of Ordinary Shares during the period.

Basic

Basic earnings per share is calculated by dividing the earnings attributable to owners of the Company and the weighted average number of Ordinary Shares for the purposes of basic earnings per share during the period, excluding Ordinary Shares held as employee trust shares.

	6 months 2014 £m	6 months 2013 £m	Full year 2013 £m (audited)
Earnings attributable to owners of the Company	**175.6**	151.8	312.8
Weighted average number of Ordinary Shares for the purposes of basic earnings per share (millions)	**1,495.0**	1,496.1	1,495.4
Basic earnings per share (pence)	**11.7**	10.1	20.9

Diluted

Diluted earnings per share is calculated by dividing the earnings attributable to the owners of the Company by the weighted average number of Ordinary Shares for the purposes of diluted earnings per share 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.

	6 months 2014 £m	6 months 2013 £m	Full year 2013 £m (audited)
Earnings attributable to owners of the Company	**175.6**	151.8	312.8
Weighted average number of Ordinary Shares for the purposes of diluted earnings per share (millions)	**1,495.0**	1,496.1	1,495.4
Effect of dilutive potential of share options and contingently issuable shares (millions)	**9.9**	5.1	5.8
Weighted average number of Ordinary Shares for diluted earnings per share (millions)	**1,504.9**	1,501.2	1,501.2
Diluted earnings per share (pence)	**11.7**	10.1	20.8

Net asset value and tangible net asset value per share

Net asset value per share is calculated as total shareholders' equity divided by the number of Ordinary Shares at the end of the period. Ordinary Shares exclude 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.

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

	30 Jun 2014 £m	31 Dec 2013 £m (audited)
Net assets	**2,795.4**	2,790.0
Goodwill and other intangible assets	**(499.7)**	(500.1)
Tangible net assets	**2,295.7**	2,289.9
Number of Ordinary Shares (millions)	**1,500.0**	1,500.0
Shares held by employee share trusts (millions)	**(4.9)**	(5.2)
Closing number of Ordinary Shares (millions)	**1,495.1**	1,494.8
Net asset value per share (pence)	**187.0**	186.6
Tangible net asset value per share (pence)	**153.5**	153.2

Notes to the condensed financial statements continued

Return on equity

The table below details the calculation of return on equity.

	6 months 2014 £m	Full year 2013 £m (audited)
Profit for the period	**175.6**	312.8
Opening shareholders' equity	**2,790.0**	2,831.6
Closing shareholders' equity	**2,795.4**	2,790.0
Average shareholders' equity	**2,792.7**	2,810.8
Return on equity for the period	**6.3%**	11.1%
Return on equity annualised	**12.6%**	11.1%

15. Financial investments

	30 Jun 2014 £m	31 Dec 2013 £m (audited)
Available-for-sale debt securities		
Corporate	**4,898.5**	4,878.1
Supranational	**339.1**	365.7
Local government	**174.8**	134.5
Sovereign	**1,138.9**	1,399.5
Securitised credit	**461.5**	227.7
Total	**7,012.8**	7,005.5
Available-for-sale debt securities		
Fixed interest rate	**6,231.7**	6,468.4
Floating interest rate	**781.1**	537.1
Total	**7,012.8**	7,005.5
Loans and receivables		
Deposits with credit institutions with maturities in excess of three months:	**154.1**	435.7
Total	**7,166.9**	7,441.2

16. Cash and cash equivalents and borrowings

	30 Jun 2014 £m	31 Dec 2013 £m (audited)
Cash at bank and in hand	**192.0**	307.5
Short-term deposits with credit institutions	**654.7**	600.8
Total	**846.7**	908.3

The effective interest rate on short-term deposits with credit institutions for the six months ended 30 June 2014 was 0.47% (year ended 31 December 2013: 0.41%) and has an average maturity of 11 days (31 December 2013: 14 days).

The table below details cash and bank overdrafts for the purposes of the cash flow statement.

	30 Jun 2014 £m	31 Dec 2013 £m (audited)
Cash and cash equivalents	**846.7**	908.3
Bank overdrafts	**(75.8)**	(55.1)
Total	**770.9**	853.2

Notes to the condensed financial statements continued

17. Insurance liabilities, unearned premium reserve and reinsurance assets

	30 Jun 2014 £m	31 Dec 2013 £m (audited)
Gross insurance (including unearned premium reserve)		
Claims reported	**3,445.8**	3,636.4
Claims incurred but not reported	**1,979.1**	1,992.7
Claims handling provision	**124.3**	128.3
Total	**5,549.2**	5,757.4
Unearned premium reserve	**1,817.9**	1,818.7
Total	**7,367.1**	7,576.1
Reinsurers' share of insurance (including reinsurance unearned premium reserve)		
Claims reported	**(440.6)**	(467.5)
Claims incurred but not reported	**(531.3)**	(449.8)
Total	**(971.9)**	(917.3)
Unearned premium reserve	**(78.6)**	(93.7)
Total	**(1,050.5)**	(1,011.0)
Net insurance (including unearned premium reserve)		
Claims reported	**3,005.2**	3,168.9
Claims incurred but not reported	**1,447.8**	1,542.9
Claims handling provision	**124.3**	128.3
Total	**4,577.3**	4,840.1
Unearned premium reserve	**1,739.3**	1,725.0
Total	**6,316.6**	6,565.1

Notes to the condensed financial statements continued

17. Insurance liabilities, unearned premium reserve and reinsurance assets continued

Movements in insurance liabilities and reinsurance assets

	Gross £m	Reinsurance £m	Net £m
Claims reported	3,969.3	(397.8)	3,571.5
Incurred but not reported	2,153.9	(511.6)	1,642.3
Claims handling provision	163.8	-	163.8
Liability adequacy provision	4.3	-	4.3
At 1 January 2013	6,291.3	(909.4)	5,381.9
Cash paid for claims settled in the year	(2,852.1)	149.1	(2,703.0)
Increase / (decrease) in liabilities:			
Arising from current-year claims	2,894.2	(250.9)	2,643.3
Arising from prior-year claims	(583.9)	96.7	(487.2)
Effect of foreign currency exchange adjustment	12.2	(2.8)	9.4
Decrease in liability adequacy provision	(4.3)	-	(4.3)
At 31 December 2013 (audited)	5,757.4	(917.3)	4,840.1
Claims reported	3,636.4	(467.5)	3,168.9
Incurred but not reported	1,992.7	(449.8)	1,542.9
Claims handling provision	128.3	-	128.3
At 31 December 2013 (audited)	5,757.4	(917.3)	4,840.1
Cash paid for claims settled in the period	**(1,361.6)**	**85.9**	**(1,275.7)**
Increase / (decrease) in liabilities:			
Arising from current-year claims	**1,398.3**	**(130.9)**	**1,267.4**
Arising from prior-year claims	**(221.1)**	**(16.3)**	**(237.4)**
Effect of foreign currency exchange adjustment	**(23.8)**	**6.7**	**(17.1)**
At 30 June 2014	**5,549.2**	**(971.9)**	**4,577.3**
Claims reported	**3,445.8**	**(440.6)**	**3,005.2**
Incurred but not reported	**1,979.1**	**(531.3)**	**1,447.8**
Claims handling provision	**124.3**	**-**	**124.3**
At 30 June 2014	**5,549.2**	**(971.9)**	**4,577.3**

Movement in prior-year net claims liabilities by operating segment

	6 months 2014 £m	Full year 2013 £m (audited)
Motor	**(149.0)**	(291.9)
Home	**(33.1)**	(43.3)
Rescue and other personal lines	**(6.6)**	(9.0)
Commercial	**(23.8)**	(51.6)
International	**(5.5)**	(39.3)
Total ongoing	**(218.0)**	(435.1)
Run-off	**(19.4)**	(52.1)
Total	**(237.4)**	(487.2)

Notes to the condensed financial statements continued

18. Fair value

The Group's assets and liabilities measured at fair value are analysed in the following table by reference to the Group's fair value hierarchy.

At 30 June 2014	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Assets:				
Investment property	**-**	**-**	**259.7**	**259.7**
Derivative financial instruments	**-**	**37.5**	**-**	**37.5**
Available-for-sale debt securities	**1,133.7**	**5,879.1**	**-**	**7,012.8**
Total	**1,133.7**	**5,916.6**	**259.7**	**7,310.0**
Liabilities:				
Derivative financial instruments	**-**	**17.5**	**-**	**17.5**
Total	**-**	**17.5**	**-**	**17.5**

At 31 December 2013 (audited)	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Assets:				
Investment property	-	-	223.4	223.4
Derivative financial instruments	-	40.7	-	40.7
Available-for-sale debt securities	1,393.7	5,611.8	-	7,005.5
Total	1,393,7	5,652.5	223.4	7,269.6
Liabilities:				
Derivative financial instruments	-	19.3	-	19.3
Total	-	19.3	-	19.3

For disclosure purposes, fair value measurements are classified as Level 1, 2 or 3 based on the degree to which fair value is observable. The measurement bases remain unchanged for each level as set out on page 122 of the Annual Report & Accounts 2013.

The following table analyses the movement in assets classified as Level 3 in the fair value hierarchy.

	Investment property £m
At 1 January 2014	**223.4**
Asset acquired	**24.1**
Increase in fair value during the period	**12.2**
At 30 June 2014	**259.7**

There were no changes in the categorisation of assets and liabilities between levels 1, 2 and 3 during the period for assets and liabilities held at 31 December 2013.

19. Related party transactions

On 27 February 2014, RBS Group announced the completion of the sale of its remaining interest of 423.2 million Ordinary Shares in the Company.

RBS Group has now sold all its Ordinary Shares in the Company except for 4.2 million shares held to satisfy long-term incentive plan awards granted by RBS to Direct Line Group management.

Transactions with RBS Group in the six months ended 30 June 2014 were similar in nature to those for the year ended 31 December 2013. However, following the sale announced in February 2014 transactions with RBS Group are no longer related party transactions, as the related party relationship ceased from that sale.

Full details of the Group's related party transactions for the year ended 31 December 2013 are included on pages 166 to 167 of the Annual Report & Accounts 2013.

Directors' responsibility statement

We confirm that to the best of our knowledge:

1. the condensed consolidated financial statements have been prepared in accordance with International Accounting Standard 34 'Interim Financial Reporting' as adopted by the European Union;
2. the interim management report includes a fair review of the information required by:
    a. Disclosure and Transparency Rule 4.2.7R being an indication of important events that have occurred during the first six months of the financial year and their impact on the condensed set of financial statements, and a description of the principal risks and uncertainties for the remaining six months of the financial year; and
    b. Disclosure and Transparency Rule 4.2.8R being related parties transactions that have taken place in the first six months of the current financial year and that have materially affected the financial position or the performance of the entity during that period; and any changes in the related parties transactions described in the last Annual Report & Accounts that could do so.

Signed on behalf of the Board

Paul Geddes
Chief Executive Officer
31 July 2014

John Reizenstein
Chief Financial Officer
31 July 2014

Independent review report to Direct Line Insurance Group plc

We have been engaged by Direct Line Insurance Group plc (the "**Company**") to review the condensed set of financial statements in the Half-Yearly Financial Report for the six months ended 30 June 2014 which comprises the condensed consolidated income statement, the condensed consolidated statement of comprehensive income, the condensed consolidated balance sheet, the condensed consolidated statement of changes in equity, the condensed consolidated cash flow statement and related notes 1 to 19. We have read the other information contained in the Half-Yearly Financial Report and considered whether it contains any apparent misstatements or material inconsistencies with the information in the condensed set of financial statements.

This report is made solely to the Company in accordance with International Standard on Review Engagements (UK and Ireland) 2410 'Review of Interim Financial Information Performed by the Independent Auditor of the Entity' issued by the Auditing Practices Board. Our work has been undertaken so that we might state to the Company those matters we are required to state to it in an independent review report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company, for our review work, for this report, or for the conclusions we have formed.

Directors' responsibilities
The Half-Yearly Financial Report is the responsibility of, and has been approved by, the Directors. The Directors are responsible for preparing the Half-Yearly Financial Report in accordance with the Disclosure and Transparency Rules of the United Kingdom's Financial Conduct Authority.

As disclosed in note 2, the annual financial statements of the Group are prepared in accordance with IFRSs as adopted by the European Union. The condensed set of financial statements included in this Half-Yearly Financial Report has been prepared in accordance with International Accounting Standard 34 'Interim Financial Reporting' as adopted by the European Union.

Our responsibility
Our responsibility is to express to the Company a conclusion on the condensed set of financial statements in the Half-Yearly Financial Report based on our review.

Scope of review
We conducted our review in accordance with International Standard on Review Engagements (UK and Ireland) 2410 'Review of Interim Financial Information Performed by the Independent Auditor of the Entity' issued by the Auditing Practices Board for use in the United Kingdom. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing (UK and Ireland) and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion
Based on our review, nothing has come to our attention that causes us to believe that the condensed set of financial statements in the Half-Yearly Financial Report for the six months ended 30 June 2014 is not prepared, in all material respects, in accordance with International Accounting Standard 34 as adopted by the European Union and the Disclosure and Transparency Rules of the United Kingdom's Financial Conduct Authority.

Deloitte LLP
Chartered Accountants and Statutory Auditor
London, United Kingdom
31 July 2014