

Trading Update for the first nine months of 2017¹

7 November 2017

Continued momentum to meet targets

Paul Geddes, CEO of Direct Line Group, commented:

"We have continued the good momentum from the first half into the third quarter, and remain on track with our targets. In-force policies grew by a third of a million or 5.1% over the last 12 months in our direct own brands, across Motor, Home, Green Flag and Direct Line for Business, demonstrating the strength of the Direct Line Group business model.

"Our Motor, Commercial and Rescue businesses continued to trade well in the quarter while the actions we've taken on Home claims costs have started to take effect. We remain focused on our target loss ratios with our strong customer relationships, propositions and trading capabilities differentiating us in the competitive marketplace.

"We have continued to invest in our business and our people with the aim of delivering good value for our customers and good returns for our shareholders. As a result, we expect to achieve a combined operating ratio around the middle of the target range of 93% to 95% for 2017 and we reiterate our medium term targets."

Results summary

	Q3 2017 £m	Q3 2016 £m	Change
Gross written premium:			
Motor	462.0	431.5	+7.1%
Home	217.0	225.9	(3.9%)
Rescue and other personal lines	110.0	108.0	+1.9%
Commercial	118.2	117.5	+0.6%
Total	907.2	882.9	+2.8%
Of which direct own brands ²	606.6	560.0	+8.3%
	30 Sep 2017 '000	30 Sep 2016 '000	Change
In-force policies	15,775	15,736	+0.2%
Of which direct own brands ²	6,838	6,504	+5.1%
	9 months 2017	9 months 2016	
Investment income yield (annualised)	2.6%	2.5%	+0.1ppt
Investment return yield (annualised)	2.8%	2.7%	+0.1ppt

Highlights and outlook

- Own brands in-force policies grew across Motor, Home, Direct Line for Business and Green Flag year on year and quarter on quarter, particularly in the Direct Line brand.
- Strong momentum in Motor, with own brands policies up 5.5% compared to 30 September 2016.
- The actions taken on Home across claims and underwriting to mitigate the high escape of water claims inflation have resulted in encouraging improvements in claims experience.
- Annualised investment income yield of 2.6% is ahead of 2017 expectations due to portfolio positioning and some one-off benefits. Realised and unrealised gains net of hedging costs in the quarter were £3.4m.
- The Group is on track to achieve a combined operating ratio around the middle of the range of 93% to 95%, assuming a normal level of claims from major weather events.

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Notes:

1. Direct Line Group's Trading Update relates to the nine months ended 30 September 2017, and contains information to the date of publication.

2. Direct own brands includes in-force policies for Home and Motor under the Direct Line, Churchill and Privilege brands, Rescue policies under the Green Flag brand.

Business update

Direct Line Group (the “**Group**”) delivered a strong performance in the first nine months of 2017, growing total gross written premium 4.2% year on year, and continued to make progress towards its targets announced at the half year 2017.

In direct own brands, the Group maintained momentum growing in-force policies 5.1% since 30 September 2016, with sales through the Direct Line brand driving the growth.

Strong momentum in Motor

In Motor, own brands in-force policies increased by around 200,000 or 5.5% and premiums grew 10.0% compared to the third quarter of 2016. During the third quarter, trading overall continued to be strong and the Group maintained good retention rates on renewal business while there were some signs new business rate increases slowed in the market. On claims, damage severity remained at elevated levels, while frequency so far this year has been better than expected, although it is too early to call this a trend.

Keeping Home profitability on course

In-force policies in Home own brands increased by around 30,000 or 1.8% since 30 September 2016 and premiums increased by 1.2% compared to the third quarter of 2016. Rate increases, coupled with the underwriting and claims actions taken over the last six months to tackle escape of water claims inflation started to have a positive effect, while weather experience in the period was benign. The Group's partnership with Nationwide will end in December and the Group will stop earning premiums from this contract by the end of 2018.

Taking Rescue and Commercial brands forward

In Rescue, total in-force policies were broadly stable compared to 30 September 2016, as the growth in Green Flag was offset by a reduction in partner policies. In the third quarter, Green Flag launched a new advertising campaign to highlight its position as a challenger brand. In October, the Group agreed to renew its rescue services partnership with Royal Bank of Scotland for a further 5 years.

Within Commercial, Direct Line for Business continued to grow, with in-force policies up 7.9% since 30 September 2016 and premiums increasing by 11.2% compared to the third quarter of 2016. The performance of the Direct Line for Business new technology platform, launched in April 2017, has been encouraging and the Group is on track to launch its next product on the platform around the end of the year. In NIG, van insurance sales were strong, while the Group chose to give up some higher premium business which would have failed to achieve the Group's return hurdle.

Improving efficiency and investing in the future

The Group is investing in multiple initiatives and systems aimed at improving customer experience, supporting growth and increasing the efficiency of the business. This investment spans policy, pricing, payment and other related data and digital systems across the business, such as the successful launch of its eTrading platform for the Direct Line for Business unit in the first half of 2017. As previously indicated, the Group expects to incur capital expenditure of an average of £80m to £100m per annum in the period 2017 to 2019.

Whilst these initiatives are making progress, the Group has decided to rework some elements of the original capital expenditure already incurred, aimed at ensuring these initiatives achieve the targeted performance levels. The impact of this on intangible assets is being reviewed and this could lead to an impairment charge at year end somewhat higher than last year's level.

In terms of solvency capital, the balance sheet does not recognise intangible assets and any such impairment would have no material impact on the Group's capital position or policy.

Progress on the Group's initiatives is supporting its expectation for 2017 to deliver a business as usual expense ratio¹ lower than 2016 (24.0%).

Note:

1. Business as usual expense ratio of 24% in 2016 is the reported expense ratio (25.3%) excluding the impairment charge of £39.3m.

Outlook

The strong performance in Motor for 2017 gives the Group confidence that even with the potential impairment it expects to deliver a combined operating ratio around the middle of the target range of 93% to 95%, assuming a normal level of claims from major weather events.

In line with the Group's previously stated targets, the full year business as usual expense ratio is expected to be lower than 2016 (24.0%) and the commission ratio is expected to be significantly lower. However, the reported expense ratio may be around or above the level in 2016, depending on the outcome of the impairment review.

The Group now expects to achieve a 2.5% investment income yield compared to its previous expectation of a 2.4% investment income yield and continues to expect a return on tangible equity ("RoTE") of at least 15%.

Beyond 2017, the Group reiterates its target of achieving a 93% to 95% combined operating ratio over the medium term, assuming a normal level of claims from major weather events, supported by reductions in its expense and commission ratios, and the Group reiterates its ongoing target of achieving at least a 15% RoTE.

Financial update

In-force policies – Ongoing operations (thousands)

As at	30 Sep 2017	30 Jun 2017	31 Mar 2017	31 Dec 2016	30 Sep 2016
Own brands	3,805	3,761	3,691	3,642	3,607
Partnerships	188	205	220	231	233
Motor total	3,993	3,966	3,911	3,873	3,840
Own brands	1,783	1,770	1,764	1,759	1,751
Partnerships	1,499	1,534	1,593	1,619	1,638
Home total	3,282	3,304	3,357	3,378	3,389
Of which Nationwide and Sainsbury's	665	688	706	719	723
Rescue	3,635	3,663	3,676	3,646	3,621
Other personal lines	4,159	4,178	4,188	4,234	4,219
Rescue and other personal lines	7,794	7,841	7,864	7,880	7,840
Of which Green Flag direct	788	759	739	729	718
Direct Line for Business	462	452	441	433	428
NIG and other	244	248	245	242	239
Commercial	706	700	686	675	667
Total	15,775	15,811	15,818	15,806	15,736

Total in-force policies have increased by 0.2% since 30 September 2016 driven by continued growth across Motor and Home's own brands, Green Flag direct and Direct Line for Business. The growth across own brands was partially offset by reductions across the Group's partnership arrangements.

Gross written premium – Ongoing operations

	Q3 2017 £m	Q3 2016 £m	9 months 2017 £m	9 months 2016 £m
Own brands	441.2	401.1	1,222.4	1,095.4
Partnerships	20.8	30.4	64.0	86.4
Motor total	462.0	431.5	1,286.4	1,181.8
Own brands	114.3	113.0	307.5	304.6
Partnerships	102.7	112.9	297.6	324.5
Home total	217.0	225.9	605.1	629.1
Of which Nationwide and Sainsbury's	51.1	56.4	148.7	161.4
Rescue	43.5	46.3	127.1	128.2
Other personal lines	66.5	61.7	196.2	177.5
Rescue and other personal lines	110.0	108.0	323.3	305.7
Of which Green Flag direct	18.3	16.4	47.7	43.0
Direct Line for Business	32.8	29.5	92.9	82.5

NIG and other	85.4	88.0	293.7	296.9
Commercial	118.2	117.5	386.6	379.4
Total	907.2	882.9	2,601.4	2,496.0

Gross written premium of £2,601.4m increased by 4.2% compared with the first nine months of 2016 and by 2.8% compared with the third quarter of 2016, mainly driven by Motor. The Direct Line brand continued to perform well.

Corporate information

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

The Annual Report & Accounts 2016 is available at: www.directlinegroup.com

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