Q4 2017 Earnings Call

Company Participants

- Adam Richard Westwood, Chief Financial Officer, Secretary & Director
- Geoffrey Richard Carter, Chief Executive Officer & Director

Other Participants

- Alan Devlin, Analyst
- Andreas van Embden, Analyst
- Ben Cohen, Analyst
- Dominic O'Mahony, Analyst
- Iain Pearce, Analyst
- Nick Johnson, Analyst

MANAGEMENT DISCUSSION SECTION

Geoffrey Richard Carter {BIO 19078443 <GO>}

Okay. Good morning, everyone. Do we have the phone lines open? Well, it looks like we do. Perfect. Well, good morning. Very warm welcome to our very first results session as a Plc. Bit of a first for us as a company, and first with me and Adam, as well. So, if you can be nice to us, that'll be greatly appreciated. I was told this is an occasion you want a song and dance routine to start things off. So, I'm just going to flatten straight into the agenda.

So, we're going to do a quick look through the 2017 highlights. Adam will then go to the financial results in more detail. We'll then, going to stand a few minutes for those of you who don't know us so well just to talk through the highlights of the Sabre story and some of our key principles. And then, we'll summarize what we've said, and we'll take a look at the outlook for 2018, as well.

Adam and I will do most of the presenting. Adam, Finance Director over on the left. Also in the front row here, are Trevor and James, our Claims Director and Chief Actuary. They have been sort of growing to the organization. Frankly, I'm just a mouthpiece I've decided. So, any difficult questions could be heading their way later.

So, with that, let's go straight onto the highlights. I think we've put forward a very strong set of numbers for 2017, and importantly, we've done pretty much what we said we do during the IPO process. We maintained our position as amongst the very best loss ratio and combined ratio in the market. And you'll hear me say several times that that is our absolute number one priority above anything else we do. You can see the 46.5% loss ratio, 68.5% combined ratio, and our expenses are very well controlled at 22%. Adam can break that down a bit more later.

Resulted in a pretty strong profit for the year £53 million after tax, and that includes a 6% increase in our underwriting profit. Very pleasing return on our solvency capital of 92%. As you can see, we own almost all our capital in the year and a quite strong robust position.

At the IPO, I believe you all know we outlined an ambition, drop over 140% to 160% (00:02:12-00:02:19) So, the loss ratio, the combined ratio and the expenses resulted in a very strong profit for the year. In IPO, we outlined the design to operate in a solvency capital range of 140% to 160%. Previously, we're at 115% in our IPO days. Very pleased and that we're right at the very top end of that solvency capital range. We've been quite clear. We have no other ambitions, preserve this cash and to preserve it to shareholders. And you hear us tell several times this morning about the attractive dividend we intend to maintain this year and going forward. We also grew with 7%. And I think that growth was in a slightly complex market environment, which we'll come back and discuss a bit more later.

On the operational highlights, I will say our success actually comes from things that are not that exciting to talk about. As a management team, we really spend our time in the weights and we find our success to incremental evolutionary benefits. So, these are not very exciting or frankly I don't want to tell our competitors what we're doing. So, these are some very high level bits of operational success.

Clearly, the big thing for us was the IPO. We completed that in quite compact time scale and we were delighted by the responses we had from the investors around this. I think importantly the company hardly missed a beat while we were distracted as directors by doing an IPO and I think that's a testament to the fantastic start we had back in the office in Dorking.

We are really pleased with the new board. (00:03:49) PLC, and (00:03:53) half of them in the phone listening to me. We've got some very strong (00:03:56) who have now joined these complementary skills, and they've already given us a very constructive challenge and given us things to think about in the futures of PLC.

ITchanges. I'm pleased to say not a lot, actually. I'm not here talking to you about a complicated IT change. Really, our existing systems do everything we need them to do or can do most everything we need them to do. The only thing we're doing is lift and shift in our own infrastructure to allow a new cloud solution. We don't expect any impact on the business from that change.

We have redesigned our websites, the customer websites, if you look at the click and buy/sell websites. That's really to ensure we don't lose customers on the click-through journey from aggregators. So we were losing slightly to many customers on that journey (00:04:42) and purchase on that site. We've tried to improve our websites to enjoy a slightly high conversion.

I already mentioned our staff who did fantastically. We've got many members of staff who've been with us a very long time. We were delighted at the IPO (00:04:58) with £3,600 worth of shares, and many of our staff on a service basis got considerably more than that. Those staff are now burning trench for this. Those shares (00:05:12) years.

So, I think a strong year on numbers. Operational highlights really more the same, nothing too adventurous on the operational side. I think on that note, Adam, I'm going to hand over to you to talk in numbers.

Adam Richard Westwood {BIO 20481660 <GO>}

Thanks, Geoff. Good morning, everyone. So, as Geoff has already highlighted, we did have the strong financial performance during 2017, and I'll now introduce a little more detail to the numbers. If you've seen us on the road, you'll know that our P&L is incredibly straightforward, the advantages of running a focused business. We're single-line insurer, focusing on UK (00:05:52). So, we've already presented a single operating segment, and we've run a straightforward, debt-free balance sheet.

So here we are. Let's talk through some of the key features of this year's results. I'm going to start with our combined ratio as this one of our most important KPIs. Our combined ratio remains incredibly strong, having improved (00:06:15) year-on-year. This is made up of 22% expense ratio and an improved 46.5% loss ratio against 47.7% in 2016. There's a slide on our underwriting result later as I'll talk to you in more detail shortly.

Moving on to the rest of our P&L, premium income is up 7% year-on-year to £210 million with net earned premium up 3%. The growth in the top line, which is about where we expect it to be was somewhat counted by the increase in our reinsurance rates in July 2017. Our first renewal subsequent to the ultimate rate increase (00:06:52) last year, which I'll talk through further in the next slide.

With a combined ratio of 68.5% for the year against 69.3% in 2016, this has generated a 6% increase in our underwriting profit being our net earned premium less our claims and operating expenses. Profit after tax has been adversely impacted by investment losses during the year. Our investment portfolio is designed to be pretty low risk, almost entirely held in short-term UK government bonds has recorded a market value. So movements in interest rates and other factors can generate gains or losses. As the investments generate held to maturity, those gains or losses unwind as the bonds returns to par value.

We've presented our adjusted profit after tax here (00:07:38) after removing amortization and tangibles and specific one-off investments – costs, totaling £7.5 million principally relating to the December IPO. It then reflects the outcome of the group's operations for the period and provides a fair year-on-year comparison

The reduction in earnings per share reflects the additional transaction cost incurred in 2017. And we've got return on tangible equity out there as well you see as a key measure going forward. It's decreased in 2017 against the prior year, which is primarily due to carrying high capital base in 2017, which leads me on to our solvency position.

Basically, we've previously announced, we came into Q4 with a fair amount of excess capital, having elected not to pay an interim dividend in November, or a final dividend for 2017. As such, given the level of profit generation since our last dividend was paid in July, we built up a solvency capital ratio of 160% at year-end, which is at right at the top of our preferred range of 140% to 160%. The next few slides will explain on some of the points I've made.

This slide delves a little further into our strong underwriting result for the year. Our expense base remains predictable, with a fairly even mix of variable and fixed costs, meaning our expense ratio is broadly consistent year-on-year, coming down a little in those areas where we've achieved economy of scale while flexing with volume in line with our agile business model. I'll flag on expenses that we expect ongoing running cost of being a listed company, drive about 0.5% to 1% to our expense base beyond 2017.

A couple of factors drive our loss ratio down in 2017. Firstly, we priced in significant rise in reinsurance cost, price on our reinsurance renewal which was pretty placed on expiring terms at time of renewal in July 2017. As a reminder, we've run an excess of loss programs to limited exposure to large losses with a retention of £1 million. The increase in reinsurance pricing of just over 40% came in below expectation. So the rise in expense is well covered. Partly as a result of this, our current year loss ratio was 57% in 2017 down on its own. This is also a result of continuing focus on writing only business which yield acceptable profit margins and our caution are reflecting increased reinsurance (00:10:04).

We've also seen significant prior year releases in 2017 totaling around 10.5% of net earned premium, which is similar to last year. We still consider some of these releases to be exceptional as positive run off on our book claims from what turned out to be strongly reserve prior years, it drives up the expectation of redundancy within our claims reserve recorded in our (00:10:26).

I previously said that 2016 I considered around half of that year's prior reserve movements to be exceptional. I'll say a similar for 2017, noting that while the exceptional environment of these reserve movements cannot continue forever; these will rundown gradually over time. The release is a little larger than we have expected at Q3 due to better than expected claims runoff particularly with respect to (00:10:50) during Q4.

Our investment portfolio, which is worth around £280 million if you include cash is incredibly straightforward reflecting our core strategy that we aim to minimize downside risk and focus our efforts on generating returns from a highly profitable core business of underwriting rather than investment yield.

We see our investment portfolios fill, which allows us to drive our underwriting engine. The bonds held which are primarily UK government securities has led to maintain a maturity pattern equivalent to the runoff of our claims book. This means that on a regulatory basis, the valuation of the discounted claims reserves moves in tandem with the valuation investments limiting volatility of the group's regulatory balance sheet. This does however mean that the mark-to-market nature of the investments introduced some short-term volatility to the IFRS results where the claims reserves are not discounted.

For example, in 2016, following Brexit, bond values increased significantly (00:11:51) in 2017 along with some market movements resulting from the increase in base rates of interest. Overall, however, this slide shows the makeup of investment portfolio is conservative and limits volatility on a regulatory balance sheet.

The ability to generate strong profits from a relatively lean capital base is a core element of Sabre's strategy. Our capital requirement is driven almost entirely by underwriting risk, given the low risk approach to other areas of such investments. This is itself driven by the level of premium income and claims reserves held. Profit in 2017 and the decision not to pay our final dividend in respect to 2017 means that we're now at the top end of solvency ranges of 140% to 160% having ended 2017 at 160%.

We mentioned throughout the IPO that we have no need to hang on to significant levels of excess capital and have the option of returning this excess to shareholders in due course. As a reminder, during the IPO, we defined our dividend policies payout 70% profit after tax, with a potential special dividends as a means of distributing excess capital to bring our solvency coverage ratio to within our target range.

So to summarize what we delivered over the past year. We've delivered leading underwriting performance as demonstrated through the strength of various underwriting ratios. This has generated strong profits for the year allowing us to continue generating significant levels of organic capital whilst maintaining a low-risk balance sheet. Most importantly, we've continued to apply service cost (00:13:29) across the principles while opening the business to a wide base of new investors.

And with that, I'll hand back to Geoff, who'll give the reminder of the Sabre's story and outline for 2018.

Geoffrey Richard Carter {BIO 19078443 <GO>}

Thanks, Adam. I'll take that. Okay. I just want to spend a few minutes just going back across the Sabre story. I'm conscious that lots of your heard this before so I shouldn't be friendly if you look at the window, so jam with me for few seconds. Those of you haven't, hopefully this will start give you an insight into how we really do business.

I guess one of the key questions we tend to get asked is what makes us so successful, what's the secret sauce for our success. Really, the big picture is much more complicated than one secret sauce. We think we have an extensive jigsaw and metrics and skills and competitive advantages that are incredibly hard to replicate. These skills have been build up over a period of over 15 years and our strategy has been very consistent for a very long time. And we are very confident in the sustainable dependability of our model I would say in that year where attempted to convert.

The overall thing for us is focus. We do fairly limited amounts of things and we're obsessed about doing them very well. So we believe we are amongst the best at what we do compared to any of our competitors in the market. We have a complete focus on loss and combined ratio. Our absolute priority is maintaining a better than market combined ratio in line with our historical average.

So that one on this slide, which I hope you can see. If not, you can see in the pack (00:15:08) hopefully. And the key pillars of our success, we'll just talk to very briefly. It's a great pleasure at the IPO and one of my fellow CEOs that he open our IPO prospectus and read it cover-to-cover and learned absolutely nothing about how we do things, which I think was absolutely spot on frankly. So we're not attempting (00:15:25) that's too much.

So, the first thing is, and these are the things that differentiate us in many ways. A very broad underwriting footprint. James hates this price, but we believe it was the right price for every risk. It's our job to figure out what that price is. We are happy to quote for almost all risks in the market. That does mean we tend to bias our converted book towards a high average premium or specialist end of the market than perhaps all the mainstream insurers. Our average premium somewhere over £600 at the moment. Now, that's significantly different to perhaps other quoted peers.

A very disciplined actuarially driven strategy. We only have one actuarial team. We don't have any difference between the reserve and the pricing thing. We're completely synchronized between reserving and pricing. We don't interfere with that pricing in our distribution groups. Whatever the prices are the command of our actuarial team are the prices that get charge without fear or favor through any of our distribution groups.

(00:16:28) that is at in-house, agile pricing model. We don't use any black box technology. All of our pricing models are built internally, and therefore, very hard to replicate, I would say. A very expensive data set. We've got complete data going back probably to 1982. Certainly very consistent over the last 15 years to 20 years as we have touched a lot of customers and even more customers in that source slightly specialist end of the market. That gives us a unique advantage in the data we have aligned to that proprietary model, aligned to the very expert pricing too.

(00:17:01) ones are robust, I would say, and effective clients management team, including extensive focus on counter field. As you may know, we outsourced those (00:17:10) loss. We don't see tremendous value in booking car into garage and variable cost that comes with that. Our focus is on controlling personal injury cost and looking at identifying controlled in field cost, that what's we spend the majority of our effort.

A quite different distribution channel, I would say, too many peers, 70% of our business comes to brokers. We think brokers have been a tremendous advantage to us. I mean, the market many of them have very strong brands, many of them have expert custom management capabilities, and many of them are very expert at retail pricing and lifetime value models. We are able to sit behind a bunch of expert brokers in the market and allows us to focus on getting the net growth right rather than confusing our pricing model between retail and net pricing sophistication.

As Adam mentioned, it's a very efficient operating model. We outsource the customer-facing ends of much of our business. We don't have volume guarantees with those outsources. So, we can either shrink or grow the business, almost with a fixed cost. We're very happy with our outsourcing partners and they do a great job for us without any loss of customer experience, but we do see flexibility in volume management.

And as Adam mentioned, a very conservative approach to risk management. We believe we're expert at underwriting. We don't claim to be investment experts and we used prudent use of reinsurance to emphasize £1 million XOL (00:18:34) cover. Nothing else complicated in our reinsurance.

What does that lead to? Market-leading underwriting performance over a very long period. So, on 72 and a bit percent 10-year combined operating ratio, a very consistent strong capital generation picture. And we believe a controlled and attractive growth across the cycle. So, we believe we will grow by an average of 10% a year. That won't be every year. We grow at the right time in the market. We won't push growth in one year. If we do that, we'd undermine our underwriting returns or shareholder returns. So, we still very definitely believe there's strong growth over there but at the right time.

If we look at strategy, the very eagle-eyed amongst you will notice this is almost identical to the past Sabre story. I think in this case, the past is a very good guide to the future. The principles we have run for the last 10 to 15 years were exactly the same principles we intend to run for the foreseeable future.

What does this mean in terms of our targets on the right-hand side of that slide? We view 80% as our maximum combined operating ratio. We look to operate around our historical average, which you can see is 74%. 80% we see as a sort of (00:19:52) on our combined ratio ambition. Very strong cash returns. So we emphasized 70% base dividend plus specialist return surplus to shareholders at appropriate times. And again emphasized high-single-digit growth across the cycle would be our view going forward.

I think (00:20:15) spend a few minutes to talk about the market. Fair to say, probably a slightly more complicated market (00:20:22) on my first time standing here, kind of got going on. Clearly, the big thing last year was Ogden. (00:20:31) talking about that. We were very fast and very prudent, improving in rate. We (00:20:34) anticipated increased number in claims cost and the anticipated increase in the insurance premiums, and put through rate very quickly to cover both of those costs. If anything, we were a bit too prudent. I would let some air out of the tires we came past the half-year stage and got over insurance pricing confirmed.

The market obviously responded to (00:20:57) a variety of rates. If you look at the top graph here, which I hope you can see, you can see the price increase coming through Q1 into Q2. I would say, our view is at the very end of Q4 and into Q1, the market has become (00:21:12) more competitive. Why is that? I think rationally it's certainly driven by reduction in personal injury claims through the MoJ portal.

If you look at the bottom graph on this page, looking at the gold bar, you can see the step down in PI frequency compared to previous years and indeed the previous periods. So we believe there is an entirely rational reason for the market to become slightly more competitive as we came out the end of last year into this. I could speculate, people might also be fond of baking some of the assumed Ogden discounts and the same whiplash benefits. A bit hot off the press I guess. There's been announcements this week about both Ogden and whiplash and we can answer some of those in more detail maybe in in the Q&A session.

Our view is it's obviously great news. The ambition continues to bring in both of those changes. It does fall up to our headlines (00:22:03) in detail, and I think our view is detail is all important in understanding how this may run through. So we watch with interest how that might develop, but at this stage, we're not really calling too many benefits we're baking at this point.

So I think if we just – start to finish with some headline thought on our 2018 performance and how that change in market competitiveness may impact. As we come into the year, we looked carefully at reduction in PI claims and reduce our premiums gently through the first quarter in line with claims inflation, ensuring the price changes did not undermine our combined ratio targets. That resulted in a fairly modest dip in premiums coming through January and February.

The price changes are now fully embedded in, and I would say we've return to a run rate roughly in line with 2017, in the last couple of weeks nudging gently ahead of the 2017 position. We've benefited from those PI claims frequencies and I'd emphasized again that the changes we've made are entirely in line with our combined ratio ambitions.

I don't have a crystal ball on pricing. We're only on Q1. I wouldn't even try to call the market at this point. There's lots of moving parts. What I would say is that with our ongoing focus on underwriting quality, we are very confident on delivering strong underwriting result this year, possibly slightly better than our historic average. So, we're very confident on underwriting result this year.

Final comments, as we stated – (00:23:55) – as we stated we're looking very likely to continue to generate capital very strongly this year. We are very aware that dividend is an important factor for most of our investors. We're already at the top of our Solvency range and we've never claimed we needed to be right at the top, at most to be in the corridor of 140% to 160%. We've been very clear that we intend to return surplus capital to shareholders in appropriate time. I think given this, we are confident on delivering attractive dividend to shareholders in 2018.

And I think on that note, we will stop the presentation and go to any Q&A, if that's okay.

Q&A

A - Geoffrey Richard Carter {BIO 19078443 <GO>}

I think there is a roving – mic's going around. Alan? (00:24:44)

(00:24:45). Just a question on the outlook and particularly on the couple of questions of claims inflation. What do you think is driving the decrease in the frequency in the portal? What do you view is your kind of tool claims inflation we have in the severity and frequency in large bodily injury, et cetera? And if you could split out how important is the smaller BI in your claims frequency, and what you're seeing in the market, what do you think the market is assuming. Thanks.

(00:25:22) in terms about claims inflation generally. I think if we go overall, what do I think BI is going down, I suspect maybe some of the claims merchant companies have move to slightly easier targets. So, this could be a foreshadowing of the whiplash changes to come I think is my guess. So, we might already have seen some of that benefit coming into the market. I guess claims inflation is driven by a few things. We will see an increase in accidental damage claim (00:25:46). The autonomy in vehicles are going to make bumpers and windscreens more expensive to fix. Our coverage is slightly older than the average markets, that's (00:25:54) us too heavily at this point. I guess the big thing for us is (00:25:58). We go with the biggest factor of our (00:26:01). I think (00:26:05) we're fully in line with our historical average, 4% to 5%, somewhere in that sort of line.

(00:26:12) do you want to add to that or was that okay?

Yeah. I think there's a few moving parts here. I think obviously we've seen the (00:26:25) and reduction of frequency, but similarly the increased technological cost is pushing up (00:26:32) and third party damage severity. So, I think there are a few moving parts that are impacting stuff. But I think what I would say is we're monitoring that very carefully, and we're making sure we're reflecting any changes in pricing.

Yeah. (00:26:46)? So, Greg (00:26:48), I think you had a question first (00:26:50).

(00:26:56) valuable points. I'm sorry. (00:27:00) KBW. Three questions. One is just remind me using a USP for your Solvency II, I've seen you're on the standard model, do you have a tailwind that's getting more data and the weighted average between standard data and your data changes? Second question is retention rates. I wonder if you can just tell me what your retention rates are if they've changed, and quote exactly what statute quoting are you quoting something of, total book retention or retention in terms of only business that you recorded just so we understand exactly. And then the one thing that puzzles me, could you just describe the demographics broadly, age, sex, I know you can't do that anymore, points, et cetera, of your business (00:27:51) because I'm wondering why your loss ratio is volatile and so low. It must be something to do with the business mix.

Okay. I will try and pick out those questions. If you talk about retention first. Retention overall is about 30%. And I think probably an important factor here is that we target our first year of profit. So we're not dependent on retention rates to support our profit flow. We make pretty much the same profit on the first year and new business policies we do (00:28:24) policy. So we don't have a retention pressure in quite the same way as other people may have.

That does split between our direct and broker book. When we talk about retention, we talk about pure retention. We don't talk about (00:28:37) and back into us through different distribution routes. So if you look at a customer we had last year and this year, they may come to us through a different broker or come from direct broker which will (00:28:46) retention in that in the existing results.

On the demographic, we are perfectly happy to write anybody. We try and target a flat margin. You can obviously see our combined ratio, which means our margin is somewhat bigger than maybe other people we target. That means we're bias towards risk that are less attractive to the mass market. So that probably means we have slightly older cars. It probably means we have a slightly younger base. It probably means we have more people who have quirky feature or a combination of features so their risk make up. What I would say is that our data set (00:29:20) price any of those risks entirely hopefully.

USP, (00:29:28) you said an USP question?

A - Adam Richard Westwood {BIO 20481660 <GO>}

Yes. So, yes, we're on a standard formula. We have a USP only in respect, which is on to taking some specific parameter, and then the calculation only in respect of our number of personal reinsurance factor that we applied to our personal liability risk.

A - Geoffrey Richard Carter {BIO 19078443 <GO>}

(00:29:48) I think saw your question (00:29:51). Yeah. Okay. Nick?

Q - Nick Johnson {BIO 1774629 <GO>}

Good morning. Nick Johnson from Numis. Two questions, firstly on the comment about modestly decreased income in the first part of this year. If you could just say whether that is in any particular part of the book or whether it's across the whole portfolio in terms of risk categories, and perhaps also the leverage on whether the decrease income with the function of price, custom numbers or mix in terms of average premium size? And then secondly, question on reduced personal injury frequency on the small end of the scale. Does the 2017 loss ratio pick take that into account, and what assumptions you're making when giving us some reserve release guidance going forward on small PI frequency? Thank you.

A - Geoffrey Richard Carter {BIO 19078443 <GO>}

Okay. Sure. So, where do the premium decrease come from in the first couple of months? I think what we said during the IPO fairly clearly is if you guys are more competitive part of the market, we tend to lose a bit more from the fringes of the mass market, where we perhaps lose (00:31:01) pick out what we view as missed price risks in the mass market. So, I think, we probably lost slightly more in that mass market. What we haven't seen is any deterioration in the volume of business that we write in the more specialist end of the market. And I think we described during the IPO the sort of heartland and the more hinterland, our heartland looks not unaffected, more insulated than these changes.

What's driving the difference down? It's a combination of price on the conversion part of that and customer numbers. So, we've lost a bit of volume and we've lost a bit of premium, price mix. So, both of those things really just curved back the last couple of weeks.

On the PI frequency, I think, James (00:31:44) you could answer that one. You have the mic.

I mean, I think what I would say is our reserving philosophy maintains the same. We continue to be absolutely consistent in the way we reserve, and that's one of thing (00:32:00) business. So, I don't think we're showing anything different in there.

Now, Adam, in terms of the reserve releases?

A - Adam Richard Westwood {BIO 20481660 <GO>}

Yeah. So, 2016, we have reserve releases of around £10.4 million 2017, £10.5 million from the prior year. As I said in my presentation, there is an exceptional element to that as those reserve releases run down the sort of normal run rate over time. The expectation was that they may run down quicker than they have done or at least that they've slightly more to come out than we initially thought. So, we'd expect a small decrease in reserve releases next year.

A - Geoffrey Richard Carter {BIO 19078443 <GO>}

John (00:32:48)?

Q - Ben Cohen {BIO 1541726 <GO>}

Thank you. Ben Cohen at Investec. I had two questions. Firstly on pricing year-to-date, could you maybe make some comments sort of following on from Nick's question in terms of what you've done versus the market? How much you are prepared to put in for the claims trends that you're seeing? And secondly, I probably missed it in the release or whatever, but have you said there's two – the benefit that you expect from the change to built-in discount rate. I'm not sure the extent to which that has been set, but some range around that would be helpful. Thanks.

A - Geoffrey Richard Carter {BIO 19078443 <GO>}

Yeah. Sure. I think pricing year-to-date, I think – as I don't want to give our precise numbers, what I would say is that our combined ratio hasn't changed at all which as a result of that. So while we brought prices down, we don't believe that's changed our – the impact on our combined ratio. We would not undermine our pricing position from doing that. I clearly don't want to give precise numbers out on that for obvious reasons.

Ogden. Ogden is an interesting one for us, and that we have quite a low reinsurance potential. So actually, we didn't take too much pain from the Ogden change, nor will we get too much net benefit. The real factor for us is what does that do to our reinsurance pricing. As Trevor (00:34:03) said, prices were up by 40% last year, (00:34:07) Adam, you said that, largely driven by Ogden. Our renewal is the end of June, start of July. So the debate for us really is how we can work with our reinsurers to establish a long term impact of Ogden and what does that do to our reinsurance price. Reinsurance is a bigger factor for us than the net position.

Q - Iain Pearce {BIO 19522835 <GO>}

Hi. Iain Pearce from Berenberg. Just on pricing and claims inflation, so it sounds like you've taken a bit of pricing in sort of first bit of this year. Do you still expect claims inflation to be running in short of long term 3% to 4% range. Does that sort of indicate that you've been overearning in the second half last year and you expect that to sort of earn through throughout 2018? And then just on broker behavior, as we've talked about some more competitive dynamics in the market, obviously, you sort of price it from an underwriting basis by using your brokers being a bit more aggressive in terms of their retail price optimization strategies and is that any benefit to you?

A - Geoffrey Richard Carter {BIO 19078443 <GO>}

Yes. So I'll take the second one while you think about the first one, Adam. I think on broker behavior, we always say different brokers feel more or less aggressive at different points in the cycle. We generally view our distribution as agnostic. We like all our brokers equally, and we don't vary our prices by the size of the book that we have them through them. We'll vary the price by the cost to do them with that broker and their long term performance but not because they're big or small. So I think different brokers are competitive at different times. It can move on a weekly basis, so there's nothing fundamental shift in there.

Adam, do you want to pick up second point?

A - Adam Richard Westwood {BIO 20481660 <GO>}

Yeah. Sure. So we mentioned we brought prices down a bit beginning of this year. The way we price generally is very cautious, so we will see a trend in the market. We'll work out what that's doing to overall cost, and then we'll adjust our prices accordingly. And therefore there's generally a delay between the thing happening and the price reduction. And obviously, while that delay is occurring, you are essentially writing a slightly better loss ratio than you might be otherwise be doing. So that's the general trend.

Q - Iain Pearce {BIO 19522835 <GO>}

Yeah. That's helpful.

A - Geoffrey Richard Carter {BIO 19078443 <GO>}

So, Andreas, I think you have – you're certainly in my eye line first anyway.

Q - Andreas van Embden {BIO 1795530 <GO>}

Andreas van Embden, Peel Hunt. Could you maybe comment just purely on policy growth in Q4 and into Q1. You mentioned you loss some volume in the mass market, but yours is stable on non-standard. As Q1 progressed, did you see volume pick up towards the end of the quarter and do you expect policy growth to be more or less in line for the full year with sort of the trends in 2017? Thanks.

A - Geoffrey Richard Carter {BIO 19078443 <GO>}

Yeah, I mean, as a rule, we don't get too obsessed by policy count. We tend to look at GWP rather than policy numbers as being our key KPI. Our policy numbers are still hovering around the mid-300,000s. They went down a bit, fairly early bit, and they've come back up a bit in the last few weeks. We don't really obsess about where that customer number goes to (00:37:05) some of the GWP number. So, yeah, it went down a bit and it's coming up (00:37:10) a bit over the last couple of weeks.

Q - Dominic O'Mahony

Thank you. Dominic O'Mahony from Exane BNP Paribas. So, three questions, two sort of on guidance this year, and then one to the more macro long term. So the first is, in terms of your combined ratio guidance for 2018, you were suggesting sort of a similar, possibly even a better number for this year. Is that net of BYD or is that a current year number given the commentary around the potential reduction in BYD? The second question is, does that imply that, actually, the weather that we've seen in the first year hasn't really affected claims in terms of (00:37:57).

And then, in terms of the more macro longer-term picture, you were talking about sort of measured growth. Quite clearly, there's limit to what you can give away here, but what are the macro trends that you see acting as a tailwind for you in that respect? If I think about your heartland as you describe it, what do you see in terms of development of people who have (00:38:22) features and is that helpful in terms of getting that growth? Thank you.

A - Geoffrey Richard Carter {BIO 19078443 <GO>}

Yeah. Sure. Let's just go through those in reverse order. (00:38:29) you can think about the first (00:38:32). I think in terms of growth, we invest heavily in data and analysis. The more of those that we get, the more of those we generate, the more opportunities we find to define our pricing. I think it's fair to say (00:38:42).

There's always new people coming into the market. We've don't really see a massive reduction in the number of drivers, we tend to insure slightly older cars. We're not really seeing the impact of what (00:38:54) thinking of Uber, (00:38:57) public transport. If you live out outside London, we don't see that reduction in car ownership really impacting. We don't see any headwinds to that growth.

So I think we see we can continue the move gently into the mass market where we find more data (00:39:12) as we find our pricing. We continue to work out (00:39:16). We have very high profitability. We will still miss a few points of credibility from the aggravated journey. We spend a lot of time trying to work out where those customers regarding how we can get a hold of them. So, I think we see there were some in the mass market, some in the – or more mass market, some in the specialist market, some are just want to find those gaps, but we're still not getting close (00:39:37).

And I think we also look – we will look at sort of gentle product expansion. What we won't be doing is launching our fintech (00:39:44) to commercial or (00:39:47). I think if this got or sort of wheels on an engine then we think our skills are quite transferrable to that. We already have a very small part of our portfolio is bank, small banks (00:39:53). We've not really unleashed our full capabilities on that yet so we see bank being an opportunity.

Of course similarly we see taxi, we do a ton of amount of taxi. Again, we really push that taxi hard, and I think we see lot of very interest (00:40:07) business starting up. So, in short (00:40:11) fintech-type businesses really focused on distribution. We are not seeing brand pressures. We're very happy to sit behind the right distribution partners, and we had very regular conversations. Everyone's looking for us to support their different distribution models.

We are quite cautious and when we do that we won't do anything that we think that undermine our returns, but we see opportunities there in sort of the new generation of distributors coming through. The second one was about weather. That's a much quicker answer (00:40:40) impact (00:40:40) what I think.

(40:41).

Yeah. And that – hopefully I was giving you a chance to think about (40:49).

A - Adam Richard Westwood {BIO 20481660 <GO>}

I think the answer is actually pretty straight forward. We always intend to write to our target loss ratio. So, our current year result would be reflective of that a little more uncertainty in the current year. So, generated current year result is slightly higher than the target ratio.

When Geoff talks about commodity ratio over the year he's talking about financial year loss ratios that would include the element of prior year development which may well include both sort of normal business as usual runoff and exceptional releases.

A - Geoffrey Richard Carter {BIO 19078443 <GO>}

Anything else that was not covered?

Just on excess of loss, what actually is your premium? And in terms of retention, are you reaching all the layers above £1 million (00:41:43)?

No. It's completely straightforward. It's completely unlimited over £1 million.

Premium?

We declared the premium in the results.

(00:41:53)

Yeah. It's a real number.

A - Adam Richard Westwood {BIO 20481660 <GO>}

Yeah. It's about 9.4%.

A - Geoffrey Richard Carter {BIO 19078443 <GO>}

Alan?

Q - Alan Devlin {BIO 5936254 <GO>}

Yeah. Thanks. Alan Devlin of Barclays. Just a couple of follow-up questions. Just one on the – you mentioned the re-entrance causes the – what you're more focused on, the 9.4% expected to come down given in (00:42:18) going to your renewals? And then secondly, could you remind us what kind of normalized investment income assumption should be if there's no mark-to-market move? Thanks.

A - Geoffrey Richard Carter {BIO 19078443 <GO>}

(00:42:30) on the fund, clearly, I expect the insurance (00:42:32) to come down as a result of autumn. Let's be clear. Clearly, there's – we said there's very positive messages coming around (00:42:42) about the detail to the work. So, we've got a very strong relationship with all our insurance panel. We'll be working this through within – probably over the next two or three months. (00:42:51). So I don't to pre-guess where that might go. On investment, Adam?

A - Adam Richard Westwood {BIO 20481660 <GO>}

Yeah. I mean, it's loan. As an investment income, as I said, it's a very, very conservative investment portfolio. I wouldn't want to go far above sort of 1.3%, 1.5% something like that (00:43:11).

Q - Alan Devlin {BIO 5936254 <GO>}

The expense ratio, I noticed it ticked and I assumed that it ticked up and then I assumed that might have been volume related in terms of overheads. But in terms of your CapEx program going forward, I wonder if you can just sort of give us an idea facing technology on race? And just remind me, do you account within the expense ratio or do you have some kind of below-the-line amortization going on?

A - Geoffrey Richard Carter {BIO 19078443 <GO>}

Yeah. First of all, I'll talk about CapEx a bit first. We don't really have any big CapEx budgets on the horizon. We're perfectly happy with our existing system. The move across to the hybrid cloud is basically pound-for-pound with the cost of running it internally. That makes no meaningful difference to us. We own our own buildings. We have room for expansion in those buildings. So, actually, we don't have any meaningful big CapEx budgets on the horizon at this moment. The expense ratio for last year?

A - Adam Richard Westwood {BIO 20481660 <GO>}

Yeah. That's fair. I think the expense ratio for last year pretty much in line, ticked up a little bit. Part of that was due to an increase in levies essentially, which are incurred on a sort of recent basis. So, generally there's a lag for them versus the earning through of our premium. Otherwise, some of the variable costs obviously moved in line with the size of the business.

A - Geoffrey Richard Carter {BIO 19078443 <GO>}

Do you have any final questions? If not, I think we'll quickly -before I put my foot in on somewhere. I think I got away with it so far. So, thank you, all, very much for your time. Any questions, me and Adam are completely available for any follow-up calls you might want to have. So, thanks very much, and thank you on the phones.
