Q2 2017 Earnings Call

Company Participants

- Jonathan Stanley Hill, Group Chief Financial Officer & Executive Director
- Lance Henry Batchelor, Group Chief Executive Officer & Executive Director

Other Participants

- Ben Cohen, Analyst
- Blair Stewart, Analyst
- James A. Shuck, Analyst
- Nick Johnson, Analyst
- Ravi Tanna, Analyst

MANAGEMENT DISCUSSION SECTION

Lance Henry Batchelor {BIO 6884486 <GO>}

Okay. Good morning everybody. Welcome to Saga's Interim Results for the six-month period that ended July 16. As you probably have worked out by now I'm Lance Batchelor, the CEO of Saga. And to my left is Jonathan Hill, the CFO. We're going to do a bit of a double act and then we'll do a Q&A at the end of our session.

It's amazing how time flies, it's been 2.5 years since we IPO'd, this is our fifth set of results as a listed company. And for the fifth time, Saga has delivered a really robust set of results. Profits are up again, and I'm particularly pleased with our strong cash generation, which has a focus on its customers, in fact we probably know about the needs of the over 50s than anybody else, but we're always looking for ways to improve and to push our insights harder, and there is a significant opportunity for us to take our knowledge of our customers a stage further, to make the most of the great brand awareness that we've got and the customer loyalty that we've got.

And over the last six months or so, we've been doing a significant amount of work within our database of 2.7 million customers to segment it in a more granular way than we have ever done before. So we now have a much better view of what segments there are within our database, where we really make our money, exactly who our high-valued customers are, what journeys they traveled as they became high-value customers, what products and services they buy from Saga and perhaps most importantly, we've got a better feel for what a potential high-value customer looks like than we've ever had before. That means we can focus our marketing spend on attracting the right kind of customer and develop the right kinds of products for them.

So, in the months and the years to come, our deeper understanding of the customer base is going to allow us to save money on what could have been wasted marketing, to spend that money on really tightly targeted acquisition of potential high-value customers. Our product development will be directed at meeting the needs of high-value customers and potentials. And we'll be looking for ways to say thank you to our loyal customers to meet more of their needs.

Now, in one sense, all of this is what we've always done. But modern data mining techniques and marketing tools, like Adobe Analytics and Adobe Target and Adobe Campaign, allow us to create much smarter and more targeted offers than we've ever been able to create before.

This is probably the most exciting and the biggest potential project going on at Saga right now. Yes, we're building a wonderful new ship. And yes, we have an effective motor panel up and running. And yes, we continue to pilot a home care solution and to develop a fresh strategy for the money sector looking forward. But getting really close to our high-value customers is a major opportunity for Saga.

Now, I'm now going to hand over to Jonathan who'll take you through the numbers in more detail. Thanks.

Jonathan Stanley Hill {BIO 16892113 <GO>}

Thanks, Lance, and good morning, everybody. Looking on, it's very pleasing to be able to report another strong set of results for the first half of 2016. We delivered a solid performance across the group, with PBT on an underlying basis up by 3.9%, excluding those derivative movements, and up overall by 8.5%. Continued strong cash generation has allowed us to further deleverage from 2.4 times at this time last year to 2.3 times at the year-end, and 2.2 times at the half-year point.

Our strengthened solvency position gives us confidence of further deleveraging in line with our medium-term target. Based on this performance and our future expectation for the business, we have done what we said we were going to do, and we've increased our dividend at the interim point by 23% to £0.027.

Now, looking at the group P&L. Revenue from continuing operations did decrease by 8.6% to £437 million, reflecting the accounting impact from the introduction of the quota share arrangement in motor insurance. And I'll cover that in a bit of detail later on in the presentation.

Excluding this accounting adjustment, revenue would have been up by around 2% on a comparable basis.

Trading profit was flat in H1 against the comparable period, but this is after the profit impact of the scheduled maintenance for the Saga Sapphire, which costs us around £5 million in profit in the first half of this year. Finance costs fell significantly as we better managed our facilities, as well as some reductions in LIBOR.

These lower finance costs were a key contributor to this 4% underlying PBT growth, excluding these derivative gains. And then with the benefit of these derivative gains, we end up at an 8.5% increase in PBT. These fair value gains and derivatives relate to hedges, where hedging accounting cannot be used, particularly on the forward hedging of the fuel for our cruise ships. Profit after tax increased by 12.8% with H1 in the prior year incurring a £3 million loss on discontinued operations.

Our core Insurance and Travel businesses have performed strongly across the first half delivering an underlying trading profit growth of 2%. We have done this despite seeing variable market conditions across our business. For example, we have benefited from the hardening of premiums in the motor insurance business, that have been impacted in the same way as everyone else by the tough market conditions in home insurance. This performance is proof of the Saga model as we benefit from the wide portfolio of businesses and our ability to drive profit across the group even with differential market conditions.

You will notice that the Insurance comparative did change slightly. At the year-end, it was noticeable that year-on-year expenses have moved materially by segment. And having reviewed the basis of allocation, we have moved from what was a more revenue-based allocation to one that's more activity-based, and therefore, going forward, that expense allocation should be more accurate and should be less volatile between segments. A breakdown of this movement is included at the back of the interim statement. Clearly, the overall profit in the Insurance business remains the same. This is just about getting better on those allocation of expenses on an ongoing basis. I will now look at each of the businesses in turn.

In motor, trading profit increased by 10%, benefiting from the earn through of the higher motor rates combined with strong claims experience, as well as from the introduction of the motor panel and the first full six months of Bennetts. Motor revenue decreased by 23% to £120 million from that quota share impact and I'll cover that later, partially offset by the trading in Bennetts business that was acquired on the 1st of July of 2015.

Core policy numbers increased during the period primarily from the inclusion of Bennetts for that six-month period. And excluding Bennetts core motor policies grew by around 2%. Overall the motor market remains highly competitive and whilst we saw rate rises, strong rate rises year-on-year in Q1, these will somewhat come off in Q2 and slowed significantly. However, we have maintained our focus on achieving the right balance between growing customer numbers and delivering profits.

So, this slide shows the motor underwriting business excluding the effects of the quota share which I'll cover on the next slides. This is trying to look at the business on a purely comparable basis. We've had a very strong six months in motor underwriting with the underlying profit from the core underwritten motor business increasing by 15% to £57.3 million. That was (8:43) about 7.3% improvement in the pure combined operating ratio. This improvement is due to two key factors. Firstly, that benefited the rate increases combined with our strong claims experience has improved the pure underwriting profit. And secondly, we had some benefits from the introduction of that arrangement fee.

Net earned premiums were lower by 7% due to two factors. Firstly, the introduction of the panel has led to a lower number of underwritten policies and lower average premiums. The lower premiums reflect the fact that a larger share of the higher-risk business is being taken by third-party underwriters, which is exactly what we expected when we set the panel up. Secondly, we have the introduction of the arrangement fee which is reported in other income.

Okay. So, this table shows the accounting impacts of this funds with our (9:44) quota share arrangement. I'm going to say while the accounting impact on the income statement of the quota share is significant on a line-by-line basis; the important number on this page is the net impact on the trading profit of £0.9 million. As guided at the time of prelims, the full-year impact of this quota share arrangement on profit is roughly 1% of overall profitability.

For comparability purposes, we have calculated these ratios at the bottom including both net earned premiums and other income given that change in the recognition of the arrangement fee. This quota share arrangement will allow us to gradually release capital from AICL supporting the continued reduction in our debt ratio and our progressive dividend policy.

In terms of the reserve releases, continued favorable claims development experienced during the six months to 31 July 2016 has enabled us to maintain a consistent level of releases in the first half with no deterioration in the reserve margin. This is being driven by large and small PI, personal claims primarily, resulting in consistent overall motor releases in the first half of this year versus first half of last year of around £40 million. The releases in the second half of the year are expected to be lower than the comparable period last year.

On Solvency II, we remain extremely well-capitalized. And as expected, our coverage ratio has increased at the half-year point as a result of the reduced SCR due to the impact of the quota share and also the reduction in best estimates. This positive movement supports our decision to enter into this agreement, this quota share agreement as we continue to move towards a more capital-efficient, broker-orientated business model. And the strong position also supports our ongoing deleveraging in H2.

Okay, on home insurance, in line with our competitors, we reported the market conditions continue to be highly competitive with no evidence of premium inflation. Revenue decreased by 6% due to a reduction in the profit share in our New India arrangement and also a small fall in our average premium compared to the first half of last year. With inflationary increases in operating expenses, this resulted in trading profit decreasing by around £4 million to £30 million.

While the panel continues to perform strongly, we believe that we are operating very efficiently. And therefore, margin improvement, as Lance has said, will be driven less by the net rate decreases coming through.

Revenue in other insurance lines grew at £47 million with increased travel insurance volumes and improved margins on private medical. Trading profit was £1.7 million higher with strong PMI performance. And also, the prior year, we had the impact of the marketing on Saga Legal Services. This is partially offset by increased costs in line with increased travel insurance volumes.

The Travel business has another really strong six months of trading offset by that scheduled maintenance of the Saga Sapphire cruise ship. In our three tour operating businesses, revenue has increased with a shift in average revenue per passenger upwards as that product mix continued to shift to more long-haul and third-party cruise products. And actually, our profit across the tour operating business, as you see in the interim's release, has increased to £8.5 million from £8.3 million.

In cruising, the Saga Sapphire was out of operation for that scheduled maintenance for a total of 63 days between April and June, which impacted both obviously the revenue and the trading profit. As a result, cruising revenue fell by 12% to £37 million. And trading profit decreased by around £2 million in cruising to around £0.50 million. But excluding the impact of that, both our revenue and our profit would have been up both in cruise and certainly across the whole travel business.

In our Emerging Businesses, these obviously include our Saga Money and our home care business. Revenue was relatively consistent with the prior year at £14 million. The overall trading loss was slightly up, but that really reflects the investment both in Saga Investment Services and our healthcare business.

Our cash flow performance during the first half of the year continued to be strong with the Group achieving an available operating cash flow of £97 million equating to 73% of trading EBITDA. Cash flow did decrease compared to the first half of last year by £42 million. Firstly, there was a lower payout from our restricted business as the travel business obtained more cash to pay the deposits on the new ship.

Secondarily, working capital in the first half of this year is much more normalized and is much more in line with the full-year expectation. And thirdly, the first half of this year also includes the payment to Acromas of £7.6 million for those tax loses that we have purchased from them, the benefit of which was recognized in last year's tax expense. Overall, this means the cash flow in the first half of the year was more consistent with what you should expect to see for the full-year outturn.

So at the interims last year, we obviously announced this net debt-to-EBITDA target of 1.5 times to 2 times for the medium term with the dividend payment ratio at 40% to 60% of net income. We then moved that ahead at the time of the prelims to 50% to 70% really reflecting the benefit of what we expected to come from the quota share arrangement.

And given our continued strong cash generation and our Solvency II position, we remain comfortable with our medium-term debt target range of 1.5 times to 2 times, net debt to EBITDA. And you should expect that distribution to shareholders will be by way of ordinary dividends in line with our guided dividend.

So stepping back a bit, 18 months into business, the business really is in great shape. However, it is important that we continue to work to ensure the efficiency and the effectiveness of our systems and processes for the future.

To this end, we have decided to modernize our retail brokers' insurance sales and administration platform over the next three years. The implementation of this new efficient and flexible platform will help to future-proof our activities whilst considerably improving the customer experience. The cost of this will be covered in our usual run rate of CapEx expenditure.

We're also in the process of introducing a new claims system which will improve the process for claims for customers as well as reducing our costs associated with claims handling. And this system is actually currently in advanced test phase.

We've started the reorganization of the back office of our Travel business to improve both efficiency and reduce our costs in that business. And we have put in place an enhanced group procurement function to drive cost efficiencies and procurement best practice across the Group.

So given the strong trading performance in the first half of the year, the Group still expects to continue to deliver profit growth in the core businesses. After continued investment in our emerging business and with the benefit of lower finance costs, we are confident of delivering growth in PBT of between 5% and 7% for the full year.

With our cash generation attributes and our enhanced solvency position, we are confident that we can deliver on our dividend policy while continuing to reduce our debt ratio towards our medium-term target range of 1.5 times to 2 times.

Thanks. And I hand back to Lance.

Lance Henry Batchelor {BIO 6884486 <GO>}

Thanks, Jonathan. So I could read these out to you, but I hope that you'll be pretty familiar by now. Those five points summarize what Saga has done in the last six months. And as I say, I hope they are very consistent over the two and a half years that we've been talking to you.

What do they mean to me? What they mean is we have a strong and a growing core business. It means that we're generating lots of cash. We can pay the debt down and we can invest in the future whilst supporting a dividend policy which is progressive within the payout ratios that we announced back in April.

So thanks very much for your attention and time. I will now open it up to questions. We don't have a mic to hand around. There are roof mics in here. So I think what we'll do is ask you to raise your hand. And then when I pick you, if you could state your name before asking your question, that'd be very kind. James. State your name, James.

Q&A

Q - James A. Shuck {BIO 3680082 <GO>}

Hi. It's James Shuck from UBS. I have three questions, please. Firstly, just on the – this is the first year you've had the – or the first period you've had the (19:43) shared. So I'm just interested to know what the profit share commission was that was booked in the first half of the year as in what line I see that coming through. And then the second question is around – on page 11 on the broking/other, so the revenue that's shown in here, £32.8 million at H1, that includes contribution from Bennetts. So could you just separately identify within that £32.8 million, what comes from Bennetts and what exactly comes from the motor panel, please?

And then thirdly, I guess the question is around the modernization over the three-year period. Now, you're quite clear that that's running within your normal capital expenditure for the year. And I guess my question is kind of what is that normal capital expenditure with any one year. In previous periods, we've asked about the potential for modernization. And you've been quite clear that you think that there is no big investment that's needed and that seems to be consistent with what's happening here. But nevertheless, it is a kind of step up, I would suggest, from what you were initially planning. So any insight into that capital expenditure and how long it's likely to drag on (21:03) would be helpful.

A - Jonathan Stanley Hill {BIO 16892113 <GO>}

And in answer – well, I'll take those three. So you -

A - Lance Henry Batchelor {BIO 6884486 <GO>}

(21:08).

A - Jonathan Stanley Hill {BIO 16892113 <GO>}

Sure. In terms of your first question, where is the profit share commission shown; you'll find it in the release on page 12 in the other income line and the quota share there. So it's clearly identified there. And the second question is that Bennetts makes up just over £10 million of the revenue within the broking and other.

And the third point, I think there's a broader point here. Every business has an ongoing requirement to evaluate that its systems are fit for purpose at any point given the developments that are going on in the worldwide market of technology and how that relates to its various businesses. As you'd expect, we do that across our businesses on a regular basis to ensure that we have the right systems for the future and where we are, how (22:03) the system which can be improved both in efficiency and effectiveness terms, that we're moving towards that right system. So I don't think anything we've said in the past – we don't see a big whizbang requirement to suddenly spend tens or hundreds of millions. We are looking at this as a natural evolution of a system which has been in the business for, I think, around...

A - Lance Henry Batchelor {BIO 6884486 <GO>}

20.

A - Jonathan Stanley Hill {BIO 16892113 <GO>}

...20 years.

A - Lance Henry Batchelor {BIO 6884486 <GO>}

Yeah.

A - Jonathan Stanley Hill {BIO 16892113 <GO>}

And it's not illogical that at a certain point, we were going to come back and face into that and look at a new system. So we are in advanced discussions with a couple of parties in terms of finalizing a position going forward over the next three years to put in place a new system. So your question then was around underlying. I think you can see that we've got a relatively consistent run rate of CapEx across the business. It moves up and down in the £5 million to £10 million (22:59). I am comfortable that what we have guided in terms of our deleveraging takes into consideration what we need to spend across the business on the assets that we have and on improving the systems that we need in the business.

Q - Nick Johnson {BIO 1774629 <GO>}

Morning. Nick Johnson from Numis. Just two questions, please. First of all, on the motor footprint. I'm just wondering if there's been any change at this stage in the ratio of customer inquiries to sales as a result of the panel coming online. I think previously, you said that you would kind of (23:40) three out of four customer inquiries, but you weren't able to quote in-house. I'm just wondering if that metric is beginning to change due to the panel being there. And then secondly, in terms of motor broking profitability, which is up sort of I think around 20% in the period against an increasing core broking customers (24:04) travelled I think. I'm just wondering if the profit per customer has a new run rate now or is that some...

A - Jonathan Stanley Hill {BIO 16892113 <GO>}

I'll cover that in a sec. Yeah.

Q - Nick Johnson {BIO 1774629 <GO>}

...sure.

A - Lance Henry Batchelor {BIO 6884486 <GO>}

Well, I'll take first of that. So we don't publish the (24:18) percentage or the ratio of inquiry to sales. But what I will tell you is that the panel is working pretty well for us. I will also say that most of the panel volume is on renewals. And we would expect that to be the case (24:32) customers that we already have that we know well and where those panels will see their (24:38). But what's interesting is you see them, as we expected, taking the higher-risk profile customers because Saga's core competency is around the lowest risk customers. But we always believed and are now seeing that the panel is taking the higher risk profile in relative terms – compared to the whole market, they're still pretty low risk – but they're the higher risk ones on our panel.

And obviously, that means we either make more margin if we choose to on those transactions or we can put that back into price in order to drive retention. So the panel is doing exactly what we want it to do. Over time, as the panel (25:13) and more members come on, we expect to see the footprint continue to grow as well. And again, we're not going to publish the proportion of conversion that we get. But I will tell you that it has improved.

Q - Nick Johnson {BIO 1774629 <GO>}

Okay, thanks.

A - Jonathan Stanley Hill {BIO 16892113 <GO>}

And in terms of the profit from broking and other, there's three major components within this year's half-year numbers. There's the first material element of the motor panel. There's the six months versus one month of Bennetts. And we also have our credit hire and repair business reported through this line as well. So actually, in terms of the underlying profit, we had a couple of million coming in from Bennetts. We had over £1 million coming in from the panel in the first half. And we had some one-offs in that credit hire and repair line, which set us back about £1.5 million, half-year-on-half-year. So actually, both the panel and Bennetts are contributing positively in the first half of this year. We just have some one-offs which haven't been repeated in the credit hire and repair lines.

A - Lance Henry Batchelor {BIO 6884486 <GO>}

(26:16).

Yes, going back to the panel. Could you please lay out what you mean by this new insurance or insurer-hosted pricing mechanism and how it works within the panel? And secondly, how long would it take to reach your optimum pricing potential within the motor panel? You've reached that down (26:40) home I think within three or four years.

Yeah.

But what would the pace be within the motor panel? Have you seen some evidence for that competitive pressure reducing that (26:51) price?

Well, firstly, the insurer-hosted pricing basically means that we'd get a real-time feed back and forth through the underwriters so that each time a quote comes in or each time a customer comes in; almost in real time, we can put that opportunity out to the whole panel. And then you want to (27:07) use the insurer-hosted pricing and can then run the algorithm and decide what they're willing to price at. That's obviously much more granular than just receiving a flat file once a week that tells us what price profiles they want to work to. The more granular it gets, the more keenly they can price if they choose to. So that gives – over time, as more and more of our underwriters move to that insurer-hosted pricing structure, that should give us more and more keen pricing (27:33) on the panel.

A - Jonathan Stanley Hill {BIO 16892113 <GO>}

We actually were getting monthly fees. But you can imagine what an underwriter wants to build in as a caution element if it can't adjust its price for a full month. So by getting IHP, they're able to move those prices and get more comfortable to put those prices more keenly.

A - Lance Henry Batchelor {BIO 6884486 <GO>}

And then on the second half of your question, it's very hard to answer the question when would we get to full efficiency. It's obviously going to depend on how rapidly new panelists join. And the profile of motor is very different than home. So on the home panel, we didn't see high levels of efficiency until we had a dozen or so underwriters on the panel. You don't need that many for motor because each motor underwriter can cover much more of the market. And so already with five underwriters including AICL on the panel, we are seeing some gains. And we can see who the next one, two or three panelists are likely to be. And we can see that they will add competitive tension to the panel and also that they'll add footprint as well to the earlier question.

Thank you.

Ravi.

Q - Ravi Tanna {BIO 16926941 <GO>}

Hi, good morning. Ravi Tanna at Goldman Sachs. Three questions, please. The first one was just on your motor claims commentary. And I think you referenced (28:51) in the profile of your drivers. But the claims inflation you guys reference at about 5% seems pretty consistent with most others in the market. So I was just wondering what disconnect – if frequency is running a bit lighter, severity running stronger or is there any kind of noticeable difference in what you're seeing (29:13)?

And the second question – and it's very a small number that (29:17) the earnings being down a little bit. And I was wondering, again, given that rates in the market have increased; what (29:26) maybe that could be a bit stronger. So I was wondering if there's particular within that. Third was really a point of clarification on the dividend. And you've got a one-third (29:38) policy over the last year. I think the interim versus final was (29:42) of how we should think about that dividend policy. If I may, a quick thought on the solvency ratio. You spoke about two areas of benefit, one being the quota share and the second being best estimates reduction. And I was wondering if you could quantify how much each of those has contributed to the solvency ratio increase.

A - Jonathan Stanley Hill {BIO 16892113 <GO>}

Should I go with this?

A - Lance Henry Batchelor {BIO 6884486 <GO>}

Yes, please.

A - Jonathan Stanley Hill {BIO 16892113 <GO>}

Well, the frequency is about how much our drivers are driving relative to where or how much they used to drive previously. So the frequency number itself is driven by behavior. And what we are clearly saying is that we are not seeing a change in our behavior. I think the severity in the inflation is driven by what's happening in the market, what's happening in the legislative environment. So that's what drives inflation. So it's not something that is related to our driver behavior. It's related to the market and the overall environment. So that's why I think why the two things are driven by different factors. But we're very clear in that we are still not seeing a change in our drivers' behavior in terms of driving patterns. And therefore, we're not getting that change in frequency.

On the ancillaries, I would say, I'm assuming that you're pleased that our resilient high-quality earnings are increasing. And what you might view as less high-quality earnings in terms of ancillaries, which is often quoted, is decreasing in (31:16) the proportion. What we're seeing is as the market inflates, you get people undertaking sales calls. And how do they ensure that they try and finalize some of those sales calls? So I think when you see an inflationary environment, you may see across the piece ancillary rates and add-on rates coming under a little bit of pressure.

And I think we said historically, approximately one-third, two-thirds in dividend. We will stick with the word approximately. And that was a rough guidance rather than a mathematical rule. We haven't given the (31:55) quota share and best estimates. What we clearly said was that quota share would gradually provide a reduction in the amount of capital we needed in the underwriter. What we said at the year-end was if we're increasing our dividend payout ratio while maintaining our deleveraging by circa 10%, if one assumes that today's profitability was to carry on and we were increasing and paying out that full 10%; you could equate that roughly to an incremental £45 million of capital release gradually over time. We haven't given the split at the half year and we're not intending to.

Q - Blair Stewart {BIO 4191309 <GO>}

Thanks. It's Blair Stewart from BofA Merrill. Two or three questions. Firstly, could you give (32:43) of where you're pricing in the whole market (32:48) stabilizing. And equally in the motor market, you've clearly bettered from the price increases (32:54). And the final question really just related to the customer database work that you're doing. And you've seen a small pickup in the active customers. Is the intension there to get a greater proportion of active customers versus the total number of customers on the database? Is that the longer-term intension? How do you see that playing out?

A - Lance Henry Batchelor {BIO 6884486 <GO>}

Well, look, on both of those – firstly, on pricing, we've all seen a fairly persistent decline in home pricing over several years. We tend not give details out on what we see. But I will tell you that broadly we've seen the stabilizing of pricing in the home insurance sector. So it's stopped dropping as precipitously as it was. And on motor, I think Jonathan covered in his presentation, earlier (33:46) we saw a rise in the first half and it's stopped now.

A - Jonathan Stanley Hill {BIO 16892113 <GO>}

I think what some of the commentators – particularly if you look at the AA stats of Q2 rates being – I think they quoted somewhere around 2% is the quarter-on-quarter. We're not fundamentally seeing something different than other market commentators in Q2, but obviously Q1-on-Q1 a year earlier was showing very strong growth as commentated on by a lot of those external indices.

A - Lance Henry Batchelor {BIO 6884486 <GO>}

And then on your database question though, I mean, I think the way to look at this is – that kind of IPO'd two-and-a-half-years ago, we were very focused on how many names did we have on the database, which was about the most granular and useful measure we had at the time. What's happening is we're gradually zooming in more and more on the customers that matter.

So for the last two years, we've talked a lot about the number of active customers that we had, which is an important metric of course as to how many people out there have some kind of a relationship with Saga.

I think the direction of Travel, I think you'll see us over the next years start to move in to how many higher value customers do we have, for example, how many products per higher value customer have we got, what's retention like amongst higher value customers. So, yes, of course, we want to drive up the number of active customers on the database, but not at any cost. It doesn't make sense to buy customer volumes in a very disruptive way.

What makes sense is for you to take a customer and migrate them up the value curve, so that they buy their second, their third and fourth product from Saga. They become truly embedded in the brand so, hopefully, multiple decades relationship, and those are the high value customers, where we make a lot of our profit.

Q - Ben Cohen {BIO 1541726 <GO>}

Thanks. Ben Cohen with Canaccord. I have two questions. Firstly, on the cross-selling part which you had announced, sort of the most important initiative. When are you going to be able to sort of put some numbers to that and the impact that that would have on the growth in the business? Or should we sort of see that as part of that kind of longer term 5% to 7% profit avenue (35:53) growth, the growth that you're looking for?

And then, again, I'll try and ask a question on the Travel side, in terms of the impacts of a weaker sterling, so you're saying that kind of customer plans aren't really changing. If that's the case, would sterling being weaker including the majority of these holidays being in (36:18) currency, should we see a pickup in growth (36:22) in the second half and then into next year because of that currency effect?

A - Lance Henry Batchelor {BIO 6884486 <GO>}

Lance here. I'll take the first and then hand over to Jonathan, who's thinking about the second one. So look, on cross-sell, internally, we are starting to develop really quite detailed metrics as to what we wanted to achieve. And that will drive itself all the way down to segment level where we decide for individual clusters of customers, what cross-sell number we are chasing. We are unlikely to publish that level of detail externally. And to pick up on your question, I would view that as part of our portfolio of options and how we drive sort of good profit, growth number each year, a long view.

We have eight different businesses, and then the way I view it is overlaying those eight businesses. We have no database, and all of the opportunities that we have within that database. And we see all of that adding up to our ability to deliver consistent profit growth, consistent solid cash, deleveraging, and a stronger dividend. And I would rather focus the story of that level then drill down into individual customer segments and then cross-sell. There's a lot of work going on in that space.

A - Jonathan Stanley Hill {BIO 16892113 <GO>}

And I would reiterate the last point is that, what we are aiming to do as a business is work with the portfolio of businesses and products that we have to drive stable, solid, robust, sustainable growth in this business while generating good cash flow to be able to delever and pay strong dividends. We haven't given any medium-term guidance. We've given one-year guidance. But we are very clear that everything we are doing adds up collectively to us to try to deliver that strong, stable, reliable growth going forward.

A - Lance Henry Batchelor {BIO 6884486 <GO>}

Which you're now seeing for five sets (38:11) and six months and going on. (38:12) And our goal is to move the levers as required in order to deliver. Clearly cross-sell is a part of the story.

A - Jonathan Stanley Hill {BIO 16892113 <GO>}

And the second question, in terms of Travel. Obviously, in our main tour operating businesses, we hedge forward a fair distance. We're pretty much 80% hedged forward in our tour operating businesses for all departures for next year. So, what you'll find is that anybody booking today and anybody who wants to book in the next weeks or months. And anybody here is welcome to join, and will get the same price as the pre-Brexit level of the exchange rates.

Clearly, there will come a point where we'll have to start pricing product outside and in the period after that, 80%. And then, we'll have to see the impacts on the pricing for the end customer as we work through that.

So clearly, an exchange here would (39:11) stay exactly where they are today than the pricing to the end customer will go up. But we don't believe that that will stop customers traveling. We just think it may make them, if they're sitting on a certain budget, choosing something slightly different than they may have chosen in the first place.

Q - James A. Shuck {BIO 3680082 <GO>}

Thank you. James Shuck from UBS. Just three follow-ups, if I may. Let's see, the profit before tax growth guidance, you gave us a 5% to 7% for full year, that you're reiterating now this half-year. I'm not so much concerned of the 8.5% that you delivered at the H1, but just more the H1 has benefited from a very high level of reserve releases, again, enables Saga to really sort of gain on this.

So I guess my question is, why are you still going to stick in to 5% to 7% for the full year story, (40:01) all other things being equal, we should be above that. I kind of connected with that point. I just don't think you should start – your point around the guidance, you've only given one-year guidance, not multi-year. I mean, my understanding is you've given – you used to have an EBITDA guidance that's multi-year of 5% to 7% which has now moved down below to PBT level, which one could argue is actually a little bit less than the 5% to 7% and as you projected further (40:26), Could you just state whether you do have multi-year targets and so on?

And secondly, on the customer segmentation on the high-value customers. I mean, that's – it's interesting to us and you've talked a little bit about some of the KPIs around retention and product developments and also improving the kind of the customer journey. You seem to indicate that was a kind of multi-year approach before you'd see tangible signs of that benefiting earnings. Is that the right take on that or were there kind of things you're doing now that will actually – going to be impactful and you can actually show us KPI and things working?

And then just finally on the Solvency II ratio. 196% for the full year. I don't know that you've given a target range, but do you have one? And just to refresh my mind, I think you talked about £40 million, I think being released from quota share. Is that – that's just coming through (41:17) over time as the book unwinds, but does that have an impact on the Solvency II ratio coming down as well?

A - Jonathan Stanley Hill {BIO 16892113 <GO>}

In terms of the first part, we are aiming to delever underlying PBT growth. So, you can take that when I refer to underlying, is excluding derivatives, because we can't control derivatives. If the exchange rate moves significantly and the fuel rate moves significantly between now and the year-end, I'm not going to have a moving target up until the last day depending on what derivatives are doing. So, underlying compared to the 3.8% that we talked about today is underlying PBT growth that is the one that I'm aiming to get to 5% to 7%.

Secondarily, you have to remember the reserve releases are reducing in the second half of the year. So, do I think we are undercooking our target? No, I don't. Secondly, we are very clear in the prelims that we were guiding on one year at 5% to 7%. We have a range of different products, as I've already said, which behave in different ways with different market circumstances. I'm not giving a multi-year target on a 2% range. We do not know what markets are going to do. In the first half of this year, we've had motor up; we've had home being difficult.

Everything we do is subject to market, subject to market conditions. So, we're not giving a multi-year target. We're very clear, our aim is to deliver solid, sustainable, underlying growth year-on-year, right, subject to underlying market conditions that we will not tie ourselves to a 2% range without any subject to. Anybody who does that, good luck to them.

Q - James A. Shuck {BIO 3680082 <GO>}

Well, you did do that?

A - Jonathan Stanley Hill {BIO 16892113 <GO>}

We didn't do that at the full year. And if you'd ask that question at full year, I've given you a very clear answer. This is a one-year target, and you will find very, very few businesses that are quoted giving multi-year 2% ranges on profit targets.

A - Lance Henry Batchelor {BIO 6884486 <GO>}

That's not to say that we are lowering our internal notable (43:13) ambition. We know what we're aiming at as a management team and – but we've agreed with our board. What we're saying is that it doesn't make sense to target your entire existence on a 2% range and put that action to the public domain in a multi-year way; because it can drive a city for ages (43:30).

A - Jonathan Stanley Hill {BIO 16892113 <GO>}

And potentially, as a profit forecast as well, which I don't think we're in the business of doing either.

A - Lance Henry Batchelor {BIO 6884486 <GO>}

Yeah. So, segmentation by value customers, KPIs, et cetera. The work is under way now. We are seeing benefits now. We are already spending our marketing dollars smarter than we were before in a more targeted way. We are already testing and learning in individual segments that we didn't know exist a year or two ago to drive better cross-sell result. We've seen really interesting and encouraging results.

There is a question around how many KPIs we choose to put out into the public domain. My concern is that we end up micromanaging ourselves in front of you and reporting on the outputs of very small groups of customers on individual tests or even that we give away a lot of commercially useful skills and so on to outside world. But this is not – it is a multi-year program. It will continue – if I run this company for 10 more years, it will continue through the whole of those 10 years. But we are seeing benefits already coming through and we expect to see those continuing in the months to come. But it's not as if we're waiting three years before it switches on.

A - Jonathan Stanley Hill {BIO 16892113 <GO>}

And in terms of Solvency II, we did expect the full year at – we weren't giving a range, but 170% was at the upper end of where we'd expect to be at the full year. We obviously have waited to see the first six months of quota share impact actually coming into the numbers, because we really wanted to work that through methodically to really – to see how that was actually coming through in the SCR. So now that we've seen that, we understand that better how it's working through mechanically. You should expect that 170% will be at the upper end of where you should expect us to be going forward.

Q - James A. Shuck {BIO 3680082 <GO>}

And just to be clear, (45:18) really one-time or we need to just reset the 170% on yearend?

A - Jonathan Stanley Hill {BIO 16892113 <GO>}

We're not going to reset to a number. We will continue to manage within a sensible range which we have internally, of which 170% is at the upper of. But the quota share itself gradually gives us an impact of releasing the amount of reserves we have to hold. And as that comes through, then that enables us to take dividends out of that underwriting business and to the group, which enables us to free up cash to be able de-lever and pay dividends. That's the way it works.

Q - James A. Shuck {BIO 3680082 <GO>}

Okay.

A - Lance Henry Batchelor {BIO 6884486 <GO>}

Anymore questions in the last couple of minutes? We have one (46:01).

Q - Blair Stewart {BIO 4191309 <GO>}

Just one sort of – it's Blair Stewart again. Just on the reserve releases, regarding those things (46:06) over the last year, that we will reduce them further. They've remained quite high in the first half of the year. You're saying that the reserve prudency is more or less unchanged. How should – if you can help us trying to model that number it's a significant number. And how does that – how should we think about not moving over the next two to three years?

A - Jonathan Stanley Hill {BIO 16892113 <GO>}

We haven't – I mean, I will reiterate what we said before. It will start to step down this year. I've already said that it will be lower in the second half of this year than it was in last year. And then it'll gradually step down over the next few years. But as quota share kicks in, we'll actually – effectively have less and less historic reserves which are there. So, I think I'm not going to give specific guidance on that. What you should expect is that, it's a gradual reduction over several years. And offsetting that, you should see the benefits of the panel and the ongoing benefits of the efficiency driver we deliver within our services business that helps to offset that, meaning we can still drive that good level of profitability within our Insurance business.

Q - Blair Stewart {BIO 4191309 <GO>}

Is that – maybe another reserve question. Does that (47:15) you gave in your releases by year? Is that fairly typical or is there anything (47:21)?

A - Jonathan Stanley Hill {BIO 16892113 <GO>}

It's fairly typical.

Q - Blair Stewart {BIO 4191309 <GO>}

Yeah. So, that gives you (47:23).

A - Jonathan Stanley Hill {BIO 16892113 <GO>}

Yeah.

Q - Blair Stewart {BIO 4191309 <GO>}

You know where it was coming from?

A - Jonathan Stanley Hill {BIO 16892113 <GO>}

Exactly. Exactly.

Q - Blair Stewart {BIO 4191309 <GO>}

Thank you.

A - Lance Henry Batchelor {BIO 6884486 <GO>}

Anyone else?

Thank you very, very much for listening. And if anyone's got further questions or follow-up questions, point them to us. I think Tim and the MHP team will make sure they reach us. And really appreciate you coming along. Thanks everyone.