Q1 2014 Sales and Revenue Call - Interim Management Statement

Company Participants

- Anthony Jonathan Reizenstein
- Paul Robert Geddes

Other Participants

- Andrew J. Crean
- Andy D. Broadfield
- Andy Hughes
- Gordon Aitken
- Greig N. Paterson
- Marcus P. Rivaldi
- William Hardcastle

MANAGEMENT DISCUSSION SECTION

Operator

Thank you for standing by, and welcome to the Direct Line Group First Quarter 2014 Interim Management Statement. At this time, all participants are in a listen-only mode. There will be a presentation followed by a question-and-answer session. I must advise you that this conference is being recorded today, Friday, the 2nd of May, 2014.

I would now like to hand the conference over to your speaker today, Mr. Paul Geddes. Please go ahead, sir.

Paul Robert Geddes {BIO 2474781 <GO>}

Thank you and good morning, ladies and gentlemen. Welcome to our Q1 update. It's only been about eight weeks since our last update, so I'm going to try and keep it brief.

And this quarter marks a change to our regular format because following RBS's disposal of its remaining stake we've now brought our quarterly reporting in line with our insurance peers. So hopefully you've all had a chance to read the statement issued this morning and will have your questions ready.

There's going to be no formal presentation today, but I'm going to run you through some of the highlights for the quarter and then talk a bit about the Motor market before taking your questions. And as usual I am joined here by John Reizenstein who is going to help me in the Q&A.

So let's start with the business highlights. You'll see from the announcement on the surface it's been a quarter of steady as she goes, although behind the scenes we are busy executing our self-help agenda.

The full year results I'll run you through are hot (01:20) further initiatives for the year. In the first quarter the focus has been on building further customer capability and propositions, whilst continuing to improve our pricing sophistication and accuracy.

We rolled out our new smartphone and tablet optimized websites giving our customers a much slicker 'quote and buy' journey. The new websites enable us to deploy more timely changes which we can then test and learn from. And I'm pleased to say that the initial results are very encouraging with a marked increase in quote to conversion rates particularly on tablets and mobiles.

The group's also launched three new propositions in the quarter. First, following a successful pilot, we've recently launched our self-install telematics proposition to add to our black box device and smartphone app. It's cheaper and easier to install and has the potential to take telematics to a much broader group of customers.

I'm pleased with the current take-up rates, which remain around one in five for the under 25's and higher in the under 21's. As a result of our multi-device strategy, we believe we're now one of the leaders in developing the telematics market in the U.K.

Second, Commercial has launched Churchill Van to its SME customers; that's in addition to our existing van offering under the Direct Line for Business and NIG brands. It's a good example of leveraging our brand strength this time in the SME that the Churchill brand is active in the PCW channel, this means Commercial has extended its distribution reach beyond direct and broker.

And finally, DLG Legal Services went live in the first quarter. We see it as a value-added part of our customer proposition. And as we said, we're not expecting any material profit from this service.

So before I move onto the Motor market, let me talk you through the headline financials. Ongoing GWP of £949 million was down 5.6% against the same quarter last year. In-force policies were down 2.1% versus the end of December and I'll come on to through the detail of that in a moment.

We made further progress on costs in Q1 with a 4% reduction versus last year, although this doesn't take account of inflation. Versus the fourth quarter, costs are slightly up on Q1 as typically this is a higher quarter on marketing spend. However, year-on-year marketing spend is down reflecting improved marketing efficiency.

Moving onto investments. We continue to see an improvement in yield as a result of the actions we've taken around the mix of our investment portfolio. Total income yield in the first quarter was 2.2% versus 2% last year and 2.1% at the year-end, which delivered income of £46.5 million which is up 16% versus Q1 last year.

The group also benefited from higher investment gains in the quarter, some of which was due to capital growth of the property portfolio. This brings us to a total return of £63 million which is up 55% versus prior year.

Now for more detail on GWP including an update on the U.K. Motor market. First quarter Motor premiums were down 10.2%, which is in line with what I said at the full year, which when I said it was going to be down about 10%. Markets remained highly competitive throughout the quarter and we've maintained our disciplined underwriting approach.

We reduced our Motor prices by 4% versus Q1 last year and we continue to reflect benefits from our claims and price initiatives and from recent legal reforms on our prices. Risk mix reduced in the first quarter albeit at a slower pace than previous quarters.

As in previous quarters, our price reductions remain lower than the level suggested in recent published surveys. As I said before, these surveys don't always provide an accurate reflection of what's actually going on in the market as they're often based on new business quote data, commonly only from PCW channel and often skewed towards young drivers where telematics quotes may have had a further distorting effect.

Our policy account was down 1.2% since the end of 2013, in line with the trend observed since the second quarter last year. We continue to take daily trading choices and we believe we are performing well in a difficult market.

In Home, in-force policies were down 1.4% versus the end of 2013, with a 5.6% reduction in GWP year-on-year. This reflects an increasingly competitive market and changes in distribution trends. Pricing in Q1 was supported by our self-help actions. This competitive market underlines the importance of our extensive self-help agenda in Home.

Whilst I'm on the subject of Home, let me give you a brief update on Q1 weather costs. At the full year we gave an initial estimate of £70 million to £90 million for Home and £20 million for Commercial. Our latest data suggests the Home cost is lower at around £60m with no change in the estimate for Commercial.

Let me comment briefly on the remaining segments. In Rescue and other personal lines, GWP was down 5.6% with IFP down 4% since the year-end. The reduction in IFPs is mainly due to a reduction in bank package account sales and this has also impacted travel policies. But if you adjust GWP for the Life business which we sold last year, Rescue and other personal lines GWP was actually up by 3% mainly due to growth in our Rescue business.

Outside of the U.K. personal lines, we continue to see growth in Commercial and International. Commercial grew IFPs by 1.5% with a 4% increase in GWP year-on-year. And as with previous quarters, this growth has come mainly from Direct Line for Business where we've seen strong performance in Landlord and Tradesman products slightly offset by a reduction in commercial vehicles.

In International, the headline GWP was down 2.6%. But if you remove the effect of exchange rate movements the underlying trend is positive with a small increase of 0.6%. In-force policies were up 3.7% overall with a 9.1% growth in German policies following another successful year-end campaign. Since the end of the first quarter, 2012, German IFPs have increased by 31.9%. In Italy, the market remains competitive although IFPs were up slightly in the first quarter.

A few comments on regulation as the regulatory environment continues to be highly dynamic, particularly in U.K. Motor. During the first quarter, the FCA published its review of add-on products as well as its business plan for the year and next. We're working closely with the regulator on these areas, and we're also looking forward to working with them on the PCW review.

Overall, our position remains unchanged. We support increased transparency, a high regulatory base line and we support reforms, which will result in a level-playing field across the industry.

So let me finish by reiterating our targets for 2014. We're currently targeting a COR between 95% and 97%, based on normal weather claims. Within this, we reiterate our Commercial COR target of better than 100%, again assuming normalized weather claims and large losses. This is also underpinned by our relentless focus on costs to achieve the £1 billion target by the end of the year. And finally, of course, our 15% ROTE target isn't time bound and remains ongoing.

So to summarize, another good quarter, progress for us, we've delivered some of our strategic initiatives already and we're busy on the rest whilst developing more initiatives for 2015 and beyond.

And with that I'll hand back to the [0:08:46].

Q&A

Operator

Your first question comes from the line of Will Hardcastle of Bank of America. Please ask your question.

A - Paul Robert Geddes {BIO 2474781 <GO>}

Morning, Will.

Q - William Hardcastle {BIO 16346311 <GO>}

Morning. Just a quick one on the expense base, first of all. You're 4% lower year-on-year. Now is that a pretty good run rate for full year or could there be any one-offs either in Q1 this year or last?

And second one, your comments on Motor are pretty clear, I just want to make sure that I'm right. Effectively, what you're saying is given the technical pricing and claims reform movements, you [00:09:31] flat margin year on year.

And perhaps could you just discuss a bit on the Home market? I'd have thought following flood losses prices might be going up, but no one's really reporting that at all. So just a few comments as to why you think that might be the case. Thanks.

A - Paul Robert Geddes {BIO 2474781 <GO>}

Okay, we'll allow you three questions.

Q - William Hardcastle {BIO 16346311 <GO>}

Apologies.

A - Paul Robert Geddes {BIO 2474781 <GO>}

No, don't worry. John, do you want to start with...?

A - Anthony Jonathan Reizenstein

Yes. Hi, Will. John here. On costs, the Q1 is normally a little bit higher because of the marketing spend and same last year, same this year. So nothing is particularly special between the two. We're pretty sure we're on track and there's no real news. Costs can be a bit lumpy or noisy quarter-by-quarter, but there's no particular noise in this quarter.

A - Paul Robert Geddes {BIO 2474781 <GO>}

Right, let me talk about Motor a little. I think the first thing I'd like to kind of get out of the way is the pricing surveys. And there are obviously three out there, ABI, the Towers Watson/Confused one and the AA one. Year-on-year, AA's saying minus 16.6%, Towers minus 19.1%, the ABI minus 6.3%. We think probably the ABI is the most accurate of these and the reason I say that it includes – it's written premium not just quotes, it's renewals and new business whereas the other survey tends to be new business, and about 90% of the markets in there.

So, we think it's a high quality survey and probably directionally is the closest to where the market is. The other ones obviously because they're new business quotes they're very sensitive, A, to the risk of mix in it and they tend to be skewed we think a bit more to younger drivers. Younger driver pricing quotes are probably down more skewed by telematics where the quotes are low, but the conversion of telematics quotes as indicated by the fact that we're only doing about a quarter to a third, suggests that they convert less.

So I think that is a reason to explain in a way why we don't think the market is down as high as the minus 16.6% or the minus 19.1%. We think it's closer probably to the ABI survey. Now, we're down about 4% and we feel justified in that 4% by what we are seeing, which is a combination of some help from the government, which we're pleased for from the impact of the changes last April. We're seeing a bit of frequency benefit, we're seeing some severity benefit.

Added on to that we've obviously got our extensive claims program and our pricing program and that in combination is making us feel happy to have passed on 4% to customers. Clearly, the market's doing a bit more than that and you can ask our competitors for what's going on for them, but that's what's going on for us.

Home, to be really clear about Home, it's the second highly competitive quarter that we've seen. The market is more challenging albeit we think we're in a strong position. Again, we think we can trade hard and make good profits in this market and we're doing that. At the time of the floods, I was asked many times does this automatically mean prices will go up and we said no. If you think about, we're now saying £60 million, so we're back within the envelope of an annualized claims cost of £80 million. We don't think it's cost the reinsurers any claims at the level we've seen at, it's a very – Home is a very profitable, attractive marketplace and lots of people are competing hard in it.

So, I wasn't surprised that the floods didn't really have much impact and I think we predicted that but it is – I'm not dressing it up, it's a more challenging, highly competitive market.

Q - William Hardcastle {BIO 16346311 <GO>}

Okay, that's clear. So just quickly – just to come back to expenses. So is the 4% lower year-on-year, is that a decent run rate to be going off for this year?

A - Paul Robert Geddes {BIO 2474781 <GO>}

Yes, I'd go back to £1 billion.

A - Anthony Jonathan Reizenstein

So I think we – we're sticking with our £1 billion we're at approximately £1 billion and if we can do better than that, we'll all be delighted.

Q - William Hardcastle {BIO 16346311 <GO>}

Okay.

A - Paul Robert Geddes {BIO 2474781 <GO>}

We are really, really focused on doing as much as we can particularly in these market conditions. Okay, pass it over to you, operator. Thanks, Will.

Operator

Thank you. Your next question comes from the line of Greig Paterson of KBW. Please ask your question.

A - Paul Robert Geddes {BIO 2474781 <GO>}

Hi, Greig. Unless it's your brother Craig.

Q - Greig N. Paterson {BIO 6587493 <GO>}

Can you hear me?

A - Paul Robert Geddes {BIO 2474781 <GO>}

Hi.

Q - Greig N. Paterson {BIO 6587493 <GO>}

All right, sure. In terms of – you remember at the full year, you provided a quarter-to-date run rate for Motor in terms of rates, in-force vehicles and mix, I wonder if you could just repeat that because I found it quite useful for the second quarter?

A - Paul Robert Geddes {BIO 2474781 <GO>}

Well, let me give -.

Q - Greig N. Paterson {BIO 6587493 <GO>}

Yes.

A - Paul Robert Geddes {BIO 2474781 <GO>}

Of Q2?

Q - Greig N. Paterson {BIO 6587493 <GO>}

Yes, yes, because remember at the – you provided that number and that turned out to be – so what is your (14:20) in the first two months?

A - Paul Robert Geddes {BIO 2474781 <GO>}

Yes, that was a one-off, Greig, I'm not going to do that again.

Q - Greig N. Paterson {BIO 6587493 <GO>}

Okay.

A - Paul Robert Geddes {BIO 2474781 <GO>}

I can tell you, what Q1 was.

Q - Greig N. Paterson {BIO 6587493 <GO>}

(14:25) was associated with the stock.

A - Paul Robert Geddes {BIO 2474781 <GO>}

Well, we were quite – if you think about it, we were quite late, we're only eight weeks in, so we've only literally seen three weeks data and I think – I don't want to make too many predictions.

Q - Greig N. Paterson {BIO 6587493 <GO>}

All right. Then so – so for instance, are you saying – I'm trying to figure out whether the run rate year-on-year in terms of pricing 4% has gone down or up.

A - Paul Robert Geddes {BIO 2474781 <GO>}

Well, if you look at the -

Q - Greig N. Paterson {BIO 6587493 <GO>}

In terms of your experience since the end of the quarter, just roughly.

A - Paul Robert Geddes {BIO 2474781 <GO>}

Oh sorry. I mean, April – I'm not calling anything new. I'm not calling green shoots, but similar trends. It's pretty bumpy and noisy because each month's different competitors take different stances on different groups of customers.

Q - Greig N. Paterson {BIO 6587493 <GO>}

So it's similar trends, in other words?

A - Paul Robert Geddes {BIO 2474781 <GO>}

Yes, and again if you look at the quarters Q2, Q2 is minus 3%, Q3 minus 5%, Q4 minus 4%, Q1 minus 4% for us and we think the market – there's nothing new to call out, we think in April that we didn't see in the first quarter. But it's a bit bumpy within the months.

Q - Greig N. Paterson {BIO 6587493 <GO>}

So, all right, similar trends, all right. And, then house, I wonder if you can give us a feel for what the year-on-year decrease in rate is that you achieved versus the market say in the first quarter?

A - Paul Robert Geddes {BIO 2474781 <GO>}

Yes, let me just get the -

Q - Greig N. Paterson {BIO 6587493 <GO>}

Exactly as you have provided for Motor.

A - Paul Robert Geddes {BIO 2474781 <GO>}

Yes, I mean, think – let me go to the AA Home survey, which had the market down on new business, sort of, 8% year-on-year and 2% quarter-on-quarter. That is new business and we think prices on new business are down for us certainly more than the price is down on renewals.

So, the new business market data is – I don't think we're down as much as the AA survey, but we're down quite a bit on new business. We're down less on renewals. If you mix it altogether it is a very competitive marketplace. But we've also done an awful lot of self-help as well to offset it. So I'm not – I'm comfortable where we stand. As I said, we're going to trade this hard, and we think we can trade it hard whilst still it being a very profitable business for us.

Q - Greig N. Paterson {BIO 6587493 <GO>}

So, I mean, what are you saying that AA was down 8%, your new business is down less than 8% and your renewals is down less than new business?

A - Paul Robert Geddes {BIO 2474781 <GO>}

Yes, exactly.

Q - Greig N. Paterson {BIO 6587493 <GO>}

And do you see – are you losing share or gaining share?

A - Paul Robert Geddes {BIO 2474781 <GO>}

Well, I mean, you've seen we've lost IFPs, I'm not going to make any forward-looking comment, other than obviously the more initiatives that we get, the more optionality which we have, but we start from a very – as I say, we start with a lot of good things about the Home business. We start with scale. We start with claims benefits being delivered. We start with some of those 30 price initiatives as I talked about year-end are on Home. We start with strong brands on Home and obviously we have plans later in the year to relaunch Direct Line. We start with obviously great partners in that and we're still investing in it.

So, we have a lot of assets. The distribution mix, I talked about before is swinging more towards PCWs and slightly less towards, for example, the bank channel and that obviously has an impact as well on IFPs. But we're a strong player on the PCW channel and we'll continue to trade very hard on the PCW channel.

Q - Greig N. Paterson {BIO 6587493 <GO>}

Right. And then just finally the – in terms of the FCA, this bolt-on results on this – the bolt-on review in the first quarter. I wonder if that's got any implications and also in terms of the FCA's business plan and the one thing that jumped out at me when I read through it was the investigation into installment income. I mean, that's a significant portion of your profit. I wonder if you want to make some comments on that.

A - Paul Robert Geddes {BIO 2474781 <GO>}

Sure. I mean the highest level comment I reiterate which is we think a strong conduct regulator enforcing a strong baseline will be good for us and good for the reputation of the industry. Good for us because we have quite a low risk appetite on conduct and it may be a different risk appetite to some.

And taking that specifically, on add-ons, we're confident with the add-ons that we sell are good value, well disclosed and all those good things. So we actually want – we want quite quick progress on the FCA following up on their study, but they've got quite a bit of work to do, because they only looked at four products and they need to discuss the remedies. But we are keen for them to implement. We don't agree with everything they're saying, but as a general thrust of it we're supportive of where they're coming out and we want that to be implemented consistently across the industry and strategically that will be good for us.

On the business plan and credit, the real emphasis you'll see there is on disclosure. If you – I'm sure you do regularly, Greig, but if you go on to our website and look at how we disclose credits, I think we're in a good place there and I'm, again, keen for them to make sure that that's true across the industry.

Q - Greig N. Paterson {BIO 6587493 <GO>}

Yes, but I mean, with the actions that we saw, do you think that there's a risk that they might just sort of put in some kind of cap or something like that?

A - Paul Robert Geddes {BIO 2474781 <GO>}

Well, that's not what they've indicated. It's obviously – that will be – politicians will obviously do that in the way they did with – some of the payday lenders, but that's not the thrust that we understand from them. We think the APRs, again, are consistent with the sorts of rates you get on credit cards. We think they're very well disclosed. Ours are particularly well disclosed, and ours are particularly clean in terms of how we structure it. So, I think it's going to be more about disclosure and clarity, both of which we're in favor of, rather than a price capping the rates.

Q - Greig N. Paterson {BIO 6587493 <GO>}

Sorry. Just to follow-up. What is your ADR (20:24) and those elements of the add-on review that you don't agree with? Those products, what do they make up of profit?

A - Paul Robert Geddes {BIO 2474781 <GO>}

Yes, so our APRs are kind of in the 20s, which again we're saying is consistent with that. I wouldn't say I disagree with that. Some of the remedies, for example, publishing claims ratios, which we just think have some problems with them, not that we've got anything to hide. We just think that they might not cause customers to buy the right products for them. So we're working with them on what is a way of people assessing value, which I think is important to be done.

The only point is they looked at four products and obviously they're trying to make conclusions across - or five products - they're trying to make conclusions across a multitude of add-on products. And, therefore, we need to make sure they go at appropriate speed to get this stuff implemented, but not so fast that they catch - unintentionally, catch products, which they haven't reviewed yet. So - we are - I think we're on the edge of working with them for quick implementation, that suits us.

Q - Greig N. Paterson {BIO 6587493 <GO>}

All right. So none of those five products are material contributors to yours, the risk that they disappear? That's what I am trying to get to.

A - Paul Robert Geddes {BIO 2474781 <GO>}

No.

Q - Greig N. Paterson {BIO 6587493 <GO>}

All right. Good. Thank you.

A - Paul Robert Geddes {BIO 2474781 <GO>}

Thanks.

Operator

Thank you. The next question comes from the line of Andy Hughes at Exane BNP Paribas. Please ask your question.

A - Paul Robert Geddes {BIO 2474781 <GO>}

Good morning, Andy.

Q - Andy Hughes {BIO 15036395 <GO>}

Good morning, guys. Hi. A couple of questions, if I could. The first one is on the Home insurance, just trying to understand what's going on going forward. So basically the decline in IFPs in the quarter wasn't anything like you trying to put prices up after the weather and then finding the market caught you out. It's actually that you find that new business today is relatively unprofitable? Is that correct?

A - Paul Robert Geddes {BIO 2474781 <GO>}

No. Neither. It's just it is more depressive. There are players in the marketplace seeking to grow. And in the quarter that's meant that we've ceded 1.4% policies. So it's a thing about the competitiveness of the marketplace and we have no expectations nor actions around flooding in terms of pricing and I didn't expect the market to do, and it didn't. Because this hasn't actually touched the sides of our weather load. It hasn't touched the reinsurers. So that wasn't an expectation.

It is a profitable marketplace with a number of players trying to grow. And I am saying I've got quite a range of options and I trade it hard. In the quarter, we lost some policies. That may be the case in the second quarter, it may not. I retain the right to trade and I've got quite a lot able to trade, I've got quite a lot of assets in the space.

Q - Andy Hughes {BIO 15036395 <GO>}

So, I guess the question was, I think when I think about Home insurance, I think about quite high retention, so when I see a sort of 1.4% drop in policy count, I'm thinking quite a significant drop in new business volumes. Was it new business or was it retention that kind of moved in the quarter? And why has this changed so much in one quarter, I guess, is the question?

A - Paul Robert Geddes {BIO 2474781 <GO>}

Yes, so retention continues to be very good and very high. So, yes, I mean, most of that was in new business, but it wasn't a huge fall. We flagged previously, I think, that the bank channel obviously has been a bit slower. And we think there's a bit of a channel shift between bank and PCWs, but again that was in line with our expectation.

So I don't want to dress it up. I've been saying it's a very competitive marketplace. It's a very attractive marketplace, because it's a very profitable marketplace. We've got a lot of assets to do very well in it and we'll continue to trade very hard and we'll have some volatility, I'm sure, over the quarter in terms of the IFPs. We have, again, a commitment to make sure that we're optimizing across a number of metrics, including profitability and making sure we look after the loss ratios. So we're balancing those things up, we're not gloomy about it. We think we can do a good job of defending our market-leading very profitable position.

Q - Andy Hughes {BIO 15036395 <GO>}

Okay. And then a small follow-up question on Home insurance and then one on costs; so, on Home insurance, do you expect the impact from the MMR that's come in, sort of, April 1 – April time?

And the question on costs was, I guess, looking at the in-force policy count, projecting it forward the kind of current trends, and I appreciate that's obviously a very difficult thing to do, that kind of implies you need to do a bit more on costs. So what's your thinking on that now? Thanks.

A - Paul Robert Geddes {BIO 2474781 <GO>}

Yes, so we don't think MMR's going to have much of an impact on us, actually, most of the market is stand-alone rather than mortgage-linked. And, yes, we will continue to focus and do as good a job as we can on costs and a more competitive market means we have to keep pushing. So we don't want to put a new target out there. We've got to deliver the £1 billion and that includes inflation and all that stuff, but do not confuse that for – we are relentlessly continuing to pursue cost opportunities as is needed in a market like this and we continue to do that.

Q - Andy Hughes {BIO 15036395 <GO>}

Thank you very much.

Operator

Your next question comes from the line of Gordon Aitken of RBC. Please ask your question.

A - Paul Robert Geddes {BIO 2474781 <GO>}

Hi, Gordon.

Q - Gordon Aitken {BIO 3846728 <GO>}

Morning, a couple of questions, please. First, on self-install, just give us an indication of to what extent that has expanded the telematics market for you? And it sounds like you have a first mover advantage there. I'm just wondering, if that is the case and when the others will catch up?

And secondly, you've revised your Home weather loss estimate from £70 million to £90 million down to £60 million, just if you can give us a bit more flavor of what's going on there and how sure can you be of that number, now what percentage of that number is in respect of paid claims? Thanks.

A - Paul Robert Geddes {BIO 2474781 <GO>}

Yes, so on telematics, crudely we think this will enable us to, kind of, offer it to customers down to as low as about a £500 premium, where before we kind of capped at 25 years, which was maybe a £1,000 premium. So it's quite a significant universe you can get at now, which won't just be young drivers, it will be drivers of high performance cars or people with less experience or with different claims records.

So good drivers that think they're better than their normal rating factors would suggest, we think will find this attractive. And we think – I think what we said before is we don't think potentially the boxes will give long-term sustainable advantage, because you can take apart a box and see what's in it and go and make them, albeit we've got a really good box and we're a bit ahead of the curve and watch this space on that. What the clever bit is the marketing proposition, the clever bit is the pricing and the IP associated with using the data, and we're up to many million miles that we're now analyzing.

And the key for us is to get ready to be able to intelligently price the renewal, which is coming up in the second half because it was only the middle of last year that we started rolling these things out. So we're working really hard to use the data, which we found to intelligently price the renewals as those come up for renewal a year after we started. But we're pretty excited by it. I mean it's still pretty small, but getting less small in new drivers and building every week. John, on weather?

A - Anthony Jonathan Reizenstein

Yes, thanks, Gordon. The reason I should put out, obviously, it's quite early, because it was the end of February. We're now eight or nine weeks later, so I'm sure we put a little bit of group in there. Since then, actually it's been a calm period for weather, quite benign, so we've been able to do the work that you need to do in the field and so on. The development curves have flattened out, it's about a third settled which is what you'd expect for this kind of event – these kinds of events.

Q - Gordon Aitken {BIO 3846728 <GO>}

Great. Thanks.

Operator

Your next question comes from the line of Andrew Crean of Autonomous. Please ask your question.

A - Paul Robert Geddes {BIO 2474781 <GO>}

Hi, Andrew.

Q - Andrew J. Crean {BIO 16513202 <GO>}

Hi, there. First question, could you tell us actually how many telematics policies you have of your 3.7 million Motor policies?

Second question, on the Motor book, obviously, your average prices are down 4%. Can you tell us what your average claims are down sort of Q1, 2014, on Q1, 2013?

And then thirdly, on the costs, if I take your costs as a percentage of premium, your efficiency ratio has actually deteriorated by about 40 basis points. Do you see a situation in the next year or two where you actually improve the efficiency of your business as opposed to chasing – costs chasing premiums down?

A - Paul Robert Geddes {BIO 2474781 <GO>}

Okay. Let me do that in order. So telematics around – got around 20,000 boxes, but building every week, because we only started at the end of last year and again, we're going to be ramping up a bit more on the self-install. So it's small. But as I say, up to a third of under 21-year-old, a quarter of under 25-year-olds and we expect that to build as we start to really push the self-install option.

Q - Andrew J. Crean {BIO 16513202 <GO>}

So when you say 20,000 boxes, is that including self-install and apps and boxes?

A - Paul Robert Geddes {BIO 2474781 <GO>}

No, not apps, that's black boxes and self-installs, so that's real telematics boxes.

Q - Andrew J. Crean {BIO 16513202 <GO>}

Yes.

A - Paul Robert Geddes {BIO 2474781 <GO>}

Let me do costs and I'll pass on to John on the claims. So last year we improved the expense ratio. We've said this year it might be a bit of a struggle to maintain it, but we'll do our very best to do that. Long-term, as we have ambitious plans to make the business more efficient for our customers by, for example, allowing customers to do more self-service. So in the long-term, we obviously want to improve that ratio, because we think there's opportunity in it, but we're kind of in that phase now, competitive part of the market. We've done a big lump on costs. The next little while is going to be a fight on the expense ratio, but the destination is obviously going to be an improvement. And as we say, day-in and day-out we're doing everything we can to try and hold that as much as we can. John?

A - Anthony Jonathan Reizenstein

Hi. Yes, Andrew, on the claims side, the main driver of stable claims performance, which in turn we can price in, is on bodily injury where the stable trends continue. There's the odd thing that's going in the other direction. There's a little bit of uptick in accident frequency in Q1, but we think that's weather actually. It was actually pretty stable in 2013 despite slightly better economy and slightly higher driver miles, so we're not panicking about that, although we're very watchful about it. So it's really continuing BI severity improvement, partly due to external government factors, partly due to our own efforts, which are enabling us to reduce prices to that modest extent.

Q - Andrew J. Crean {BIO 16513202 <GO>}

But I suppose the point I'm trying to say is, taking BI and accident frequency and everything else, are average claims falling at 4% or more or less?

A - Anthony Jonathan Reizenstein

Well, I think just doing it on a quarterly basis is a little bit – you will get a bit of volatility between quarters. We (32:04) give you our current (32:05) ratio and commented on it at the half year. But we're quite happy from a ratio perspective, which is why we're restating our COR target with the way things are going.

Q - Andrew J. Crean {BIO 16513202 <GO>}

Okay. I understand. Thank you.

A - Paul Robert Geddes {BIO 2474781 <GO>}

Okay.

Operator

And your next question comes from the line of Andy Broadfield of Barclays. Please ask your question.

Q - Andy D. Broadfield {BIO 7273415 <GO>}

Good morning. Just two follow-ups on the telematics, actually. One, to get your opinion - there's been a bit of pooh-poohing of the - by you and by a lot of your peers of the market data from Confused.com and one or two others, because it's quotes, not actual. So my question to you on that one was, do you think it's just a matter of time for that conversion rate to become - to go much higher and therefore for the difference between the quote levels and the reality to narrow? And presumably with your products you'd hope that was the case.

And the second question is then, if that is the case then how does that - if your plans for telematics come to fruition, how does that impact your cost ratio, which again is a follow-up to Andrew's previous question, because presumably the telematics product is a lower premium per policy product?

A - Paul Robert Geddes {BIO 2474781 <GO>}

Yes. Okay. Let me do the first bit. I don't think telematics will be at 100% any time soon, but we think it will grow. We think self-install does lower some of the barriers that's capped off where the black boxes got, because frankly it's less hassle. It's not permanent in your car, if you don't like it you can always take it out and send it back. So I think the penetration will go up, I think the self-install, again, doesn't take the car off the road, you don't need to take it into a workshop to get it fitted and it's not permanent in your car. So I think it has some attractions which should edge it up. But I don't think it's ever going to get to 100%, so I think it will be a fact of life on the surveys.

Again, I would return you to the ABI survey, it doesn't have any of those things you have to worry about. So I think it's a survey that requires people to look at it quite hard. I think it's the best of the surveys, albeit they're all just surveys, none of them are perfect. In terms of the...

Q - Andy D. Broadfield {BIO 7273415 <GO>}

Just to come back on that, I guess we're trying to look forward rather than backwards and the AA survey, they're all backwards looking, but we're trying to anticipate a little bit what the gap between where we are today and where we're going to go and if the quotes are suggesting prices are going to continue to go down, then I guess that's what we're trying to...

A - Paul Robert Geddes {BIO 2474781 <GO>}

Okay. Well, let John explain a little bit about how a telematics world will change the P&L.

A - Anthony Jonathan Reizenstein

Hi, Andy. The economics of - so per individual customer, telematics will increase the cost ratio and reduce the loss ratio. And it will also, we believe, improve persistency. So from a lifetime value perspective, we're very much in favor. When you macro that across the portfolio, obviously you're going to get mix effects as well, so telematics makes us more competitive in higher premium segments, premium segments which are still higher premium, relatively, that won't necessarily worsen our cost ratio as much. So we think there are some good things - a number of good things about telematics, both from an individual customer perspective and from a portfolio perspective.

Q - Andy D. Broadfield {BIO 7273415 <GO>}

Thank you. Okay.

Operator

And your next question comes from the line of Marcus Rivaldi of Morgan Stanley. Please ask your question.

Q - Marcus P. Rivaldi {BIO 5739374 <GO>}

Good morning, everybody. Just another follow-up on telematics, please, because I guess people are trying to also work out whether you would be a net beneficiary or loser from the telematics phenomenon as it builds. So when you look at your portfolio, I think last year average premium about £360 in the Motor book, how much of your policy count would be above that £500 pricing point, would you say and have you got any sense about how that would compare versus the wide market? Thank you.

A - Paul Robert Geddes {BIO 2474781 <GO>}

Yes, that's not a sum we disclose and it's a bit early to say, other than clearly telematics is a more poker (36:26) proposition in a higher premium business, because it's worth more to the customer and the relative cost is less to us. And, obviously, over the last few years, we have de-risked and we have an appetite to take more risk where we can find it and telematics will be one of the tools to help us find it.

Not the only tool, we're doing lots and lots of further work on technical pricing and we want to find the sub-segments within our premium business that's profitable for us. So I think we've long said, we're not limited by our risk appetite, we're increasingly not limited by our technical capabilities. So we do want to be a bigger player in slightly higher premium business and telematics is one of the tools that will help us deliver that.

Q - Marcus P. Rivaldi {BIO 5739374 <GO>}

Okay, without being specific then, would you say you'd be a net beneficiary or a net loser do you think from...

A - Paul Robert Geddes {BIO 2474781 <GO>}

Yes, we think net beneficiary, A, from that viewpoint in terms of the mix of our book there is an opportunity in that part of the market for us. Secondly is, by being big, we do have lots of clever pricing people and technology people and we're working with clever people. I think later today we might be disclosing some of the people we're working with.

I think there's an RNS out 10 minutes ago disclosing that we're working with a company called The Floow, which is linked to Sheffield University, and Trakm8 in terms of devices. So we are putting quite a lot of effort and resource against this and, again, we think that should position us well and we can use it in Van, and we are using it in Van and commercial vehicles as well.

Q - Marcus P. Rivaldi {BIO 5739374 <GO>}

Great, thank you very much.

A - Paul Robert Geddes {BIO 2474781 <GO>}

Okay, operator.

Operator

Sorry?

A - Paul Robert Geddes {BIO 2474781 <GO>}

No, it's fine, yes.

Operator

Your next question comes from the line of Andy Hughes at Exane BNP Paribas. Please ask your question.

Q - Andy Hughes {BIO 15036395 <GO>}

Hi guys, a couple of follow-up questions, if I could. The first one was in response to the accident frequency increase in Q1. Obviously a bit worried about this, I know you said that your frequency last year was down, but across the industry it was actually up and, obviously, we're seeing an increase in miles driven. And now your risk mix is down 2% year-on-year, so if your frequency is up, could you talk a bit more about that, because obviously that's a concern with declining premiums?

And the second point was on telematics. When I look at what other people are doing with telematics and they're able to use breakdown companies to install these things and they're able to capture claims, which are not necessarily insurance related, used for the telematics box initially. Why aren't you doing the same thing through Green Flag as other people are doing through the RAC? Thank you.

A - Paul Robert Geddes {BIO 2474781 <GO>}

I'll do the second bit first. That point is not lost on us, so I am not going to announce anything. But we think it's an asset to own a rescue business like Green Flag. Green Flag had a good quarter. And we think having – owning a rescue business and being an insurer is a useful set of assets to have as telematics develops, but I can't really say anything more than that.

A - Anthony Jonathan Reizenstein

Just on the Q1, I don't want to worry you, Andy. It's a slight uptick, and...

A - Paul Robert Geddes {BIO 2474781 <GO>}

We think it's weather.

A - Anthony Jonathan Reizenstein

We think it's weather. It's one quarter and we're not worrying about it. As you say drive miles are slightly up, but we didn't notice any frequency increase during 2013 as a result of that, so we just don't believe it is economic related at this point, but it could become so in the future.

Q - Andy Hughes {BIO 15036395 <GO>}

Just to follow-up on the telematics, there's nothing on your telematics box that's different to any others. So you expect with your telematics box you would still – it would notify you straight away if it had been involved in an accident, basically, so you'd be able to capture first notification of loss in a large proportion of cases, is that right?

A - Paul Robert Geddes {BIO 2474781 <GO>}

No. We think we've got a really neat self-install box that is very easy for people to fit, so that is a bit of a differentiating factor. Its functionality we think is as rich as other people out there, and it's really small. So if you look – because the OBD ports go into the footwell of your cars or all over the place, having a really slim one is an advantage in terms of getting the fit right which for us is pretty high.

Now what we then do with having a box like that, what we've said today is we can offer this to an increasing universe of slightly higher premium drivers. Quite how – what the winning proposition is as a rescue proposition, as an OBD, as an engine diagnostic proposition is, what you give free, what you charge for, I think is very much up in the air and I am going to keep my powder dry on this call about what our thinking is on that. But we're certainly moving full steam ahead on the insurance side of it. Owning Green Flag gives us more options as well.

Q - Andy Hughes {BIO 15036395 <GO>}

Any idea what roughly the unit cost of the box is, for you?

A - Paul Robert Geddes {BIO 2474781 <GO>}

That will be – we're not going to disclose that, but it's a lot less than...

A - Anthony Jonathan Reizenstein

Less than a black box and more than an app.

A - Paul Robert Geddes {BIO 2474781 <GO>}

Yes, it's a lot less than the installed cost of a black box.

Q - Andy Hughes {BIO 15036395 <GO>}

Okay. Thank you.

Operator

And your next question comes from the line of Greig Paterson of KBW. Please ask your question.

Q - Greig N. Paterson {BIO 6587493 <GO>}

Yes, thanks. Can you hear me, everyone?

A - Paul Robert Geddes {BIO 2474781 <GO>}

Yes, of course.

Q - Greig N. Paterson {BIO 6587493 <GO>}

Yes. You made a slightly strange statement there when you were talking about self-install, you said all a person has to do is go to a workshop. I wonder if you can just explain, because to me that's – I thought that...

A - Paul Robert Geddes {BIO 2474781 <GO>}

No, no. All they need to do is just, sometimes open the flap, sometimes not, shove the box in and then it's up and running. The black box, the former black box, you had to go and get it fitted and that was a hassle. It was a cost. And there was a permanence to it that we think might have been a psychological barrier to people taking it up. But when it's a little box, we mail it to you, you put it in, it works, if you don't like it, you take it out, we think it's a better proposition for everyone.

Q - Greig N. Paterson {BIO 6587493 <GO>}

And is it very difficult, I mean, do you have to do something to put it in or is it...

A - Paul Robert Geddes {BIO 2474781 <GO>}

It's - the fitment rates are high and I think, as we promised you, at some stage we will send all of you boxes and you can give it a go.

Q - Greig N. Paterson {BIO 6587493 <GO>}

And the second question is what is its limitations in terms of data recording versus the fitted boxes? I wonder, can it - what does it have to...

A - Paul Robert Geddes {BIO 2474781 <GO>}

No, it's all the same...

Q - Greig N. Paterson {BIO 6587493 <GO>}

...and is it monitoring the - is it connected to the electronics of the car, the engine management, what's the story?

A - Paul Robert Geddes {BIO 2474781 <GO>}

So it's got all the good telematics bits you'd want, plus it's got some OBD functionality.

Q - Greig N. Paterson {BIO 6587493 <GO>}

OBD, sorry?

A - Paul Robert Geddes {BIO 2474781 <GO>}

So, I think we get - we learn stuff about the car by the fact that it's plugged in. So the fact that it's plugged in gives us power and it gives us some extra data and it's in the box, got all the bits you'd want to know from a telematics in terms of accelerometers and GPS.

Q - Greig N. Paterson {BIO 6587493 <GO>}

All right. Perfect. Thank you.

Operator

And there are no further questions at this stage, please continue.

A - Paul Robert Geddes {BIO 2474781 <GO>}

Great. Okay, guys. Well, thank you for all those questions. And you know where we are if you've got any follow-ups and we'll speak to you obviously with a slightly fuller H1 in a few months. Thanks very much indeed.

Operator

That does conclude our conference for today. Thank you for participating. You may all disconnect.
