Q2 2018 Earnings Call

Company Participants

- Alistair Hargreaves, Head of Service
- Cristina Nestares, Chief Executive Officer-UK Insurance
- David Graham Stevens, Chief Executive Officer & Director
- Geraint Jones, Chief Financial Officer & Director

Other Participants

- Andrew J. Crean, Analyst
- Barrie Cornes, Head-Research Insurance
- Dhruv Gahlaut, Analyst
- Dominic O'Mahony, Analyst
- Edward Morris, Analyst
- James A. Shuck, Analyst
- Philip Ross, Analyst
- Thomas Seidl, Analyst
- Wajahat Rizvi, Analyst

MANAGEMENT DISCUSSION SECTION

David Graham Stevens {BIO 6807391 <GO>}

Good morning, everyone. I'm David Stevens. I'm the CEO. Welcome to our 2018 Half Year Results, and thank you very much for coming out on this August morning to hear what we have to say. A brief introduction for myself. I'm very happy to stand in front of you, reporting on these positive set of results characterized by growth pretty much across the board and the company, growth in customers, growth in turnover, growth in profits and growth in dividends.

One particular milestone I'd like to flag up is the arrival at profitability of our EU insurance companies, as we're calling them, somewhat preempting Brexit at Spain, Italy and France, flexibly (00:00:47) making a profit for the first time.

Talking more about our numbers will be Geraint, the CFO. Talking about the group numbers, Cristina, UK Insurance CEO. And Alistair, Head of Service for the UK, talking about the core UK business. And then, I'll come back and talk about price comparison and then international insurance. Thank you.

Geraint Jones {BIO 19738535 <GO>}

Thank you, David. Good morning, everyone. I've been trying to work out all week why Investor Relations have seen it fit to include a picture of me with egg on my face at the results, but I can't quite figure that out yet. I'm going to do my usual run through the result highlights. I'll talk about capital and the dividend, and I'll finish up with a brief update on Admiral Loans.

To start off, this is our usual highlights slide. David has given the flavor already. I'll pick up a few more words. The top line figures are at the top, continued really good growth across the group, plus 14% on both customers and turnover measures in H1, £1.7 billion of turnover, 6.25 million of customers. All parts of the group are growing. Those are both record figures. Similar rates of growth in solvency 2017. Pre-tax profit was up to £212 million, plus 9%. EPS was up similarly. Both of those are record figures. Another very positive return on equity

and you probably agree, 54% is basically in line with last year, reflecting strong profitability especially in balance sheet. And our interim dividend is £0.60 per share was largely up in line with earnings per share. And finally our solvency ratio still definitely qualifying as very strong, just under 200%.

Next slide, looks at customer and turnover growth across the group. Looks a familiar picture from last time. All the arrows are green. Particularly impressive growth again in Households up around 40%, period-on-period in customers and turnover. That means that we added nearly 120,000 household policies in the first six months.

Our International Insurance businesses had a nearly 20%. Customers and turnover was improved in the results nicely as you'll see shortly. And a couple of nice individual milestones to report. Elephant hits 200,000 vehicles in the last day of first half. And L'olivier in France moved past 150,000 in the same month.

Of course, not at all to forget UK Motor, which is cars and vans. We reviewed very well in the first half, 14% in terms of turnover, 12% in customer numbers, netted over 200,000 cars in the first half, moved past £4 million. And the total you see there includes over 200,000 insured vans. Our combined price comparison businesses grew a bit more modestly, turnover was up 6% to nearly £80 million.

Moving on now to look at profit. As you've seen already, we made £212 million pre-tax in the first half, £211.7 million to be precise, that's 9% up half year-on-half year. We'll go into detail on the various segments throughout the presentation, so I'll just make some high-level comments here. The main contributor clearly is still UK Insurance. Profit was up 9% to £247 million.

Bad weather hit the Household results and there was a loss there of £2 million, that was around £7 million lower than it would have been with normal weather. Motor result was strong £250 million of profit in the first half, 11% up. There were a few offsetting practice as usual within that result of higher other revenue as a result of the growth was an important driver. Just to remind the UK Car insurance profit is still on reserves at Ogden at minus 0.75%.

It's particularly pleasing to see a big improvement in the international Insurance results, which moved from a loss of £10 million in the first half 2017 to basically break even in the first half of this year while it's growing the top line by the 20% period-on-period. Net results made up of a third of profit in ConTe in Italy. And actually a combined profit since David has already mentioned from our European insurance for the first time. That was just under £3 million. Net total figure was slightly offset by a loss, albeit improved period-on-period around £3 million at Elephant in the U.S. Very pleasing international results.

Price comparison, as you can see, was essentially flat with a good increase in profit at Confused.com in the UK, offset by lower profits in Europe with Compare.com in the U.S. broadly flat period-on-period.

Loans, I'll come on to very shortly but the increased loss we saw there was entirely reflecting the significant growth of our business in the first half compared to the first half of last year. And other which is everything else, we put a detail again in the back of the slides so you can see the whole breakdown. But the main points as you can see, firstly, 2017 investment income comes from realized gains on investments held in the parent company, not repeated in 2018. And then secondly, higher shares in charges and the increase there in the current year is mainly driven by changes in vesting assumptions for variable awards.

Moving away from income statement, let's take a look at capital. This slide shows our Solvency position at the half year in terms of the amount of capital, capital requirements and resulting ratio. At the end of June, the half year point is 196% down from 205% at the end of 2017

and 214% in the middle of last year. Main movements in the current year, as we expect, economic profits in the period (00:06:04) interim dividend and an increase in the capital requirement which is due to growth.

In the ratio in the six months is due to the combination of that small increase in the capital requirement and a very small reduction in own funds. The basis of the capital requirement is still the standard formula plus the capital add-on. And in terms of internal model, our team has made very substantial progress this year in preparing our application, and we're having good, positive interactions with the PRA. We do expect, however, that those discussions will carry on a bit longer than planned, and we now expect to apply the model approval into 2019 rather than towards the end of this year.

But in terms of what that means to the endpoints of model approval, in a good scenario, it doesn't really change. We'd be looking at the middle of 2019 for approval. On a less good scenario, we won't be looking at the end of 2019 for approval. When we report our full year results in early 2019, we'll be in a much better position to give clearer guidance on that and hopefully start to share some numbers with you as well.

In terms of future guidance to solvency, another repeat of what I said six months ago, we think that 150% is a good indicator of the upper end of the target range once we get through model approval. And up until that point, we won't make further comment on surplus capital that we're currently holding.

Moving on to the interim dividend. As you can see, we've declared £0.60 per share, 7% higher than 2017's interim, and is 97% of the first half earnings. Not too much more to say on the dividend, moves largely in line with profits as we guided and that you've seen before. To repeat the former policy on the right-hand side of the slide, and I'd reiterate that unless or until we say otherwise, the guidance for dividend is in the 90% of the payout ratio, and we've got the relevant dates on the slide as well.

Now, one of the pillars of the Admiral Group strategy is diversification beyond insurance, and Admiral loans is the most important part of that right now. This slide gives a brief update on our progress in H1. As you can see, we've continued to grow quite significantly and over £200 million of loans were outstanding at the end of June. We're very satisfied with the way the business is going, including with the quality of the business we're making. We continue to be prudent in terms of risk profile.

We finalized the next stage of the external funding for the business at the end of June. The majority of that balance is funded externally rather than from group resources. Now, the new funding will see us well in 2019 and plans are well underway for the future stages.

The loss for the period, as you can see, was £6 million, and the guidance for the full year slightly raised to £10 million to £12.5 million of loss. And that change is due to growth from the front loading of costs in that period rather than anything adverse. But I'd also say at this point, we currently expect 2019's result will be better than 2018, obviously subject to thing developing as we are currently expecting to. We plan to have Scott Cargill, who's the CEO of Admiral Financial Services, who's in the room today. He will present to the full year and give a more detailed look at Admiral Financial Services.

That's it from me. I'll leave you with a couple of highlights. Firstly, more growth, group growth, plenty of it. Secondly, a really pleasing improvement in the international results. Third, continued improvements in Household and Loans. The results of the first half were impacted by weather on Households, strong growth for Loans. And last but certainly not least, a very strong solvency position maintained after paying a record interim dividend.

So, over now to Cristina and Al to talk more about the UK.

Cristina Nestares {BIO 18674745 <GO>}

Good morning, everybody. Alistair and I will cover the results for the UK Insurance operations. I'm going to start talking about the results for Motor and the pricing of the market in Admiral. And then, Alistair will cover some aspects of our Motor operation including claims, expenses and customer services. And then, I will finish talking about our Household results.

First, this picture, it shows Innov8. It's an annual event that we hold with staff from all parts of the business and they come together to work on innovative ideas. Some of the ideas coming out this year included application or more applications for robotics and also ideas in certain (00:10:23).

Now, before we go into the details, this is a reminder of the pros of our Motor and Household business over the past few periods. In summary, we have seen very strong growth in Household and good growth in Motor. For the first half of the year, our Motor book grew by 12% and that includes an 8% growth in the number of cars on cover and also the growth of our (00:10:46) book which is now around 210,000 customers. Household grew by 42% in this period and profit in Motor grew by 11% in the first half. And as Geraint said, the Household result was impacted by the weather.

In terms of loss ratios, this slide shows the current best estimate loss ratios with the numbers in bracket showing the movement in the ratio in the first half of the year. Now, the best estimate that we showed them to be conservative especially for the most recent years. So, the changes that you see in the first half are normal, are in line with we normally show and they reflect positive back year development. The 2017 year currently at 74%, looks like it's going to be a good year. However, we continue to experience some distraction in the pattern of settlement, large claims with uncertainty although we expect some changes to this in the next few months. And finally, we have included some additional information in the appendix of the presentation including best estimate ratios on an underwriting basis and also profit sensitivities on a number of different loss ratio change.

Moving on to look at reserve releases. You see another large release of 26% of premium above the long-term average of circa 15%. The large release is driven by positive prior-year development as well as a slight reduction in the reserve margin. The margin remains prudent and significant which is consistent with trends over the past few periods. As usual, we would expect continued large reserve releases in the future if things develop as suspected.

In terms of commutation, we have fully committed all years up to and including 2016 in the first half of 2018 as we would normally would. There was no commutation in the first half of 2017 due to the open situation. Therefore, there is around £30 million adverse impact on the income statement which impacts the comparison with previous periods.

Moving on to pricing in the market. It's clear that market prices have declined in the first half. We have put a graph on the left that shows two indexes. The ABI index is in green and it reflects or is based on business written, so it includes new business and renewals, and it shows a small decrease in Q2. The Confused index in blue, it focuses more on new business puts, so it tends to show much more radical changes and it overstates in both directions. But it shows an 11% decrease in Q2 year-on-year.

On the graph on the right, you have Admiral's Times Top. The graph is indexed to 100 in June 2017. If you focused your attention from January this year, you can see that we have been losing (00:13:47) and that is because we have kept our prices dropped. That is we have not increased prices in the first half of this year.

Now it's hard to predict the outlook of a market for the rest of the year but we believe that the reduction that we've seen in prices are unlikely to continue for much longer. So we think that we might not see premiums dropping as fast as in previous cycle, and this is due to the underlying claims inflation, the government's response, which are likely to be pushing to the future, as Alistair will explain, and also more rational players in the market.

In Admiral, we have always focused on a balance between growth and margin. And recently, during Q3, we have done a small price increase to reflect the underlying claims ratio.

And now I'm going to pass it to Alistair to talk more about our claims.

Alistair Hargreaves {BIO 20595748 <GO>}

Good morning. My name is Alistair Hargreaves. I've worked in Admiral for around 10 years in a number of different roles in the UK business. I'm currently Head of Service, responsible for Marketing, Claims and Operations. So I'm going to start talking about claims.

On the left-hand side, we see the market claims frequency over the last five years. There's a long term trend that's a gradually declining frequency, and some fluctuations due to winter weather. Most recently, there were some very positive reductions in 2017, which were reversed in the first quarter of 2018 largely due to particularly bad winter weather. Our own claims frequency trends are very similar.

On the right-hand side is an exhibit to get a sense of the relative type of claims cost that drive our ultimate loss ratios, which shows the three key components; damage claims, largely bodily injury claims, and small bodily injury claims. Large bodily injury claims are large in value, they're very small in volume and hence results in some volatility.

This year, we continue to reserve at a discount rate of minus 0.75%. And this, combined with expected changes in the discount rates, make it harder to comment on large bodily injury claims. So, I can't say that after seeing a relatively low level of new large bodily injury claims in 2017, we have seen them increase somewhat in the first half of 2018. This is prudently reflected in the current year loss ratio and these large claims take time to develop and will be influenced by any changes to the discount rate. On all the years, we continue to see positive developments on large bodily injury claims over time.

On the next slide, we see drivers of the small bodily injury and damage costs. The graph on the left-hand side shows the 12-month rolling total of small bodily injury claim notifications for the market. There's a declining trend through 2017 and this is leveled off with lower levels of notifications maintained in 2018. On the right hand graph, we see market severity for damage claims. This shows continuing inflation at the rate of 6% due to increasing technology within cars. Our experience on both BI and damage is broadly in line with that of the market.

So, they are the underlying trends, but to understand the claims outlook we also have to consider the change to the Ogden discount rate and whiplash reforms. It's been signaled that the Ogden discount rates will move from minus 0.75% to between north of 1%, reducing the average severity of large bodily injury claims. The whiplash reforms include increasing small claims track and new tariff system is intended to reduce the cost of small bodily injury claims. The key point in this slide is that although both of these measures are within the Civil Liability bill, the expected timing is different

Following royal assent, the discount with Ogden (00:17:47) is currently expected to be completed with September 2019. The whiplash changes are also dependent on a new portal to allow customers to notify whiplash claims direct, and these changes are currently expected by April 2020 at the earliest.

In summary, overall Admiral claims trends continue to be similar to those in the market, relatively low frequency and small bodily injury frequency, with pressure on damage severity and an increase in new large bodily injury claims. The most significant development in 2019 is likely to be the increase in the Ogden discount rate.

So moving on from claims cost, let's take a look at the expense ratio. In the first half of 2018, our expense ratio increased largely as a result of increased acquisition cost due to faster growth. The graph also shows the comparison to the market, which is more difficult because of the change in data available but we maintained a sizeable advantage.

On the right hand, we show that there are two drivers of our expenses ratio advantage; a higher average premium and our lower cost per policy. Interestingly, the mathematical advantage from higher average premium only equates to 4% to points of our expense ratio advantage. We continue to have high-risk, high premium policies but our growth in recent years, combined with others in more high-risk business has somewhat reduced this difference.

However, the most important component of our expense ratio advantage is the actual cost per policy, a key component is acquisition cost, which is over a third of total expenditures excluding levies. I'll talk a little bit more about this. Our acquisition approach, a disciplined marketing spend and embracing price comparison keeps cost down. But a key driver of acquisition cost is the number of customers who are newly acquired, or to flip it, the number of customers who stay with us. Consistency is a measure that reflects the proportion of customers who stay with us for a full term and then also stayed to start a new policy at renewal. The graph shows we have better consistency than the market. However, we do not expect this to be the case necessarily. A greater share of our customers come to us for price comparisons, and we have a higher proportion of higher risk, higher premium customers. Both of these factors should result in lower consistency.

So, why do our customers stay? Well, it's always important to remain competitive on price. But another key factor is our service. On the left-hand side, we see indicators of customer satisfaction. Our customers stay because they receive great service. Underlying this is our culture, which Cristina will touch on in a moment. But the key point here is our people including agents, who serve the customers directly and others who work on products, projects or technology really care about the service that we deliver to our customers.

And the right-hand side is an example, showing calls received from active customer. The types of calls we receive is something that we focused on. Ease of service is important. Can we make changes to say the task at hand is called. This exhibit shows reduction in calls for 15%. This reduction means we have less calls to answer and it's also saving the customer effort which is good for the customer, and hence consistency.

The improvements are due to a number of initiatives that include improvements to allow customers to make more changes for that policy online. Online service is an area of focus for us. We also have live chat, online claims notifications and we're trailing a total loss portal.

That's all for me. Now, I'll pass it back to Cristina.

Cristina Nestares {BIO 18674745 <GO>}

So, let's take a look at the Household results. A key thing for the Household business since we launched five years ago has been stronger and we have continued with the trend in the first half of the year. The factors, the drivers we have remain the same, the growth of price comparison channel which we believe continue in the future, but also the growth of our direct and cross-sell activities. We use MultiCover to sell car and homes from existing customers.

In terms of the results, we have mentioned a few times that they been impacted by two weather events. The freeze that affected much of the country in March and also the flash flooding that impacted mainly the East Midlands in May. As you can see on the graph on the left, these two weather events added 25 points to our loss ratio and they accounted for £7.5 million. As a result, we have posted a loss of around £2 million. However, if we exclude the impact of these weather events, we would have shown a profit of £5.6 million.

One key advantage that we have able to replicate from our Motor book to our Household operation is our excellent expense ratio. As you can see on the graph, our expense ratio continues to improve and (00:22:50) advantage versus the market, which is around 45%. This is particularly relevant when considering our strong rate of growth as expenses in insurance tend to be frontloaded. This advantage is based on a more efficient operation and on our acquisition strategy. For the remainder of the year, we expect to continue growing and to return to profitability of course whether permitted.

Now, before finishing, I would like to highlight one aspect of our business that we're particularly proud of, which is our culture. We believe in Admiral that people who like what they do, do it better. And also, that behind happy staff, you have a lot of happy customers. So, we came this year number three in the Best Workplaces survey. But also, we are the only company that has been part of this Sunday Times 25 Best Big Companies to Work For since the inception of this survey back in 2001.

Also this year, for the first time, they have published a study of Best Workplaces for Women and we are very pleased to come number three. But also, I guess, the more important I think our inclusive culture is also reflected on our paying structure and we have the lowest pay gap among major UK insurers.

So, in summary, good growth both in motor and especially in household. We have growth our car book by 8% despite not putting prices down in the first half. We have improved our result for motor and the household result has been impacted by the weather. And finally, we expect a more stable UK Motor pricing outlook mainly due to current claims inflation pressure.

And now, over to David to talk about our international results.

David Graham Stevens {BIO 6807391 <GO>}

So, before going to price comparison and international insurance, we have a picture here of the inaugural European Insurance Master Chef competition where our employees from Spain, France initially gathered to compete and our CEO in the front row volunteered to judge. Big success from the Welsh management team who is very keen to get involved next year. We're confident we can teach the Spanish, Italian and French a thing or two about gourmet cuisine.

Price comparison first. For Confused, a good six months. 6% growth in turnover, 29% growth in profit before tax to just under £6 million. Small increase in market share but most of that increase in profitability is around operational efficiency particularly reallocation of digital spends or the more efficient digital media.

The European insurance price comparison Rastreator and LeLynx had a tough year, slow growth and some shrinkage in margin.

Two factors involved there with the major one was the launch in France as a third television advertising price comparison. So, now, you have (00:25:46) compared to market and (00:25:50) as TV advertising. Great news for insurers that sell/buy price comparison and ultimately potentially great news for the sector as a whole as we collectively educate the French motorists upon the most efficient way of buying insurance. But as something of a headwind in terms of the efficiency of marketing for the LeLynx in the first half.

Going over to the state in Compare. The biggest thing of influence on Compares is obviously in the first half with a very strong change in sentiment in the U.S. auto insurance market. This shows the U.S. auto insurance combined ratio and 108%, although it might not sound too frightening for those of you familiar with the UK insurance market, was something of a shock to the U.S. auto insurance market. And the focus in 2016 and 2017 was very much on repairing margin, increasing prices.

As you can see, the combined is coming down on earned ratio and a number of major insurers are now writing business profitability, and our team to grow the top line as well as repair margins. That's led to those insurers particularly competing more aggressively for the attention of the 25% to 30% of U.S. motorists who shop every year. And that caused some inflation in the marketing arena, an arena in which Compare competes.

As a result of that, the operational improvements we made in the first half has been offset by a more challenging marketing environment in a loss of, say, roughly flat year-on-year. Conversely though, because more insurers are interested in growing their business, more insurers are interested in participating in Compare. And we've seen two or three quite substantial insurers coming to us during the first half of 2018 and asking to get involved such that by the end of the year, we are expecting to be in a situation where 16 of the top 25 insurers in the U.S. are represented on compare in some way or another.

Now, I have to caveat that because it might be that they're only in one state. It might be they're – one of their brands. But 15 will be there by the end of the year. And that's a very positive progress and good for the long-term prospects of the business. I haven't cracked the top four I mentioned last time that in concept, the third biggest brand from all state have got involved last year. And we've made further progress with insurance direct brand coming on board in a test mode just early in the second half of 2018. So that's progress but still a way to go in terms of cracking the top four.

U.S. insurance, Elephant, very strong first half, a return to substantial growth, 10%, in six months up to 200,000 customers. And that's the persistency strategy beginning to pay off in terms of customer growth as well as the attractiveness of the underlying business. Fee business is still loss-making, it's still on the right-hand side. That loss is on a whole account basis (00:28:57) turnover worth 11%, down from 16% a year ago. Roughly 1.5% of that is a more benign hail season in Texas than the previous year but still substantial progress that seeped through into a $4 million loss for us on the business as a whole. And then very proud to see that in our biggest states we're now outperforming the market as a whole on loss ratio.

EU insurance come up a couple of times already but very happy to see the business reporting a profit of €3 million, continuation of a trend. And over that period, we've also been increasing the reserve strength across Spain and France building on the conservatism that we've already seen historically in the UK and Italy.

So, I'm very encouraged by that and particularly encouraged by the fact that we haven't had to buy profitability by stopping growing, 18% growth alongside the emergence of profitability. I won't go into more detail because there's a European Investor Day on September 17. Just to set expectations, we're not planning a dramatic announcement (00:30:10) on that day.

We've had a number of investors over the last few years who's after more color, more detail on our international businesses, and we'll give you that, and we'll give you about the markets in which they operate as well. Also a chance to meet some of the management team there, important part of the Admiral talent core, and hopefully give you the two cents the opportunity to get a feel for the valuation relevance of the EU business over the medium to long term.

So in summary, increased profits from Confused, a return to growth lower losses in Elephant, and European insurance profitable.

Now, I do like to wrap up with a longer-term perspective. Investor Relations has put this picture in first which is me thanking staff in Wales for 10 years of service. I noticed my colleague is staring glassy-eyed into the distance which may be a subliminal suggestion from Investor Relations that I can't go on too long.

So, I'll keep it short. And so first on the core UK business and the long-term trend. One of the long-term trends is the growing importance of focused, listed UK personal lines played in the market or perhaps to be truly up-to-date, focused listed in price and private equity owned

You tape up the line players who now represent or the end of 2017 represents 40% of the market. It's higher now. And by the end of the year, we'd expect it to be (00:31:42) approaching 50% and that's a function of obviously companies floating. But it's also a function of those companies having above average growth notably ourselves, Hastings and Esure.

So, what – well, I think the so what is that when you have the market completely dominated by players that have that personal line installments from the UK and the discipline of the market, you get a more rational, collectively more competent market and that is good news for everyone. It leads to increased stability in our view, good news to shareholders who don't like the variability that the market historically has delivered. Good news for customers who don't like the roller-coaster pricing of extreme cyclicality that has been a feature of the UK market over the last few decades.

So, I think a better context for us going forward and for our peers, this is the business that accounts for the majority of the value now. Going forward, I'm convinced that our diversifications will deliver incremental value to our shareholders. Taking the same sort of time perspective and looking at our business, where the bubble size is defined by the number of policyholders or more recently loan recipient. I can't do price comparison on that model, so it's in the numbers at the bottom, but it's not in the bubble size.

What you see in 2010 is an irrelevant diversification in terms of size, but not irrelevant in terms of losses at minus £13 million, its losses beyond UK Car and Confused. 2014 is still looking pretty irrelevant in terms of size, but it's looking even more relevant in terms of losses at minus £30 million-plus.

And now 2018, I think the visual way of saying that these diversifications are relevant and importantly are also less expensive. So, we're spending less on this in 2018 than we were in 2010. So, I think a healthier environment for the core business and good prospects with diversifying businesses.

Thank you for your attention. Happy to take questions.

Q&A

Operator

Ladies and gentlemen, at this time, we will begin the question-and-answer session.

Q - David Graham Stevens {BIO 6807391 <GO>}

(00:34:20) second, just point of clarity, I'm not sure if I heard it right. When you were looking at the second half of this year in terms of motor, did you say the rate of increase would accelerate or decelerate? I just didn't quite hear that.

And then, in terms of reserve strengthening in Spain and France, was that – was it some strengthening that went on in the first half of this year or you're talking about the last few years? I'm just trying to understand if it was a headwind or if it was...

We're taking a conservative approach towards earnings. That's been most relevant in the UK and Italian market because they're exposed to bigger bodily injury claims. We have extended that into France and Spain (00:35:09) become more material. I was mainly making the point to say that we haven't delivered improved those results by accelerated release of reserves pulling forward (00:35:27)...

So, what's been the change there?

It's been changed over time in favor of (00:35:35) over a number of years. Cristina, are you happy to take the first two points?

A - Cristina Nestares {BIO 18674745 <GO>}

Yes. Second question is decelerate. So, basically we have seen in Q2 strong decreases in prices, and we think it's unlikely that it's going to continue for much longer given the claims inflation. In terms of ABI initiative, we are fully supportive. We think it's a market feature, but there are changes between (00:36:01) renewals, and there are things that we can all collectively do to make it easier, the journey for our customers, especially focusing on furthermore customers. I also believe that due to price comparisons, motor insurance is one of the most transparent industries in the market when it comes to prices.

Q - David Graham Stevens {BIO 6807391 <GO>}

(00:36:18)...

A - Cristina Nestares {BIO 18674745 <GO>}

We don't give (00:36:25)...

A - David Graham Stevens {BIO 6807391 <GO>}

Other questions? Gentleman over there?

Hi, morning. Tony Evans (00:36:33) from UBS. Two quick ones for me. So, on the Motor pricing outlook, I know that you're highlighting that it's still uncertain and that you're expecting stable pricing from here. I wondered why stable if we are seeing signs of high claims inflation across the market Admiral and peers. Admiral is now increasing prices a little bit in Q3. And Q2, there was a sharp deterioration, as you mentioned. It feels like perhaps pricing should be rising a little bit at the market level.

And secondly on the Admiral Loans portfolio, when would you expect this to return to profits (00:37:08) to make a profit?

Do you want to do the pricing and maybe start in the audience. I'll now talk briefly about the prospects for loans, Cristina?

A - Cristina Nestares {BIO 18674745 <GO>}

. Two aspects that we have to consider. The first one is 2017 is probably going to be the best year in the (00:37:25) so we start with a very healthy margin, and that's why we might then see increases in prices there.

A - Geraint Jones {BIO 19738535 <GO>}

Let me start by saying that the ambition for this business is that we are looking to change something that's meaningful and sustainable. And certainly over time become a very significant contributor to the group profit. We – as Geraint said before, we're playing the markets that are personal loans and car finance and that's our focus.

Over the last few years, we've recruited our team, which is experienced in these markets. We're seeing distribution moving in our favor, particularly for a direct and price comparison, distribution lines or familiar for Admiral Group generally. And over the last few years, we've been building and testing our underlying capabilities and we're happy with the early progress of the year.

Over time, I'd also like to – we would expect the whole – when we get to our certain skill, we'll built a free an expense advantage and something that we are starting to have a strong believe in. So, positive start and I look forward to do more at full year.

Q - Wajahat Rizvi {BIO 19928187 <GO>}

Wajahat Rizvi, Deutsche Bank. Couple of questions on me, please. One on the UK car Insurance top line growth. So, part of that I guess would be the reinsurance renewal and your competitiveness being restored mostly often. But is there anything else or any other initiatives or anything which are driving that growth because the growth is pretty sharp compared to last year?

And the second one would be on price comparison business. So, you've talked about our diversification pillar of your business model. There, your strategy seem to be a stark contrast to your peers who are looking to diversify in other verticals of energy and other stuff where you're focusing on the car market. So, just wondering if you can comment on that in terms of diversification.

A - David Graham Stevens {BIO 6807391 <GO>}

So I'll do price comparison. Alistair, would you want to do growth of the UK car base and what's driving it?

A - Alistair Hargreaves {BIO 20595748 <GO>}

I'll do it. Yes. Okay. So I think in terms of that 12% customer growth, Cristina showed our (00:39:54) which is higher than last year. So there's partly our competitiveness in the first half. And the other thing that's maybe a bit different is the bond that's included in those numbers. So Cristina mentioned we've now got just over 200,000 bonds on cover.

A - David Graham Stevens {BIO 6807391 <GO>}

Thank you

Price comparison, I think you have to look at the world, Confused and the others primarily. So in the Confused context, where you have four established players in the mature market, what we've chosen to do there as a source of differentiation is to focus particularly on an offering to drive of which is car insurance, car finance, and other car-related products, where I think it's important to differentiate in a world where you have maturity and established players.

Internationally, we're investing in diversification. On one of the bullets in terms of the lower margin in the European insurance entities – price comparison entities was around investing in diversification, and energy would be a case in point in France, for example, where last month we launched an energy vertical. In Spain, we've launched recently a mortgage vertical and a car buying and selling vertical. So, we are broadening the product offer in those markets where price comparison is still very much an emerging phenomenon and where we're typically in leadership positions.

And then we'll go on forward.

Q - Edward Morris {BIO 16274236 <GO>}

Thanks. Edward Morris, JPMorgan. First question is just on the impact of weather. You told us how much it cost you in the home business. But I wonder if you could indicate whether there is any impact in Motor which the profitability affected the tone in the first half in weather?

And the second question is on the new financing for loans business, the warehouse arrangement that you have. Can you just explain how the economics of that work? Is there a certain limit that it runs up to and ultimately is it something that you would look to securitize or what is the (00:42:01)

A - David Graham Stevens {BIO 6807391 <GO>}

On the loan part of the question, I think what would be valuable for our investors is a deeper dive in the loans in general. And that's what Scott would deliver at the full year results. So one of the important elements of that will be understanding the funding we put in place and the options going forward. So forgive me if I defer the answer for six months on that one.

The first part of the question is around household? Sorry on non-household, yeah.

A - Geraint Jones {BIO 19738535 <GO>}

(00:42:27) despite what we see on frequency Q1 2018 that's debt showing weather impact and going forward, one. Thank you.

Q - Dominic O'Mahony

Thank you. Dominic O'Mahony, Exane BNP Paribas. So two questions for me. First is on the impact of commutations. This shows a negative impact during this period. I was thinking about going forward. Clearly, 2017 is better than 2016. The 2017 also seems to be quite a good year across the market. So two parts I guess it is. If 2017 improves by a point or two, are you expecting to see a negative impact on computation of value?

And then more broadly going forward, should we get used to the idea of sort of small negatives when you commute which then unwind into positive (00:43:19) in future years? And then, my second question is just on (00:43:23) UK Car, 26 points is well above your 15% long-term figure. Could you just help us understand what that would have been without the slight relaxation in figures (00:43:34)? I think this time – six months ago, you told us it would have been more aligned with that long-term figure. Does that still hold? Thank you.

A - Geraint Jones {BIO 19738535 <GO>}

Thomas mentioned that the reason we – community reinsurance is when we have the option is (00:43:47) economic sense to do so. So, reinsurance is cheapest to us if we could use it as early as we can. If we think there's enough headroom and the possibility of underwriting it, then we'll choose to do that as soon as possible. What tends to happen is when we book an underwriting, you're at loss-making point to earlier on (00:44:00). It means that we're recognizing an accounting loss platform.

I think it's probably fair to assume that we will carry on doing that as long as our underwriting years continue to look profitable. And we will have this sort of £30-ish million negative impact usually in H1, which then addresses the plan of the underwriting year we released. So, I think there probably is a trend.

And on the reserve release – on non-reserve releases, I think 20%, you're right, is quite a bit above the long-term average. We've reduced the size of the margin, while that we understand that a certain release that have been closer to the long-term average but still above (00:44:36).

A - David Graham Stevens {BIO 6807391 <GO>}

I think a question coming on the phone, I don't quite know how to accept it. But is there any questions on the phone?

Operator

The first question from the telephone is from the line of James Shrink (sic) [James Shuck] (00:44:51) of Citi. Please go ahead.

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

It's James Shuck from Citi. Good morning, everybody. So, I had three questions, please. Firstly, just on the Chase, the Munich Re agreement, that car insurance has been in place for kind of 20 years plus, as long as I can remember. I'm just wondering why now has been the time to change the allocation of the installment income so that you actually keep that because that's obviously driven quite a high proportion and increasing the other revenue per vehicle?

Second question around claims inflation, just returning to the large bodily injury size. So, you're saying there's a kind of uptick in the claims inflation from large BI. I've been hearing that the propensity to PPO would actually fallen very sharply. And I would have thought that would have been an offsetting impact. So, could you just explain a little bit about what's driving that negative development on large BI whether that a frequency thing or severity side of things.

And then thirdly, just around your systems and capabilities, I guess we're really having an update from where you are like in UK, mostly I'm referring to our UK Insurance, I should say in terms of your kind of capability. So, are you moving to kind of more flexible products? Do you have things in the pipeline that can allow much more tailored approach towards customers?

We know that there's a number of things in the pipeline from many of your competitors. So, I'm just keen to know how far advance you are on that side of things, please? Thank you.

A - David Graham Stevens {BIO 6807391 <GO>}

Geraint, do you want to take – thank you, James. Do you want to take Munich Re, Geraint; and Cristina, systems analyst PPO?

A - Geraint Jones {BIO 19738535 <GO>}

Good morning, James. On the Munich Re coinsurance contract has – you're quite right to be the place for quite a long time since the early part in 2000. We've made a couple of reasonably significant changes to the arrangement over those years, which generally move more the profit to Admiral and away from Munich Re, which is our objective because they're not in the room.

But the most recent change we made is to keep all of the installment income where previously they kept their 40%. The – on the face of it, that sounds like a very dramatic change. But actually, it means that we will less profit commission back from Munich Re because they learned best profit. And so, the net overall impact of that is actually quite small, positive to Admiral Group clearly. But that's the fact which line

in the income statement that change flows through, i.e., more installment income, less profit commission. The overall change is not that material.

A - David Graham Stevens {BIO 6807391 <GO>}

As presumably large BI and...

In terms of large BO, I was talking about the trends for new large BO. So, essentially frequency rather than severity. In terms of the PPO, I think we haven't seen large numbers of PPOs. Anyway, they tend to be used in specific circumstances. But logically a lower discount rate makes the lump sum option more favorable.

A - Geraint Jones {BIO 19738535 <GO>}

In terms of systems, we completed our migration to the Guidewire system and it went well. We don't talk more about it because it's been (00:48:00). As we said at the time, it allowed us to launch new products but also to improve overall operations. And just to give you a few examples. After the launch or the migration to Guidewire, we have been able to launch MultiCover which allow us to sell several products under the same policy and to price them together. We have also done a move to online (00:48:22) in the past and Alistair was talking about the reductions in calls and that's partly because we have a better system that allowed us to do these changes. So, overall, pleased with our system, but is an area that we continue investing heavily and are always keen to improve.

A - David Graham Stevens {BIO 6807391 <GO>}

Back to the room. So at the back row and then one in front. Yes, that one.

Q - Barrie Cornes {BIO 2389115 <GO>}

Morning. Barrie Cornes at Panmure Gordon. I've got a couple of questions from me. First of all, just wondered with the relatively good weather, whether or not you anticipate any substance claims on the horizon on the Household book. And secondly with the announcements the last couple of days, just wondered what your views were on M&A within the sector (00:49:06) very happy to continue organic growth? Thank you.

A - Cristina Nestares {BIO 18674745 <GO>}

Yes. We're mindful of the work given very unusual weather. I mean we had a weather extreme followed by dry and hot summer, so we're going to keep a close eye with it. We have seen smaller spikes in July but this is too early. Normally, we will tend to see this in September and October. So it's a bit early to comment. We're keeping an eye.

A - David Graham Stevens {BIO 6807391 <GO>}

And obviously interesting to see eSure bought out (00:49:39) you can tell to a hurried change in one of our exhibit. I think it perhaps supports the view that the sector as a whole is looking more and more interesting to sophisticated financial investors. In terms of our own growth plans, we've always grown organically. We don't dismiss the possibility that we could buy something at some point particularly perhaps to accelerate the growth of some of our secondary – common secondary products but we haven't come across anything yet that we feel is an appropriate purchase.

One forward and then we'll go back to the very back.

Q - Thomas Seidl {BIO 17755912 <GO>}

Thanks. Thomas Seidl, Bernstein. First on Compare.com, you used to have (00:50:17). So I have to ask you David. So can you explain how the competitiveness is increasing there and how it influences your outlook for Compare.com given it seems to stagnate right now?

Secondly, in the home, you just took out the £7 million events but clearly there must be a normal weather ratio for this business. So what would be a normal level of weather losses given you're much more diversified book right now? And then on large bodily injury. Can you just give us how much in the current year reported losses large bodily injury claims have gone up in percentage?

A - David Graham Stevens {BIO 6807391 <GO>}

So household weather, do you want to take that one Cristina?

A - Cristina Nestares {BIO 18674745 <GO>}

Yes. So the £7.5 million that I was mentioning, the only thing certain because of this two weather events that includes normal weather. And we normally don't give results split by the different (00:51:12)

A - David Graham Stevens {BIO 6807391 <GO>}

So On BI, it's particularly too early to try and quantify something that is very volatile in terms of numbers. And is it's very unpredictable in terms of ultimate cost. So, it would be misleading to try and put a specific number on the pattern we've seen in the first half of 2018 versus the first half of 2017.

What was the other one? Compare. Yes. Sorry. Okay. Well, I think what you have is you have a number of ways of driving business in the U.S. And particularly, the digital ways like Google and buying leads, it's simply the supply and demand. And so, the cost of being number one on Google or buying digital leads has increased in the U.S. market. So, that's the short-term negative.

Long term, the whole thesis behind Compare is actually the top four are eating up this market and they've just gone over 50% market share, and the other – you might say the other 600 because there's a large number of insurers. But actually, the other – the next 30 are collectively moving share and that's because they can't compete in the marketing context. Logically, Compare is a huge opportunity for them in the sense to core marketing dollars and function in a way that lets them actually grow their businesses efficiently.

That will happen if they give us their prices across a number of states, and if they pay us the revenue for sale that is the true reflection of the alternative cost of driving business. So, their appetite for doing that I think it materially increased by the term in the cycle and by the level of marketing aggression of some of the biggest players.

Q - Thomas Seidl {BIO 17755912 <GO>}

(00:53:01)

A - David Graham Stevens {BIO 6807391 <GO>}

One follow-up?

Q - Thomas Seidl {BIO 17755912 <GO>}

Yeah. (00:53:04) isn't there an issue that in the United States you have with Geico insurer which is likely to undercut any price Compare.com can offer. So as a customer, if I look for the cheapest price, you don't have Geico on the platform so why would I go in the platform?

A - David Graham Stevens {BIO 6807391 <GO>}

Well. I think that exaggerates Geico's overall competitors. I think off the top of my head, their market share is low teens. Yes, they would be a great addition to the platform. But when you take 20 insurers and put them up against Geico, you beat Geico as a material percentage of the time. If you have one or two insurers against Geico, you're much less likely to. So panel Brexit (00:53:49) is important.

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

Good morning. It's Andrew Crean, Autonomous. Three questions, please. Can I clarify on some £30 million shortfall in first half 2018 profit versus first half 2017 on the commutations? Are you saying that that will be made up in the second half? I'm not sure I totally understand the situation there.

Secondly, the slide you had on the expense ratio advantage I think 8 points was per policy. How has that impacted if you throw the shared scheme costs in, and why shouldn't you throw the share scheme costs in? So, they seem to be a fairly permanent part of P&L taking up 10% of the profits.

And then thirdly, on PCW, could you say whether you get any insights in your underwriting from the PCW businesses that you have because they don't look as though they are substantial or will be substantial contributions to the P&L and best case and strategy and why wouldn't one sell it?

A - David Graham Stevens {BIO 6807391 <GO>}

Do you want to do commutations?

A - Geraint Jones {BIO 19738535 <GO>}

Commutations. Hopefully, I didn't promise that £30 million would reverse fully in the second half. What it does mean is that we've commuted all years up to and including 2016. And so, the reserve releases that will come from those years recently been commuted will be bigger than they would have been otherwise. And so, you'll see a release in H2 from 2016 almost inevitably that will now be bigger because we've done our conversation. Whether all that £30 million comes back in the second half will depend on how much we bring the 2016 loss ratio down.

The timing impact was the fact that we didn't do a commutation in the first half of 2017. So, there's a – if you compare like-for-like, there's a £30 million adverse in first half of 2018. What we did do in 2017 was the commutation is actually in the second half of the year because the second half of 2017 was impacted adversely. So, one (00:55:46) full year versus full-year you probably see a commutation 2017 and a commutation in 2018, and it'll be more like-for-like if that makes sense.

A - David Graham Stevens {BIO 6807391 <GO>}

On the...

(00:55:55)...

On the profit share, profit shares run around 1.5% to 2% of turnover. We're not sure how some of those payments are accounted for equivalent payments in other insurance and whether they are included in the expense ratio. Clearly, there's transparency, and if people want to take that cost and spread it across pro rata, they got the information to do that.

In terms of price comparison, price comparison has been an important adjunct to our core insurance business over the years helping us grow the opportunity in the UK initially and subsequently abroad. And also, helping us have a deeper insight into the way the consumer was behaving. And we value that over and above the P&L impact. Having said that, it isn't as core as the businesses insurance and some of the diversifications into other insurance lines and lending. And if people are – we – as Henry used to say, everything's for sale apart from this wife. And I

I supposed I led my life through that.

Dhruv?

Q - Dhruv Gahlaut {BIO 16209870 <GO>}

Good morning. Dhruv Gahlaut, HSBC. Three questions. First, on the investment portfolio as in – should we expect any changes from your – in the next 12 months? Secondly, you've grown strongly in the motor segment. Has the risk changed materially and how should we think of that for the second half?

And lastly, in terms of Compare.com, losses have been broadly flat but could you say how the revenues have done, as in have you seen, the peaks are done, revenues are done, could you just draw some line there? Thanks.

A - David Graham Stevens {BIO 6807391 <GO>}

Investment assets, you've got the breakdown at the back of the pack. It looks basically the same as it did six months ago. I think we always look for options to try and not (00:58:03) but I think there's still returns. And we continue to do that. I wouldn't expect radical change.

A - Geraint Jones {BIO 19738535 <GO>}

In the motor book, no significant change.

A - David Graham Stevens {BIO 6807391 <GO>}

And in Compare, marginally up on the top line because we're not chasing the volume buying loss-making businesses. We're saving our powder a bit until we've got what we expect to be in prudent panel (00:58:25) later in the year or early next year, depending on how quick (00:58:29) takes.

A - Geraint Jones {BIO 19738535 <GO>}

Sorry, I couldn't help it. What time do we need to stop (00:58:40)? We need to stop now.

Q - Philip Ross {BIO 20618440 <GO>}

Okay. I'll make it very quick....

A - David Graham Stevens {BIO 6807391 <GO>}

You got one question.

Q - Philip Ross {BIO 20618440 <GO>}

Phi Ross from Berenberg. On UK household insurance, you mentioned the expense ratio come down around 5 percentage points partly due to efficiencies. I wonder if there's any specifics on that or whether it's driven partly by growth, partly by distribution as well?

A - Cristina Nestares {BIO 18674745 <GO>}

No. It's a continuation of improvement. The bigger we get, the easier it takes to be more efficient.

A - David Graham Stevens {BIO 6807391 <GO>}

So, there's one more. I promised one and then we're going to stop. I'm sorry about that.

Thank you. Good morning. (00:59:17). Just one point of clarification. You made it clear that you're not going to look at excess capital return until you get the results from the PRA back. So, that means even if we have a change of the Ogden rate and you have some visibility that was potentially at H1 2019, there still will not be in excess capital turn until we get the (00:59:39) from the PRA?

A - Geraint Jones {BIO 19738535 <GO>}

The hypothetical situation you get in Ogden rate change which results in more capital. Then it's likely we wouldn't hold on to that capital. But I wouldn't say that we were radically below where we currently are until we get into (00:59:56) model currently. Does that make sense?

Q - David Graham Stevens {BIO 6807391 <GO>}

Yeah.

A - Geraint Jones {BIO 19738535 <GO>}

Lovely.

A - David Graham Stevens {BIO 6807391 <GO>}

Thank you for coming and see you in six months.