Y 2017 Earnings Call

Company Participants

- Anthony Jonathan Reizenstein, CFO
- Michael Holliday-Williams, MD of Personal Lines and Executive Director
- Paul Robert Geddes, CEO and Executive Director
- Penelope Jane James, Executive Director
- Steven Maddock, COO

Other Participants

- Alan Devlin, Director
- Andreas Evert Cornelis de Groot van Embden, Financials Analyst
- Andrew John Crean, Managing Partner, Insurance
- Arjan Van Veen, Executive Director & Equity Research Analyst of Insurance
- David Bracewell, Research Analyst
- Dhruv Gahlaut, Analyst
- Greig N. Paterson, MD, SVP and U.K. Analyst
- James Austin Shuck, Director
- Kamran Hossain, Analyst
- Ravi Tanna, Equity Analyst
- Unidentified Participant, Analyst
- Wajahat Rizvi, Research Analyst

Presentation

Paul Robert Geddes {BIO 2474781 <GO>}

(technical difficulty)

for joining us here at Goldman Sachs for our full year results presentation, going into the detail behind the headline results we announced a few weeks ago. And a bit of a break from my usual format as I'm joined not only by our outgoing but also our incoming CFOs. Today marks John's 22nd and final sets of results and what a set of results to borrow from. I'm also delighted to welcome Penny James, our new CFO, as of Thursday. And Penny will be sharing some of her thoughts with you later. And as ever, other members of my team are here in the audience.

So without further ado, let's kick off as ever with the highlights. 2017 is the fifth successive year that we've delivered a strong financial performance. Our clear strategy and determination to make insurance much easier and better value for our customers have been the driving force behind these results. And 2017 was a great year for the group. We grew premiums by 3.6%. And within that, our own brands were up 9.3% versus 2016 with great results and largely driven by another excellent year for our Direct Line brand. Our continued focus on improving efficiency, combined with growth in direct own brands, meant we improved both the underlying expense ratio and the commission ratio. Operating profit from ongoing operations was GBP 611 million. Combined ratio was a very strong at 91.8%. And RoTE came in at 21.7%.

This excellent set of results and strong capital generation means we are today proposing a final dividend of 13.6p and a special dividend of 15p. Finally, our high-quality balance sheet is reflected in our solvency capital ratio of 162% even after those dividends.

I'm going to come back later in the presentation to tell you more about the initiatives we're going to be taking to deliver our medium-term targets and, in particular, our technology plan to support them.

So now for the final time, let me hand over to John.

Anthony Jonathan Reizenstein

Thanks, Paul. Good morning, everyone. Let me give you an overview of the main features of the results as ever with more detail in the prelim.

As Paul said, this is an excellent set of results and the highest annual profit we've reported in our 5-year history as a listed company. We grew premiums again in 2017, up 3.6% with a particularly strong results in Motor. Ongoing operating profit of GBP 610.9 million was GBP 207 million higher than prior year, which, of course, was impacted by Ogden. At the profit before tax level, we delivered GBP 539 million versus GBP 353 million in 2016, including a net positive GBP 33 million contribution from runoff and restructuring. Finance costs were GBP 66 million higher due to a one-off charge relating to the successful debt refinancing action we took at the end of 2017. The combined ratio was 91.8%, nearly 6 points better than 2016 reported and in line with 2016 pre-Ogden. And weather-adjusted combined operating ratio was towards the lower end of the target range.

Moving down to operating profit by segment. Motor and Commercial, which were impacted by Ogden in 2016, delivered significantly better results. This helped offset lower prior year in claims inflation in Home. Rescue and other personal lines profit was pretty flat.

Turning to premiums on Slide 6. The strong momentum across our own brand during 2017 enabled us to deliver overall premium growth of 3.6%. This growth was predominantly driven by Motor, shown here in the dark blue; while our volume growth combined with strong pricing, Motor premiums were 8.5% ahead of prior year. Home premiums were down around 4% due to partner business (though the picture here) is looking up. And we'll talk about that later.

We continue to grow Rescue premiums, shown in green. This was mainly due to our (inaudible) brand, Green Flag. Finally, Commercial, where premiums were pretty flat. It was such a strong year for Direct Line for Business, which grew premiums by 12% in 2017, helping to offset pressure in NIG, which was down 3%.

On the (inaudible) the overall premium growth was driven by direct own brands, with Motor, Green Flag and Direct Line for Business all reporting double-digit growth. And Home was also ahead of prior year.

Looking at policy count. In this chart, we've highlighted our direct own brand, which continued to grow momentum and another year of strong growth overall, especially in our disruptive brands, Green Flag and Direct Line for Business, which were up 10% and 8%, respectively. Motor grew policy count by 5.6%, which showed our unique proposition cutting through. Home grew a little as well, up 2%, which is a good result in a very competitive market.

Elsewhere in the group, in the broker channel, NIG policy count was flat due to distinct pricing. The reduction in Motor and Home partner volume continued in '17. With our recent work with RBS/NatWest, it's showing positive growth sign. Other personal lines policies were broadly flat as growth in Rescue linked was offset by Rescue partners and Travel.

Looking at expense and commission ratios on Slide 10, starting with the expense ratio, which is in dark blue. Growing premium has provided for the leverage to improve the underlying expense ratio in 2017. The reported expense ratio of 25.3% was flat versus prior year. But if you exclude the impairment charge in both years, the underlying ratio was 0.5 point better and in line with our ambition to reduce the ratio at the time. We incurred an impairment charge on IT of GBP 56.9 million. Our total cost base, excluding that, increased by around GBP 28 million in 2017. This was mainly due to higher levies and to our higher premiums. Flat staff and marketing costs, alongside growing premiums, show we've been getting efficiency improvements.

The commission ratio, shown in light blue, was 9.1% in 2017 and 2.4 points better than the prior year. About half of this improvement reflects changes to business mix and new partnership arrangements. And the other half relates primarily to differences in weather, the escape of water in prior year as we've automatically flow through to partners via the commission line. Overall, we are pleased with the ratio improvement we delivered in 2017 and are confident that we can deliver on our ambition to lower these ratios over time.

Moving on to the loss ratio. The headline loss ratio improved by 3.5 points to 57.4%, mainly due to movements in prior year reserve releases. As for the current year loss ratio, which excludes weather, this is stable. At a segmental level, Motor delivered a strong improvement in current year ratio, which was offset by higher ratios in Home and Commercial. Prior year releases remained significant at GBP 392 million or 12.4% of earned premiums. This was lower than recent years although higher than 2016, which was impacted by the Ogden rate change.

Home weather was benign again in the second half, taking the total for the year to GBP 13 million against the budget of GBP 65 million. And note that the weather load for Home for 2018 is GBP 55 million, reflecting lower volumes as Nationwide runs off; and the Commercial weather load for 2018 is GBP 20 million.

Overall, we've improved our cost and commission ratios while holding our attritional loss ratio steady. So successfully delivered what we set out to do, mainly to improve current year profitability. We expect this trend of improving the contribution from current year to continue over time. Over time, the balance between current year and prior year will shift within our 93% to 95% medium-term combined operating ratio target. The point where this will balance and reach its maturity is several years away.

Looking quickly at operating profit. Here, you can see total ongoing operating profit increased by GBP 207 million to GBP 611 million due to significant increases in Motor and Commercial, which were impacted by Ogden in 2016. Motor recouped GBP 49 million of this Ogden cost in the first half of 2017. The contribution from the non-Motor businesses was GBP 247 million. That's 40% profit in 2017, showing the benefit for our diversified strategy. Commercial performed well and, again, contributed strongly to the group. Rescue has been a solid performer with strong potential we can realize.

Let's look in a bit more detail at each of the segments, starting with Motor. Motor pricing was very strong in 2017, albeit stronger in the first half than the second half. Our prices, which exclude IPT, were up 9.5% over the year, ahead of the ABI figures. As we said at the half year, the reduction in risk mix reflects the way we deploy the Ogden price change as we put through higher increases for younger drivers where the exposure is greater.

Strong EBITDA sales and high retention reported an overall increase in premiums of 8.5%. And we grew policy count by 3.8%. Motor profit was up GBP 215 million to GBP 364 million. And much of this movement is explained by the change to the Ogden rate, which reduced Motor profit by around GBP 150 million in 2016. The underwriting net result also reflects a material improvement in the current year loss ratio as a result of strong trading. We benefited from 2 tailwinds in terms of current year performance. First, there was a one-off benefit from having fixed our reinsurance costs ahead of the Ogden rate change. Secondly, we had better claims experience than we expected. These 2 tailwinds, combined with the strong pricing, enabled us to improve our margins. And this was reflected in a 4.4 points improvement in the current year loss ratio. We think these tailwinds, which will have benefited a number of property insurers, may also explain why pricing wasn't so strong in the second half of the year. At this point, we are reviewing -- we are viewing the better-than-expected claims data in 2017 as one-off. We have not changed our view of long-term claims inflation being 3% to 5% per annum.

Finally, at the end of December, we renewed our excess loss reinsurance at a somewhat increased cost, reflecting a change in the Ogden discount rate. We renewed all layers. But retained 10% of the first risk layer. We were pleased with the overall outcome, which looks better than some of the industry commentary we've read.

Next to Home. Now at the half year, we highlighted a number of actions we've taken to mitigate escape of water inflation. And we're pleased with the actions that helped return this to more normal levels. We believe we were one of the first to respond to Escape of Water; we increased our own brand prices in 2017, particularly on new business in the first half. This contributed to an overall pricing increase of 2.6% across own brands. The shift towards price comparison websites continued in 2017. And as we've written more volume to this typically low premium channel, this led to an overall reduction in own brand average premiums to 1.4%. When you take into account our pricing actions, IPT increases and last year's premium disclosure, we're very pleased that in a market with more customers shopping around, we're able to grow own brand policy count and premiums.

Moving to operating profit. Home profit was down GBP 38 million to GBP 129 million due to lower prior year from the December 2015 storms. So we're up against a tough comparator. The Escape of Water inflation also had an impact in the year. However, the operating profit overall was still above our normalized level as a result of another benign weather year with only GBP 13 million of weather losses versus our budgeted level of GBP 65 million.

Now to the other 2 businesses. Commercial delivered a very strong result, GBP 74 million of operating profit, which is the highest since group was listed. Excluding the impact of Ogden in 2016, profit was up 11%. And Commercial combined operating ratio was 93.4%, which is similar to 2016 before the Ogden change. Commercial current year loss ratio was up a bit in 2017. We interpreted the claims data cautiously at the year-end. And the reserving, therefore, looks conservative. And weather was also benign in 2017.

Finally, Rescue and other personal lines profit was broadly flat with a combined profit of GBP 44 million. Within that, Rescue achieved a slightly better result, offset by a reduction in other personal lines.

Moving on to investment. Overall investment return rose a little to GBP 175.4 million in 2017. And that's due to very strong gains both on property and on credit. You can see that the low U.K. interest rate environment continued to impact the group's net investment income, down GBP 10 million to GBP 140.1 million after hedging. As a reminder, our investment objective is to match the duration of our U.K. liabilities and protect the group's capital. We diversified credit exposure away from the U.K. and then hedged to bring the currency and interest rate elements back to sterling floating rate. So while high U.S. interest rates on our U.S. portfolio helped top line investment income, currently low U.K. rates are reflected in the higher hedging number and, therefore, lowering our investment income.

The result of all this is a net income yield on a sterling floating rate basis of 2.1% in 2017. And for 2018, we expect the trend to continue with a net investment yield after hedging back to sterling floating rate should be again around 2.1%. Again, the performance of our property portfolio has been very strong since the commencement of that portfolio in 2012. Given the current levels of the U.K. property market, we don't expect significant gains on property in 2018. Overall, therefore, we anticipate a total investment return in the region of GBP 150 million in 2018.

Now looking at how we get from headline ongoing operating profit to profit after tax on Slide 17. The run-off segment continued to benefit from positive prior year releases. And there's a partial offset by GBP 12 million of restructuring and other one-off costs. So combined, these 2 items contributed GBP 32 million to the overall result.

Moving down to finance costs. These included a one-off charge of GBP 66.1 million, which relates to the buyback of Tier 2 debt following the restricted Tier 1 issue. And that brings us down to a profit after tax of GBP 434 million, GBP 155 million higher than the prior year.

Now looking ahead, we are changing our guidance on the reporting of run-off and restructuring. We've previously guided to run-off and restructuring broadly offsetting one another over the full year period 2015 to 2018. As at the end of 2017, the net result of these 2 lines was actually a profit of GBP 43 million. We've decided to stop reporting these separately and to report a single -- simple, single operating profit line. We will, of course, highlight any material future one-offs. And the simplification has no impact on our targets.

With regard to finance costs, these will reduce to approximately half the previous annual charge of around GBP 40 million, with the restricted Tier 1 coupon of approximately GBP 15 million being reported in movement in equity.

In a moment, I'll hand over to Penny, who's going to take you through our capital position and also talk about the outlook for DLG. I believe our prospects are excellent and that DLG is well placed to continue to produce great returns for shareholders. Here's a summary of how things have turned out in the five years since we went public.

The first couple of years, our priority was to put the fundamentals right, pricing claims and cost efficiency. Over that period, we held our direct own brands policy count flat. But we came out of that period in 2015. That's the year we sold International. And have been growing direct own brand customer numbers steadily since then. These have grown around 5% in each of the last two years. Throughout our time as a listed company, we've stayed focused on our combined operating ratio target, shopping that target frequently and more recently extending it to the medium term. And we've managed capital effectively in order to translate that combined operating ratio and profit to strong return on tangible equity. All this has delivered great shareholder returns, as illustrated by the chart at the bottom right-hand corner.

I'm confident DLG is well positioned to bring you great returns in the future as it's done in the past. Thank you for your support, for -- and debate with me over the last five years and in the next hour.

And now, I'm delighted to pass it back -- on to Penny.

Penelope Jane James {BIO 15157212 <GO>}

Thanks, John. Firstly, I'd like to thank John for his extraordinary patience putting up with all my questions and curiosity over the past few months. Many of you already know me.

So I won't go through my background here. But if we haven't already met, please catch me afterwards and make an acquaintance.

Now I've had some luxury of a lengthy handover period. Since November, I spent most of my time visiting different parts of the business. I've been everywhere, from the customer-facing areas to digital, from NIG to marketing, from partnerships to accident repair centers. And in this time, I've observed many things about DLG that I think give us that distinctive advantage. But there are 2 that I want to highlight to you.

First. And most important, is customer centricity. Whether in a call center talking to customers or talking with a car mechanic or discussing strategy with the ex-CO, one thing is clear and consistent from this organization. And that's the focus on the customer. You can feel it in the direct line proposition, which is quite distinct. You can feel it in the unscripted customer calls. And you can feel it in the sensitivity with which our call handlers deal with our customers. Customer centricity is consciously part of the culture here at DLG. And I believe it's what delivers the direct own brands growth that John's been talking about.

Second is the depth of talent. Some of my new colleagues have been here for some years and have been the driving force behind the success you've seen on the slide before this. But others are much newer to the organization. And like myself, hopefully, bring fresh thinking in the leading areas such as data, procurement, technology, Green Flag and so on. But there's also plenty of opportunity for us to improve. I believe we can further leverage these strengths and build our capabilities across all our channels. So I'm enthusiastic about the direction we're going. And as always, further to go on costs and efficiency.

Paul will talk in detail later about our view of where we stand and what we're doing. But in summary, I believe there are some great differentiating strengths, an energized team and lots to do. So I'm really excited about what lies ahead.

Now coming back to the numbers. Let's take a look at the balance sheet that I've inherited. Here, we have our first full year of operating under the Solvency II partial internal model. And I'm very pleased to be presenting strong capital generation. It's important to note the figures are still draft and won't be finalized until the regulatory returns go in, in May.

Let's take -- looking at the slide, moving from left to right. We start the year with a surplus above requirements of GBP 910 million. Despite the growth in the business during the year, a couple of requirements actually reduced very slightly by around GBP 14 million. There are lots of moving parts. But it's worth noting that whilst we're still growing, we're also seeing a reduction in our net reserve. This reflects claims settling on all the years, the new year's mainly being reinsured down to around the GBP 1 million level; and recognition of the cautious approach to reserving the group has taken, evidenced by a history of prior year positive development.

Capital generation from our operating activities was GBP 487 million. Whilst there are some differences between the basis and Solvency II (for us) that creates variations year-on-year, generation post CapEx should broadly reflect the (RFS) profit over time, though currently, we're in a period of higher capital investment. Capital expenditure was GBP 94 million and in line with our previous guidance of GBP 80 million to GBP 100 million per year on average between 2017 and 2019. And that reflects the investment across the business, which Paul will be discussing later.

Our successful debt refinancing at the end of 2017 slightly strengthened the overall position. And finally, we've announced dividends totaling GBP 486 million for the year, which I'll now turn to.

The strong financial performance and capital position have enabled the group to rebase the regular dividend and recommend a special. The board's recommended a final regular dividend of 13.6p, an increase of 40p on last year and consistent with the guidance given at half year. In addition, the board's declared a special dividend of 15p.

Turning to solvency. At the half year, the group announced in normal circumstances, the board expects to operate to the ratio of around the middle of the risk appetite range of 140% to 180%. After the final and special dividends are taken into account, the group's estimated solvency ratio was actually 162%. This guidance to the level of solvency in normal conditions remains unchanged. But I would remind people that the nature of capital modeling includes some inherent volatility. And therefore, people should anticipate a small variation year-on-year even in normal circumstances.

Before I hand over to Paul, I'd like to close on outlook and targets. I inherit a strong and well-managed balance sheet, a history of prudent reserving and the current underwriting heavily de-risked through reinsurance. As you've heard, this is a business, which had shown real momentum, disciplined underwriting and an ongoing focus on efficiency. This, together with the investment across a range of initiatives gives me confidence to reiterate the medium-term targets. From a cost perspective, it's important the group maintains its focus on progressive improvements and efficiency. So we plan to continue to reduce our expense ratio and our commission ratio. Assuming current claims trends continue, we aim to deliver a 93% to 95% combined ratio through the medium term. And as our investments in business yield benefits, we expect to see a further rebalancing of our profitability between prior year towards current year. This is a key focus area for me.

Having rephased the regular dividend by 40% in 2017, we now seek to grow the dividend in line with the business.

And finally, on capital, we expect to be around the middle of 140% to 180% risk appetite range in normal circumstances. Of course, we maintain an ambition in the long term to achieve at least a 15% return on tangible equity. It's good to see that in striving to achieve these objectives, the team remain absolutely committed to invest in the future of this business. So that it's well-placed strategically and operationally for the changing environment ahead.

And with that, I'll hand over to Paul, to give you a real flavor of what we're actually doing.

Paul Robert Geddes {BIO 2474781 <GO>}

Thank you, Penny and John. Penny, it's great to have you here. John, we'll come back to you later. So as we've been through in 2017, we've delivered some great numbers. And these numbers haven't been achieved by accident, they're results of concerted management action on our priorities, which as we set out six months ago are: to maintain revenue growth, to reduce our expense and commission ratios and to deliver underwriting pricing excellence to fuel growth and good loss ratios. As you can see, we've delivered across all 3. Our own brands have driven our revenues higher. We've delivered good improvements to both our commission and underlying expense ratios. And we've delivered that growth at good attritional loss ratios. All of which, combine to grow our current year profits by GBP 87 million, albeit, as John said, including someone one-offs.

The key to this momentum, we continue to deliver initiatives to improve the business. And to explain the next wave of initiatives we're investing in, let's look at our channel strategies. So here's a chart, which we showed last year when I talked about returning our direct business to growth, having spent the previous phase optimizing our business of PCWs. This time, we've also included partnerships. We believe that our strength at all 3 channels is a major advantage for us at DLG. We start from a strong position, with leading brands in the specific channels supported by group-wide excellence, at customer service, great digital front ends and claims excellence.

Today, I'm going to set out our plans to push forward on all 3 channels at once. On Direct, our most advantaged channel, we want to keep up the momentum, particularly pushing hard into SME and Rescue. We also think we can do that in a way that's increasingly efficient for our customers and ourselves. On PCWs, which is where about 3/4 of Motor policies and about 2/3 of Home policies are bought, our ambition is to have the best capabilities. And when we have them, to grow in this channel. And partnerships, which took a bit of a backseat to our own brand business during the early part of the plan. But behind the scenes we've been investing in our digital capability such that today, not only is our major home partnership returning to growth. But we're now in a position where selectively we'll start to target and to win new partnerships.

Sitting behind these initiatives for all 3 channels is a unified group-wide data and technology plan, which I'll update you on in a moment. Let's start by going deeper into all of these channels starting with Direct. And as you know, we're really excited about our Direct business. We've reestablished growth and still see lots of opportunity. And not just in our core Motor and Home business. We're going to be instrumental in driving the micro SME top -- the micro SME market to go direct and we want to shake up the direct risky market and get a much bigger share of the value. So our objectives here are pretty simple. First, a trust to continue to fuel our brand and customer advantages to maintain that growth. The second is there are many ways we can improve our efficiency of how we deal with customers. So let's talk through some of the initiatives we've got here.

First, we're just launching 2 brand-new unique Direct Line propositions on Home and Motor and are pretesting. So they may be our best yet. You may already have seen our new fast response launch on Home on the TV over the weekend. Direct Line customers are going to get these new propositions on top of the many unique propositions we've already given them. And as you know, we have a fantastic new SME system, which we've rolled out already to Bed & Breakfast owners and to Hair & Beauty traders. And we're going to push forward significantly on that rollout to get to 75% of our target market by the end of this year.

Green Flag, as you know, we've put back into a single business unit under new management. And they're developing an exciting new plan, which we'll share with you soon.

Turning to efficiency, we're going to enable customers to do more for themselves by self service. And we see an opportunity in automated processes and increasingly straight through processing. These things, we believe, customers will actually prefer or they won't notice. But they're going to significantly improve our efficiency in running the business.

Let's now move on to PCWs where, as you know, we have the best brand in Churchill and a great price fighting brand in Privilege. We've done a lot of work to be good on PCWs. We're competent in pricing and fraud, which matter a lot in this area. And that's enabled us to be competitive and to have a steady share at adequate margins. But our ambitions are much greater. We're investing to have class-leading capabilities. And when we have these, we want to grow this channel. So what do we need to do to achieve that? Well first of all, as part of our overall IT systems, we're investing in the latest-generation pricing engine and with it, a series of application forward initiatives. We're also, in parallel, developing an alternative pricing model using new maps to machine learning to come up with a model, which is equally predictive. But importantly, non-correlated with our existing pricing models. We're also steadily pushing out our quote footprint and have high ambitions to keep Churchill in great face at the top of the preference for PCW brands.

Finally, partnerships, which we're going to split into 3. First, our Home partnerships. We have some stability here, having secured the RBS and NatWest partnership. And our objective is to grow that partnership and selectively, to acquire new ones. The work we've been doing behind the scenes to knit our systems together with theirs to enhance the journey for both customers and branch staff is working very well. We significantly increased new business sales and thereby, stabilized the book. So here, we want to use platform to add new partners.

For Rescue and travel, our ambition is a bit different. These are businesses finely priced, which we like to get because they can add useful scale. But the economics also need to work for us. We have a bit more of a mixed picture here. We've recently extended our travel partnership with Nationwide and won the RBS Rescue partnership. Our objective here is to create a platform for growth. And our next initiative is the development of a brand-new travel system.

Now for Motor, where the role of partnerships is strategic and our objective is to be the partner of choice for car manufacturers. Why? Well the current transformation of the motor industry provides both risks and opportunities to insurers. We want to partner with motor manufacturers to be in that value chain, working with them to create exciting new propositions for customers. That's why we have introduced the relationship with Tesla and our partnerships with Peugeot-CitroÃ«n. And today, I'm absolutely delighted to announce that we've signed a letter of intent with Volkswagen to be their insurance partner in the U.K. for their brand Audi, Fiat, Å koda, Volkswagen and Volkswagen Commercial for at least five years. I hope you'll agree, overall, a really exciting ambitious sets of initiatives across our 3 main channels.

But clearly, to deliver these requires us to have the technology to support them. So let's take a look at where we are in technology, where we've been making real progress. Our systems are resilient and stable. And we have excellent digital and mobile front ends helping us to win in the marketplace today. Our mobile sales for Direct Line have doubled in the past year, supported by class-leading loads times. We continue to improve our web purchase journey with NPS scores up 3.3percentage points in the last year alone.

We've also done a lot on claims where we're very mature in our running of Guidewire's claim center. And we also have technology to allow customers to use mobile in the claims process. And to be able to fight claims fraud. And this has helped us to significantly increase our claims' NPS score up a further 2 points in the year. And detect significantly more fraud than the market average.

But we have more to do. We need to complete rolling out our self-service functionality and our legacy systems are both expensive to run and lack agility and flexible. So here, our objectives are pretty clear. We want to support the channel strategies that I've just outlined. First, by seeking the leading position on pricing and fraud capabilities. Second, by giving us agility and flexibility on products and propositions. Third, by progressing our story of self-service, automation and straight-through processing. And finally, by enabling us to add partners with agility and speed and giving them the functionalities they want.

At the same time, we have another big objective. We also see IT as a major lever in delivering our expense ratio reduction. So our initiatives here are quite clear, we want to complete the build of the latest-generation system to give us that functionality, which I'll cover in a moment. Then we want to run these systems in a much more efficient way. We've already significantly increased our procurement capability, achieving better deals with fewer partners. We have a preference to rent rather than buy infrastructure. And increasingly, our cloud usage. And we have a plan to reduce and ultimately decommission our expensive mainframe.

So let me next go on to focus on the completion of those later-generation systems, which unlocks both the functionality and the cost savings. A reminder of our approach here, we have a preference to buy rather than to build and to select products proven in their respective markets, avoiding a one-size-fits-all model. This approach also enables us to keep our systems up-to-date as we benefit from ongoing releases and upgrades from our partner suppliers. Finally, we will test rigorously and take a phased rollout approach to manage risk.

On our core personal lines business, the functionality, as I said, is good front end and good on the claim side with Guidewire's claim center. What we're working on now is completing the full implementation of the Guidewire insurance suite whilst implementing the Towers Watson Radar Live pricing and underwriting engine, along with supporting systems and infrastructure, which we will connect to a comprehensive set of external data. This will help us deliver against all 4 of the objectives I set out in the previous chart.

Here, as you know, we have to rework the data architecture. But the new data architecture is agreed, taken the impairment. And we're partnering with a systems integrator to complete this deployment. We're building and testing our initial major release this year to start rolling out next year.

Elsewhere, we talked about our SME system, which is going to be rolling out 75% target trades this year. And in other personal lines, we're building a new travel system, which we'll also roll out this year.

So a lot of progress on our underlying systems. We've done what we need to do to get us back on track and we're very excited by the opportunities they'll bring. The systems we're implementing will enable us to move forward on all the initiatives in our channels and they underpin our medium-term target.

So in summary, 2017 was a great year. We successfully delivered against our priorities, helping us to deliver strong and highly cash generative earnings. The strong cash generation has helped us both invest in the long term of the business. And at the same time, deliver to shareholders today with total dividends of GBP 0.354 in 2017.

With that, let me go to questions.

Questions And Answers

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

All right. Shall we go further this way? So Ravi?

Q - Ravi Tanna {BIO 16926941 <GO>}

It's Ravi Tanna, Goldman Sachs. Three questions, please. The first one was just on your investment income guidance. I know you've got a medium-term profit growth target. But obviously with today's guidance on the current stable underwriting and fading investment income, at least in 2018, I was just wondering if you could talk to us how you're likely to handle that and whether there's scope for de-risking on the investment portfolio at all. The second one is on the SCR. Could you give us a sense as to whether this is likely to be an ongoing tailwind that will help Solvency development? And if so, by how much each year? Then, the third one was just on your comment around "footprint." Just curious to know exactly what the parameters are there and to what extent you're looking to increase your volumes and in what pockets of the market.

A - Anthony Jonathan Reizenstein

I'm going to answer the first one. Yes. Thanks, Ravi. So yes. So we've said -- we said profit guidance, we, of course, haven't given -- we don't give profit growth guidance. We give dividend growth guidance on our regular dividends, which we've said is 2% to 3%. And we've sort of aligned that to the growth of the business covering individual lines. Obviously, we want our costs to go, every company does. And today, we've got -- the (inaudible) for that are fairly transparent. So we've said medium-term core target within the range of 93% to 95%. We -- so far we've been delivering that and obviously, expect that to continue. And we've talked about growth in the business and all the things we're doing to get that growth. So we've got some of the parts to P&L going in the right direction there, along with installments now, which tend to go -- to track what's happening with volume generating. Then on the investment side, yes, the investment income, we're saying, is going to be down year-on-year '17 to '18. Once it's got to that point, I think the scope for it to grow a little bit with volume obviously depends then on how much we distribute the dividend as to whether AUM actually grow or not, they have always grown. Then, I think we are -- we'd be looking more to interest rate. I mean, in a way, it's more a Penny question because you've got a nice dividend future than a mean question. But I think based on where I've been talking with my colleagues on the investment side, the upside on investment is probably more on U.K. interest rates than any other individual driver. We're taking roughly the amount of risk we want to take. There probably is some scope to take a bit more investment risk. We've not yet found a new investment class that excites us in that sense. And so there could be some tactical move. I don't expect anything major. But I think you want to keep your powder dry. Then -- but interest -- U.K. interest rates, we could actually take a bit more risk on U.K. interest rates because we're quite short, we've got a lot of cash. I don't think we'd see now as the moment to do it. But that's a potential for improvement in interest rates and for us to take a bit more of that risk at the yield curve, assuming it ever does improve in the U.K. That's an upside. Do you want to...

A - Penelope Jane James {BIO 15157212 <GO>}

No. I think we are grateful. I've been looking into U.K. interest rates at the moment here. Shall I take SCR? SCR, early stage to give a definitive number. But directionally, if you look at the way the reinsurance program changed in 2014, then I think you should expect those reserves will continue to tick down over time. There are lots and lots of moving parts in an SCR calculation. So it's volatile to a number of things. But those are the things being equal, you'd expect to see, I think, some tick down over time, again, in the SCR, which gives us an option around how we deploy that for growth and for the book.

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

Our quote footprint has kind of 2, 3 buckets here. So first of all, our quotes for things which we just don't do today, like, U.K. (inaudible). We don't do homes with pre-existing subsidence. So here you need some genuinely new equities to learn because we haven't written those before. We don't have much kinds of experience. So that's kind of -- there are some initiatives to stop tracking some of those. Then there's kind of, within the existing parameters, things which we don't quote for because we don't like the historic performance. And again, we need to kind of continue to grow our expertise there. And so those are both pushing out the quote footprint. It's not going to be a sudden single bang, which takes us to a 100% quotability. I think the most important one, though, that we've said here under alternative pricing is not the quotes we return today at all, it's increasing our competitive quote footprint. So today, as you know, we have single pricing model, which means that either all our brands are pretty competitive or none of our brands are competitive. So we've got a bunch of very, very clever people, using (EMA's) machine learning to go off and use our fantastic claims data to model it in new ways. And so far the experience is pretty encouraging that they can model at least as good loss ratio. But importantly, non-correlating with our business. So we increase the number of customers we can choose and we're working on how to deploy it. Now obviously, we need to actually write some business to get some claims, check that, that claims experience comes through in reality. But that's probably the most significant in terms of the volume from quote footprint versus the pushing out on the overall envelope. This expressive quote footprint is important.

Right. Thank you. Yes. We go...

Q - Arjan Van Veen {BIO 5197778 <GO>}

Arjan Van Veen, UBS. Thanks for the additional disclosure on the systems changes. Just curious to see, is that when you're going to roll them out? Could you talk maybe a bit about legacy systems and how quickly they kind of get turned off after the rollout? And a question for Penny, you're on the board of another peer that's -- has much lower cost ratio. So could you maybe indicate some areas where you think, it requires a little bit of (FAT) on the expense side?

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

Very good. So yes, I mean, systems, it's going to be multiple years to fully be able to switch off all legacy systems and mainframes. But that's not to say that as we reduce our usage of mainframes, we won't be able to save some money. So it's not -- clearly, there is a drop when you get rid of mainframe. But we'll be reducing our costs in the meantime. And that's just one of the parts of us running our systems more effectively. As I said, we've got fantastic new procurement capability. We're really leveraging our scale. We probably inherited a little bit of a bank-like approach to cost management on IT. And we now have a very different approach, which is really leveraging our scale, consolidating in fewer partners, as I say, renting versus buying infrastructure. So we've got -- it's not the end of the cost savings that comes through on IT. It's actually quite progressive. Steve's got a great plan on that. Penny, (FAT)...

A - Penelope Jane James {BIO 15157212 <GO>}

Look, I think -- I don't want to comment on (Admiral) in particular. But what I said -- acknowledge is there's a different model here. So there are some costs that are incurred in this business that are done so for good reasons. So the Direct play, the marketing costs are different, et cetera, et cetera. So I don't think we should necessarily compare the 2 head on. We need to be mindful of what that cost is generating. There are some areas where the cost are higher than you would choose. I think property costs, we have some legacy issues there. They're probably not going away in a hurry. IT, it's clearly an overhead. I think we've got the right actions in place to address those and bring those down. But it will take time to actually get to decommissioning, as Paul suggested. Then there are some broader areas, where I think you can generally just continue to tighten. So

I think Paul mentioned procurement, which is a great example where it feels as though we've made it from not being top of the list to having quite a sophisticated approach to it in the last year. So I think that one is not working. So yes. So I don't think you should look at every cost line. There are some business trouble differences that are still a little ways to go, I think.

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

Yes. I think -- listen, I mean, I acknowledge, I think it's fantastic to have Penny around next to the table. She does bring a -- bring the challenge on that area and there's not one we need to. But it's -- investors say, having fresh blood and fresh energy on that, I think, is really important. And as you know, we've got targets to continue to reduce our expense ratio, which we're all behind. Good. The next -- James and Alan here.

Q - James Austin Shuck {BIO 3680082 <GO>}

James Shuck from Citi. I had 3 questions, please. Firstly, on the LTIPs. So the LTIPs, they kind of -- pretty vested at around 17.5% -- of 20.5% return on tangible. You're probably making 21.7%. There was a little bit of a headwind -- or a tailwind, I should I say, with low weather. That might take off a little bit going forward. But I'd just love to see whether incentive is to actually drive the RoE higher and why that's the appropriate level for the LTIPs. That's the first question. Secondly, just a nondiscretionary, really, on the reserving, if I look at the mix between the IBNR and case reserves, there's a sharp drop in the IBNR in 2017. Would like to know what's explaining that, too. Partly opt in. But I would expect case reserves to have fallen as well. Then thirdly, around the GDPR, just interested around this right to be forgotten and what that might mean for things like no claims bonuses and the like, particularly in Motor.

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

Good. So LTIPs, you'll have noticed, our (own cave) has stretched our RoTE targets by 250 basis points. So a new application that went further.

Q - James Austin Shuck {BIO 3680082 <GO>}

Or -- well, part of the reason why that happened is because the gearing level's gone up a little bit...

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

Yes. So -- but half of that increase is the debt, which is worth about 130 basis points. And the rest is just further stretching within -- the RemCo has a job to do, as you rightly point out, to stretch the targets just to keep the carrot sufficiently the right distance from the horse to make it motivating. And I think -- so that -- I think your observation explains why they put 250 basis points on the target.

Q - James Austin Shuck {BIO 3680082 <GO>}

Maybe to help you understand just a bit sort of why that is a stretch. Because if I look at the RoTE in recent years, you're consistently making that kind of number. So it's sort of you don't have to do anything. And then you get paid out fully on the offsets.

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

Yes. I think -- listen, I think, delivering 20.5% RoTE, I think, is a very good performance. And I think to increase the targets in one go by 250 basis points, I think, is quite a change. And I think they've done their job to make the target more stretching. Whilst I think (it's harder) coming in, said, okay, we're putting some numbers in the mid 20s up. I think that would have been -- send all sorts of inappropriate signals about the business and prospects and all sorts of other things. But I think that they were mindful of the need to make sure the targets were more consistent with consensus at the top end. And I think a 250 basis point increase, we think, is quite a move. You can always argue, I'm sure you can give feedback that you want more. But management thinks it's quite a big increase. IBNR?

A - Anthony Jonathan Reizenstein

(inaudible) Yes. Well first of all, we haven't changed anything in how we reserve or in the things we have. You're right, Ogden is the main reason why that has changed, as Ogden and IBNR had moved into outstanding claims reserves once we did the case review, which was earlier in the first half of '17. The other thing, you might expect the ratio to -- of IBNR to outstanding claims to reduce. As the old years, which had the very high deductible on the insurance runoff. So we're not surprised that there's some reduction in that ratio. But there's nothing -- there's no underlying change in policy or reserving that should worry us.

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

Mike, on the GDPR? Just wait for the mic. We'll pause. Mike, mic.

A - Michael Holliday-Williams

Thanks. It is complicated and we will abide by the legislation. There's always been a right to be forgotten. And so I think -- we think it's -- when you look at NCD, there's a legitimate use for NCD as well. So we'll be using that as part of it. At the end of the day, GDPR is all about collecting consensus of the right things. And that's what we'll be focused on, really. So we don't think it's a -- this is a major issue, really, if that's what you were hinting at. That make sense?

Q - James Austin Shuck {BIO 3680082 <GO>}

Makes sense.

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

No. Stuff like convictions, I think we've got a more sensible outcome than some people initially could be concerned about. Do you want to mention convictions?

A - Michael Holliday-Williams

Yes. See, I think the right to use convictions when you're waiting is one of our biggest concerns in the insurance market. And again, that seems to have been expected, that we can use that. And that would have been a concern because it's directly related to risk. But also, within insurance industry, we go to take off that conviction at the right moment. So that's what we'll be making sure that we do as well.

Q - James Austin Shuck {BIO 3680082 <GO>}

My (confirm) would be that people are more inclined to claim for things like scratches and things like that because then they can just -- have the right to be forgotten. And then they get across and you (provide it).

A - Michael Holliday-Williams

No. No. No. That is not -- we share NCDs on a (Q) database and trying to make it easier to share it around the industry. And so we'll be collecting consent to do that.

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

That's right. Alan?

Q - Alan Devlin {BIO 5936254 <GO>}

Alan Devlin from Barclays. A couple of questions. First of all, wanted to get some more color on your comments on claims inflation. And you had a favorable year this year. But you're not -- you're giving a guidance of 3% to 5% going forward. Can you give some more color of what's going on? Then just second on the reinsurance, taking 10% of the first (million-prime) there, not much more working there. Did you consider taking more of that -- retaining more of that risk? Or would you consider it out in the future?

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

Yes. I mean, we've always said that having a balance sheet gives us the optionality to be selective on the lower layers and to get -- use that to get a good price. And we think we did use that. So 90% is pretty perfect for us in terms of the level of placement of that when you get a CET1. And we think we got a good deal. Time will tell. You'll see our actual costs at the half year. But we think it's a bit commercially sensitive to share that now. I think on Motor claims, we are treating it as a business as usual. We'll resume in terms of 3% to 5% inflation. There's some reasons to think of it -- well, we think that it might not. So yet more benign reasons are Jackson and the MedCo initiatives may have had some impact, a positive impact on small bodily injury. Those were a few years ago. So we may be seeing some positives from that. Driver miles inflation is kind of pretty modest as a result of, we think, the fuel price increase as a result of the Sterling's weakness. Car tech may be helping. We're incentivizing people to have cars that automatically brake. Then also weather. Weather is another reason it might be a one-off because we had some good weather this year. So there's a mixture there of stuff you could say, are they cyclical, really, or are they structural? Obviously, going the other direction, cars are just getting much more expensive to repair. And that trend continues. So I think for those of us that (inaudible) and repair centers, you see a total loss of a car that's not that damaged because of all the sensors in there, bags and stuff that goes into it. So we think it's a safe working assumption for 3 to 5. And we will continue to track it. Obviously, we have better experience of that in 2017, which is why we booked 4.5% better attritional loss ratio in the year. And of course, we had the benefit of the reinsurance protection as well.

Yes. (inaudible) Tom?

Q - Unidentified Participant

(Tom Eivani) from Exane BNP Paribas. Just one follow-up on the LTIP question. The return on tangible equity target obviously went up. But not in your targets for the market. We attempted to increase them in line. Just joking. Wondered just in terms of the competitive environment a number -- you're growing ahead of market, a number of your competitors are talking about their ambitious growth plan. You seeing any signs, in particularly Motor, of competition coming in? And in terms of pricing and margins. Then thirdly, on the Rescue. One of your big competitors has been flagging challenges, I guess, in that market. What are your reflections on that? Is this actually a positive for you? Or is it just something that makes you think again about your plans there?

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

So RoTE targets. Let me tell you what our 15% is. What it isn't is a cap on our RoTE. We're incentivize, maybe, not to change its full taste. But we're incentivized now to keep pushing that up another 250 basis points. And it doesn't stop us delivering the returns. What it is, it's a thing which we use in making decisions every day about initiatives and growth. And I think we've been saying it (inaudible) an RoTE that would help us grow (inaudible) which probably would make us a small business, we'll be a bit less profitable. So I think in that role, I think you can understand 15% target. We're supposed to get it easier with the personal debt restructuring. In terms of competitive markets, I mean, I think we're still calling the most of market rational to the extent of -- follow up, Mike, on the detail. Basically, we're saying that market gave us some of the gains. And you can kind of see it pretty much when the government announced the intentions to revise up in September. That changed peoples' views of what that cost would be. Then it was probably our very good claims experience. So I think that the markets are rational, albeit prices are coming down. And I think, as we've always said, prices should come down in a competitive market when (inaudible) come down. And I think that's good for all stakeholders. I think the Home market is actually quite competitive. We -- again, not calling it irrational. But more supply than demand in Home. It's an attractive-looking market. So whilst we are positively seeing some pricing inflation, we don't think that's quite sufficient to cover claims inflation. So that market, we're saying, is rational. But very competitive. And that should season, I think, the view of how we see that particular market developing going forward. We're not necessarily going to see returns at sort of previous years. You probably start to see the '17 performance as kind of a new level that we'll work from. Rescue. What I was going to say, I think we quite love the Rescue market. And we're probably on the insurgent side. As we've said, we're doing pretty competitive advertising, which I'm sure, if you haven't seen, you should, which is naming competitors. And I think we quite like them. We quite like where that market's developing for us.

A - Anthony Jonathan Reizenstein

More to come there.

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

So it's Greig, KBW. Just 3 quick questions. One is Escape of Water. You've been a bit cryptic on the timing of when these remedial actions will start to kick in on their own right. I wonder if you could talk about that. Second point is you mentioned the commercial attritional loss ratio ticked up. And you spoke about claims taken and you want to be conservative. Are we seeing some negative trends there? I mean, that surprised me. You want to talk about those trends you're seeing there? Then also, I see that the commercial liability lines prior to the (inaudible) was quite high. I was wondering to what extent that is sustainable or not, or if it's a one-off.

A - Michael Holliday-Williams

(inaudible). I mean. clearly, we talked about Escape of Water at the half year. And we kind of indicated that we think that the inflation, we got a grip of the claims inflation there. Just to remind that it wasn't just about putting prices up to cover Escape of Water. It's very much underwriting and across the claims supply chain, where we've implemented actions. I'll bend to say they have stabilized now. Whilst we won't recover all that inflation of the past, we think there is stability in there now. And we call out -- it feeds into our view that long term claims inflation is still at 3% to 5%. And we've got good grip of that situation.

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

Is that 3% to 5% in the Home as well?

A - Michael Holliday-Williams

In Home as well. Yes.

A - Anthony Jonathan Reizenstein

Absolutely. Just to it make easier for you, Greig. On Commercial, on the reserving at the year-end, we don't think -- I don't think there are trends. And my Commercial colleagues agree, we haven't seen any adverse trends in the claims data. But they were -- there are often blips. And we've decided to treat those conservatively. We'll tell you if they develop in trend. But we don't see that yet, certainly not calling that. Commercial general liability has been a very strong performer for many years. And it's (inaudible) certainly, it's quite long tail. And always has, (Jon) is nodding, very good runoff from that portfolio. And I think we all expect that to continue.

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

Yes. Then we'll go to the other side of the room.

Q - David Bracewell {BIO 16394801 <GO>}

It's David Bracewell here from Redburn. Two questions. One on the kind of change in the mix in terms of moving to your own brand policies. My expectation is that has a higher margin than maybe the partnership business. And therefore, I'm going to expect that we hope to see some kind of improvement to the guidance on the combined ratio there as you kind of continue that shift to own brand. So perhaps can you tell me why you haven't changed the guidance there? Then the second question, a quick one, I think, on multipricing. Given the reinsurance yields you've had and the change in price, should we expect you to be able to increase prices in 2018 to offset that? Or did you kind of get that in 2017 in terms of (prices)?

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

Yes. So we were pricing with a view of what the reinsurance would be. And so we're slightly to the right side of that in terms of what we're seeing. So we've already done that.

And brand mix, John??

A - Anthony Jonathan Reizenstein

Yes. I mean, you're absolutely right. We're saying that we're going to see that move. And we're seeing it already. And because -- partly because (inaudible) partners. Even on these partners back into an NIG growth. And brands would like to upgrade them. And brands have a -- they're on the same commission cost. They do have a distribution cost, a bit different. They can have a slightly worse loss ratio, particularly Home partners had a very good loss ratio. There's a few moving parts. Bottom line is it's all kind of built into our plan. So our plan, which of course shows the 93% to 95% with the expense ratio and commission ratio coming down, it will build on this very trend you're looking to see. So I can't say it's going to make it better than we've said. But it will underpin what we have said, if that makes sense.

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

Great. We'll move to this side of the room.

Q - Andreas Evert Cornelis de Groot van Embden {BIO 1795530 <GO>}

Andreas van Embden, Peel Hunt. Two questions, please. First of all, on moving to Radar Live and your pricing model in Motor. What were you missing up to now in your pricing agility? And where will this take you? Does this take you into intra-day pricing, for example, across all your channels? And where do you think it's -- in which channel do you think it's going to be most useful? And secondly, on Rescue as you grow that business. Could you comment on whether you see any synergies between your insurance business, particularly the Motor book and Rescue as you scale up?

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

Yes. I mean, listen, we talk here about Green Flag impound. But we also have a very important business in linked. And linked is a big part of our plan as well. And all our initiatives will support that channel and package accounts, which is the third channel. So yes, in terms of cross-selling, that's kind of a feature of our plans. If you're asking about whether we should have a Green Flag insurance -- most insurance plan, I think we've got plenty of insurance plans on that in terms of Motor insurance. Was that -- sorry.

Q - Andreas Evert Cornelis de Groot van Embden {BIO 1795530 <GO>}

How much are Motor policies, Direct Line Motor policies or others do you sell through your partnerships in Rescue or Green Flag? And percentage of policies, are you selling -- the funnel...

A - Anthony Jonathan Reizenstein

Well we don't -- the partnerships are separate. So the Rescue partnerships is separate from the insurance partnerships.

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

Generally, if you split the book up, there's a lot of volume of policies that we do, as we've said, for very low margin. But if you give us Rescue scales, which is really important, you get more vans near more motorways and in more cities from that. So -- and then we've got kind of the 2 businesses which are better on margin, which are the standalone and then the linked. And I think we've talked mainly about the standalone business here. What we're saying is that there's a very good linked business as well, which we are -- we have good -- we have good levels of selling Rescue into our car insurance customers. We're pretty -- quite mature at that. I think most -- more of the opportunity we see is the standalone business. Again, sort of standalone types.

A - Anthony Jonathan Reizenstein

And that's the one with the highest margin. That's the piece of Rescue that has the highest margin.

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

Pricing, you get lots of stuff from Radar Live. So we get lots more external data. We get more accuracy at modeling. We get faster deployment. Intra-day is a functionality which we, at some stage, could choose to deploy. We need to work out the merits and demerits of it. Intra-day, you're not learning much about claims. You're learning something about how other people price in the market. So it gives us the full kit. What we switch on, leave it to us. But we see a lot of value in the first things I mentioned, which we're going to benefit from. And application fraud is another big (leverage) Steve?

A - Steven Maddock

(inaudible)

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

Yes. Sorry. The other thing is it's not much more efficient to run. So at the moment, we model separately from deploying, which is not only accurate -- I mean, accuracy and takes in lag. But also is lots of work. So we're going to remove work from it. So it's really good. Very excited about that.

Right. Yes. (inaudible).

Q - Wajahat Rizvi {BIO 19928187 <GO>}

Waj Rizvi from Deutsche Bank. I have 3 questions. First one on Home loss ratio. Can you talk a little bit about the dynamics of attritional loss ratio? And like -- and from the change in business mix? I seem to understand that there's some offsets in reducing commission ratios and higher attritional loss ratios, which is the dynamics of the 2. And the second one would be on systems. So I think we talked that it will take some time for you to switch off the mainframe. So it is fair to assume that expense ratio or expense benefit would be a bit back-end loaded from this technology? And finally, just a numbers question. So you're changing runoff, you're putting it in operating. The guidance of runoff offsetting restructuring cost, is that still valid for the next few years?

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

You do 1 and 3. And I'll do (inaudible).

A - Anthony Jonathan Reizenstein

Yes. And so on the last one, we're including it. There's nothing to report. By implication, there shouldn't be too much to report. It's not going to make any difference, really. Not much difference. We weren't expecting to make much difference. Obviously, there could be changes. So if Ogden -- if the Ogden rate changes, we'll get a benefit in runoff as well as a benefit in Motor and Commercial. Maybe we'll -- we'll probably report that separately.

A - Penelope Jane James {BIO 15157212 <GO>}

If there's anything significant, we'll report it...

A - Anthony Jonathan Reizenstein

The expectation is not going to be dramatic. That's why we -- on the Home loss ratio. And the way maybe to think about this is if you take the 2017 core, which is actually just under 90%. And you probably need to add for weather, which is the main normalizing point. You probably need to add 4 to 5 points. So that comes to about a normalized core of 94%, 95%. You got to think about the partners, they will take a bit of the difference in the commission ratio when that happens. But you end up about 94%, 95%. Then looking forward, you got a few moving parts on Home. So you've got nationwide premium reduction, NEP reduction, over one year. So there won't be any '19. And then there will be half a year basically in '18. And that's a reasonably large part of our NEP. On the other hand, they do take quite a lot of commission. So the commission ratio is going to come down, I expect, quite significantly in 2018. And on the accident loss year on the attritional loss ratio side, they have low attritional loss ratios relative to the rest of our business. And there's a little bit of strain because of that. And -- but I think, overall, you probably going to see -- we think there will be an improvement in core, in Home, normalized, because of that commission ratio reduction, which is quite significant. And that we're broadly balanced in our view, broadly balanced to a reduction in premiums. There's a few moving parts. But that should give you some more guidance to help, if that helps.

Do you want me to continue...

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

Yes. I mean, basically, we've given a few clues to quite a lot of moving opportunities that we have in IT costs. So across the basket of all those, we see opportunities kind of, yes, the mainframe kind of usage comes down. Then you get a big saving at the end. But there are other moving parts that Steve has got in plan to reduce. I think we'll give him some flavor of them in terms of procurement and -- Steve, do you want to (give it a try)?

A - Steven Maddock

I think Paul's right that there are -- yes. I mean, Paul's right. I mean, there's a number of initiatives that -- and leaders that we're following here. I mean, Paul's reference, first thing we do is we go and strike better deals. That gets an immediate benefit for us. As we, in effect, implement these new systems and we are, in effect, replatforming most the front-end systems in the business, you'll get a gradual reduction in your mainframe usage over time as you migrate to these new systems. That's, I think, an ongoing feature. You then get to sort of final decommissioning. That gives us another kick in terms of benefit. And of course, in parallel to that, any system that you're not addressing by replatforming, we're reengineering to make the underlying net usage, reduce it, eliminate it or get a better deal on it. So there's about 4 levers that we're pulling. And each of those has an impact over the life of our plan.

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

Right. (inaudible).

Q - Andrew John Crean {BIO 16513202 <GO>}

Andrew Crean with Autonomous. Three questions, if I can. Firstly, on Motor PCW, I think your market share has been broadly flat. And I think with this new pricing machine, you're anticipating building market share there. Can you share with us some of your ambitions, say, for this year in terms of policy downgrades from the pricing? Secondly, CapEx. Are you still driving to GBP 80 million, to a GBP 100 million for this year? And I think you said there's a bit of a bubble. Will that drop down from '19 onwards? Then finally on whiplash and Ogden, can you say a little bit about what you anticipate, the legislative position is on that? And if you don't get anything through parliament on Ogden, what happens?

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

I'll start with the last one. So on the government's national time table, introduced legislation to get kind of 2 parts of whiplash in by next April. There's quite a lot of work to be done by all parties to get that to happen. There's a lot of systems work to be done. So -- and of course, they need to get it passed. But our planning assumption is that, that will happen for next April. But there's some risks to that, I think, in terms of legislation and then all the systems work needs to be done to enact it. Because there's quite a lot of technical changes to make that work. And Steven -- I was going to say bore you at the break. But he can tell you at the break with his MIB hat on about all the work that needs to be done to make that happen. Now whether Ogden hitches along for the ride of the civil liabilities bill or not is a debate. And so there are pros and cons to whether it does hitch along for the ride. There's obviously dangers of it attaching. But it's up to the government to get that done. They've said that, a quite and clear intention to get it done. And it's up to them. We're unclear on the legislative vehicle they're going to use to do it. And obviously, what happens, it depends on what -- if it doesn't happen, it depends in why it doesn't happen, whether it's just a timing thing. But of course, really what matters is that it does eventually happen because we're talking about claims that we'll be settling in a few years' time. So it's not month-critical to that extent. Clearly, if it fails for a specific reason, if the government goes back on its commitment, that would be very different to the schedule we've timed. And of course, really, what matters is the reinsurance. Materially, it's the reinsurance cost. So we've got -- the next real thing is next year's renegotiation of the reinsurance contract. So we got pretty good protection this year. And of course, that reinsurance contract was struck with some expectations, will be late-changing, not full. Did I give you enough? Do you want to do -- I mean, PCWs. Listen, a lot of initiatives we talked about are not this year. Will be -- so the alternative pricing will be -- we're aiming to get some experience this year. But I think this is a medium life of the plan ambition that we're setting out here on PCWs. There's a lot to it. And I think you should take it as quite a big stake in the ground today that we're saying there's no reason we see we shouldn't be leading-edge at PCWs. And we know what the deltas are. And we think that we have the systems work and the initiatives set to close that application fraud pricing we've talked about. And as I say, alternative pricing approach.

A - Penelope Jane James {BIO 15157212 <GO>}

CapEx, I think we haven't given guidance for between -- beyond 2019. Clearly, we're still going to be investing in the business here and there. I think we are in a bubble at the moment. So we're in a bit of the upper end of that range. I think we'll stay at the upper end of that range in the short term. But I don't think it means that we'll stop investing in the business in 2019. I might peel back a bit then.

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

Yes. Kamran?

Q - Kamran Hossain {BIO 17666412 <GO>}

It's Kamran Hossain from RBC. Just one big picture question. So you talked a lot about the changed distribution model, how you're able to access all the 3 main channels. When you think about partnerships, one of the Big 4 price comparison websites last week set out its ambitions to partner with banking apps. So straight in via API into their apps, they can offer all sorts of services. Do you see any -- I mean, when you think about that change in the market or the potential change in the market, is it a threat? Is it an opportunity? Does it change the way the affinity might work going forward? Because obviously a lot of the big affinity deals, especially on the Home side, are with banks. So any thoughts on the big picture question?

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

Yes. I mean, generally, we've seen this leg of our strategic permit as giving us some strategic optionality. And I think one of the things we want to do is if we're not a great retailer, we'd certainly like to be the smart and efficient manufacturer behind other great retailers. We are -- I think that gives us some strategic optionality if our retail brands don't win in the marketplace, which we hope they will, working with other people. We think all those people will need people like us to have our excellence at all the things, which we're really great at. So -- and I think that's revealed on our approach on Motor, which other people could view as a hostile trend. We're running straight towards it and saying, "Okay. You motor manufacturers have a lot of assets, increasing a bunch of assets in terms of how people will purchase or not, cars. And the data we'll get out of them. We want to partner with you." And so I think there's risks and opportunities. I think that by mitigating the risks as being partners, being overly reminded to partner with people that have different distribution models. Then I think banks clearly have a variety of partnership models in mind. I think there are some real benefits of how you partner with them. We've really turned around our business at NatWest/RBS by really closely linking our systems in there to make it really, really easy for their customers to get a great price from us. And that's really working well. So I think that model has some advantages versus putting it into a PCW. But I would say that. And of course, even PCWs, you're absolutely right. We write about 40% of our business on PCW in Home. So we're in that channel, too. So I think it's great to be up -- it's great to be across all the channels, I think net all of that, because I don't think any of us can necessarily say the way the future is exactly going.

Yes.

Q - Dhruv Gahlaut {BIO 16209870 <GO>}

Dhruv Gahlaut, HSBC. Two questions. Firstly, on the runoff book. Could you quantify all the reserve, which is still tied there in the capital in that book? Secondly, just going back to the RBS renewal on your partnership, would we expect to see any change there in terms of numbers, et cetera?

A - Anthony Jonathan Reizenstein

Yes. I mean, it's slightly a historic reference to the renewal. It's a couple of years back until moving on to the next one at some stage. But (that's the nature of budget).

Q - Dhruv Gahlaut {BIO 16209870 <GO>}

(inaudible)

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

So Dhruv, that's quite mature in Home. Rescue is a more recent deal. And that's reflected in our numbers. But there's no big change. Mike?

A - Michael Holliday-Williams

(inaudible) Yes. Sorry. We're in (pitch on trouble) with them. And as we say, things like Travel and Rescue, it's really a volume -- we like to have the volume because it means you can have more people that know more languages. But it's pretty fine-margin stuff. So we kind of do take it or leave it a little bit. But Travel's the one with RBS accounting pitch, having got Home and Rescue.

A - Anthony Jonathan Reizenstein

I think we're just...

A - Penelope Jane James {BIO 15157212 <GO>}

It's probably a good answer.

A - Anthony Jonathan Reizenstein

Yes. I think the reserves are -- actually, it's in the prelim. It's about GBP 265 million in the runoff book. We hadn't published the capital number. And you'd expect it to use on our capital in other parts because of the PPO nature of it. We haven't mentioned the number (that maybe we'll get).

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

Good. Last one. Last one.

Q - Unidentified Participant

(inaudible) Let's see. So price comparison, you talked about the capability part of the game. Isn't that mainly a cost game? And so my question is, how often do we come out top on the business you quote and price, comparing Home and Motor? Second question on partnerships, same thing. I mean, the capabilities. But are the partners basically just giving the business to the lowest price, for the best price. And hence it's a winner's curse if you win a partnership? And thirdly, on the price increases you and the market has done. Has that led to increased switching rates in Home and Motor?

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

Very good. So to deal with the last one first. So retention's up a bit in Motor, down a little bit in Home. But I mean, plus or minus 1% on both. But still Direct Line tracking levels, mid-80s in retention. And people are shopping around. People shopping around, I think, a bit more on Home, driven by their prior year disclosure premium. And again, that's encouraging. We think that's the right thing to do. We've kept excellent retention rates. But down just a little bit on Home, just up a little bit on Motor. Partnerships, we use the word selective, because you're right, partnerships fall into 2 buckets: Commodity partnerships, which generally goes to the wire. And there probably is winner's curse on it; and then there's probably strategic partnerships, where people come to us. And they do come to us and go, "We love what you're doing in Direct Line. We love your digital front ends. We love your API links. We love your extra repair centers. We love your propositions. We love your award-winning customer experience stuff." So they come to us. And then they're looking. People with brand tend to want to work with somebody that understands about brands and giving time differentiation through a brand experience. So those are the sorts of partnerships we want to win. We're happy to win some more commodity ones, specifically where it gives us scale at Travel and Rescue. Then we're happy to walk away from quite a lot of them as well. So the word selective is quite important there. I think on PCWs, we keep a stable, quite big share of it. We're pretty competitive. We win a lot every week. So we are pretty competitive. We quite actually can benchmark. There's a couple of peers that this is what they do all the time, PCWs. And we can quite specifically say, "Okay. Here's what they do, here's what we do. Here's how they get a bit more competitive and still do it at good loss ratios. And we know what those deltas are. And we think we have the plans and the capabilities over the next couple of years to close on that." Lots about application fraud. Some of it is having price models specifically gated up for PCW customer rather than the direct customer because we tend to have, as I said, one pricing model. So we have it in our sights. There's nothing I see in our way. I think on pricing as well, you got to look at -- the marginal costs is what really matters here. The cost of an extra policy, which increasing will be direct and self-service. So actually, we should be -- we shouldn't be held back on the marginal cost basis. And we should, again, benefit from the group's brands because we have fantastic brands. And brands still matter in PCWs, particularly in terms of better retention rates. And we benefit from the group's fantastic claims, fantastic accident repair centers. So we have a lot of assets. And actually going from where we are now to where we want to be, these all -- this is a small wins thing. We're pretty good to be winning so much business today to keep that business stable.

Q - Unidentified Participant

And application fraud, is it a major improvement you are going through?

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

Yes. We catch more fraud than anyone else at claims. That's a great place to capture, better not catching it. We redeem -- rather not get any of it on the books. And so we know where are the few things we want to do. So we're pushing forward progressively on that. We're not bad at it. Without that, we wouldn't be after any business. But we have some good initiatives there.

Right. Thank you very much. (We should just check) anyone on the phones?

Operator

(Operator Instructions) So at the moment, no questions coming through. So I'll hand back over to you.

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

Thanks very much. Before I conclude here, we'll switch off the lines. But nothing huge to announce now. But I thought we got to -- we just have one final slide, which is just to say to goodbye to John. Some pictures of John. The great benefit, John and I is he's actually getting older through the whole journey. (inaudible). So John...

A - Anthony Jonathan Reizenstein

Let me practice my interview.

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

(inaudible).

So John, a fantastic selection of non-work things to do. On John's behalf, we also (inaudible) to the fantastic board member Penelope's going to be absolutely a terrific CFO. Fantastic colleague. Fantastic friend. And if you think about where we've come from, your questions reveal we -- lot of things there ought to do in the business. And Penny's still got a lot of opportunities.

But I think John's done a cracking job here. He's been a fantastic colleague, been a fantastic friend, been a fantastic CFO. And I'd just like to wish him all success in the future. Could you join me?