Direct Line Group

8 March 2021

DIRECT LINE INSURANCE GROUP PLC
PRELIMINARY RESULTS FOR THE YEAR ENDED 31 DECEMBER 2020
DELIVERED A GOOD FINANCIAL PERFORMANCE AND SUPPORTED OUR CUSTOMERS, PEOPLE AND SOCIETY DURING AN UNCERTAIN YEAR

PENNY JAMES, CEO OF DIRECT LINE GROUP, COMMENTED

"Despite the many challenges we faced in the year as a result of the Covid-19 pandemic, we traded well and prioritised support for our customers, our people and local communities. Own brands policies grew by 2.2%, and our model of disciplined underwriting delivered a combined operating ratio of 91.0%. This has enabled us to return capital to shareholders during the year and today declare a final dividend of 14.7 pence per share, up by 2.1% over 2019[1], and announce a share buyback.

"I am proud that our people, even when working remotely, have continued both to care for our customers and to help us build an insurance company of the future. Thanks to their commitment we have made great progress on our transformation programme, designed to drive a step change in our competitiveness and deliver profitable growth. As a small thank you we are awarding all employees shares worth £350.

"We are a business that is proud to deliver strong returns to shareholders and to challenge itself to be a force for good. We chose to invest £93 million in a range of measures to support our customers, our people and local communities. We also want to do everything we can to tackle climate change and last year committed to set science-based targets to reduce our carbon emissions.

"Turning to the year ahead, we feel confident that we can build on the momentum we've created and become a tech and data driven insurance company of the future with our customers at its heart."

Results summary

	FY 2020 £m	FY 2019 £m	Change
In-force policies (thousands)	**14,615**	14,789	(1.2%)
Of which: direct own brands[2] (thousands)	**7,454**	7,290	2.2%
Gross written premium	**3,180.4**	3,203.1	(0.7%)
Of which: direct own brands[2]	**2,225.6**	2,227.8	(0.1%)
Operating profit[3]	**522.1**	546.9	(4.5%)
Combined operating ratio[3,4]	**91.0%**	92.2%	1.2pts
Profit before tax	**451.4**	509.7	(11.4%)
Return on tangible equity[3]	**19.9%**	20.8%	(0.9pts)
Dividend per share – interim (pence)[5]	**7.4**	7.2	2.8%
– final (pence)[5]	**14.7**	14.4	2.1%
– special (pence)	**14.4**	–	n/a
	31 Dec 2020	31 Dec 2019	Change
Solvency capital ratio post-dividends and share buyback[6,7]	**191%**	165%	26pts

Financial highlights

- Direct own brands in-force policies grew by 2.2% driven by strong segments of growth across the business, including Home, Commercial and Green Flag Rescue, whilst Motor was broadly stable. Total in-force policies reduced due to lower partnerships and Travel volumes.
- Direct own brands gross written premium was stable with growth across Home and Commercial direct own brands and Green Flag Rescue offset by lower average premiums in Motor. Overall gross written premium reduced by 0.7% due to falling partnership and Travel premium.
- Increased major weather costs of £43.0 million (2019: £6.0 million) contributed to lower operating profit of £522.1 million, £24.8 million (4.5%) lower than 2019 (£546.9 million). Covid-19 restrictions reduced claims frequency in Motor and Commercial, although this was partially offset by investment in initiatives to protect our customers, people and society, lower investment asset returns and the impact of the Covid-19 pandemic on Travel. Overall, the impact of the Covid-19 pandemic was a modest net benefit to the result.
- Combined operating ratio improved to 91.0% (2019: 92.2%). Normalised combined operating ratio[3] of 91.7%, was ahead of target of 93% to 95% predominantly due to the lower claims frequency in Motor.
- Progress on the Group's transformation continued to drive improved current year profitability via increased pricing and underwriting sophistication in Commercial and improved counter-fraud capability in Motor.
- Profit before tax of £451.4 million was £58.3 million lower than 2019 following the reduction in operating profit alongside £39.4 million of restructuring and one-off costs as the Group invested in cost saving initiatives.

- Proposed final ordinary dividend of 14.7 pence per share, increased 2.1%[1], and announcing a share buyback programme of up to £100 million. Intention to move back towards the middle of the Group's capital risk appetite range assuming more normal circumstances.

Strategic highlights

We continued to transform at pace into the insurance company of the future with Commercial and Rescue which are the most progressed, beginning to deliver improved financial performance.

- Commercial delivered growth at stronger margins as its investment in technology and the adoption of agile ways of working has enabled it to expand its product offering with more sophisticated pricing.
- Motor is live on our new platform for Privilege, and Churchill has begun rolling out its new business on this platform, enabling future operational efficiencies, improved customer experience and pricing capability. Direct Line is scheduled to follow in the first half of 2021.
- We launched a new 'superhero' creative campaign highlighting Direct Line's unique propositions across multiple products at improved economics.
- Strong growth in Darwin, which is now live on four price comparison websites ("**PCWs**"), with over 50,000 in-force policies at the end of 2020.
- Green Flag continued to enhance its digital offering with the launch of a new claims system and enhancements to its 'Green Flag Rescue Me' app.
- We embedded agile ways of working across trading, digital and technology functions targeting increased pace of change and reduced cost.
- We launched a new property site strategy, fundamentally repositioning the way we use our buildings, accelerating £85 million of future costs into 2021 to generate long-term savings in excess of £10 million per annum from 2022.

Customer, people and society highlights

Invested £93 million in a range of initiatives to support our customers, people and society through the uncertainty caused by the Covid-19 pandemic and stepped up our action on tackling climate change:

- Customer: we supported over 450,000 customers through a range of measures and continue to do so during the most recent lockdown through "Mileage MoneyBack".
- People: we successfully moved the majority of our people to remote working and offered flexibility to help them manage home and work commitments. Despite all the challenges our people went the extra mile and in recognition all employees will be receiving £350 worth of free shares and all eligible employees who are not usually paid bonuses or incentives will receive a £400 bonus in their April salary.
- Society: we donated over £7 million to charities and good causes via the "DLG Community Fund" and the "ABI Covid-19 Support Fund" helping thousands of people in need of additional support.
- Planet: we achieved our 2020 climate targets and have committed to go further by setting Science Based Targets ("**SBT**"). We published our first Task Force on Climate-related Financial Disclosure ("**TCFD**") report and sustainability report and became a 100% carbon neutral business by offsetting our emissions as we work towards reducing our emissions year on year.

For further information, please contact

PAUL SMITH
DIRECTOR OF INVESTOR RELATIONS
Mobile: +44 (0)7795 811263

LISA TREMBLE
GROUP CORPORATE AFFAIRS AND SUSTAINABILITY DIRECTOR
Mobile: +44 (0)7795 234801

Notes:

1. The 2019 final dividend of 14.4 pence was subsequently cancelled and paid as a special interim dividend in 2020.
2. Direct own brands include in-force policies for Home and Motor under the Direct Line, Churchill, Darwin and Privilege brands, Rescue policies under the Green Flag brand and Commercial under the Direct Line for Business and Churchill brands.
3. See glossary on pages 48 to 50 for definitions and appendix A – Alternative performance measures on pages 51 to 54 for reconciliation to financial statement line items.
4. A reduction in the ratio represents an improvement as a proportion of net earned premium, while an increase in the ratio represents a deterioration. See glossary on pages 48 to 50 for definitions.
5. The Group's dividend policy includes an expectation that generally one-third of the regular annual dividend will be paid in the third quarter as an interim dividend and two-thirds will be paid as a final dividend in the second quarter of the following year.
6. Estimates based on the Group's Solvency II partial internal model.
7. The solvency capital ratio as reported at 31 December 2019 is after taking into account the then expected 14.4p final dividend and the £150 million share buyback announced on 3 March 2020. The impacts of the cancellation of the dividend (as announced on 8 April 2020) and of the share buyback programme (as announced on 19 March 2020 after £30 million of the buyback had been executed) would have added 24 percentage points to the ratio as reported to give an adjusted solvency capital ratio of 189%.

Forward-looking statements disclaimer

Certain information contained in this document, including any information as to the Group's strategy, plans or future financial or operating performance, constitutes "forward-looking statements". These forward-looking statements may be identified by the use of forward-looking terminology, including the terms "aims", "ambition", "anticipates", "aspire", "believes", "continue", "could", "estimates", "expects", "guidance", "intends", "may", "mission", "outlook", "over the medium term", "plans", "predicts", "projects", "propositions", "seeks", "should", "strategy", "targets" or "will" or, in each case, their negative or other variations or comparable terminology, or by discussions of strategy, plans, objectives, goals, future events or intentions. These forward-looking statements include all matters that are not historical facts. They appear in several places throughout this document and include statements regarding the intentions, beliefs or current expectations of the Directors concerning, among other things: the Group's results of operations, financial condition, prospects, growth, strategies and the industry in which the Group operates. Examples of forward-looking statements include financial targets and guidance which are contained in this document specifically with respect to the return on tangible equity, solvency capital ratio, the Group's combined operating ratio, percentage targets for current-year contribution to operating profit, prior-year reserve releases, cost reduction, reductions in expense and commission ratios, investment income yield, net realised and unrealised gains, capital expenditure and risk appetite range. By their nature, all forward-looking statements involve risk and uncertainties because they relate to events and depend on circumstances that may or may not occur in the future and/or are beyond the Group's control. Forward-looking statements are not guaranteeing future performance.

The Group's actual results of operations, financial condition and the development of the business sector in which the Group operates may differ materially from those suggested by the forward-looking statements contained in this document, for example directly or indirectly as a result of, but not limited to:

- United Kingdom ("**UK**") domestic and global economic business conditions;
- the direct and indirect impacts and implications of the coronavirus Covid-19 pandemic on the economy, nationally and internationally, on the Group, its operations and prospects, and on the Group's customers and their behaviours and expectations;
- the trade and co-operation agreement between the UK and the European Union ("**EU**") regarding the terms, following the end of the Brexit transition period, of the trading relationships between the UK and the EU and its implementation, and any subsequent trading and other relationship arrangements between the UK and the EU and their implementation;
- the terms of trading and other relationships between the UK and other countries following Brexit;
- market-related risks such as fluctuations in interest rates and exchange rates;
- the policies and actions of regulatory authorities and bodies (including changes related to capital and solvency requirements or to the Ogden discount rate or rates or in response to the Covid-19 pandemic and its impact on the economy and customers) and changes to law and/or understandings of law and/or legal interpretation following the decisions and judgements of courts;
- regulations and requirements arising out of the FCA pricing practices review and changes in customer and market behaviours and practices arising out of that review and such regulations and requirements;
- the impact of competition, currency changes, inflation and deflation;
- the timing, impact and other uncertainties of future acquisitions, disposals, partnership arrangements, joint ventures or combinations within relevant industries; and
- the impact of tax and other legislation and other regulation and of regulator expectations, interventions and requirements and of court, arbitration, regulatory or ombudsman decisions and judgements (including in any of the foregoing in connection with the Covid-19 pandemic) in the jurisdictions in which the Group and its affiliates operate.

In addition, even if the Group's actual results of operations, financial condition and the development of the business sector in which the Group operates are consistent with the forward-looking statements contained in this document, those results or developments may not be indicative of results or developments in subsequent periods.

The forward-looking statements contained in this document reflect knowledge and information available as of the date of preparation of this document. The Group and the Directors expressly disclaim any obligations or undertaking to update or revise publicly any forward-looking statements, whether because of new information, future events or otherwise, unless required to do so by applicable law or regulation. Nothing in this document constitutes or should be construed as a profit forecast.

Neither the content of Direct Line Group's website nor the content of any other website accessible from hyperlinks on the Group's website is incorporated into, or forms part of, this document.

Financial summary

	FY 2020 £m	FY 2019 £m	Change
In-force policies (thousands)	**14,615**	14,789	(1.2%)
Of which: direct own brands (thousands)	**7,454**	7,290	2.2%
Gross written premium	**3,180.4**	3,203.1	(0.7%)
Of which: direct own brands	**2,225.6**	2,227.8	(0.1%)
Net earned premium	**2,960.5**	2,984.9	(0.8%)
Underwriting profit	**267.8**	232.1	15.4%
Instalment and other operating income	**159.2**	180.2	(11.7%)
Investment return	**95.1**	134.6	(29.3%)
Operating profit	**522.1**	546.9	(4.5%)
Restructuring and other one-off costs	**(39.4)**	(11.2)	n/a
Finance costs	**(31.3)**	(26.0)	(20.4%)
Profit before tax	**451.4**	509.7	(11.4%)
Tax	**(84.2)**	(89.8)	6.2%
Profit after tax	**367.2**	419.9	(12.6%)
Key metrics			
Current-year attritional loss ratio[1,2]	**62.3%**	71.6%	9.3pts
Loss ratio[1,2]	**57.9%**	61.9%	4.0pts
Commission ratio[1,2]	**8.6%**	7.1%	(1.5pts)
Expense ratio[1,2]	**24.5%**	23.2%	(1.3pts)
Combined operating ratio[1,2]	**91.0%**	92.2%	1.2pts
Investment income yield[2]	**2.1%**	2.4%	(0.3pts)
Net investment income yield[2]	**1.8%**	2.1%	(0.3pts)
Investment return yield[2]	**1.6%**	2.2%	(0.6pts)
Basic earnings per share (pence)	**25.8**	29.5	(12.5%)
Diluted earnings per share (pence)	**25.5**	29.2	(12.7%)
Return on tangible equity[2]	**19.9%**	20.8%	(0.9pts)
Return on equity	**13.1%**	15.5%	(2.4pts)
Dividend per share – interim (pence)	**7.4**	7.2	2.8%
– final (pence)	**14.7**	14.4	2.1%
– total ordinary (pence)	**22.1**	21.6	2.3%
– special (pence)	**14.4**	–	n/a
Share buyback actioned (10.4 million shares)	**30.0**	–	n/a
Share buyback proposed[4]	**100.0**	150.0	n/a
	31 Dec 2020	31 Dec 2019	Change
Net asset value per share (pence)	**199.7**	193.4	3.3%
Tangible net asset value per share (pence)	**141.5**	142.0	(0.4%)
Solvency capital ratio post-dividends[3,4]	**191%**	165%	26pts

Notes:

1. A reduction in the ratio represents an improvement as a proportion of net earned premium, while an increase in the ratio represents a deterioration. See glossary on pages 48 to 50 for definitions.
2. See glossary on pages 48 to 50 for definitions and appendix A – Alternative performance measures on pages 51 to 54 for reconciliation to financial statement line items.
3. Estimates based on the Group's Solvency II partial internal model.
4. The solvency capital ratio as reported at 31 December 2019 is after taking into account the then expected 14.4p final dividend and the £150 million share buyback announced on 3 March 2020. The impacts of the cancellation of the dividend (as announced on 8 April 2020) and of the share buyback programme (as announced on 19 March 2020 after £30 million of the buyback had been executed) would have added 24 percentage points to the ratio as reported to give an adjusted solvency capital ratio of 189%.

CEO REVIEW

I am proud of what the Group has achieved during 2020. Once again, we have demonstrated financial resilience by delivering another good set of results, whilst supporting our customers, our people and local communities through the challenges of the pandemic. Despite the disruption and uncertainty that 2020 has brought, we have made real progress towards becoming a technology-driven business which can adapt quickly to the changing world around us and deliver more for our customers at speed. We could not have done this without our highly engaged people, who have demonstrated the commitment and flexibility needed to do what it takes for our customers and to drive forward our business plans regardless of their personal circumstances. I am grateful to them for their dedication, skill and support.

Business performance and the impact of Covid-19

In 2020, we delivered another year of strong profitability at the same time as growing our direct own brand policy count. The investments we've made in systems and capability over the last few years are showing through in this growth and are contributing to underlying improvements in current year underwriting profitability. Overall, Covid-19 led to a modest net benefit to the result. Despite the impact of Covid-19, we made further progress in delivering the change required to implement the Group's transformation plans.

We traded well through the year, delivering growth in our Home, Commercial and Green Flag Rescue businesses despite prolonged periods of lockdown when new business shopping dropped significantly. Retention has held up well. In contrast average premiums have fallen as risk mix has reduced, with fewer new drivers on the road as no driving tests have been conducted for parts of the year and fewer new cars have been purchased. In the midst of these trends we are happy to see direct own brand policy growth of 2.2% and gross written premium broadly flat.

At a headline level we delivered operating profit of £522.1 million, a combined operating ratio of 91.0% and a return on tangible equity of 19.9%, well ahead of our target of at least 15% over the long-term. Operating profit of £522.1 million was £24.8 million lower than 2019 (£546.9 million) due to higher major weather costs of £43.0 million (2019: £6.0 million) and reduced prior-year reserve releases, partially offset by improved current-year profitability.

Overall, the impact of the pandemic led to a modest net benefit to our financial result, with the effects concentrated in four main areas:

- Reduction in motor claims frequency falling to below normal levels from Q2
- Increase in Travel claims, relating to both claims volumes and claims handling costs as well as additional commission payments
- An estimated £6 million in Covid-19 related business interruption claims
- Investments to support our customers, people and society totalling £93 million

Motor claims frequency levels were significantly lower than normal due predominantly to lockdown restrictions leading to claims frequency falling to around half normal levels during Q2. Whilst it increased during the second half of the year, claims frequency did not return to pre-Covid-19 levels during 2020. However, severity costs have increased due to the costs of making accident repair centres Covid-19 safe, longer repair times and consequently higher credit hire costs. We have seen an increase in the volume of claims within our Travel business and so have also incurred additional claims handling costs supporting our customers. In terms of business interruption, our standard wordings were clear from the outset and we were not party to the FCA's test case nor the appeal to the Supreme Court, which has been relevant to many commercial insurers, and our overall Covid-19 related business interruption claims are estimated at £6 million.

Consistent with our 'Force for Good' vision, we have invested extensively in our customers in the form of premium refunds, waived fees and reduced premiums, and also in our people by protecting jobs at the most critical points in lockdown, preserving salaries and incentives in return for flexibility and investing in strengthening home working capability. And finally we have invested in society: we have helped local communities with over £7 million of donations helping 100,000s of households and contributing to the ABI Covid-19 Support Fund. In total these initiatives represent an impact of around £93 million, of which £34 million is within our operating expenses and £59 million is within our loss ratio.

A further effect was felt in our investment portfolio where we saw investment return fall from £134.6 million in 2019 to £95.1 million in 2020, reflecting the dual impact of lower reinvestment rates and a small number of writedowns in the investment portfolio. When we look at some of the volatility in the market over the period we are pleased with the overall performance of the portfolio.

Prior to the pandemic we had set out to achieve improvements in our current year loss ratio and therefore to improve the profitability of the business we write. Offsetting this we had expected to see the level of releases from prior year business reduce, reflecting changes in the level of Motor excess of loss reinsurance some years ago. During 2020, prior-year reserve releases reduced to £173.8 million (2019: £294.5 million). Although the improvements in our loss ratio undoubtedly benefited from the impact of the Covid-19 pandemic, we are confident we have made progress in increasing the underlying current-year contribution to operating profit.

Overall we have sought to do the right thing by all our stakeholders throughout 2020, and believe the underlying performance and quality of change delivery in the year indicate we are on the right track to deliver on our targets.

Strategic update

In 2020 we saw a number of trends emerging through the year. Ultimately this tells us that our strategy is the right one. Those trends are:

- Consumers' willingness to interact digitally has been transformed. Digitalisation is at the heart of our technology transformation so this trend is entirely aligned with our plans.
- Agility is a must. We need to be quicker at implementing changes to fulfil changing customer needs.

- The working model has changed. Knowing our people can deliver from home has provided an opportunity to change how we use our offices in a way that supports what our people tell us they want and offers opportunities to recruit people irrespective of geography.
- Car technology continues to evolve rapidly. Having the largest owned repair network of any UK insurer gives us the opportunity to develop further commercial insights.
- Cross collaboration is a must. We can achieve more by working together; co-operation across industries is essential to tackling climate change and ensuring greater diversity.

2020 was always a critical change delivery year on our path to building the insurance company of the future – technology and data led but with the customer at its heart. I have been very pleased by our ability to continue delivering major transformational change, even from our homes.

The following table outlines some of our key achievements:

Objective	Progress to date
Best at direct	– Launched a new Direct Line 'Superhero' creative campaign highlighting the brand's unique propositions – Launched Direct Line's new "Mileage MoneyBack" proposition for Motor customers – Continued to extend modular product offerings on the new Direct Line for Business platform with the launch of Van and Tradesperson renewals, helping to drive growth of 92% in Van policies in 2020 – Green Flag continued to deliver exceptional customer service, driving higher Net Promoter Score values in 2020, and be the only rescue brand in the market to be awarded 'Superbrand' status
Win on PCWs	– Churchill Motor began the rollout on our new Motor platform for new business in Q1 2021, with Privilege new business and renewals now live on the new platform and migration of back book underway – Increased PCW focus including in Churchill Home helped deliver 55% year on year growth in PCW new business volumes in the second half of 2020 – Darwin launched on two more PCWs, helping fuel rapid growth to over 50,000 policies in 2020 – Churchill business named "Growth company of the year" at the 2020 National Insurance awards and delivered 62% growth in gross written premiums in 2020
Extend our reach.	– Agreed a two-year extension with NatWest Group for Home – Enhanced API capabilities with the creation of a 'sandbox' environment to enable potential Home partners to link and test API interface – Renewal of U K Insurance Business Services Limited contract with Drover and partnering with Trov, increasing our presence in the on-demand mobility market
Technical edge	– Launched a new market leading Motor counter fraud operating system – Expanded electric vehicle repair capabilities with increased training and investment in dedicated equipment – Commercial continued the roll-out of its new pricing and underwriting system with refreshed pricing on Fleet, contractors and Direct Line for Business Van – Commercial launched a free on-line risk management portal for every NIG policyholder enabling customers to 'ask the expert', the only insurer to offer this service – Green Flag launched a new cloud-based claims system and refreshed the "Green Flag Rescue Me" app, driving greater volumes through these digital channels
Nimble and cost efficient	– New operating model, incorporating agile ways of working, embedded across trading, digital and technology to enable us to test, learn and adapt to deliver customer value faster – Increased the proportion of service interactions carried out through digital channels – Auto Services improved capacity through extended operating hours to 7 days a week – Launched a new property strategy following the success of remote working in 2020, in addition to the two site closures announced in Q1 2020 – Migrated to a new mainframe platform as part of our technology transformation which will aim to reduce ongoing costs
Great people	– Our people continued to deliver our transformation agenda while working remotely – Our engagement scores remained high as we focused on the security and well-being of our people throughout the year – All employees will be receiving £350 worth of free shares and all eligible employees who are not usually paid bonuses or incentives will receive a £400 bonus in their April salary

Many of the foundation blocks are now in place and we are increasingly moving to extracting benefits from the technology we have implemented rather than focusing purely on technology delivery.

As we transform the business both in terms of the technology we use and our agility, we are changing the way the organisation works. We have found through 2020 that we can create and protect the culture of the Group, even with almost everyone working from home, and our regular people surveys tell us that our people want the personal flexibility that homeworking offers. Our intention, therefore, is to take this opportunity to change the way we use our premises in future so they support collaboration, training and teamwork rather than being an everyday place of work for most people.

We will remain focused around our core hub sites so our people can get together, but believe our approach gives both cost savings and advantages for our people, allowing us to support greater social mobility and assist us in identifying top talent. To this end we are reviewing our office site property strategy and have chosen to buy out our Bromley lease, the run costs of which were above market rate. This will accelerate the costs from the future 17 years of the lease and so we will take a charge to Solvency II own funds in 2021 of £85 million as we effectively de-leverage the business and, in return, make savings in excess of £10 million per annum from 2022, incremental to our original cost target plans. We will have greater freedom to create the nature of property usage this business needs.

In September 2020 the FCA released its General insurance Pricing Practices Final Report, which remains a key focus for us. It included their proposed remedy package aiming to ensure retail home and motor insurance products offer fair value to customers. The FCA recognised that insurers do not make excessive profits and their key proposal was that firms should offer renewal prices no higher than the equivalent new business prices through the same sales channel. The consultation period ended on 25 January 2021 and we look forward to understanding the final details some time in Q2 2021.

This is an area where we have already been proactive for several years by implementing a range of measures to reduce the differential in pricing between our new business and renewal customers. We are supportive of the aims of the FCA and believe that, in a world where prices become less of a differentiator, our strong brands, diversified business model and the capabilities we are building will enable us to win in the future market. On the way there is uncertainty around the detailed application of the rules, the timelines for implementation and the nature of short-term volatility as the market rebalances. We have prepared for a range of outcomes and we continue to work with the FCA to assist them in navigating some of the issues and are seeking to help shape the right outcome for our customers and shareholders. When combined with whiplash reform, currently due to be effective from May 2021, a mixed picture in terms of lockdowns in H1 and uncertainty over the long-term level of driving in our new "normal", there are clearly many moving parts.

That said, capital generation has been strong and our perception is that the level of risk in the system, with vaccines rolling out and a Brexit deal in place, is beginning to reduce. As a result we are declaring a final dividend of 14.7 pence per share and announcing a share buyback programme, as we reiterate our target of operating around the middle of our risk appetite range of 140% to 180% in normal circumstances. The share buyback will be for up to £100 million, with an initial tranche of up to £50 million expected to be completed by the time of the half-year results.

Looking into 2021 we will be continuing the roll-out of our technology transformation and increasingly turning our attention to utilising these new platforms to deliver benefits for our customers. Our plans include:

- Continuing the migration of Direct Line and Churchill Motor policies onto our new platform, enabling us to improve customers' online journey and extend our product range even further.
- Continuing the journey towards greater digitalisation, applying advanced analytical techniques to enhance the customer experience.
- Rolling out a new policy and pricing system for Green Flag enabling it to grow beyond traditional breakdown services and look after customers' motoring needs in and out of an emergency.
- Being ready to be well placed for customers and at a competitive advantage to other players in a post FCA pricing practices market.

We are also heavily focused on improving efficiency in order to help meet our cost targets by:

- Continuing organisational transformation to further digitalise customer journeys, automate business processes and adopt new ways of working, as we aim to step change both customer experience and the efficiency of our cost base.
- Realising the benefits of agile ways of working throughout the organisation, with the aim of reducing the cost and increasing the pace of change.

These plans are designed with fantastic customer experience and propositions at their heart. Supporting our activities and central to the long-term sustainability of the business, we have deeply embedded and fundamental principles:

- Our values sit at the very heart of our everyday behaviours.
- Our sustainability pillars bring environmental, social and governance ("**ESG**") factors into the heart of our strategic thinking, whether that's our customers, our people, our society, our planet, or the importance of strong governance – they all play central roles in helping deliver our business in a sustainable way.

Motor – Lockdown-related claims frequency benefits and progress towards sustainability of earnings

In 2020, the Motor division delivered an operating profit of £363.5 million and a combined operating ratio of 87.7% (2019: £302.6 million and 94.8% respectively). Motor was significantly impacted by Covid-19 disruption leading to reduced claims frequency, together with some underlying progress in reducing the current year loss ratio.

After strong gross written premium growth in Q1 of 6.2%, the lockdown restrictions from Q2 onwards reduced new car sales and the number of new drivers entering the market. This reduction in new business volumes and risk mix, alongside broader market deflation as claims frequency remained low throughout H2, caused a reduction in average premiums. Furthermore, the Group offered premium refunds to all customers where miles driven were lower than expected at policy inception. These factors helped lead to a 2.1% reduction in gross written premium in 2020 compared to 2019. Recognising

the take-up of the refund scheme, we also launched a "Mileage MoneyBack" proposition for all Direct Line customers. We see this as an initial step towards making insurance more personalised to the individual.

Motor's current year loss ratio improved by 14.6 percentage points to 66.6%. This was predominantly due to lockdown restrictions leading to claims frequency falling to around half normal levels during Q2 and, whilst it increased during the second half of the year, claims frequency did not return to pre-Covid-19 levels. This was partially offset by claims severity, which increased outside our medium-term expectations of 3% to 5% following longer repair times and the consequential impact on credit hire costs, alongside additional cleaning costs. Excluding these impacts of Covid-19 we made progress on the underlying current year loss ratio in Motor, with a new counter fraud platform delivered during 2020, helping offset lower prior-year reserve releases.

The motor excess of loss reinsurance programme renewed on 1 January 2021. We renewed all layers below £10 million (excess £1 million) but retained 25% of the risk. Above £10 million we now have an aggregate retention of £37.5 million. With reinsurance prices rising, we believe this structure provides an appropriate balance of risk and value for the Group.

Home – Improved PCW competitiveness

The 2020 Home result delivered an operating profit of £101.4 million and a combined operating ratio of 87.1% (2019: £150.6 million and 80.3% respectively).

Home delivered a strong trading performance with own brand in-force policies growing by 4.1% to 1.8 million due to the PCW channel where new business sales increased by over 30%, reflecting our increased focus and competitiveness. Total Home gross written premium was down 1.5% on 2019 as a number of Partnerships continued to run off, with own brand premiums remaining broadly flat. Own brand average premiums were 3.8% lower than prior year due to the mix change towards lower risk and therefore lower average premium policies in the PCW channel, alongside continuation of existing pricing actions to support retention.

Operating profit was £49.2 million lower than 2019 due to £27.0 million of major weather costs (2019: £3.0 million) alongside a reduction in prior-year reserve releases. Whilst Home saw some changes in claims mix during 2020, we estimate that the overall impact of the Covid-19 pandemic was not significant.

Normalised for weather, the combined operating ratio was 90.3%[1] (2019: 86.9%) due to a reduction in prior-year reserve releases. The current year attritional loss ratio improved by 0.8 percentage points between 2019 and 2020.

Rescue and other personal lines – Growth in Green Flag, challenging year for Travel

This segment comprises Rescue, including our challenger brand Green Flag, as well as other personal lines products – Pet, Travel, Creditor and our mid- to high-net worth business, UK Select.

Rescue operating profit grew by £6.0 million to £51.2 million (2019: £45.2 million) and Green Flag delivered strong in-force policy growth despite Covid-19 lockdowns impacting new business sales during Q2 and Q4. Although claims frequency was lower during lockdown periods, we still fulfilled around 90% of the number of rescues completed in 2019. Rescue reported a combined operating ratio of 76.5% compared to 81.5% in 2019.

Improved operating profit in Rescue was offset by a loss of £44.4 million in other personal lines as a result of the impact on our Travel business of Covid-19 restrictions. The loss was the result of a cautious stance on claims reserving, increased claims handling costs arising from the cost of training more staff to handle the significant volume of claims and additional commission payments, particularly on packaged bank account business.

Rescue and other personal lines gross written premium was 4.2% lower than 2019 at £417.8 million (2019: £436.0 million) largely due to the impact of Covid-19 restrictions reducing new business shopping in Rescue alongside the pausing of new business sales in Travel during Q2 and Q3. In-force policies fell 3.7% over the period. However, in Rescue, our Green Flag brand continued to deliver growth, increasing in-force policies by 4.8% to 1.1 million and gross written premium by 5.2% to £83.1 million.

Commercial – Beginning to realise the benefits of transformation

Within Commercial we have two main businesses, NIG and other and Commercial direct own brands. Commercial direct own brands include Direct Line for Business and commercial products sold under the Churchill brand primarily on PCWs.

Commercial delivered an operating profit of £50.4 million in 2020 (2019: £54.6 million) and a combined operating ratio of 95.5% (2019: 95.7%). Excluding the impact of major weather, the operating result increased £8.8 million, demonstrating the success of Commercial's strategic transformation and improving current year profitability. In respect of Business Interruption claims, our estimate has reduced from £10 million to £6 million.

Commercial direct own brands and NIG and other delivered strong gross written premium growth of 9.3% and 6.6% respectively. Increased van insurance sales were key to the growth in Commercial direct, via the new platform for Direct Line and through the PCW channel for Churchill. NIG continued to benefit from improvements arising from re-platforming its products. In-force policies continued to grow for Commercial direct own brands by 3.5% to 560,000 and for NIG and other by 7.3% to 251,000.

Note:

1. See glossary on pages 48 to 50 for definitions and appendix A – Alternative performance measures on pages 51 to 54 for reconciliation to financial statement line items.

Climate

The impact of climate change has far reaching implications for economies around the world. Our Planet pillar, which aims to protect our business from the impact of climate change and give back to the planet more than we take out, drives our approach. We recognise that our actions as a business can contribute to climate risk mitigation and help accelerate the transition to a low carbon and sustainable future. We take this seriously and have continued to challenge ourselves to reduce emissions and energy consumption through greater transparency.

We have previously published our Scope 1 and 2 emissions[1], but this year we wanted to go further. For the first time we broke down our emissions across our offices and our accident repair centres to help us to focus our plans on where we can have the most impact. Alongside this we evaluated our Scope 3 emissions[1] starting with those under our direct control and purchased goods and services which make a substantial contribution to our overall emissions. Our first comprehensive TCFD report provides us with a roadmap to strengthen our strategic response in tackling climate change and we see the Bank of England's Climate Biennial Exploratory Scenario ("**CBES**"), in which the Group has been invited to participate, as a way to help enhance our climate change scenario analysis capability.

The Group's focus in 2021 is to evaluate the Scope 3 emissions[1] arising out of our investment portfolio and we will begin to scope out Science Based Targets, which are a set of goals to provide a clear route to reduce emissions, to submit to the Science Based Target Initiative ("**SBTi**") for approval. Finally, we know that we are on a journey and cannot reduce our emissions overnight, therefore we became carbon neutral through offsetting, as we work to reduce our emissions over time.

Note:

1. See glossary on pages 48 to 50 for definitions.

UK economy and Brexit

Following the recession in 2020, economic uncertainty is expected to remain high throughout H1 2021 as a result of the Covid-19 pandemic, although the UK Government has acted to support UK businesses and employees and prevent lasting damage to the economy. However, the uncertainty surrounding the pandemic makes the overall impact and recovery progress unclear.

The disruption to global trade and supply-chains caused by the pandemic could increase the risk of inflation in the long-term. The Group's investment portfolio is positioned defensively and additional steps could be taken, such as further shifting the portfolio towards 'defensive' sectors or increasing more allocation to cash. The portfolio also contains a proportion of short-maturity bonds which could be sold relatively quickly if necessary.

As a UK based business with UK customers, we identified the biggest potential financial exposure for the Group, from a disruptive or disorderly Brexit, would be to market volatility. We continue to work through the operational effects for customers and supply chains but the potential effects have been helped by a trade deal which has avoided otherwise expected tariffs on EU goods needed to serve our customers.

Dividend and capital management

The Group's solvency capital ratio, prior to any dividends or incremental capital returns, was 213% as at 31 December 2020. The Board has recommended a final dividend of 14.7 pence, an increase of 2.1% on the special interim dividend of 14.4 pence announced at the time of our interim results, which reflected a full catch up of the cancelled 2019 final dividend.

Reflecting the strength of the Group's capital position, and in line with our dividend policy to return capital to shareholders which is expected to be surplus to the Group's requirements for a prolonged period, the Group intends to commence a share buyback programme of up to £100 million, with an initial tranche of up to £50 million expected to be completed by the time of the half-year results.

After the proposed final dividend and £100 million share buyback, the estimated solvency capital ratio was 191% as at 31 December 2020. The Group has outstanding Tier 2 debt issued in 2012 with nominal value of £250 million and a first call date during the first half of 2022. Excluding this debt, the Group's solvency ratio after the proposed final dividend and share buyback would be 172%. In February 2021, the Group acquired the head lease of its Bromley office site, which reduced the Group's coverage ratio by an additional 6 percentage points.

Assuming a return to more normal circumstances, the Group intends to move towards the middle of its risk appetite range of 140% to 180% of its solvency capital requirement, consistent with its previously stated target.

Outlook

The capability delivered as the Group looks to transition from technology transformation into business transformation underpins the improvement in the current-year profitability and provides a platform for growth, underwriting improvements and cost efficiency. Through increased digitalisation and self-serve, enabled by new ways of working, we aim to deliver significant customer and efficiency improvements and underpin our target of an operating expense ratio of 20% by 2023. The new ways of working during 2020 have enabled us to think more ambitiously about how we use our office space and we have therefore launched a property strategy which aims to help deliver incremental savings to this target. In addition, greater pricing sophistication and counter-fraud initiatives aim to continue the improvement in the current year loss ratio. The Group remains on track to maintain the contribution from current-year operating profit at more than half of the Group's total operating profit and we reiterate our ongoing target of achieving at least a 15% return on tangible equity per annum.

The Group targets a combined operating ratio of 93-95% for 2021 and over the medium term, normalised for weather, although we acknowledge there will be increased uncertainty for a period as we progress through the implementation of the FCA pricing practices proposals and as the market reacts to the ongoing Covid-19 pandemic.

2020 has been a testing year for everyone and I am proud of how we have responded as a Group, demonstrating throughout the resilience of our business model. We had strong momentum coming into the Covid-19 crisis and have delivered a good financial result whilst simultaneously navigating the Covid-19 pandemic, supporting our various stakeholders and staying true to our vision and purpose throughout. Given the progress we are making on our transformation, we enter 2021 with real momentum and are confident in delivering our vision of being a technology and data led insurance company of the future with our customers at its heart.

PENNY JAMES

CHIEF EXECUTIVE OFFICER

Note:

1. See glossary on pages 48 to 50 for definitions.

FINANCE REVIEW

Performance

Operating profit[1]

	FY 2020 £m	FY 2019 £m
Underwriting profit	**267.8**	232.1
Instalment and other operating income	**159.2**	180.2
Investment return	**95.1**	134.6
Operating profit	**522.1**	546.9
Of which:		
Current-year operating profit[1]	**348.3**	252.4
Prior-year reserve releases	**173.8**	294.5

Notes:

1. See glossary on pages 48 to 50 for definitions and appendix A – Alternative performance measures on pages 51 to 54 for reconciliation to financial statement line items.

The Group again delivered an operating profit in 2020 above £500 million and saw underlying progress towards achieving more than 50% of the profit arising from the current year. The results have been affected by the usual variability around weather events but the addition of the factors surrounding Covid-19 make them more difficult to navigate than in previous years.

First, the Group experienced major weather event claims of £43.0 million in 2020, below our expectations of £64 million but higher than the very benign weather experienced in 2019 (£6.0 million).

Second, the impact of the Covid-19 pandemic can be seen across all the main lines within the income statement, with the largest impact from reduced claims frequency in Motor. Whilst it is difficult to be exact about the impact of Covid-19 on the results, as the length of the pandemic has made initially 'one-off' impacts now more business as usual in their nature, for example motor market pricing, this review will indicate the broad direction of these impacts.

Overall the Group incurred £93 million in supporting customers, our people and society as part of our "Force for Good" initiatives. This support included customer refunds, job protection, charity donations and supplier support measures. Over this period the Group has not taken any Government support. The cost of these initiatives are all recognised in the underwriting result.

Furthermore, within the underwriting result there are four additional factors: a net reduction in motor claims from significantly reduced driving, partly offset by higher claims severity; a reduction in motor premiums as a result of fewer new drivers and market wide premium deflation; additional travel claims and claims handling costs; and business interruption claims in Commercial. These factors together had a net positive impact on the underwriting result.

Outside of the impact from Covid-19, prior year releases reduced to £173.8 million during 2020 (2019: £294.5 million), reflecting changes in the level of Motor excess of loss reinsurance some years ago and were materially offset by improvements in the underlying current year loss ratio across Motor and Commercial.

Overall this delivered an increase in underwriting profit to £267.8 million (2019: £232.1 million).

Lower motor premium and claims volumes, primarily arising from the Covid-19 pandemic, led to a reduction in instalment and other operating income to £159.2 million (2019: £180.2 million).

Investment return decreased to £95.1 million (2019: £134.6 million), reflecting the dual impact of lower reinvestment rates and lower valuations on property in the investment portfolio.

Taking all of this together, operating profit decreased by £24.8 million to £522.1 million (2019: £546.9 million) and current-year operating profit, as a proportion of total operating profit, improved to 66.7% (65.4% on a normalised basis). Whilst current-year profitability has benefited from the impact of Covid-19 related factors in 2020, the Group remains on track for its target of achieving more than half of the Group's annual operating profit from current-year earnings by the end of 2021.

In-force policies and gross written premium

In-force policies (thousands)

At	**31 Dec 2020**	30 Sep 2020	30 Jun 2020	31 Mar 2020	31 Dec 2019
Direct own brands	**3,943**	3,971	3,972	3,944	3,921
Partnerships	**118**	118	119	121	122
Motor	**4,061**	4,089	4,091	4,065	4,043
Direct own brands	**1,837**	1,808	1,782	1,771	1,765
Partnerships	**801**	808	814	826	829
Home	**2,638**	2,616	2,596	2,597	2,594
Rescue	**3,400**	3,396	3,380	3,424	3,450
Travel	**3,499**	3,536	3,567	3,607	3,648
Pet	**145**	148	152	155	157
Other personal lines	**61**	61	62	63	122
Rescue and other personal lines	**7,105**	7,141	7,161	7,249	7,377
Of which: Green Flag direct	**1,114**	1,110	1,070	1,082	1,063
Direct own brands	**560**	554	546	547	541
NIG and other	**251**	244	239	238	234
Commercial	**811**	798	785	785	775
Total in-force policies	**14,615**	14,644	14,633	14,696	14,789
Of which: direct own brands	**7,454**	7,443	7,370	7,344	7,290

Own brand policies increased to 7.5 million (2019: 7.3 million) driven by growth in Home, Commercial and Green Flag Rescue, whilst Motor was broadly stable. Total in-force policies reduced slightly to 14.6 million (31 December 2019: 14.8 million) primarily due to reductions in Home partnerships, as Prudential and Sainsbury's partnerships are closed to new business, and the impact of Covid-19 on Travel sales.

Gross written premium

	H2 2020 £m	H2 2019 £m	**FY 2020 £m**	FY 2019 £m
Direct own brands	**788.7**	820.1	**1,567.6**	1,591.7
Partnerships	**22.9**	31.0	**49.3**	59.9
Motor	**811.6**	851.1	**1,616.9**	1,651.6
Direct own brands	**218.0**	214.0	**411.6**	407.7
Partnerships	**83.8**	89.3	**166.3**	178.9
Home	**301.8**	303.3	**577.9**	586.6
Rescue	**85.7**	84.6	**166.7**	167.5
Travel	**62.7**	75.1	**134.0**	151.3
Pet	**36.4**	36.4	**72.8**	72.6
Other personal lines	**22.9**	23.4	**44.3**	44.6
Rescue and other personal lines	**207.7**	219.5	**417.8**	436.0
Of which: Green Flag direct	**43.9**	41.0	**83.1**	79.0
Direct own brands	**84.7**	75.8	**163.3**	149.4
NIG and other	**193.8**	178.3	**404.5**	379.5
Commercial	**278.5**	254.1	**567.8**	528.9
Total gross written premium	**1,599.6**	1,628.0	**3,180.4**	3,203.1
Of which: direct own brands	**1,135.3**	1,150.9	**2,225.6**	2,227.8

Gross written premium of £3,180.4 million (2019: £3,203.1 million) reduced by 0.7% with strong premium growth in Commercial offset by lower Motor and Home partnership premiums and the impact of Covid-19 disruption in Travel. Direct own brands gross written premium was broadly stable at £2,225.6 million (2019: £2,227.8 million). Growth across Commercial, Green Flag Rescue and Home own brands was offset by Motor.

Motor

Motor in-force policies grew by 0.4% to 4.1 million with own brand in-force policies up by 0.6% at 3.9 million. Strong retention was partially offset by a slow down in the new business market as new car sales fell and fewer new drivers entered the market. The Group saw good growth in the PCW channel as both Churchill and Darwin strengthened their propositions.

The Group offered premium refunds to all customers where miles driven were expected to be lower than anticipated at policy inception. Furthermore, the Group launched a "Mileage MoneyBack" proposition for all Direct Line customers such that customers would be able to receive a refund at the end of the policy period where they had driven less than expected. Gross written premium reduced by 2.1% to £1,616.9 million primarily due to lower average premium.

Motor own brand average premium[1] reduced 2.0% during 2020 due predominantly to a 4.0% impact from reducing risk mix following lower new car sales and fewer new drivers entering the market. Motor risk-adjusted prices, before taking account of lower claims frequency, increased by 1.8%. Market premium deflation accelerated through 2020 as claims frequency remained low.

Home

In-force policies for Home's own brands increased by 4.1% in 2020 to 1.8 million policies. Retention and new business were strong with particular strength in PCW new business which grew over 30%. This reflected the Group's increased focus on, and capability in, the PCW channel. Partnership volumes reduced by 3.4%; Prudential and Sainsbury's partnerships are closed to new business and continued to run off in line with expectations.

Gross written premium was 1.5% lower than 2019, primarily due to the reduction in partnership volumes. Own brands gross written premium increased by 1.0% as growth in in-force policies was offset by lower average premium.

Home own brand average premium[2] reduced by 3.8% primarily reflecting a change in mix towards lower risk and consequently lower average premium policies in the PCW channel. Risk adjusted prices reduced by 1.2% reflecting initiatives taken to reduce claims inflation and actions taken to reduce the differential between new business and renewal prices.

Rescue

Rescue in-force policies reduced by 1.4% to 3.4 million and gross written premium reduced by 0.5% to £166.7 million.

Green Flag Rescue continued to grow its higher average premium direct business during 2020, increasing in-force policies by 4.8% to 1.1 million and gross written premium by 5.2% to £83.1 million. Other Rescue lines, which include the linked channel, where cover can be purchased with a Group Motor policy, and Rescue partnerships, saw in-force policies and gross written premium reduce by 4.2% and 5.5% respectively.

Other personal lines

Other personal lines (comprising Travel, Pet, Creditor and policies tailored to mid- to high-net worth customers) in-force policies reduced by 5.7% to 3.7 million primarily due to lower Travel, following the Group's suspension of sales in Q2 and Q3, as a result of the Covid-19 lockdown, and continued reductions in packaged bank volumes. Gross written premium for Other personal lines decreased by 6.5% with reductions across all lines except Pet, where premium levels were maintained.

Commercial

Commercial in-force policies of 811,000 increased by 4.6% compared with 2019, reflecting strong growth in both Commercial direct own brands and NIG and other.

Commercial direct own brands grew in-force policies by 3.5% supported by the growth in Van for Direct Line, where the product was added to the new commercial direct platform, and for Churchill where Van is sold through the PCW channel. Gross written premium increased by 9.3% to £163.3 million with increases across all Commercial direct product lines.

NIG and other in-force policy numbers were 7.3% higher and gross written premium grew by 6.6% to £404.5 million. This reflected growth across all categories as the book continued to benefit from improvements arising from the re-platforming of the products on its award-winning electronic trading platform and improvements in Van pricing.

Notes:

1. Average incepted written premium excluding IPT for Motor own brands (covering 96.5% of Motor) for year end 31 December 2020.
2. Average incepted written premium excluding IPT for Home own brands for year end 31 December 2020.

Underwriting profit and combined operating ratio[1]

	FY 2020	FY 2019
Underwriting profit (£ million)	**267.8**	232.1
Loss ratio	**57.9%**	61.9%
Commission ratio	**8.6%**	7.1%
Expense ratio	**24.5%**	23.2%
Combined operating ratio	**91.0%**	92.2%

Note:

1. See glossary on pages 48 to 50 for definitions and appendix A – Alternative performance measures on pages 51 to 54 for reconciliation to financial statement line items.

Overall underwriting profit increased to £267.8 million (2019: £232.1 million) with an improvement in the combined operating ratio to 91.0% (2019: 92.2%).

The loss ratio improved significantly to 57.9% (2019: 61.9%) as higher major weather-related claims and lower prior-year reserve releases were more than offset by the net positive effect of Covid-19 related factors. These included reduced claims frequency in Motor, only partially offset by premium deflation in Motor, higher claims handling costs in Travel and a cautious estimate of Travel claims. The improvement in the loss ratio was partially offset by a higher commission ratio and higher expense ratio. The commission ratio increased primarily as a result of increased profit share payments, particularly on packaged bank accounts, and volume related commission payments to PCWs, while the expense ratio increased due to investment in initiatives to protect our customers, people and society. Excluding costs related to the protection of our customers and people against the Covid-19 pandemic, the Group made progress in reducing its underlying expense base.

Ratio analysis by division

	Notes	Motor £m	Home £m	Rescue and other personal lines £m	Commercial £m	Total Group £m
For the year ended 31 December 2020						
Net earned premium	3	**1,484.8**	**555.8**	**422.9**	**497.0**	**2,960.5**
Net insurance claims	3	**888.1**	**309.1**	**261.1**	**255.3**	**1,713.6**
Prior-year reserve releases	20	**100.6**	**10.8**	**5.6**	**56.8**	**173.8**
Major weather events		**n/a**	**(27.0)**	**n/a**	**(16.0)**	**(43.0)**
Attritional net insurance claims		**988.7**	**292.9**	**266.7**	**296.1**	**1,844.4**
Loss ratio – current-year attritional		**66.6%**	**52.7%**	**63.0%**	**59.6%**	**62.3%**
Loss ratio – prior-year reserve releases		**(6.8%)**	**(1.9%)**	**(1.3%)**	**(11.4%)**	**(5.9%)**
Loss ratio – major weather events[1]		**n/a**	**4.8%**	**n/a**	**3.2%**	**1.5%**
Loss ratio – reported	3	**59.8%**	**55.6%**	**61.7%**	**51.4%**	**57.9%**
Commission ratio	3	**3.2%**	**8.1%**	**16.4%**	**18.7%**	**8.6%**
Expense ratio	3	**24.7%**	**23.4%**	**23.9%**	**25.4%**	**24.5%**
Combined operating ratio	3	**87.7%**	**87.1%**	**102.0%**	**95.5%**	**91.0%**
Current-year combined operating ratio		**94.5%**	**89.0%**	**103.3%**	**106.9%**	**96.9%**
For the year ended 31 December 2019						
Net earned premium	3	1,507.7	573.6	425.2	478.4	2,984.9
Net insurance claims	3	1,043.3	268.4	284.4	251.5	1,847.6
Prior-year reserve releases	20	180.5	41.4	7.6	65.0	294.5
Major weather events		n/a	(3.0)	n/a	(3.0)	(6.0)
Attritional net insurance claims		1,223.8	306.8	292.0	313.5	2,136.1
Loss ratio – current-year attritional		81.2%	53.5%	68.7%	65.6%	71.6%
Loss ratio – prior-year reserve releases		(11.9%)	(7.2%)	(1.8%)	(13.6%)	(9.9%)
Loss ratio – major weather events[1]		n/a	0.5%	n/a	0.7%	0.2%
Loss ratio – reported	3	69.3%	46.8%	66.9%	52.7%	61.9%
Commission ratio	3	2.6%	9.7%	6.4%	18.5%	7.1%
Expense ratio	3	22.9%	23.8%	22.1%	24.5%	23.2%
Combined operating ratio	3	94.8%	80.3%	95.4%	95.7%	92.2%
Current-year combined operating ratio		106.6%	87.6%	97.2%	109.2%	102.1%

Notes:

1. Home and Commercial claims for major weather events, including inland and coastal flooding and storms.

The current-year attritional loss ratio excludes prior-year reserve releases and claims costs from major weather events, although in 2020 it was impacted by Covid-19 disruption. The Group's current-year attritional loss ratio of 62.3% improved by 9.3 percentage points compared to 2019, due to reduced Motor claims frequency alongside improved underlying current year performance across all lines. Home and Commercial experienced increase major weather costs, up £24.0 million and £13.0 million respectively compared to 2019.

Prior-year reserve releases reduced in 2020 to £173.8 million (2019: £294.5 million), equivalent to 5.9% of net earned premium (2019: 9.9%) and were concentrated towards more recent accident years. In 2019 prior-year reserve releases included a £16.9 million reserve strengthening in relation to the change in the Ogden discount rate to minus 0.25%. Assuming current claims trends continue, prior-year reserve releases are expected to remain a significant contribution to profits. The sensitivity analysis on page 22 includes information on the effect of claims inflation.

The Group's current-year combined operating ratio improved by 5.2 percentage points to 96.9% (2019: 102.1%) as a 9.3 percentage point improvement to the current-year attritional loss ratio was partly offset by a 1.3 percentage point increase in claims due to major weather events, a 1.5 percentage point increase in the commission ratio and a 1.3 percentage point increase in the expense ratio.

Motor

The motor result has been significantly affected by the factors surrounding Covid-19 with the current-year attritional loss ratio improving by 14.6 percentage points to 66.6% (2019: 81.2%). The majority of this reduction reflects lower levels of claims frequency as driving patterns evolved through the year. A relatively normal first quarter was followed by a halving of claims frequency during the second quarter with less significant but still lower levels of claims frequency through the rest of the year. While claims frequency was down as fewer miles were driven, claims severity was higher than the Group's medium-term expectation of 3% to 5% inflation per annum. Claims severity has been impacted by longer repair times and consequent greater credit hire costs and additional cleaning and by extending the scope of vehicle replacement as part of the customer initiatives.

Although it is not possible to entirely adjust for all of the above factors, the Group believes that it made some underlying progress in reducing the current year loss ratio during the year.

In total, prior-year reserve releases were £79.9 million lower year on year at £100.6 million. The 2019 prior-year reserve releases included a strengthening of £15.9 million as a result of the change in the Ogden discount rate to minus 0.25% from an assumed rate of 0%.

Overall Motor's reported combined operating ratio improved by 7.1 percentage points to 87.7% (2019: 94.8%). The improvements in the current-year attritional loss ratio were offset by a 0.6 percentage point increase in the commission ratio, primarily due to increased volume related commission payments to PCWs, a 1.8 percentage point increase in the expense ratio and a 5.1 percentage point reduction in prior-year reserve releases.

Home

The current-year attritional loss ratio, excluding major weather event claims, improved by 0.8 percentage points to 52.7%. Home has experienced a change in mix towards more accidental damage claims and fewer theft claims during 2020 with continuing positive trends in escape of water severity. Whilst the Covid-19 pandemic is believed to have contributed positively to these trends the impact is not significant.

The commission ratio of 8.1% was 1.6 percentage points lower than 2019 due to lower profit share payments to partners.

Home's combined operating ratio increased by 6.8 percentage points to 87.1% (2019: 80.3%). This was driven primarily by a 5.3 percentage point reduction in prior-year releases and a 4.3 percentage point increase in major weather costs partly offset by an improvement in the current-year attritional loss ratio. Normalised for weather, the combined operating ratio was 3.4% percentage points higher than 2019 at 90.3%[1] (2019: 86.9%).

Rescue and other personal lines

The combined operating ratio for Rescue and other personal lines increased by 6.6 percentage points to 102.0% (2019: 95.4%) due predominantly to Travel which incurred increased claims handling costs supporting customers throughout 2020 and higher commissions to partners. The Group has taken a cautious stance in its reserving for travel claims.

The combined operating ratio for **Rescue** of 76.5% was 5.0 percentage points better than 2019's ratio of 81.5%. Lower claims frequency during the Covid-19 lockdown alongside lower claims costs due to fewer long-distance recoveries, was partially offset by supplier network support payments and free rescue given to NHS staff. Approximately half of the improvement in the combined operating ratio is expected to be one-off.

Other personal lines combined operating ratio increased by 14.4 percentage points to 118.5%. The increase is entirely due to Travel where the Group incurred increased claims handling costs supporting customers throughout 2020, has taken a cautious stance in its reserving and has incurred additional commission payments, particularly on packaged bank account business.

Commercial

The current-year attritional loss ratio in Commercial improved by 6.0 percentage points to 59.6%. This was driven by improvements to underwriting through pricing and risk selection as well as frequency benefits in motor lines since the end of Q1. This was partially offset by Covid-19 related business interruption claims at £6 million.

Prior-year reserve releases were £8.2 million lower at £56.8 million, primarily due to lower general liability reserve releases on older accident years. 2019's result included a £1.0 million strengthening of prior-year reserves as a result of the change in the Ogden discount rate to minus 0.25% from an assumed rate of 0%.

The combined operating ratio for Commercial improved slightly by 0.2 percentage points to 95.5% (2019: 95.7%) as an improvement in the current-year attritional loss ratio of 6.0 percentage points was largely offset by an increase in claims related to severe weather, a reduction in prior-year reserve releases and an increase of 0.9 percentage points on the expense ratio.

Note:

1. See glossary on pages 48 to 50 for definitions and appendix A – Alternative performance measures on pages 51 to 54 for reconciliation to financial statement line items.

Operating expenses before restructuring and one-off costs

	Note	FY 2020 £m	FY 2019 £m
Staff costs[1]		**255.6**	261.5
IT and other operating expenses[1,2]		**196.0**	158.0
Marketing	9	**106.6**	113.9
Insurance levies	9	**80.4**	81.5
Depreciation and amortisation[3,4]	9	**85.8**	78.8
Total operating expenses before restructuring and one-off costs		**724.4**	693.7

Notes:

1. Staff costs and other operating expenses attributable to claims handling activities are allocated to the cost of insurance claims.
2. IT and other operating expenses include professional fees and property costs.
3. Depreciation and amortisation includes a £6.6 million impairment charge for year ended 31 December 2020 (2019: £1.3 million), which relates to capitalised software development costs for ongoing IT projects primarily relating to development of new systems.
4. Includes depreciation on right-of-use assets of £14.8 million (31 December 2019: £14.2million).

Operating expenses before restructuring and one-off costs increased by £30.7 million to £724.4 million (2019: £693.7 million). This resulted in an increase in the expense ratio of 1.3 percentage points to 24.5% (2019: 23.2%). The increase in costs was entirely due to investment in initiatives for our customers, people, suppliers and the wider society in the context of the Covid-19 pandemic. In total these initiatives are estimated to have increased operating expenses by £34 million and in some cases had the effect of delaying cost saving programmes which were planned for 2020. Adjusting for these initiatives, operating expenses were broadly flat year on year and we reiterate our 20% expense ratio ambition for 2023.

Instalment and other operating income

	Note	FY 2020 £m	FY 2019 £m
Instalment income		**109.3**	114.0
Other operating income:			
Revenue from vehicle recovery and repair services	6	**24.0**	28.3
Vehicle replacement referral income	6	**12.2**	19.1
Legal services income	6	**8.8**	11.3
Other income[1]	6	**4.9**	7.5
Other operating income		**49.9**	66.2
Total instalment and other operating income		**159.2**	180.2

Note:

1. Other income includes mainly fee income from insurance intermediary services.

Instalment and other operating income, which is primarily driven by premium and claims volumes, decreased by £21.0 million to £159.2 million. Instalment income fell primarily due to lower motor premium, whereas lower other operating income reduced due to Covid-19 related lower motor claims frequency.

Investment return

	Note	FY 2020 £m	FY 2019 £m
Investment income		**127.1**	146.4
Hedging to a sterling floating rate basis		**(20.3)**	(22.1)
Net investment income		**106.8**	124.3
Net realised and unrealised (losses)/gains excluding hedging		**(11.7)**	10.3
Total investment return	5	**95.1**	134.6

Investment yields

	FY 2020	FY 2019
Investment income yield[1]	**2.1%**	2.4%
Net investment income yield[1]	**1.8%**	2.1%
Investment return yield[1]	**1.6%**	2.2%

Note:

1. See glossary on pages 48 to 50 for definitions and appendix A – Alternative performance measures on pages 51 to 54 for reconciliation to financial statement line items.

Total investment return decreased by £39.5 million to £95.1 million (2019: £134.6 million) with a reduction in investment income and write downs on investment property. Lower reinvestment rates, following interest cuts made by both the US Federal Reserve and the Bank of England during Q1 2020, led to a lower net investment income yield of 1.8% (2019: 2.1%).

Realised and unrealised losses excluding hedging were predominantly driven by lower investment property valuations and a reduction in gains from bond disposals. Overall the investment portfolio performed well in the context of challenging market conditions.

In 2021, the Group expects a net investment income yield of around 1.5% with minimal gains.

The Group's investment strategy aims to deliver several objectives, which are summarised below:

- to ensure there is sufficient liquidity available within the investment portfolio to meet stressed liquidity scenarios;
- to match periodic payment orders ("**PPO**") and non-PPO liabilities in an optimal manner; and
- to deliver a suitable risk-adjusted investment return commensurate with the Group's risk appetite.

Investment holdings

At 31 December	**2020** **£m**	2019 £m
Investment-grade credit[1]	**3,736.6**	3,676.8
High yield	**349.0**	390.8
Investment-grade private placements	**103.9**	104.0
Credit	**4,189.5**	4,171.6
Sovereign[1]	**25.5**	99.8
Total debt securities	**4,215.0**	4,271.4
Infrastructure debt	**264.5**	278.1
Commercial real estate loans	**206.7**	205.7
Cash and cash equivalents[2]	**1,168.2**	896.3
Investment property	**292.1**	291.7
Equity investments[3]	**3.2**	—
Total investment holdings	**6,149.7**	5,943.2

Notes:

1. Asset allocation at 31 December 2020 includes investment portfolio derivatives, which have a mark-to-market asset value of £7.7 million included in investment grade credit and £0.3 million in sovereign debt (31 December 2019 £81.8 million and nil respectively). This excludes non-investment derivatives that have been used to hedge interest on subordinated debt and operational cash flows.
2. Net of bank overdrafts: includes cash at bank and in hand and money market funds.
3. Equity investments consist of an equity fund which is valued based on external valuation reports received from a third-party fund manager.

At 31 December 2020, total investment holdings of £6,149.7 million were 3.5% higher than at the start of the year. Total debt securities were £4,215.0 million (31 December 2019: £4,271.4 million), of which 2.6% were rated as 'AAA' and a further 54.4% were rated as 'AA' or 'A'. The average duration at 31 December 2020 of total debt securities was 2.8 years (31 December 2019: 2.5 years).

At 31 December 2020, total unrealised gains, net of tax, on available-for-sale ("**AFS**") investments were £83.9 million (31 December 2019: £47.5 million).

Reconciliation of operating profit

	Note	**FY 2020** **£m**	FY 2019 £m
Motor	3	**363.5**	302.6
Home	3	**101.4**	150.6
Rescue and other personal lines	3	**6.8**	39.1
Commercial	3	**50.4**	54.6
Operating profit	3	**522.1**	546.9
Restructuring and one-off costs	3	**(39.4)**	(11.2)
Finance costs	10	**(31.3)**	(26.0)
Profit before tax	3	**451.4**	509.7
Tax		**(84.2)**	(89.8)
Profit for the year attributable to the owners of the Company		**367.2**	419.9

Operating profit by segment

All divisions contributed to profit in 2020, demonstrating the diversity of the Group's multi-product, multi-brand and multi-channel portfolio. Motor operating profit increased significantly primarily due to the reduction in claims frequency whereas Home operating profit reduced primarily due to higher weather-related costs and lower prior-year reserve releases. Commercial continued to generate strong profit despite higher weather claims while improved Rescue operating profit of £51.2 million (2019: £45.2 million) offset a weak result in other personal lines, mainly from Travel.

Restructuring and one-off costs

In order to support its cost reduction targets, the Group announced approximately £60 million of restructuring and one-off costs across 2019 and 2020 at its Capital Markets Day in November 2019. The Group incurred £39.4 million of restructuring and one-off costs in 2020 bringing the total cost to date to £50.6 million. As part of the Group's response to the Covid-19 pandemic to support its people it paused some elements of its restructuring programme. The Group expects the remaining £9 million in relation to this cost reduction programme to be incurred during 2021.

In addition, the Group is reviewing its office site property strategy and has bought out the lease of its Bromley office thus accelerating payment of an existing long-term liability. This transaction will incur restructuring costs of £85 million in 2021.

Finance costs

Finance costs increased to £31.3 million (2019: £26.0 million) primarily due to interest on the £260 million Tier 2 subordinated debt issued in June 2020.

Effective corporation tax rate

The effective tax rate for 2020 was 18.7% (2019: 17.6%), which was slightly lower than the standard UK corporation tax rate of 19.0% (2019: 19.0%) driven primarily by tax relief for the Tier 1 coupon payments partly offset by disallowable expenses. The effective rate is higher than 2019 which benefited from the release of an overprovision from a prior year.

On 3 March 2021 the Chancellor announced that the rate of UK corporation tax will increase to 25% from 1 April 2023. This is not reflected in the figures above as it was not substantively enacted at the balance sheet date, however the effect is not expected to be material.

Profit for the year and return on tangible equity[1]

Profit for the year was lower at £367.2 million (2019: £419.9 million) in line with the reduction in operating profit as well as increased restructuring and one-off costs and finance costs.

Return on tangible equity decreased to 19.9% (2019: 20.8%) due primarily to a £24.4 million decrease in adjusted[1] profit after tax to £384.1 million (2019: £408.5 million). Profit after tax was adjusted for restructuring and one-off costs and coupon payments in respect of Tier 1 notes.

Note:

1. See glossary on pages 48 to 50 for definitions and appendix A – Alternative performance measures on pages 51 to 54 for reconciliation to financial statement line items.

Earnings per share

Basic earnings per share decreased by 12.5% to 25.8 pence (2019: 29.5 pence). Diluted earnings per share decreased by 12.7% to 25.5 pence (2019: 29.2 pence) mainly reflecting the reduction in profit after tax.

Net asset value

At 31 December	Note	**2020 £m**	2019 £m
Net assets[1]	13	**2,699.7**	2,643.6
Goodwill and other intangible assets	13	**(786.8)**	(702.5)
Tangible net assets	13	**1,912.9**	1,941.1
Closing number of Ordinary Shares (millions)	13	**1,351.8**	1,366.6
Net asset value per share (pence)	13	**199.7**	193.4
Tangible net asset value per share (pence)	13	**141.5**	142.0

Note:

1. See glossary on pages 48 to 50 for definitions and appendix A – Alternative performance measures on pages 51 to 54 for reconciliation to financial statement line items.

Net assets at 31 December 2020 increased to £2,699.7 million (31 December 2019: £2,643.6 million) and tangible net assets decreased to £1,912.9 million (31 December 2019: £1,941.1 million) reflecting the 2020 retained profit and increases in available-for-sale reserves. This was offset by additional expenditure on intangible assets as the Group continued to invest in the business.

Balance sheet management

Capital management and dividend policy

The Group aims to manage its capital efficiently and generate long-term sustainable value for shareholders, while balancing operational, regulatory, rating agency and policyholder requirements.

The Group aims to grow its regular dividend in line with business growth.

Where the Board believes that the Group has capital which is expected to be surplus to the Group's requirements for a prolonged period, it intends to return any surplus to shareholders. In normal circumstances, the Board expects that a solvency capital ratio around the middle of its risk appetite range of 140% to 180% of the Group's solvency capital requirement ("**SCR**") would be appropriate and it will therefore take this into account when considering the potential for special distributions.

In the normal course of events the Board will consider whether or not it is appropriate to distribute any surplus capital to shareholders once a year, alongside the full-year results.

The Group expects that one-third of the annual dividend will generally be paid in the third quarter as an interim dividend, and two-thirds will be paid as a final dividend in the second quarter of the following year. The Board may revise the dividend policy from time to time. The Company may consider a special dividend and/or a repurchase of its own shares to distribute surplus capital to shareholders.

The Board has recommended a final dividend of 14.7 pence per share (2019: 14.4 pence), an increase of 2.1% on the special interim dividend of 14.4 pence announced at the time of our interim results, which reflected a full catch up of the cancelled 2019 final dividend. The Board has also approved a share buyback of up to £100 million, with an initial tranche of up to £50 million expected to be completed by the time of the half-year results. This reflects the Board's continued confidence in the Group's capital position and the sustainability of its earnings. In normal circumstances, the Board expects the Group to operate around the middle of its solvency capital ratio risk appetite range of 140% to 180%.

After the dividend and share buyback, the estimated solvency capital ratio was 191% as at 31 December 2020. The Group has outstanding Tier 2 debt issued in 2012 with nominal value of £250 million and a first call date during the first half of 2022. Excluding this debt, the Group's solvency ratio after dividend and share buyback would be 172%. In February 2021, the Group acquired the head lease of its Bromley office site, which reduced the Group's coverage ratio by an additional 6 percentage points.

The final dividend will be paid on 20 May 2021 to shareholders on the register on 9 April 2021. The ex-dividend date will be 8 April 2021.

Capital analysis

The Group is regulated under Solvency II requirements by the PRA on both a Group basis and for the Group's principal underwriter, U K Insurance Limited. In its results, the Group has estimated its Solvency II own funds, SCR and solvency capital ratio as at 31 December 2020.

Capital position

At 31 December 2020, the Group held a Solvency II capital surplus of £1.22 billion above its regulatory capital requirements, which was equivalent to an estimated solvency capital ratio of 191%, after the proposed final dividend and share buyback.

The Group's SCR and solvency capital ratio are as follows:

At 31 December	**2020**	2019
Solvency capital requirement (£ billion)	**1.34**	1.32
Capital surplus above solvency capital requirement (£ billion)	**1.22**	0.85
Solvency capital ratio after proposed final dividend and share buyback	**191%**	165%

Movement in capital surplus

	2020 **£bn**	2019 £bn
Capital surplus at 1 January	**0.85**	0.89
Capital generation excluding market movements	**0.59**	0.60
Market movements	**(0.02)**	0.06
Capital generation	**0.57**	0.66
Change in solvency capital requirement	**(0.02)**	(0.06)
Surplus generation	**0.55**	0.60
Capital expenditure	**(0.16)**	(0.19)
Tier 2 debt issue	**0.26**	–
Cancellation of 2019 year-end distribution and reinstatement for 2020 half-year[1]	**0.12**	–
Interim dividend[2]	**(0.10)**	(0.10)
Final dividend[2]	**(0.20)**	(0.20)
Share buyback	**(0.10)**	(0.15)
Net surplus movement	**0.37**	(0.04)
Capital surplus at 31 December	**1.22**	0.85

Note:

1. Relates to the cancellation of the 2019 cash dividend (£197 million) and share buyback (£120 million); offset by the special dividend subsequently declared at half-year 2020.
2. Foreseeable dividends included above are adjusted to exclude the expected dividend waivers in relation to shares held by the employee share trusts, which are held to meet obligations arising on the various share option awards.

In 2020, the Group generated £0.57 billion of Solvency II capital and added £0.26 billion via a Tier 2 debt issue, whilst cancelled distributions added £0.12 billion to own funds. This was offset by £0.16 billion of capital expenditure and distributions of £0.40 billion. Capital expenditure reflects the significant investment the Group is making in building future capability, including the development of the next generation core personal lines IT systems. In 2021 capital expenditure levels are expected to reduce to around £120 million. In addition, £85 million of restructuring costs in relation to the purchase of the Bromley office lease will decrease capital generation in 2021.

Change in solvency capital requirement

	2020 £bn
Solvency capital requirement at 1 January	**1.32**
Model and parameter changes	**–**
Exposure changes	**0.02**
Solvency capital requirement at 31 December	**1.34**

The Group's SCR has increased by £0.02 billion in the year due to exposure changes. Model and parameter changes were largely offsetting.

Scenario and sensitivity analysis

The following table shows the impact on the Group's estimated solvency capital ratio in the event of the following scenarios as at 31 December 2020. The impact on the Group's solvency capital ratio arises from movements in both the Group's solvency capital requirement and own funds.

	Impact on solvency capital ratio	
Scenario	**31 Dec 2020**	31 Dec 2019
Deterioration of small bodily injury motor claims equivalent to that experienced in 2008/09	**(6pts)**	(7pts)
One-off catastrophe loss equivalent to the 1990 storm "Daria"	**(8pts)**	(9pts)
One-off catastrophe loss based on extensive flooding of the River Thames	**(8pts)**	(9pts)
Change in Solvency II reserving basis for PPOs to use a real discount rate of minus 1%[1]	**(10pts)**	(8pts)
100bps increase in credit spreads[2]	**(9pts)**	(9pts)
100bps decrease in interest rates with no change in the PPO real discount rate	**(3pts)**	1pt

Notes:

1. The PPO real discount rate used is an actuarial judgement which is reviewed annually based on the economic outlook for wage inflation relative to the PRA discount rate curve.
2. Only includes the impact on AFS assets (excludes illiquid assets such as infrastructure debt) and assumes no change to the SCR.

Own funds

The following table splits the Group's own funds by tier on a Solvency II basis.

At 31 December	**2020 £bn**	2019 £bn
Tier 1 capital before foreseeable distributions	**1.84**	1.80
Foreseeable dividend and share buyback	**(0.30)**	(0.35)
Tier 1 capital – unrestricted	**1.54**	1.45
Tier 1 capital – restricted	**0.38**	0.37
Tier 1 capital	**1.92**	1.82
Tier 2 capital – subordinated debt	**0.53**	0.26
Tier 3 capital – deferred tax	**0.11**	0.09
Total own funds	**2.56**	2.17

During 2020, the Group's own funds increased from £2.17 billion to £2.56 billion. Tier 1 capital after foreseeable distributions represents 75% of own funds and 143% of the estimated SCR. Tier 2 capital relates solely to the Group's £0.53 billion subordinated debt. The amount of Tier 2 and Tier 3 capital permitted under the Solvency II regulations is 50% of the Group's SCR and of Tier 3 alone is less than 15%. Therefore, the Group currently has no ineligible capital. The maximum amount of Restricted Tier 1 capital permitted as a proportion of total Tier 1 capital under the Solvency II regulations is 20%. Restricted Tier 1 capital relates solely to the Tier 1 notes issued in 2017.

Reconciliation of IFRS shareholders' equity to Solvency II own funds

At 31 December	**2020 £bn**	2019 £bn
Total shareholders' equity	**2.70**	2.64
Goodwill and intangible assets	**(0.79)**	(0.70)
Change in valuation of technical provisions	**0.04**	(0.06)
Other asset and liability adjustments	**(0.11)**	(0.08)
Foreseeable dividend and share buyback	**(0.30)**	(0.35)
Tier 1 capital – unrestricted	**1.54**	1.45
Tier 1 capital – restricted	**0.38**	0.37
Tier 1 capital	**1.92**	1.82
Tier 2 capital – subordinated debt	**0.53**	0.26
Tier 3 capital – deferred tax	**0.11**	0.09
Total own funds	**2.56**	2.17

Leverage

The Group's financial leverage increased by 5.6 percentage points to 24.2% (2019: 18.6%). The increase was primarily due to the issue of £260 million of Tier 2 subordinated debt in June 2020.

At 31 December	**2020 £m**	2019 £m
Shareholders' equity	**2,699.7**	2,643.6
Tier 1 notes	**346.5**	346.5
Financial debt – subordinated debt	**516.6**	259.0
Total capital employed	**3,562.8**	3,249.1
Financial-leverage ratio[1]	**24.2%**	18.6%

Notes:

1. Total IFRS financial debt and Tier 1 notes as a percentage of total IFRS capital employed.

Credit ratings

Moody's Investors Service provide insurance financial-strength ratings for U K Insurance Limited, the Group's principal underwriter. Moody's rate U K Insurance Limited as 'A1' for insurance financial strength (strong) with a stable outlook.

Reserving

The Group makes provision for the full cost of outstanding claims from its general insurance business at the balance sheet date, including claims estimated to have been incurred but not yet reported at that date and associated claims handling costs. The Group considers the class of business, the length of time to notify a claim, the validity of the claim against a policy, and the claim value. Claims reserves could settle across a range of outcomes, and settlement certainty increases over time. However, for bodily injury claims the uncertainty is greater due to the length of time taken to settle these claims. The possibility of annuity payments for injured parties also increases this uncertainty.

The Group seeks to adopt a conservative approach to assessing liabilities, as evidenced by the favourable development of historical claims reserves. Reserves are based on management's best estimate, which includes a prudence margin that exceeds the internal actuarial best estimate. This margin is set by reference to various actuarial scenario assessments and reserve distribution percentiles. It also considers other short and long-term risks not reflected in the actuarial inputs, as well as management's view on the uncertainties in relation to the actuarial best estimate.

The most common method of settling bodily injury claims is by a lump sum. When this includes an element of indemnity for recurring costs, such as loss of earnings or ongoing medical care, the settlement calculations apply the statutory discount rate (known as the Ogden discount rate) to reflect the fact that payment is made on a one-off basis rather than periodically over time. The current Ogden discount rate is minus 0.25% for England and Wales, minus 0.75% in Scotland, and 2.5% in Northern Ireland.

The Group reserves its large bodily injury claims at the relevant discount rate for each jurisdiction, with the overwhelming majority now reserved at minus 0.25% as most will be settled under the law of England and Wales. The Ogden discount rate will be reviewed again at the latest in 2024. There has been an ongoing reduction in large bodily injury exposures as a result of continued positive prior-year development of claims reserves, and a higher proportion of reserves being covered by reinsurance as a result of the decision to opt for a lower reinsurance attachment point from 2014 onwards.

If the claimant prefers, large bodily injury claims can be settled using a PPO. This is an alternative way to provide an indemnity for recurring costs, making regular payments, usually for the rest of the claimant's life. These claims are reserved for using an internal discount rate, which is progressively unwound over time. As it is likely to take time to establish whether a claimant will prefer a PPO or a lump sum, until a settlement method is agreed the Group makes assumptions about the likelihood that claimants will opt for a PPO. This is known as the PPO propensity.

The Covid-19 pandemic has led to the largest shock to the UK economy on record and the outlook remains unusually uncertain at year end 2020. Much depends on the evolution of the pandemic and measures taken to protect public health, as well as the transition to the new trading arrangements between the EU and the UK. In addition to concerns about

general indicators of economic health, such as falls in gross domestic product ("**GDP**"), rising unemployment and rising public sector debt ratios, the Group's reserves are exposed to the risk of changes in claims development patterns and claims inflation resulting from the pandemic. Changes in claims frequency present greater uncertainty for the unearned part of the business, whereas uncertainty over the level of claims severity has a greater impact on the earned claims reserves. Claims severity risk is particularly acute with respect to care costs for large bodily injury claims and car repair costs due to potential supply chain interruptions. The Group has therefore developed additional claims inflation scenarios, which look at 100 basis point changes in the claims inflation assumed in the actuarial best estimate over the next two years and these can be found in the table below.

The Group's prior-year reserve releases were £173.8 million (2019: £294.5 million) with good experience in large bodily injury claims being a key contributor.

Looking forward, the Group expects to continue setting its initial management best estimate with an appropriate degree of conservatism. Assuming current claims trends continue, the contribution from prior-year reserve releases is expected to remain significant.

Claims reserves net of reinsurance

At 31 December	**2020** **£m**	2019 £m
Motor	**1,678.9**	1,799.1
Home	**289.5**	266.3
Rescue and other personal lines	**104.8**	88.5
Commercial	**518.5**	516.1
Total	**2,591.7**	2,670.0

Sensitivity analysis – the discount rate used in relation to PPOs, changes in the assumed Ogden discount rate and claims inflation

The table below provides a sensitivity analysis of the potential net impact of a change in a single factor (the internal discount rate used for PPOs, the Ogden discount rate or claims inflation) with all other assumptions left unchanged. Other potential risks beyond the ones described could have additional financial impacts on the Group.

	Increase / (decrease) in profit before tax[1,2]	
At 31 December	**2020** **£m**	2019 £m
PPOs[3]		
Impact of an increase in the discount rate used in the calculation of present values of 100 basis points	**45.9**	48.5
Impact of a decrease in the discount rate used in the calculation of present values of 100 basis points	**(62.7)**	(66.5)
Ogden discount rate[4]		
Impact of the Group reserving at a discount rate of 0.75% compared to minus 0.25% (2019: 0.75% compared to minus 0.25%)	**43.7**	53.3
Impact of the Group reserving at a discount rate of minus 1.25% compared to minus 0.25% (2019: minus 1.25% compared to minus 0.25%)	**(61.1)**	(75.0)
Claims inflation		
Impact of a decrease in claims inflation by 100 basis points for two consecutive years (new scenario in 2020)	**32.4**	–
Impact of an increase in claims inflation by 100 basis points for two consecutive years (new scenario in 2020)	**(32.2)**	–

Notes:

1. These sensitivities are net of reinsurance and exclude the impact of taxation.
2. These sensitivities reflect one-off impacts at 31 December and should not be interpreted as predictions.
3. The sensitivities relating to an increase or decrease in the real discount rate used for PPOs illustrate a movement in the time value of money from the assumed level of 0% for reserving. The PPO sensitivity has been calculated on the direct impact on the change in the real internal discount rate with all other factors remaining unchanged.
4. Ogden discount rate sensitivity has been calculated on the direct impact of a permanent change in the discount rate in England and Wales with all other factors remaining unchanged. The Group will consider the statutory discount rate when setting its reserves but not necessarily provide on this basis. This is intended to ensure that reserves are appropriate for current and potential future developments.

The PPO sensitivity above is calculated on the basis of a change in the internal discount rate used for the actuarial best estimate reserves as at 31 December 2020. It does not take into account any second order impacts such as changes in PPO propensity or reinsurance bad debt assumptions.

Tax Management

The Board recognises that the Group has an important responsibility to manage its tax position effectively. The Board has delegated day-to-day management of taxes to the Chief Financial Officer and oversight is provided by the Audit Committee.

These arrangements are intended to ensure that the Group: complies with applicable laws and regulations; meets its obligations as a contributor and a collector of taxes on behalf of the tax authorities; and manages its tax affairs efficiently, claiming reliefs and other incentives where appropriate.

Tax authorities

The Group has open and cooperative relationships with the tax authorities with whom it deals in the countries where the Group operates, namely the UK, the Republic of Ireland, South Africa and India.

Tax policy and governance

The Group's tax policy has been reviewed and approved by the Audit Committee. The Group Tax function supports the Chief Financial Officer in ensuring the policy is adhered to at an operational level.

For more information please see our published Group Tax policy on the Group's website at https://www.directlinegroup.co.uk/en/who-we-are/governance/other-policies.html.

Total tax contribution

The Group's direct and indirect tax contribution to the UK Exchequer is significantly higher than the UK corporation tax that the Group pays on its profits. The Group collects taxes relating to employees and customers on behalf of the UK Exchequer and other national governments. It also incurs a significant amount of irrecoverable value added tax relating to overheads and claims. Taxes borne and collected in other tax jurisdictions have not been included in this note as the amounts are minimal in the context of the wider UK Group.

During 2020 the sum of taxes either paid or collected across the Group was £888.0 million. The composition of this between the various taxes borne and collected by the Group is shown below.

Total taxes borne

At 31 December	2020 £m
Current-year corporation tax charge	**95.2**
Irrecoverable value added tax incurred on overheads	**79.1**
Irrecoverable value added tax embedded within claims spend	**158.6**
Employer's national insurance contributions	**39.8**
Other taxes	**9.1**
Total	**381.8**

Total taxes collected

At 31 December	2020 £m
Insurance premium tax	**397.0**
Value added tax	**11.3**
Employee's pay as you earn and national insurance contributions	**97.9**
Total	**506.2**

Principal risks and uncertainties

We carefully assess the principal risks facing us. Principal risks are defined as having a residual risk impact of £40 million or more on a 1-in-200 years basis, taking into account customer, financial and reputational impacts.

Principal risks	Risk commentary
Insurance risk is the risk of loss due to fluctuations in the timings, amount, frequency and severity of an insured event relative to the expectations at the time of underwriting.	Key drivers of the outlook for Insurance risk across our business plan include reserve, underwriting, distribution, pricing and reinsurance risks. Issues relating to Covid-19 have been a key area of focus for the Group in 2020 and a main driver of the increasing trend in insurance risk. Claims trends have been significantly impacted particularly during the lockdown period. This has led to uncertainty in claims reserving and pricing. In 2021 and beyond, Covid-19, Brexit and potential recession may have an impact on claims inflation together with market and customer behaviour. We continue to monitor this closely. In response to this uncertainty we have used stress testing to understand the potential impacts of an economic downturn on frequency and severity of claims costs. Finally, climate change presents a risk of more frequent extreme events and key risk indicators are being continually enhanced to monitor related risks across Home, Motor and Commercial.
Market risk is the risk of loss resulting from fluctuations in the level and in the volatility of market prices of assets, liabilities and financial instruments.	Key drivers of market risk are the sensitivity of the values of our assets and investments to changes in credit spreads, and our exposure to losses as a result of changes in interest rate term structure or volatility. Concerns about the Covid-19 pandemic and Brexit fallout could impact equity and credit markets within the global economy leading to credit spread increases, foreign exchange rate volatility, interest rate changes and devaluation of UK property assets. To address this, we have an investment strategy which is approved by the Board and includes limiting exposure to individual asset classes and the number of illiquid investments we hold. We also use risk reduction techniques such as hedging foreign currency exposures with forward contracts.
Operational risk is the risk of loss due to inadequate or failed internal processes or systems, human error or from external events. The key risks within this category are Cyber, Technology & Infrastructure, Operational Resilience, Change, People, Information Management, Outsourcing, Partnerships and Fraud.	Operational risks can arise within all areas of the business and can manifest themselves through inadequate or failed internal processes or systems, human error or from external events. Our approach is proactively to manage our operational risks to mitigate potential customer harm, regulatory or legal censure, financial and reputational impacts. The decreasing trend in Operational risk is driven mainly by the good progress made by the business in delivering technology improvements, We have in place operational processes and systems, including prevention and detection measures. These include processes which seek to ensure we can absorb and/or adapt to internal or external events that could impact customer operations and the wider business. With the majority of staff now working from home, we continue to work to improve the performance of our IT systems, focusing on improving both system stability and capability. With significant strategic investment we continue actively to strengthen our change implementation controls to further mitigate potential impacts from risk events. We continue to deliver sustainable improvements to the overall security control environment, designed to enable us to respond to malicious and unintended threats from both internal and external entities. Processes are also in place to automate controls to enhance risk monitoring. We operate a strong control environment through the delivery of the Procurement & Supply Chain target operating model, which is focused on delivering active monitoring and management of key suppliers. Our risk management framework is designed to enable us to capture risk information in a complete and consistent way, enabling proactive trend analysis, root cause analysis and read across to facilitate early warnings and a 'learning' risk environment.

Principal risks	Risk commentary
Regulatory and compliance risk describes the risks leading to reputational damage, regulatory or legal censure, fines or prosecutions and other types of non-budgeted operational risk losses associated with the Group's conduct and activities.	We maintain a constructive and open relationship with our regulators and have a strong culture of delivering on our commitments to our customers. Pricing practices within the general insurance market is a key area of focus for the FCA and for the Group. We continue to devote a lot of attention to this area as we prepare for the implementation of the FCA's pricing practices remedies, expected in Q2 2021. Our existing conduct risk management framework is designed to deliver fair outcomes to customers and minimise our risk exposure. The framework is supported by a set of conduct pricing principles designed to enable the fair pricing of business across our book. We continue to develop our approach to anticipate regulatory developments and to ensure that we can continue to provide good outcomes for our customers. We carry out planned risk-based monitoring of customer processes as well as more targeted thematic reviews to help us manage the risk of unfair customer outcomes. We have maintained regular and open dialogue with both the FCA and PRA on our responses to Covid-19, outlining actions taken with the aim of ensuring that good customer outcomes are achieved and that the Group remains financially and operationally resilient. We have worked closely with UK regulators on our Brexit preparations, and with the Central Bank of Ireland to establish an Irish Branch in preparation for the end of the Brexit transition period. Finally, we have put in place a strong governance and accountability framework as part of the Senior Managers and Certification Regime, and carry out an annual declaration process to ensure the ongoing fitness and propriety of the Group's Senior Managers and Certified Functions.
Credit risk is the risk of loss resulting from default in obligations due from and/or changes in the credit standing of issuers of securities, counterparties or any debtors to which the Group is exposed.	To manage credit risk, we set credit limits for each counterparty and actively monitor credit exposures. In addition, we only purchase reinsurance from reinsurers with at least an A- rating and, for liabilities with a relatively long period of time to settlement, this rating is at least A+. Finally, we also have well defined criteria to determine which customers are offered and granted credit.
Strategic risk is the risk of direct or indirect adverse effects resulting from strategies not being optimally chosen, implemented or adapted to changing conditions.	Strategic risk is influenced by internal and external developments such as the Covid-19 pandemic, Brexit and the FCA's Pricing Practices Review. In addition, the adoption of Agile ways of working is designed to allow the business to more quickly identify and react to risks to the implementation of the Group's strategic goals. To manage our risks, we have taken the following steps: — we agree, monitor and manage performance against the Board-approved plan and targets; — the Board leads an annual strategy and five-year planning process which considers our performance, competitor positioning and strategic opportunities; — as part of the timetable for the Strategic Plan, the Risk Function carries out a risk review of the Plan which is documented in the Group's Own Risk and Solvency Assessment and presented to the Board; and — we identify and manage emerging risks using established governance processes and forums.

Proactive risk management through the Covid-19 pandemic

The Covid-19 pandemic created an unprecedented set of circumstances in the UK, as the country moved to national lockdowns. To minimise transmission of the Covid-19 virus, people across the UK were asked to remain at home, including working from home where possible and restricting any travel.

For the Group, the Covid-19 pandemic presented a series of challenges in seeking to protect its people, maintain customer operations, and safeguard the business.

In responding to the pandemic, management demonstrated strong proactive leadership, took accountability and showed a clear understanding of risk as they transitioned the business to a home working model. We transitioned our people to working from home prior to the national lockdown being called, while maintaining service continuity for our customers.

Throughout the pandemic, the Risk Function worked closely with business areas to perform key risk and control assessments to inform decision making, including assessments of risks introduced through mass homeworking, which enabled us to take mitigating action where necessary. The results of this exercise informed management of our critical supply chain.

Collaboration took place across the business to manage other Group responses to the pandemic, such as: the management of the surge in customer claims related to Travel; the assessment of additional scenarios relating to operational resilience; and documenting how the pandemic may evolve, in order to identify and mitigate risk.

Throughout this challenging period, business functions have continued to work together proactively to ensure that our customers receive appropriate levels of service and support, whilst still delivering business performance.

UK recession and global financial instability

The risk of a further UK-wide recession and global financial instability is ongoing. The economic uncertainty is expected to remain high throughout H1 2021, as a result of the Covid-19 pandemic, and the Group continues to monitor the worst-case impact.

As a result of the Covid-19 pandemic, the UK Government has acted to support UK employees and prevent lasting damage to the economy. However, the uncertainty surrounding the pandemic makes the overall impact and recovery progress unclear. The disruption to global trade and supply-chains caused by the pandemic could increase the risk of inflation in the long-term.

For the Group, the investment portfolio is positioned relatively defensively; however, if the UK recession were to worsen significantly, additional steps could be taken such as further shifting the portfolio towards 'defensive' sectors or increasing more allocation to cash.

Globally, the economic shock caused by the Covid-19 pandemic initially resulted in credit spreads in Europe and the US moving to levels last seen in the 2008/09 credit crisis, and equity markets posted extremely steep percentage falls. Whilst markets have recovered to a degree, there still remains uncertainty over the duration and continued impact of the pandemic.

The Group portfolio contains a proportion of short-maturity bonds which could be sold relatively quickly if necessary. Recent stress and scenario testing has highlighted that the largest impacts would be on the Group's asset portfolio. The Group believes that the risks from global financial instability are being appropriately monitored.

Potential effects of Brexit

The Brexit transition period following the UK leaving the EU ended at 11pm on 31 December 2020. A trade and co-operation agreement had been agreed, tariffs on goods entering the UK from the EU were avoided and the more severe risks identified in connection with a so-called 'no-deal' Brexit have not materialised.

Key risks identified as potentially arising in the context of disruption following the end to the transition period included financial impacts (for example, if credit spreads widened) and operational impacts (for example, if goods were delayed at the EU/UK border). Other risks identified included risks of changes to the value of sterling, inflation, recession, recruitment and retention of people, impacts on travel, and potential changes to tax and regulation.

Some of these risks could still occur to some degree and we continue to monitor developments.

The Group has a small amount of business in the Republic of Ireland, servicing a small Irish part of a UK partner's wider business. Accordingly, following approval from the Central Bank of Ireland the Group established an Irish branch in the Republic of Ireland with effect from the end of the transition period.

Emerging risks

Emerging risks are defined in the Group as newly developing risks that are often difficult to quantify but may materially affect the Group. Emerging risks are usually highly uncertain risks which are external to the Group. The Group has in place an emerging risks process which enables it to:

— have a proactive approach to emerging risk management;

— identify, manage and monitor a broad range of potential emerging risks; and

— mitigate the impact of emerging risks which could impact the delivery of the Plan.

The Group records emerging risks within an Emerging Risk Register. An update on emerging risk is presented to the Board Risk Committee annually and is supplemented by deep dives into selected emerging risks. During 2020, the Group Risk Function worked with first line of defence subject matter experts to enhance the quality and detail of emerging risk updates.

The Covid-19 pandemic was not included within the Emerging Risk Register as an Emerging Risk, as it has emerged and is impacting and is reflected in our current Group risk profile. However, 'Global Pandemic' remains on the Emerging Risk Watchlist for monitoring, which focuses on the potential for a similar type of outbreak in years to come. Many of the lessons from the Covid-19 situation can be applied to how the Group would respond to another global pandemic.

The Covid-19 pandemic continues to challenge the way the industry operates, both now and in the future. Second line of defence and first line of defence subject matter experts continue to monitor potential threats and opportunities which may impact the Group and the wider industry, as the 'new normal' becomes clearer.

Key emerging risks are outlined below:

Climate change

The Group recognises that climate change potentially poses material long-term financial risks to the business and is receiving increased scrutiny from regulators and investors. Climate change risks can be divided into three categories: physical, transition and liability risks. All three of these categories can manifest themselves through a range of existing risks within the material risk register, including insurance, market, operational, strategic and reputational risks.

Following the issue of the PRA's Supervisory Statement SS3/19, the Group has appointed the Chief Risk Officer as the Senior Management Function holder for Climate Change and put an initial plan in place to address the expectations set out in the supervisory statement.

The Group has updated risk policies and minimum standards explicitly to reference the risks from climate change, and we reviewed climate-related key performance indicators for energy usage and emissions across the business throughout H2 2020, to help inform future climate-related financial disclosures.

The risks and impacts of climate change are wide ranging; the Group is focusing increasingly on climate change, with related risk management activity which includes monitoring climate change through the Emerging Risk process, forming a Climate Change working group and continuing its journey to implement the recommendations of the Financial Stability Board's Taskforce on Climate-related Financial Disclosures (TCFD).

As part of embedding the management of these climate-related financial risks in 2021, the Group will take part in the Bank of England's Climate Biennial Exploratory Scenarios exercise. This stress testing exercise aims to understand the impact on the Group of future climate scenarios incorporating physical and transition risks.

Ethical use of data

The Group identified the 'failure to establish an ethical way to use data' as an Emerging Risk in H2 2019, with activity underway to mitigate against associated risks. The industry and policymakers' view of this risk is still emerging, as legislation and regulation in this area is yet to mature; however, it is a growing area of focus for the Group's regulators and for the Group itself.

A group of stakeholders including the Chief Data Officer and the Privacy & Information Management team has been established to provide visibility of the challenge for the Group, and a working group has been established to gather external views and create visibility for the required timelines, and to provide the focus required to move development of a data ethics framework at an appropriate pace.

The Group has been outlining a proposed approach for the management and governance of data ethics. Work will continue in 2021 to confirm and embed the proposed principles-based approach. In addition, we have commenced work to determine how the Group could best incorporate emerging data ethics considerations into current customer conduct processes and fora.

CONSOLIDATED INCOME STATEMENT

For the year ended 31 December 2020

	Notes	**2020 £m**	2019 £m
Gross earned premium		**3,189.3**	3,202.6
Reinsurance premium		**(228.8)**	(217.7)
Net earned premium	4	**2,960.5**	2,984.9
Investment return	5	**95.1**	134.6
Instalment income		**109.3**	114.0
Other operating income	6	**49.9**	66.2
Total income		**3,214.8**	3,299.7
Insurance claims		**(1,730.4)**	(1,917.3)
Insurance claims recoverable from reinsurers		**16.8**	69.7
Net insurance claims	7	**(1,713.6)**	(1,847.6)
Commission expenses	8	**(254.7)**	(211.5)
Operating expenses (including restructuring and one-off costs)	9	**(763.8)**	(704.9)
Total expenses		**(1,018.5)**	(916.4)
Finance costs	10	**(31.3)**	(26.0)
Profit before tax		**451.4**	509.7
Tax charge		**(84.2)**	(89.8)
Profit for the year attributable to owners of the Company		**367.2**	419.9
Earnings per share:			
Basic (pence)	12	**25.8**	29.5
Diluted (pence)	12	**25.5**	29.2

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2020

	2020 £m	2019 £m
Profit for the year attributable to the owners of the Company	**367.2**	419.9
Other comprehensive income		
Items that will not be reclassified subsequently to the income statement:		
Actuarial loss on defined benefit pension scheme	**(0.4)**	(7.3)
Tax relating to item that will not be reclassified	**0.3**	1.3
	(0.1)	(6.0)
Items that may be reclassified subsequently to the income statement:		
Cash flow hedges	**(0.1)**	(0.7)
Fair value gain on AFS investments	**47.4**	118.1
Less: net gains on AFS investments transferred to income statement on disposals	**(1.1)**	(16.5)
Tax relating to items that may be reclassified	**(9.9)**	(17.3)
	36.3	83.6
Other comprehensive income for the year net of tax	**36.2**	77.6
Total comprehensive income for the year attributable to owners of the Company	**403.4**	497.5

CONSOLIDATED BALANCE SHEET

As at 31 December 2020

	Note	2020 £m	2019 £m
Assets			
Goodwill and other intangible assets		**786.8**	702.5
Property, plant and equipment		**146.1**	143.4
Right-of-use assets		**137.8**	149.2
Investment property		**292.1**	291.7
Reinsurance assets	14	**1,129.2**	1,251.3
Deferred acquisition costs		**172.2**	176.2
Insurance and other receivables		**848.2**	846.5
Prepayments, accrued income and other assets		**126.0**	120.2
Derivative financial instruments		**73.4**	121.5
Retirement benefit asset		**9.0**	9.7
Financial investments	15	**4,681.4**	4,673.4
Cash and cash equivalents	16	**1,220.1**	948.6
Total assets		**9,622.3**	9,434.2
Equity			
Shareholders' equity		**2,699.7**	2,643.6
Tier 1 notes	18	**346.5**	346.5
Total equity		**3,046.2**	2,990.1
Liabilities			
Subordinated liabilities	19	**516.6**	259.0
Insurance liabilities	20	**3,617.0**	3,819.6
Unearned premium reserve	21	**1,497.1**	1,506.0
Borrowings	16	**51.9**	52.3
Derivative financial instruments		**57.2**	30.5
Provisions		**114.8**	74.3
Trade and other payables, including insurance payables		**549.9**	478.1
Lease liabilities		**152.4**	164.4
Deferred tax liabilities		**8.7**	9.6
Current tax liabilities		**10.5**	50.3
Total liabilities		**6,576.1**	6,444.1
Total equity and liabilities		**9,622.3**	9,434.2

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2020

	Share capital (note 17) £m	Employee trust shares £m	Capital reserves £m	AFS revaluation reserve £m	Foreign exchange translation reserve £m	Retained earnings £m	Share-holders' equity £m	Tier 1 notes (note 18) £m	Total equity £m
Balance at 1 January 2019	150.0	(35.2)	1,450.0	(36.8)	0.8	1,029.4	2,558.2	346.5	2,904.7
Profit for the year	–	–	–	–	–	419.9	419.9	–	419.9
Other comprehensive income	–	–	–	84.3	(0.7)	(6.0)	77.6	–	77.6
Dividends and appropriations paid (note 11)	–	–	–	–	–	(420.7)	(420.7)	–	(420.7)
Shares acquired by employee trusts	–	(10.4)	–	–	–	–	(10.4)	–	(10.4)
Credit to equity for equity-settled share-based payments	–	–	–	–	–	18.4	18.4	–	18.4
Shares distributed by employee trusts	–	15.4	–	–	–	(15.4)	–	–	–
Tax on share-based payments	–	–	–	–	–	0.6	0.6	–	0.6
Balance at 31 December 2019	150.0	(30.2)	1,450.0	47.5	0.1	1,026.2	2,643.6	346.5	2,990.1
Profit for the year	**–**	**–**	**–**	**–**	**–**	**367.2**	**367.2**	**–**	**367.2**
Other comprehensive income	**–**	**–**	**–**	**36.4**	**(0.1)**	**(0.1)**	**36.2**	**–**	**36.2**
Dividends and appropriations paid (note 11)	**–**	**–**	**–**	**–**	**–**	**(312.5)**	**(312.5)**	**–**	**(312.5)**
Shares acquired by employee trusts	**–**	**(23.8)**	**–**	**–**	**–**	**–**	**(23.8)**	**–**	**(23.8)**
Share redemption	**(1.1)**	**–**	**1.1**	**–**	**–**	**–**	**–**	**–**	**–**
Shares cancelled following buyback	**–**	**–**	**–**	**–**	**–**	**(30.0)**	**(30.0)**	**–**	**(30.0)**
Credit to equity for equity-settled share-based payments	**–**	**–**	**–**	**–**	**–**	**18.5**	**18.5**	**–**	**18.5**
Shares distributed by employee trusts	**–**	**13.7**	**–**	**–**	**–**	**(13.7)**	**–**	**–**	**–**
Tax on share-based payments	**–**	**–**	**–**	**–**	**–**	**0.5**	**0.5**	**–**	**0.5**
Balance at 31 December 2020	**148.9**	**(40.3)**	**1,451.1**	**83.9**	**–**	**1,056.1**	**2,699.7**	**346.5**	**3,046.2**

CONSOLIDATED CASH FLOW STATEMENT

For the year ended 31 December 2020

	Notes	2020 £m	2019 £m
Net cash generated from operating activities before investment of insurance assets		**268.8**	88.2
Cash generated from investment of insurance assets		**315.9**	373.9
Net cash generated from operating activities		**584.7**	462.1
Cash flows used in investing activities			
Purchases of goodwill and other intangible assets		**(140.7)**	(175.7)
Purchases of property, plant and equipment		**(20.1)**	(11.9)
Net cash flows from acquisition of subsidiaries		**(0.2)**	—
Net cash used in investing activities		**(161.0)**	(187.6)
Cash flows used in financing activities			
Dividends and appropriations paid	11	**(312.5)**	(420.7)
Finance costs (including lease interest)		**(30.2)**	(26.4)
Principal element of lease payments		**(12.5)**	(13.1)
Purchase of employee trust shares		**(23.8)**	(10.4)
Proceeds on issue of subordinated Tier 2 notes		**257.2**	—
Shares purchased in buyback		**(30.0)**	—
Net cash used in financing activities		**(151.8)**	(470.6)
Net increase / (decrease) in cash and cash equivalents		**271.9**	(196.1)
Cash and cash equivalents at the beginning of the year	16	**896.3**	1,092.4
Cash and cash equivalents at the end of the year	16	**1,168.2**	896.3

1. Accounting policies

Basis of preparation

The financial information included in this preliminary announcement has been prepared in accordance with the recognition and measurement criteria of International Financial Reporting Standards ("**IFRS**") as endorsed by the EU on 31 December 2020 and by the UK's Government Department of Business, Energy and Industrial Strategy ("**BEIS**") in 2021. The BEIS has been given the power of endorsing and adopting international accounting standards while the UK Endorsement Board ("**UKEB**") is still being established. However, this announcement does not itself contain sufficient information to comply with IFRS. The financial information set out in this preliminary results announcement does not constitute the statutory accounts for the year ended 31 December 2020. The financial information is derived from the statutory accounts, which comply with IFRS, within the Group's Annual Report & Accounts 2020. These accounts were signed on 5 March 2021 and are expected to be published in March 2021 and delivered to the Registrar of Companies following the Annual General Meeting to be held on 13 May 2021. The independent Auditor's report on the Group accounts for the year ended 31 December 2020 was signed on 5 March 2021, is unqualified, does not draw attention to any matters by way of emphasis and does not include a statement under S498(2) or (3) of the Companies Act 2006. This audit opinion excludes disclosures surrounding capital adequacy calculated under the Solvency II regime as these are outside of the audit scope.

Going concern

The Group has sufficient financial resources to meet its financial needs, including managing a mature portfolio of insurance risk. The Directors believe the Group is well positioned to manage its business risks successfully in the current economic climate. The Finance review on pages 11 to 23 describes the Group's capital management strategy, including the capital actions taken in the year to ensure the continued strength of the balance sheet. The Group's financial position is also covered in that section, including a commentary on cash and investment levels, reserves, currency management, insurance liability management, liquidity and borrowings. Additionally, note 3 to the consolidated financial statements in the Group's Annual Report and Accounts 2020 describes capital management needs and policies. The note also covers insurance, market, liquidity and credit risks which may affect the Group's financial position.

The Directors have assessed the principal risks of the Group over the duration of the planning cycle. These included the implementation of the FCA's Pricing Practices Review, possible adverse implications of Brexit, change risk and possible challenging market conditions due to the impact of Covid-19 on the economy and customer behaviour. The 2020 Plan modelled a number of different scenarios which were directly and indirectly influenced by the Covid-19 pandemic. These included delay to improvements in technological capability, the impact of Covid-19 on claims frequency levels and the impact of Brexit on the investment return. The key judgements applied were in relation to the likely time period of Covid-19 related restrictions, and the subsequent impact on customer behaviour and the economic recovery.

In addition, the Group's Risk Function has carried out an assessment of the risks to the Plan and the dependencies for the success of the Strategic Plan. This included running stress tests on the Plan to consider the 1 in 8 years and 1 in 25 years loss simulations based on the internal economic capital model.

A reverse stress test was also performed to identify the most probable combination of stresses that would result in capital loss and thus threaten the viability of the Group, i.e. a reduction of own funds to below the solvency capital requirement.

In all scenarios, it was concluded that the Group's solvency capital requirement would not be breached following the implementation of management actions.

Therefore, having made due enquiries, the Directors reasonably expect that the Group has adequate resources to continue in operational existence for at least 12 months from 5 March 2021 (the date of approval of the financial statements). Accordingly, the Directors have adopted the going concern basis in preparing the financial statements.

Adoption of new and revised standards

The Group has adopted the following new amendments to IFRSs and International Accounting Standards ("IASs") that became mandatorily effective for the Group for the first time during 2020. None of these amendments require changes to existing accounting policies. Amendment to IFRS 16 'Leases Covid-19 – Related Rent Concessions' permits lessees, as a practical expedient, not to assess whether particular rent concessions occurring as a direct consequence of the Covid-19 pandemic are lease modifications and instead to account for those rent concessions as if they are not lease modifications. 'Amendments to References to the Conceptual Framework in IFRS Standards' amends some references to previous versions of the Conceptual Framework in IFRS Standards and their accompanying documents and IFRS Practice Statements. Amendments to IFRS 3 'Business Combinations' narrows and clarifies the definition of a business. They also permit a simplified assessment of whether an acquired set of activities and assets is a group of assets rather than a business. Amendments to IAS 1 and IAS 8: 'Definition of Material' clarifies and aligns the definition of 'material' and provides guidance to help improve consistency in the application of that concept whenever it is used in IFRS Standards. The Group adopted 'Interest Rate Benchmark Reform – Amendments to IFRS 9, IAS 39 and IFRS 7 with an effective date of 1 January 2020 in 2019.

Accounting developments

New IFRS standards and amendments that are issued, but not yet effective for the 31 December 2020 reporting period and have not been early adopted by the Group are disclosed below. The Group intends to adopt these standards, if applicable, when they become effective, except for Amendments to IFRS 9 'Financial Instruments', as explained below.

In July 2014, the IASB issued the final version of IFRS 9 'Financial Instruments' which replaced IAS 39 'Financial Instruments: Recognition and Measurement' and all previous versions of IFRS 9; it was endorsed by the EU in 2016. IFRS 9 addresses the classification, measurement and derecognition of financial assets and financial liabilities, introduces new rules for hedge accounting and a new impairment model for financial assets; it is effective for annual periods beginning on or after 1 January 2018, however adoption by the Group has been deferred as described below.

Accounting developments continued

In September 2016, the IASB issued 'Amendments to IFRS 4: Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts' to address issues arising from the different effective dates of IFRS 9 and IFRS 17 'Insurance Contracts'. Amendments to IFRS 4 was endorsed by the EU in November 2017.

The Group conducted a high-level assessment of the three aspects of IFRS 9 and based on current information, the impact of applying the expected loss model for the first time is currently immaterial. The Group does not expect any other significant impact on its financial statements. The Group satisfies the exemption criteria within Amendments to IFRS 4. As the International Accounting Standards Board has now deferred the effective date of IFRS 17 to 1 January 2023, in June 2020 'Amendments to IFRS 4 - deferral of IFRS 9' was issued which also defers the effective date for the implementation of IFRS 9 so as to remain in line with IFRS 17. These amendments were endorsed by the EU in December 2020 and the UK's BEIS in January 2021. The Group will continue applying the temporary exemption from applying IFRS 9 as introduced by Amendments to IFRS 4 'Insurance Contracts'.

IFRS 17 was issued by the IASB in May 2017 to replace IFRS 4. IFRS 17 is currently effective for reporting periods beginning on or after 1 January 2023. Comparative figures are required. IFRS 17 is a comprehensive new accounting standard for all insurance contracts covering recognition and measurement, presentation and disclosure. The overall objective of IFRS 17 is to provide an accounting model for insurance contracts that is more useful and consistent for insurers and to replace the requirements of IFRS 4 that allowed insurers to apply grandfathering of previous local accounting policies.

The core of IFRS 17 is the general model, supplemented by an optional simplified premium allocation approach which is permitted for the liability for the remaining coverage for short duration contracts. The general model measures insurance contracts using the building blocks of: discounted probability weighted cash flows; an explicit risk adjustment; and a contractual service margin representing the unearned profit of the contract which is recognised as revenue over the coverage period.

An initial assessment of the impact of IFRS 17 on the Group's financial statements has been completed and work has now started on the design and build of the systems that will provide the foundation for reporting under IFRS 17 from 1 January 2023. The Group expects to be able to apply the simplified premium allocation approach to all material insurance and reinsurance contract groups. As the standard was not endorsed by the EU before 31 December 2020, it will instead require endorsement by the UKEB.

2. Critical accounting judgements and key sources of estimation uncertainty

Full details of critical accounting judgements and key sources of estimation uncertainty used in applying the Group's accounting policies are outlined on pages 167 to 168 of the Annual Reports & Accounts 2019. There have been no significant changes to the principles or assumptions of these critical accounting judgements and key sources of estimation uncertainty during the year ended 31 December 2020 except that an estimation uncertainty for the fair value of investment properties has been included this year. This is because the valuation in the financial statements is based on valuations by independent registered valuers and the techniques used include some unobservable inputs. The value of investment properties in the Group's balance sheet at 31 December 2020 is £292.1 million (31 December 2019: £291.7 million). In addition, disclosure of the Group's "General insurance: outstanding claims provisions and related reinsurance recoveries" estimate has been updated as the Group's reserves are exposed to the risk of changes in claims development patterns and claims inflation resulting from the Covid-19 pandemic. The Group has therefore developed additional claims inflation scenarios, which look at 100 basis point changes in the claims inflation assumed in the actuarial best estimate over the next two years. The outcome of this sensitivity analysis is included on page 22.

3. Segmental analysis

The table below analyses the Group's revenue and results by reportable segment for the year ended 31 December 2020.

	Motor £m	Home £m	Rescue and other personal lines £m	Commercial £m	**Total Group £m**
Gross written premium	1,616.9	577.9	417.8	567.8	**3,180.4**
Gross earned premium	1,635.3	581.9	425.6	546.5	**3,189.3**
Reinsurance premium	(150.5)	(26.1)	(2.7)	(49.5)	**(228.8)**
Net earned premium	1,484.8	555.8	422.9	497.0	**2,960.5**
Investment return	62.8	10.3	3.4	18.6	**95.1**
Instalment income	80.1	19.2	3.0	7.0	**109.3**
Other operating income	38.4	0.2	8.9	2.4	**49.9**
Total income	1,666.1	585.5	438.2	525.0	**3,214.8**
Insurance claims	(889.2)	(316.5)	(279.1)	(245.6)	**(1,730.4)**
Insurance claims recoverable from / (payable to) reinsurers	1.1	7.4	18.0	(9.7)	**16.8**
Net insurance claims	(888.1)	(309.1)	(261.1)	(255.3)	**(1,713.6)**
Commission expenses	(47.4)	(45.0)	(69.4)	(92.9)	**(254.7)**
Operating expenses before restructuring and one-off costs	(367.1)	(130.0)	(100.9)	(126.4)	**(724.4)**
Total expenses	(414.5)	(175.0)	(170.3)	(219.3)	**(979.1)**
Operating profit	**363.5**	**101.4**	**6.8**	**50.4**	**522.1**
Restructuring and one-off costs					**(39.4)**
Finance costs					**(31.3)**
Profit before tax					**451.4**

	Motor	Home	Rescue and other personal lines	Commercial	Total Group
Underwriting profit / (loss)	**182.2**	**71.7**	**(8.5)**	**22.4**	**267.8**
Loss ratio	59.8%	55.6%	61.7%	51.4%	**57.9%**
Commission ratio	3.2%	8.1%	16.4%	18.7%	**8.6%**
Expense ratio	24.7%	23.4%	23.9%	25.4%	**24.5%**
Combined operating ratio	**87.7%**	**87.1%**	**102.0%**	**95.5%**	**91.0%**

3. Segmental analysis continued

The table below analyses the Group's revenue and results by reportable segment for the year ended 31 December 2019.

	Motor £m	Home £m	Rescue and other personal lines £m	Commercial £m	Total Group £m
Gross written premium	1,651.6	586.6	436.0	528.9	3,203.1
Gross earned premium	1,653.2	598.8	427.4	523.2	3,202.6
Reinsurance premium	(145.5)	(25.2)	(2.2)	(44.8)	(217.7)
Net earned premium	1,507.7	573.6	425.2	478.4	2,984.9
Investment return	88.6	16.7	5.6	23.7	134.6
Instalment income	83.8	20.5	2.8	6.9	114.0
Other operating income	51.3	0.6	11.1	3.2	66.2
Total income	1,731.4	611.4	444.7	512.2	3,299.7
Insurance claims	(1,086.8)	(276.2)	(285.2)	(269.1)	(1,917.3)
Insurance claims recoverable from reinsurers	43.5	7.8	0.8	17.6	69.7
Net insurance claims	(1,043.3)	(268.4)	(284.4)	(251.5)	(1,847.6)
Commission expenses	(39.9)	(55.7)	(27.2)	(88.7)	(211.5)
Operating expenses before restructuring and one-off costs	(345.6)	(136.7)	(94.0)	(117.4)	(693.7)
Total expenses	(385.5)	(192.4)	(121.2)	(206.1)	(905.2)
Operating profit	302.6	150.6	39.1	54.6	546.9
Restructuring and one-off costs					(11.2)
Finance costs					(26.0)
Profit before tax					509.7

	Motor	Home	Rescue and other personal lines	Commercial	Total Group
Underwriting profit	78.9	112.8	19.6	20.8	232.1
Loss ratio	69.3%	46.8%	66.9%	52.7%	61.9%
Commission ratio	2.6%	9.7%	6.4%	18.5%	7.1%
Expense ratio	22.9%	23.8%	22.1%	24.5%	23.2%
Combined operating ratio	94.8%	80.3%	95.4%	95.7%	92.2%

4. Net earned premium

	2020 £m	2019 £m
Gross earned premium:		
Gross written premium	**3,180.4**	3,203.1
Movement in unearned premium reserve	**8.9**	(0.5)
	3,189.3	3,202.6
Reinsurance premium paid and payable:		
Premium payable	**(231.0)**	(215.9)
Movement in reinsurance unearned premium reserve	**2.2**	(1.8)
	(228.8)	(217.7)
Total	**2,960.5**	2,984.9

5. Investment return

	2020 £m	2019 £m
Investment income:		
Interest income from debt securities	**98.6**	108.4
Interest income from cash and cash equivalents	**2.5**	7.9
Interest income from infrastructure debt	**5.8**	7.0
Interest income from commercial real estate loans	**6.5**	6.9
Interest income	**113.4**	130.2
Rental income from investment property	**13.7**	16.2
	127.1	146.4
Net realised gains / (losses):		
AFS debt securities	**1.1**	16.5
Derivatives	**69.9**	(9.5)
Investment property	**–**	(0.7)
	71.0	6.3
Net unrealised losses:		
Impairment of loans and receivables	**(2.7)**	–
Derivatives	**(90.2)**	(12.6)
Investment property	**(10.1)**	(5.5)
	(103.0)	(18.1)
Total	**95.1**	134.6

The table below analyses the realised and unrealised gains and losses on derivative instruments included in investment return.

	Realised 2020 £m	Unrealised 2020 £m	Realised 2019 £m	Unrealised 2019 £m
Derivative gains / (losses):				
Foreign exchange forward contracts[1]	**57.4**	**(50.8)**	(56.8)	103.4
Associated foreign exchange risk	**28.1**	**(45.7)**	53.4	(123.8)
Net gains / (losses) on foreign exchange forward contracts	**85.5**	**(96.5)**	(3.4)	(20.4)
Interest rate swaps[1]	**(26.2)**	**(23.0)**	(16.8)	(33.6)
Associated interest rate risk on hedged items	**10.6**	**29.3**	10.7	41.4
Net (losses) / gains on interest rate derivatives	**(15.6)**	**6.3**	(6.1)	7.8
Total	**69.9**	**(90.2)**	(9.5)	(12.6)

Note:

1. All foreign exchange forward contracts and certain interest rate swaps are measured at fair value through profit and loss. There are also interest rate swaps designated as hedging instruments.

6. Other operating income

	2020 £m	2019 £m
Revenue from vehicle recovery and repair services	**24.0**	28.3
Vehicle replacement referral income	**12.2**	19.1
Legal services income	**8.8**	11.3
Other income[1]	**4.9**	7.5
Total	**49.9**	66.2

Note:

1. Other income mainly includes fee income from insurance intermediary services.

7. Net insurance claims

	Gross 2020 £m	Reinsurance 2020 £m	Net 2020 £m	Gross 2019 £m	Reinsurance 2019 £m	Net 2019 £m
Current accident year claims paid	**1,056.4**	**(18.1)**	**1,038.3**	1,232.9	(0.2)	1,232.7
Prior accident year claims paid	**876.6**	**(123.0)**	**753.6**	870.7	(25.1)	845.6
Decrease in insurance liabilities	**(202.6)**	**124.3**	**(78.3)**	(186.3)	(44.4)	(230.7)
Total	**1,730.4**	**(16.8)**	**1,713.6**	1,917.3	(69.7)	1,847.6

Claims handling expenses[1] for the year ended 31 December 2020 of £208.2 million (2019: £202.9 million) have been included in the claims figures above.

Note:

1. Includes costs in respect of low value leases of £0.8 million (2019: £0.3 million).

8. Commission expenses

	2020 £m	2019 £m
Commission expenses	**180.9**	171.2
Expenses incurred under profit participations	**73.8**	40.3
Total	**254.7**	211.5

9. Operating expenses

	2020 £m	2019 £m
Staff costs[1,2]	**270.3**	267.3
IT and other operating expenses[1,2,3]	**220.2**	163.4
Marketing	**106.6**	113.9
Insurance levies	**80.4**	81.5
Depreciation and amortisation[1,4,5]	**86.3**	78.8
Total operating expenses (including restructuring and one-off costs)	**763.8**	704.9
Of which restructuring and one-off costs	**39.4**	11.2
Total excluding restructuring and one-off costs	**724.4**	693.7

Notes:

1. Restructuring and one-off costs of £39.4 million (2019: £11.2 million) are included as follows: staff costs of £14.7 million (2019: £5.8 million), other operating expenses of £24.2 million (2019: £5.4 million) and depreciation of £0.5 million (2019: £nil).
2. Staff costs and other operating expenses attributable to claims handling activities are allocated to the cost of insurance claims.
3. IT and other operating expenses include professional fees and property costs.
4. For year ended 31 December 2020, depreciation and amortisation include a £6.6 million impairment charge (2019: £1.3 million), which relates to capitalised software development costs for ongoing IT projects primarily relating to development of new systems.
5. Includes depreciation on right-of-use assets of £14.8 million (2019: £14.2 million).

9. Operating expenses continued

The table below analyses the number of people employed by the Group's operations.

	At 31 December		Average for the year	
	2020	2019	**2020**	2019
Insurance operations	**8,022**	7,963	**8,010**	8,388
Repair centre operations	**1,441**	1,444	**1,454**	1,384
Support	**1,344**	1,355	**1,388**	1,350
Total	**10,807**	10,762	**10,852**	11,122

The aggregate remuneration of those employed by the Group's operations comprised:

	2020 £m	2019 £m
Wages and salaries	**393.5**	387.2
Social security costs	**43.6**	41.9
Pension costs	**26.2**	25.5
Share-based payments	**18.5**	18.4
Total	**481.8**	473.0

10. Finance costs

	2020 £m	2019 £m
Interest expense on subordinated liabilities[1]	**29.1**	23.1
Net interest received on interest rate swap[2]	**(4.1)**	(3.4)
Unrealised losses on interest rate swap[2]	**1.9**	—
Unrealised (gain) / loss on designated hedging instrument[2]	**(1.2)**	0.1
Unrealised loss / (gains) on associated interest rate risk on hedged item[2]	**0.9**	(0.8)
Amortisation of arrangement costs, discount on issue and fair value hedging adjustment of subordinated liabilities	**(1.3)**	0.3
Interest expense on lease liabilities	**6.0**	6.7
Total	**31.3**	26.0

Notes:

1. On 5 June 2020, the Group issued subordinated Tier 2 notes at a fixed rate of 4.0%.
2. As described in note 19, on 27 April 2012 the Group issued subordinated guaranteed dated Tier 2 notes with a nominal value of £500 million at a fixed rate of 9.25%. On the same date, the Group also entered into a 10-year interest rate swap to exchange the fixed rate of interest on the notes for a floating rate. This was treated as a hedging instrument. On 8 December 2017, the Group redeemed £250 million nominal value of the notes and the hedging agreement was redesignated accordingly. On 31 July 2020, the Group identified that the hedge no longer met the criteria of hedge effectiveness under IAS 39 and, under the rules of the standard, the accumulated hedging adjustment has begun to be amortised to the income statement from the date of the last successful hedge effectiveness test over the remaining life of the subordinated debt using an effective interest rate calculation.

11. Dividends and appropriations

	2020 £m	2019 £m
Amounts recognised as distributions to equity holders in the period:		
2020 interim dividend of 7.4 pence per share paid on 4 September 2020	**100.4**	—
2020 special interim dividend of 14.4 pence per share paid on 4 September 2020	**195.5**	—
2019 first interim dividend of 7.2 pence per share paid on 6 September 2019	**–**	98.6
2018 final dividend of 14.0 pence per share paid on 16 May 2019	**–**	191.8
2018 special dividend of 8.3 pence per share paid on 16 May 2019	**–**	113.7
	295.9	404.1
Coupon payments in respect of Tier 1 notes[1]	**16.6**	16.6
	312.5	420.7
Proposed dividends:		
2020 final dividend of 14.7 pence per share	**199.3**	—
2019 final dividend of 14.4 pence per share	**–**	198.0

Note:

1. Coupon payments on the Tier 1 notes issued in December 2017 are treated as an appropriation of retained profits and, accordingly, are accounted for when paid.

11. Dividends and appropriations continued

The proposed final dividends for 2020 have not been included as a liability in these financial statements.

The Board has also approved a share buyback of up to £100 million, with an initial tranche of up to £50 million expected to be completed by the time of the half-year results.

On 3 March 2020, the Group announced that the Board had approved a share buyback of up to £150 million. On 19 March 2020, the Board cancelled that share buyback programme given the uncertainty in the capital markets at the time, driven by the rapidly emerging Covid-19 pandemic.

Following the cancellation of the dividend as announced on 8 April 2020, the final dividend for 2019 was not paid. A special interim dividend of 14.4 pence per share reflecting a full catch-up of the cancelled 2019 final dividend was paid on 4 September 2020.

The trustees of the employee share trusts waived their entitlement to dividends on shares held to meet obligations arising on the Long-Term Incentive Plan, Deferred Annual Incentive Plan and Restrictive Share Plan awards, which reduced the total dividends paid for the year ended 31 December 2020 by £1.6 million (2019: £1.5 million).

12. Earnings per share

Earnings per share is calculated by dividing earnings attributable to the owners of the Company less coupon payments in respect of Tier 1 notes by the weighted average number of Ordinary Shares during the year.

Basic

Basic earnings per share is calculated by dividing the earnings attributable to the owners of the Company less coupon payments in respect of Tier 1 notes by the weighted average number of Ordinary Shares during the period, excluding Ordinary Shares held as employee trust shares.

	2020 **£m**	2019 £m
Earnings attributable to owners of the Company	**367.2**	419.9
Coupon payments in respect of Tier 1 notes	**(16.6)**	(16.6)
Profit for the calculation of earnings per share	**350.6**	403.3
Weighted average number of Ordinary Shares (millions)	**1,356.5**	1,367.2
Basic earnings per share (pence)	**25.8**	29.5

As noted in note 11, the Group cancelled the share buyback programme on 19 March 2020. At the time of cancellation, the Group had repurchased 10.4 million Ordinary Shares.

Diluted

Diluted earnings per share is calculated by dividing the earnings attributable to the owners of the Company less coupon payments in respect of Tier 1 notes by the weighted average number of Ordinary Shares during the period adjusted for the dilutive potential Ordinary Shares. The Company has share options and contingently issuable shares as categories of dilutive potential Ordinary Shares.

	2020 **£m**	2019 £m
Earnings attributable to owners of the Company	**367.2**	419.9
Coupon payments in respect of Tier 1 notes	**(16.6)**	(16.6)
Profit for the calculation of earnings per share	**350.6**	403.3
Weighted average number of Ordinary Shares (millions)	**1,356.5**	1,367.2
Effect of dilutive potential of share options and contingently issuable shares (millions)	**18.6**	15.3
Weighted average number of Ordinary Shares for the purpose of diluted earnings per share (millions)	**1,375.1**	1,382.5
Diluted earnings per share (pence)	**25.5**	29.2

13. Net assets per share and return on equity

Net asset value per share is calculated as total shareholders' equity (which excludes Tier 1 notes) divided by the number of Ordinary Shares at the end of the period excluding shares held by employee share trusts.

Tangible net asset value per share is calculated as total shareholders' equity less goodwill and other intangible assets divided by the number of Ordinary Shares at the end of the period excluding shares held by employee share trusts.

The table below analyses net asset and tangible net asset value per share.

At 31 December	2020 £m	2019 £m
Net assets	**2,699.7**	2,643.6
Goodwill and other intangible assets[1]	**(786.8)**	(702.5)
Tangible net assets	**1,912.9**	1,941.1
Number of Ordinary Shares (millions)	**1,364.6**	1,375.0
Shares held by employee share trusts (millions)	**(12.8)**	(8.4)
Closing number of Ordinary Shares (millions)	**1,351.8**	1,366.6
Net asset value per share (pence)	**199.7**	193.4
Tangible net asset value per share (pence)	**141.5**	142.0

Note:

1. Goodwill has arisen on acquisition by the Group of subsidiary companies and on acquisition of new accident repair centres. Intangible assets are primarily comprised of software development costs.

Return on equity

The table below details the calculation of return on equity.

	2020 £m	2019 £m
Earnings attributable to owners of the Company	**367.2**	419.9
Coupon payments in respect of Tier 1 notes	**(16.6)**	(16.6)
Profit for the calculation of return on equity	**350.6**	403.3
Opening shareholders' equity	**2,643.6**	2,558.2
Closing shareholders' equity	**2,699.7**	2,643.6
Average shareholders' equity	**2,671.7**	2,600.9
Return on equity	**13.1%**	15.5%

14. Reinsurance assets

	2020 £m	2019 £m
Reinsurers' share of general insurance liabilities	**1,071.6**	1,190.1
Impairment provision[1]	**(46.3)**	(40.5)
Total excluding reinsurers' unearned premium reserves	**1,025.3**	1149.6
Reinsurers' unearned premium reserve	**103.9**	101.7
Total	**1,129.2**	1,251.3

Note:

1. Impairment provision relates to reinsurance debtors, allowing for the risk that reinsurance assets may not be collected, or where the reinsurer's credit rating has been significantly downgraded and may have difficulty in meeting its obligations.

15. Financial investments

	2020 £m	2019 £m
AFS debt securities		
Corporate	**4,021.0**	3,925.6
Supranational	**21.3**	31.3
Local government	**35.6**	29.2
Sovereign	**25.2**	99.5
Total	**4,103.1**	4,085.6
HTM debt securities		
Corporate	**103.9**	104.0
Total debt securities	**4,207.0**	4,189.6
Total debt securities		
Fixed interest rate[1]	**4,184.5**	4,166.5
Floating interest rate	**22.5**	23.1
Total	**4,207.0**	4,189.6
Loans and receivables		
Infrastructure debt	**264.5**	278.1
Commercial real estate loans	**206.7**	205.7
Total loans and receivables	**471.2**	483.8
Equity investments[2]	**3.2**	–
Total	**4,681.4**	4,673.4

Notes:

1. The Group swaps a fixed interest rate for a floating rate of interest on its US dollar and Euro corporate debt securities by entering into interest rate derivatives. The hedged amount at 31 December 2020 was £971.1 million (2019: £955.8 million).
2. An equity fund which is valued based on external valuation reports received from a third-party fund manager.

16. Cash and cash equivalents and borrowings

	2020 £m	2019 £m
Cash at bank and in hand	**224.9**	223.1
Short-term deposits with credit institutions[1]	**995.2**	725.5
Cash and cash equivalents	**1,220.1**	948.6
Bank overdrafts[2]	**(51.9)**	(52.3)
Cash and bank overdrafts[3]	**1,168.2**	896.3

Notes:

1. This represents money market funds.
2. Bank overdrafts represent short-term timing differences between transactions posted in the records of the Group and transactions flowing through the accounts at the bank.
3. Cash and bank overdrafts disclosure note is included for the purposes of the consolidated cash flow statement.

The effective interest rate on short-term deposits with credit institutions for the year ended 31 December 2020 was 0.25% (2019: 0.79%) and average maturity was 10 days (2019: 10 days).

17. Share capital

Issued and fully paid: equity shares	**2020**			2019	
	Number of shares	**Share capital**	**Capital redemption reserve**	Number of shares	Share capital
Ordinary Shares of 1010/11 pence each[1]	**millions**	**£m**	**£m**	millions	£m
At 1 January	**1,375.0**	**150.0**	**–**	1,375.0	150.0
Shares cancelled following share buyback[2]	**(10.4)**	**(1.1)**	**1.1**	—	—
At 31 December	**1,364.6**	**148.9**	**1.1**	1,375.0	150.0

Notes:

1. The shares have full voting dividend and capital distribution rights (including wind up) attached to them; these do not confer any rights of redemption.
2. On 3 March 2020, the Group announced a share buyback of Ordinary Shares for an aggregate purchase price of £150 million. On 19 March 2020 the buyback programme was cancelled, given the uncertainty in the capital markets at the time driven by the rapidly emerging Covid-19 pandemic. At the time of cancellation, the Group had repurchased 10,448,395 Ordinary Shares for an aggregate consideration of £30,014,567 as reflected in retained earnings. The shares were subsequently cancelled giving rise to a capital redemption reserve of an equivalent amount as required by the Companies Act 2006.

Employee trust shares

The Group satisfies share-based payments under the Group's share plans primarily through shares purchased in the market and held by employee share trusts.

At 31 December 2020, 12,753,755 Ordinary Shares (2019: 8,445,670 Ordinary Shares) were owned by the employee share trusts at a cost of £40.3 million (2019: £30.2 million). These Ordinary Shares are carried at cost and at 31 December 2020 had a market value of £40.7 million (2019: £26.4 million).

18. Tier 1 notes

	2020	2019
	£m	£m
Tier 1 notes	**346.5**	346.5

On 7 December 2017, the Group issued £350 million of fixed rate perpetual Tier 1 notes with a coupon rate of 4.75% per annum.

The Group has an optional redemption date of 7 December 2027. If the notes are not repaid on that date, a fixed rate of interest per annum will be reset. The notes are direct, unsecured and subordinated obligations of the issuer ranking pari passu and without any preference amongst themselves.

The Tier 1 notes are treated as a separate category within equity and the coupon payments are recognised outside of the profit after tax result and directly in shareholders' equity.

The Group has the option to cancel the coupon payment. Cancellation becomes mandatory if: the Solvency condition[1] is not met at the time of, or following, coupon payment; there is non-compliance with the SCR or the minimum capital requirement; the Group has insufficient distributable reserves; or the relevant regulator requires the coupon payment to be cancelled.

Note:

1. All payments shall be conditional upon the Group being solvent at the time of payment and immediately after payment. The Issuer will be solvent if (i) it is able to pay its debts owed to senior creditors as they fall due and (ii) its assets exceed its liabilities.

19. Subordinated liabilities

	2020 £m	2019 £m
Subordinated Tier 2 notes	**516.6**	259.0

£250 million 9.25% subordinated Tier 2 notes due 2042

Subordinated guaranteed dated notes with a nominal value of £500 million were issued on 27 April 2012 at a fixed rate of 9.25%. On the same date, the Group also entered into a 10-year interest rate swap to exchange the fixed rate of interest for a floating rate of 3-month LIBOR plus a spread of 706 basis points which was credit value adjusted to 707 basis points with effect from 29 July 2013. This was treated as a designated hedging instrument.

On 8 December 2017, the Group repurchased £250 million nominal value of the subordinated guaranteed dated notes for a purchase price of £330.1 million including accrued interest of £2.7 million and associated transaction costs of £0.6 million. The designated hedging agreement was adjusted accordingly.

The remaining notes, with a nominal value of £250 million, have a redemption date of 27 April 2042 with the option to repay the notes on 27 April 2022. If the notes are not repaid on that date, the terms of the notes provide that the rate of interest will be reset at a rate of the 6-month LIBOR plus 7.91%. If LIBOR has been discontinued by this time, the terms of the notes provide for an ultimate fallback rate of interest of 9.25% for subsequent interest periods. The terms of the notes do not automatically provide for the transition of LIBOR to SONIA, which would require a separate agreement between the Group and the noteholders.

The Group has the option, in certain circumstances, to defer interest payments on the notes but to date has not exercised this right.

During 2020 the Group identified that the hedge no longer met the criteria of hedge effectiveness under IAS 39 ('Financial Instruments: Recognition and Measurement') and, under the rules of the standard, the accumulated hedging adjustment has begun to be amortised to the income statement from the date of the last successful hedge effectiveness test over the remaining life of the subordinated debt using an effective interest rate calculation.

£260 million 4.0% subordinated Tier 2 notes due 2032

On 5 June 2020, the Group issued subordinated Tier 2 notes at a fixed rate of 4.0%. The notes have a redemption date of 5 June 2032 and may be redeemed at the option of the Group commencing on 5 December 2031 until the maturity date.

The Group has the option, in certain circumstances, to defer interest payments on the notes but to date has not exercised this right.

The 2032 and 2042 notes are unsecured, and subordinated obligations of the Group and rank pari passu and without any preference among themselves. In the event of a winding-up or of bankruptcy they are to be repaid only after the claims of all other senior creditors have been met and will rank at least pari passu with the claims of holders of other Tier 2 capital.

20. Insurance liabilities

	2020 £m	2019 £m
Insurance liabilities	**3,617.0**	3,819.6

Gross insurance liabilities

Accident year	2011 £m	2012 £m	2013 £m	2014 £m	2015 £m	2016 £m	2017 £m	2018 £m	2019 £m	2020 £m	Total £m
Estimate of ultimate gross claims costs:											
At end of accident year	2,698.1	2,372.7	2,184.0	2,094.5	2,118.1	2,157.7	2,217.3	2,300.1	2,110.4	1,847.3	
One year later	(99.3)	(163.3)	(117.6)	20.7	(30.0)	(86.7)	(116.2)	(62.3)	(67.2)		
Two years later	(94.6)	(118.9)	(153.0)	(38.4)	(143.5)	(53.3)	(103.1)	(52.0)			
Three years later	(89.3)	(49.3)	(21.0)	(144.9)	(62.4)	(82.8)	(42.4)				
Four years later	(60.9)	(9.9)	(102.1)	(50.2)	(22.9)	(46.1)					
Five years later	(21.2)	(79.2)	(50.8)	(51.6)	(22.0)						
Six years later	(60.3)	(36.2)	(27.4)	(33.6)							
Seven years later	(25.1)	(23.8)	(14.0)								
Eight years later	(27.9)	(1.6)									
Nine years later	(11.0)										
Current estimate of cumulative claims	2,208.5	1,890.5	1,698.1	1,796.5	1,837.3	1,888.8	1,955.6	2,185.8	2,043.2	1,847.3	
Cumulative payments to date	(2,183.0)	(1,873.8)	(1,683.5)	(1,682.6)	(1,688.8)	(1,693.8)	(1,665.8)	(1,740.8)	(1,467.3)	(895.7)	
Gross liability recognised in balance sheet	**25.5**	**16.7**	**14.6**	**113.9**	**148.5**	**195.0**	**289.8**	**445.0**	**575.9**	**951.6**	**2,776.5**
2010 and prior											**762.5**
Claims handling provision											**78.0**
Total											**3,617.0**

Net insurance liabilities

Accident year	2011 £m	2012 £m	2013 £m	2014 £m	2015 £m	2016 £m	2017 £m	2018 £m	2019 £m	2020 £m	Total £m
Estimate of ultimate net claims costs:											
At end of accident year	2,644.4	2,271.8	2,093.9	1,971.0	1,926.7	1,922.2	2,016.9	2,125.9	1,941.2	1,674.5	
One year later	(131.5)	(146.7)	(123.6)	(29.7)	(67.0)	(18.9)	(79.7)	(41.4)	(34.5)		
Two years later	(82.1)	(107.8)	(134.4)	(42.0)	(77.8)	(38.2)	(65.3)	(27.1)			
Three years later	(76.5)	(35.6)	(27.8)	(100.7)	(30.4)	(43.7)	(14.0)				
Four years later	(48.7)	(11.6)	(64.3)	(41.3)	(24.1)	(16.9)					
Five years later	(37.3)	(54.2)	(38.9)	(52.5)	(20.7)						
Six years later	(37.0)	(30.4)	(17.7)	(8.3)							
Seven years later	(20.4)	(14.6)	(10.6)								
Eight years later	(23.0)	(1.2)									
Nine years later	(6.6)										
Current estimate of cumulative claims	2,181.3	1,869.7	1,676.6	1,696.5	1,706.7	1,804.5	1,857.9	2,057.4	1,906.7	1,674.5	
Cumulative payments to date	(2,159.5)	(1,856.3)	(1,664.4)	(1,653.8)	(1,638.5)	(1,678.8)	(1,637.6)	(1,731.4)	(1,459.3)	(878.0)	
Net liability recognised in balance sheet	**21.8**	**13.4**	**12.2**	**42.7**	**68.2**	**125.7**	**220.3**	**326.0**	**447.4**	**796.5**	**2,074.2**
2010 and prior											**439.5**
Claims handling provision											**78.0**
Total											**2,591.7**

20. Insurance liabilities continued

Movements in gross and net insurance liabilities

	Gross £m	Reinsurance £m	Net £m
Claims reported	3,001.0	(809.8)	2,191.2
Incurred but not reported	924.9	(295.4)	629.5
Claims handling provision	80.0	–	80.0
At 1 January 2019	4,005.9	(1,105.2)	2,900.7
Cash paid for claims settled in the year	(2,103.6)	25.3	(2,078.3)
Increase / (decrease) in liabilities:			
Arising from current-year claims	2,311.3	(169.2)	2,142.1
Arising from prior-year claims	(394.0)	99.5	(294.5)
At 31 December 2019	3,819.6	(1,149.6)	2,670.0
Claims reported	2,916.0	(829.3)	2,086.7
Incurred but not reported	825.4	(320.3)	505.1
Claims handling provision	78.2	–	78.2
At 31 December 2019	3,819.6	(1,149.6)	2,670.0
Cash paid for claims settled in the year	**(1,933.0)**	**141.1**	**(1,791.9)**
Increase / (decrease) in liabilities:			
Arising from current-year claims	**2,057.3**	**(169.9)**	**1,887.4**
Arising from prior-year claims	**(326.9)**	**153.1**	**(173.8)**
At 31 December 2020	**3,617.0**	**(1,025.3)**	**2,591.7**
Claims reported	**2,762.0**	**(842.8)**	**1,919.2**
Incurred but not reported	**777.0**	**(182.5)**	**594.5**
Claims handling provision	**78.0**	**–**	**78.0**
At 31 December 2020	**3,617.0**	**(1,025.3)**	**2,591.7**

Movement in prior-year net claims liabilities by operating segment

	2020 £m	2019 £m
Motor	**(100.6)**	(180.5)
Home	**(10.8)**	(41.4)
Rescue and other personal lines	**(5.6)**	(7.6)
Commercial	**(56.8)**	(65.0)
Total	**(173.8)**	(294.5)

21. Unearned premium reserve

Movement in unearned premium reserve

	Gross £m	Reinsurance £m	Net £m
At 1 January 2019	1,505.5	(103.5)	1,402.0
Written in the period	3,203.1	(215.9)	2,987.2
Earned in the period	(3,202.6)	217.7	(2,984.9)
At 31 December 2019	1,506.0	(101.7)	1,404.3
Written in the period	**3,180.4**	**(231.0)**	**2,949.4**
Earned in the period	**(3,189.3)**	**228.8**	**(2,960.5)**
At 31 December 2020	**1,497.1**	**(103.9)**	**1,393.2**

22. Related parties

Transactions between the Group's subsidiary undertakings, which are related parties, have been eliminated on consolidation and accordingly are not disclosed.

Full details of the Group's related party transactions for the year ended 31 December 2019 are included on page 209 of the Annual Report & Accounts 2019.

23. Post balance sheet event

On 10 February 2021, U K Insurance Limited signed a contract in relation to its Bromley site to surrender the current lease and DL Insurance Services Limited signed a contract to purchase the head lease. The cost of surrendering the lease was £91 million and the value of the fixed asset capitalised will be in the region of £17 million. This will reduce the Group's Solvency II pre-tax own funds by around £85 million.

Corporate information

Direct Line Insurance Group plc is a public limited company registered in England and Wales, (company number 02280426). The address of the registered office is Churchill Court, Westmoreland Road, Bromley, BR1 1DP.

Statutory accounts information

The Annual Report & Accounts 2019 were signed on 2 March 2020 and were delivered to the Registrar of Companies following the Annual General Meeting held on 14 May 2020. The Annual Report & Accounts 2019 is available at: https://www.directlinegroup.co.uk/content/dam/dlg/corporate/images-and-documents/investors/results-and-reports/2020/Annual%20Report%202019.pdf.downloadasset.pdf

At the time of the publishing of the Preliminary Results for 2020 the Annual Report and Accounts 2020 had not been published. Once published, the Annual Report and Accounts 2020 will be available on the Group's website at www.directlinegroup.co.uk

GLOSSARY

Term	Definition and explanation
Actuarial best estimate ("ABE")	The probability-weighted average of all future claims and cost scenarios. It is calculated using historical data, actuarial methods and judgement. A best estimate of reserves will therefore normally include no margin for optimism or, conversely, caution.
Assets under management ("AUM")	This represents all assets managed or administered by or on behalf of the Group, including those assets managed by third parties.
Association of British Insurers ("ABI")	The trade body that represents the insurance and long-term savings industry in the UK.
Available-for-sale ("AFS") investment	Available-for-sale investments are non-derivative financial assets that are designated as such, or are not classified as loans and receivables, held to maturity, or financial assets at fair value through profit or loss.
Average written premium	The total written premium at inception divided by the number of policies.
Capital	The funds invested in the Group, including funds invested by shareholders and Tier 1 notes. In addition, subordinated liability in the Group's balance sheet is classified as Tier 2 capital for Solvency II purposes.
Carbon emissions	**Scope 1** – covers direct emissions from owned or controlled sources, including fuels used in office buildings, accident repair centres and owned vehicles. **Scope 2** – covers indirect emissions from the generation of purchased electricity, steam, heating and cooling for office buildings and accident repair centres. **Scope 3 under our direct control** – includes indirect emissions that occur in the Group's value chain, under its direct control, such as waste disposal and business travel. **Total Scope 3** – includes all other indirect emissions that occur in the Group's value chain, excluding investments.
Claims frequency	The number of claims divided by the number of policies per year.
Claims handling provision (provision for losses and loss-adjustment expense)	Funds set aside by the Group to meet the estimated cost of settling claims and related expenses that the Group considers it will ultimately need to pay.
Combined operating ratio	The sum of the loss, commission and expense ratios. The ratio measures the amount of claims costs, commission and operating expenses, compared to net earned premium generated. A ratio of less than 100% indicates profitable underwriting. **Normalised combined** operating ratio adjusts loss and commission ratios for weather and changes to the Ogden discount rate. (See page 51 alternative performance measures.)
Commission expenses	Payments to brokers, partners and price comparison websites for generating business.
Commission ratio	The ratio of commission expense divided by net earned premium. (See page 51 alternative performance measures.)
Company	Direct Line Insurance Group plc.
Current-year attritional loss ratio	The loss ratio for the current accident year, excluding the movement of claims reserves relating to previous accident years and claims relating to major weather events. (See page 51 alternative performance measures.)
Current-year combined operating ratio	This is calculated using the combined operating ratio less movement in prior-year reserves. (See page 51 alternative performance measures)
Current-year normalised operating profit	This is calculated using the normalised operating profit adjusted for prior-year reserve movements. (See page 51 alternative performance measures.)
Direct own brands	Direct own brands include Home and Motor under the Direct Line, Churchill, Darwin and Privilege brands, Rescue under the Green Flag brand and Commercial under the Direct Line for Business and Churchill brands.
Earnings per share	The amount of the Group's profit after deduction of the Tier 1 coupon payments allocated to each Ordinary Share of the Company.
Expense ratio	The ratio of operating expenses divided by net earned premium. (See page 51 alternative performance measures.)
Finance costs	The cost of servicing the Group's external borrowings and including the interest on right-of-use assets.
Financial Conduct Authority ("FCA")	The independent body responsible for regulating the UK's financial services industry.
Financial leverage ratio	Tier 1 notes and financial debt (subordinated Tier 2 notes) as a percentage of total capital employed.
Gross written premium	The total premiums from contracts that were incepted during the period.

Term	Definition and explanation
Group	Direct Line Insurance Group plc and its subsidiaries.
Incremental borrowing rate ("IBR")	The rate of interest that a lessee would have to pay to borrow over a similar term and security, the funds necessary to obtain an asset of a similar value to the right-of-use asset in a similar economic environment.
Incurred but not reported ("IBNR")	Funds set aside to meet the cost of claims for accidents that have occurred but have not yet been reported to the Group. This includes an element of uplift on the value of claims reported.
In-force policies	The number of policies on a given date that are active and against which the Group will pay, following a valid insurance claim.
Insurance liabilities	This comprises insurance claims reserves and claims handling provision, which the Group maintains to meet current and future claims.
International Accounting Standards Board ("IASB")	A not-for-profit public interest organisation that is overseen by a monitoring board of public authorities. It develops IFRS standards that aim to make worldwide markets transparent, accountable and efficient.
Investment income yield	The income earned from the investment portfolio, recognised through the income statement during the period (excluding unrealised and realised gains and losses, impairments and fair value adjustments) divided by the average assets under management ("**AUM**"). The average AUM derives from the period's opening and closing balances for the total Group. (See page 51 alternative performance measures.)
Investment return	The investment return earned from the investment portfolio, including unrealised and realised gains and losses, impairments and fair value adjustments.
Investment return yield	The investment return divided by the average AUM. The average AUM derives from the period's opening and closing balances. (See page 51 alternative performance measures.)
Loss ratio	Net insurance claims divided by net earned premium. (See page 51 alternative performance measures.)
Management's best estimate ("MBE")	These reserves are based on management's best estimate, which includes a prudence margin that exceeds the internal ABE.
Net asset value	The difference between the Group's total assets and total liabilities, calculated by subtracting total liabilities (including Tier 1 notes) from total assets.
Net earned premium	The element of gross earned premium less reinsurance premium ceded for the period where insurance cover has already been provided.
Net insurance claims	The cost of claims incurred in the period less any claims costs recovered under reinsurance contracts. It includes claims payments and movements in claims reserves.
Net investment income yield	This is calculated in the same way as investment income yield but includes the cost of hedging. (See page 51 alternative performance measures.)
Ogden discount rate	The discount rate set by the Lord Chancellor and used by courts to calculate lump sum awards in bodily injury cases.
Operating expenses	These are the expenses relating to business activities excluding restructuring and one-off costs. (See page 51 alternative performance measures.)
Operating profit	The pre-tax profit that the Group's activities generate, including insurance and investment activity, but excluding finance costs, restructuring and one-off costs. **Normalised operating profit** is operating profit adjusted for weather and changes to the Ogden discount rate. (See page 52 alternative performance measures.)
Periodic payment order ("PPO")	These are claims payments as awarded under the Courts Act 2003. PPOs are used to settle some large personal injury claims. They generally provide a lump-sum award plus inflation-linked annual payments to claimants who require long-term care.
Prudential Regulation Authority ("PRA")	The PRA is a part of the Bank of England. It is responsible for regulating and supervising insurers and financial institutions in the UK.
Reinsurance	Contractual arrangements where the Group transfers part or all of the accepted insurance risk to another insurer.
Reserves	Funds that have been set aside to meet outstanding insurance claims and IBNR.
Restructuring costs	These are costs incurred in respect of the business activities where the Group has a constructive obligation to restructure its activities.
Return on equity	This is calculated by dividing the profit attributable to the owners of the Company after deduction of the Tier 1 coupon payments by average shareholders' equity for the period.

Term	Definition and explanation
Return on tangible equity ("RoTE")	This is adjusted profit after tax divided by the Group's average shareholders' equity less goodwill and other intangible assets. Profit after tax is adjusted to exclude restructuring and one-off costs and to include the Tier 1 coupon payments. It is stated after charging tax using the UK standard rate of 19%. (See page 52 alternative performance measures.)
Right-of-use ("ROU") asset	A lessee's right to use an asset over the life of a lease, calculated as the initial amount of the lease liability, plus any lease payments made to the lessor before the lease commencement date, plus any initial direct costs incurred, minus any lease incentives received.
Science-based targets ("SBT")	Science-based targets are a set of goals developed by a business to provide it with a clear route to reduce greenhouse gas emissions. An emissions reduction target is defined as 'science-based' if it is developed in line with the scale of reductions required to keep global warming below 2˚C from pre-industrial levels.
Scope 1, Scope 2, Scope 3 under our direct control and total Scope 3	Please refer to the glossary definition for carbon emissions on page 48.
Solvency II	The capital adequacy regime for the European insurance industry, which became effective on 1 January 2016. It establishes capital requirements and risk management standards. It comprises three pillars: Pillar I, which sets out capital requirements for an insurer; Pillar II, which focuses on systems of governance; and Pillar III, which deals with disclosure requirements.
Solvency capital ratio	The ratio of Solvency II own funds to the solvency capital requirement.
Tangible equity	This shows the equity excluding Tier 1 notes and intangible assets (for comparability with companies which have not acquired businesses or capitalised intangible assets). (See page 52 alternative performance measures).
Tangible net assets per share	This shows the amount of tangible equity allocated to each ordinary share (for comparability with companies which have not acquired businesses or capitalised intangible assets). (See page 52 alternative performance measures).
Underwriting result profit / (loss)	The profit or loss from operational activities, excluding investment return and other operating income. It is calculated as net earned premium less net insurance claims and total expenses, excluding restructuring and one-off costs.

APPENDIX A – ALTERNATIVE PERFORMANCE MEASURES

The Group has identified Alternative Performance Measures ("**APMs**") in accordance with the European Securities and Markets Authority's published Guidelines. The Group uses APMs to improve comparability of information between reporting periods and reporting segments, by adjusting for either uncontrollable or one-off costs which impact the IFRS measures, to aid the user of the annual report and accounts in understanding the activity taking place across the Group. These APMs are contained within the main narrative sections of this document, outside of the financial statements and notes, and may not necessarily have standardised meanings for ease of comparability across peer organisations.

Further information is presented below, defined in the glossary on pages 48 to 50 and reconciled to the most directly reconcilable line items in the financial statements and notes. Note 3 on page 35 of the consolidated financial statements presents a reconciliation of the Group's business activities on a segmental basis to the consolidated income statement. All note references in the table below are to the notes to the consolidated financial statements on pages 33 to 47.

Group APM	Closest equivalent IFRS measure	Definition and / or reconciliation	Rationale for APM
Combined operating ratio	Profit before tax	Combined operating ratio is defined in the glossary on page 48 and reconciled in note 3 on page 35.	This is a measure of underwriting profitability and excludes non-insurance income, whereby a ratio of less than 100% represents an underwriting profit and a ratio of more than 100% represents an underwriting loss.
Commission ratio	Commission expense	Commission ratio is defined in the glossary on page 48 and reconciled in note 3 on page 35.	Expresses commission expense, in relation to net earned premium.
Current-year attritional loss ratio	Net insurance claims	Current-year attritional loss ratio is defined in the glossary on page 48 and is reconciled to the loss ratio (discussed below) on page 53.	Expresses claims performance in the current accident year in relation to net earned premium.
Current-year combined operating ratio	Profit before tax	Current-year combined operating ratio is defined in the glossary on page 48 and is reconciled on page 53.	This is a measure of underwriting profitability, excluding the effect of prior-year reserve movements.
Current-year normalised operating profit ratio	Profit before tax	Current-year normalised operating profit ratio is defined in the glossary on page 48 and reconciled on page 53.	Expresses a relationship between current-year normalised operating profit and normalised operating profit.
Expense ratio	Total expenses	Expense ratio is defined in the glossary on page 48 and reconciled in note 3 on page 35.	Expresses underwriting and policy expenses in relation to net earned premium.
Investment income yield	Investment income	Investment income yield is defined in the glossary on page 49 and is reconciled on page 52.	Expresses a relationship between the investment income and the associated opening and closing assets adjusted for portfolio hedging instruments.
Investment return yield	Investment return	Investment return yield is defined in the glossary on page 49 and is reconciled on page 52.	Expresses a relationship between the investment return and the associated opening and closing assets adjusted for portfolio hedging instruments.
Loss ratio	Net insurance claims	Loss ratio is defined in the glossary on page 49 and reconciled in note 3 on page 35.	Expresses claims performance in relation to net earned premium.
Net investment income yield	Investment income	Net investment income yield is defined in the glossary on page 49 and is reconciled on page 52.	Expresses a relationship between the net investment income and the associated opening and closing assets adjusted for portfolio hedging instruments.
Normalised combined operating ratio	Profit before tax	Combined operating ratio is defined in the glossary on page 48 and reconciled on page 53.	This is a measure of underwriting profitability excluding the effects of weather, Ogden discount rate changes and restructuring and one-off costs. It also excludes non-insurance income. A ratio of less than 100% represents an underwriting profit and a ratio of more than 100% represents an underwriting loss.
Operating expenses	Total expenses	Operating expenses are defined in the glossary on page 49 and reconciled in note 3 on page 35.	This shows the expenses relating to business activities excluding restructuring and one-off costs.

Group APM	Closest equivalent IFRS measure	Definition and / or reconciliation	Rationale for APM
Operating profit	Profit before tax	Operating profit is defined in the glossary on page 49 and reconciled in note 3 on page 35.	This shows the underlying performance (before tax and excludes finance costs and restructuring and one-off costs) of the business activities.
Return on tangible equity	Return on equity	Return on tangible equity is defined in the glossary on page 50 and is reconciled on page 54.	This shows performance against a measure of equity that is more easily comparable to that of other companies.
Tangible equity	Equity	Tangible equity is defined in the glossary on page 50 and is reconciled on page 54.	This shows the equity excluding Tier 1 notes and intangible assets for comparability with companies which have not acquired businesses or capitalised intangible assets.
Tangible net assets per share	Net assets per share	Tangible net assets per share is defined in the glossary on page 50 and reconciled in note 13 on page 41.	This shows the equity excluding Tier 1 notes and intangible assets per share for comparability with companies which have not acquired businesses or capitalised intangible assets.
Underwriting profit	Profit before tax	Underwriting profit is defined in the glossary on page 50 and is reconciled in note 3 on page 35.	This shows underwriting performance calculated as net earned premium less net claims and operating expenses, excluding restructuring and one-off costs.

Investment income and return yields[1]

	Notes[2]	2020 £m	2019 £m
Investment income	5	**127.1**	146.4
Hedging to a sterling floating rate basis[3]	5	**(20.3)**	(22.1)
Net investment income		**106.8**	124.3
Net realised and unrealised (losses) / gains excluding hedging		**(11.7)**	10.3
Investment return	5	**95.1**	134.6
Opening investment property		**291.7**	322.1
Opening financial investments		**4,673.4**	4,737.8
Opening cash and cash equivalents		**948.6**	1,154.4
Opening borrowings		**(52.3)**	(62.0)
Opening derivatives asset[4]		**81.8**	11.8
Opening investment holdings		**5,943.2**	6,164.1
Closing investment property		**292.1**	291.7
Closing financial investments	15	**4,681.4**	4,673.4
Closing cash and cash equivalents	16	**1,220.1**	948.6
Closing borrowings	16	**(51.9)**	(52.3)
Closing derivatives asset[4]		**8.0**	81.8
Closing investment holdings		**6,149.7**	5,943.2
Average investment holdings[5]		**6,046.5**	6,053.7
Investment income yield		**2.1%**	2.4%
Net investment income yield[1]		**1.8%**	2.1%
Investment return yield		**1.6%**	2.2%

Notes:

1. See glossary on page 49 for definitions.
2. See notes to the consolidated financial statements.
3. Includes net realised and unrealised gains / (losses) of derivatives in relation to AUM.
4. See footnote 1 on page 17 (Investment holdings).
5. Mean average of opening and closing balances.

Normalised combined operating ratio[1]

	Home 2020	Home 2019	**Commercial 2020**	Commercial 2019	**Total 2020**	Total 2019
Loss ratio	**55.6%**	46.8%	**51.4%**	52.7%	**57.9%**	61.9%
Commission ratio	**8.1%**	9.7%	**18.7%**	18.5%	**8.6%**	7.1%
Expense ratio	**23.4%**	23.8%	**25.4%**	24.5%	**24.5%**	23.2%
Combined operating ratio	**87.1%**	80.3%	**95.5%**	95.7%	**91.0%**	92.2%
Effect of weather						
Loss ratio	**3.4%**	7.2%	**0.4%**	3.7%	**0.7%**	2.0%
Commission ratio	**(0.2%)**	(0.6%)	**–**	–	**–**	(0.1%)
Combined operating ratio normalised for weather	**90.3%**	86.9%	**95.9%**	99.4%	**91.7%**	94.1%
Effect of Ogden discount rate						
Loss ratio	**–**	–	**–**	(0.2%)	**–**	(0.6%)
Combined operating ratio normalised for weather and Ogden discount rate	**90.3%**	86.9%	**95.9%**	99.2%	**91.7%**	93.5%

Note:

1. See glossary on page 48 for definition.

Normalised operating profit[1]

	Total 2020 £m	Total 2019 £m
Operating profit	**522.1**	546.9
Effect of:		
Ogden discount rate	**–**	16.9
Normalised weather – claims	**(20.8)**	(59.0)
Normalised weather – profit share	**1.3**	3.7
Normalised operating profit	**502.6**	508.5
Prior-year adjustments		
Prior-year reserve movement	**173.8**	294.5
Ogden discount rate	**–**	16.9
Prior-year normalised operating profit	**173.8**	311.4
Current-year normalised operating profit	**328.8**	197.1
Current-year normalised operating profit ratio	**65%**	39%

Note:

1. See glossary on page 49 for definition.

Operating expenses[1]

	Note[2]	**2020 £m**	2019 £m
Operating expenses (including restructuring and one-off costs)	9	**763.8**	704.9
Less restructuring and one-off costs	9	**(39.4)**	(11.2)
Operating expenses	9	**724.4**	693.7

Notes:

1. See glossary on page 49 for definition.
2. See notes to the consolidated financial statements.

Return on tangible equity[1]

	2020 £m	2019 £m
Profit before tax	**451.4**	509.7
Add back: restructuring and one-off costs	**39.4**	11.2
Coupon payments in respect of Tier 1 notes	**(16.6)**	(16.6)
Adjusted profit before tax	**474.2**	504.3
Tax charge (2019 and 2020 UK standard tax rate of 19%)	**(90.1)**	(95.8)
Adjusted profit after tax	**384.1**	408.5
Opening shareholders' equity	**2,643.6**	2,558.2
Opening goodwill and other intangible assets	**(702.5)**	(566.8)
Opening shareholders' tangible equity	**1,941.1**	1,991.4
Closing shareholders' equity	**2,699.7**	2,643.6
Closing goodwill and other intangible assets	**(786.8)**	(702.5)
Closing shareholders' tangible equity	**1,912.9**	1,941.1
Average shareholders' tangible equity[2]	**1,927.0**	1,966.3
Return on tangible equity	**19.9 %**	20.8 %

Notes:

1. See glossary on page 50 for definition.
2. Mean average of opening and closing balances.

ADDITIONAL INFORMATION

We confirm that to the best of our knowledge:

1. the financial statements within the Annual Report & Accounts, from which the financial information within these Preliminary Results have been extracted, are prepared in accordance with International Financial Reporting Standards, issued by the IASB as adopted by the EU on 31 December 2020 and by the UK's Government Department of Business, Energy and Industrial Strategy in 2021, and give a true and fair view of the assets, liabilities, financial position and profit or loss of the Group and the undertakings included in the consolidation taken as a whole; and

2. the management report within these Preliminary Results includes a fair review of the development and performance of the business and the position of the Group, and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties faced by the Group.

Signed on behalf of the Board

PENNY JAMES
CHIEF EXECUTIVE OFFICER

5 March 2021

LEI: 213800FF2R23ALJQOP04