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# Transcription

**Title: RSA Q3 2018 Trading Update**

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**Speakers: Stephen Hester, Scott Egan**

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## Presentation

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### Operator

Hello, and welcome to the RSA third quarter 2018 trading update call. Throughout this, all participants will be in listen-only mode, and afterwards there will be a question and answer session. And just to remind you this call is being recorded.

So, today, I'm pleased to present Stephen Hester, Group Chief Executive, and Scott Egan, Group Chief Financial Officer. Gentlemen, please go ahead.

### Stephen Hester

Yes, good morning everyone and thank you very much for joining this call, and sorry to spring it on you at short notice. Clearly the call is to discuss our third quarter – RSA's third quarter trading update, which we released this morning, clearly about a month earlier than we would normally have done so. And as you will have seen from the release, the reason why we released it early is because we, unfortunately, have to report that in our UK and London market business, we have a unexpected loss for the quarter, and that obviously has an impact on the group's results, and therefore that was why we had to bring it forward. Although the quarter wasn't developing particularly well in that business, it was at the end of quarter, that's when you tot up a bunch of the large losses and when all your reserve reviews take place, and so it was really in the last week that it, sort of, pushed us over the edge in terms of wanting to speak to the market early. And clearly, we are very disappointed to have to do that and very disappointed in effect have to profit warn. It's not something that we set out to do, and we will be working extremely hard to put right those elements that are more than just volatility, and clearly, we'll try to unpack some of that for you.

However, I think that what we should say first is that, as you all know, the great majority of our group's market valuation and profitability and indeed revenues lie outside the UK, and in every single one of our businesses outside the UK, we have reported a very strong quarter, and although, of course, each of those businesses has had some areas that are going better and some areas that are going worse, overall, as you can see the great majority of the group is in strong shape in the third quarter with trends looking in reasonable shape as we look forward. And therefore, at the moment, our primary headache is in the UK results, and once Scott has taken you through the numbers that we've given today, I will come back before we open to Q and A and go through a little bit about what we are doing specifically in the UK to make sure that we can improve on these results.

So, Scott, with that, do you want to take us through what we've been able to say today?

### Scott Egan

Okay. Thanks, Stephen. Good morning everyone, and I'd just reinforce what Stephen said, thank you for joining the call at short notice today. I'll give a brief overview before handing back to Stephen.

For good order, just please note that that the Q3 numbers we're announcing today are near final but are subject to our usual quarterly close processes. Overall, strong performances in our non-UK businesses in Q3 have been overshadowed by poor results in the UK. I'll provide the group headlines before unpacking the UK result in a bit more detail.

So, starting with the top line, net written premiums of circa £4.9 billion year to date are up 1% on an underlying basis at constant rate of exchange. Headline net written premium is lower due to reinsurance costs in Q1, as I've explained previously. Q3 discrete premiums are up 4% compared to the same period last year at constant FX. Regional premium trends in Q3 were comparable to those that we described in H1, and we continue to see good momentum in Scandinavia and Canada, and there's no change to the premium trends in the areas where the most underwriting action is required, specifically the UK where volumes are being impacted the most.

Turning to profitability. The group's non-UK businesses performed strongly in the third quarter. In Q3 discrete, Scandinavia is on track to report a combined ratio of around 84%, Canada around 94.5%, Ireland around 88% and the Middle East around 81%. This would be more than offset by a difficult and volatile quarter for our UK business, reporting a Q3 discrete underwriting loss of approximately £70 million and a combined ratio of around 110%.

Looking at the UK in more detail, the deterioration is split between weather, large losses and, to a lesser extent, attritional claims. On weather, we saw a number of events, specifically, the further development of claims relating to the flash flooding in

the UK in May, a marine loss on a tornado in Iowa and an increase in household subsidence claims in Q3 as a result of the dry summer weather. The latter will have a tail into Q4, and we expect that it will have an impact market-wide for UK household insurers.

Moving to large losses, we incurred a number of what we call super large losses in the third quarter. These are individual losses over £10 million, and our marine book was particularly impacted. While large losses increased in Q3 compared to H1, the spike does set within our normal tolerance levels, and at this stage, we believe it to be due to volatility rather than underwriting issues. Of course, we'll take our normal detailed review of all the large claims. On a year to date basis, the large loss ratio in the UK is almost 3% lower than at this stage last year.

The UK attritional loss ratios stepped out slightly in Q3, and at around 49% year to date, has returned to end-2017 levels. Improvements in household as a result of our pricing and claims actions were offset by increases in marine and personal motor, primarily caused by market-wide capacity issues in repair networks for motor claims and London-market business in marine.

In summary, we believe that a large proportion of the deterioration that we've seen in the UK in Q3, whilst disappointing, was linked to volatility. This will be confirmed in Q4, and further action plans will be formulated for any underlying issues. At this stage, we see only a modest feedthrough into 2019 from Q3.

Importantly, we've now reached the retention level on our group volatility cover, meaning that we move into Q4 with protection against both large and weather losses over £10 million. At this point, it's hard to forecast exactly what the recovery in the programme will be, but there is more likely to be some. And, finally, our strong capital position has further improved from half year, with a Solvency II coverage ratio of approximately 172% at the end of quarter three.

With that, I'll pass back to Stephen.

## Stephen Hester

Terrific. Thank you very much, Scott. So, clearly, the UK business or UK and London market business, because that element of business is international as you know, this is now the second year in a row where we have a substantial headache from the business, and of course, in both years, large amounts of that are, if you like, externally oriented. Last year, it was – at this time last year, it was the hurricane which hit the rest of the insurance industry very hard, and this year there are some elements that are also shared elsewhere, although some is a bit more idiosyncratic to our book. So, although as Scott has mentioned to you, we do consider very substantial amounts of the loss in the third quarter to be random volatility, clearly, we don't really want our business to have continuing high amounts of random negative volatility, and at some point, the averages have to be a trend as opposed to individual volatility.

As far as we can tell, as mentioned, the weather clearly is random, and the large losses we believe not to have been bad underwriting, but nevertheless we do need to try to make some room in our PnL or improve or both. And I think the backdrop in thinking about this, at least as it relates to the commercial line's element, which is the lion's share of the UK losses in the third quarter, clearly, the London market, the wholesale markets, the large commercial markets are particularly soft. We've seen that in Lloyd's of London, we've seen that in red actions of people withdrawing capacity. The marine market is possibly one of the worse areas in it, which happens to have been a long-term specialty area of RSA as well. And so, there are a whole range of soft market issues and overcapacity market issues, which everyone is and has been grappling with, and which was evident last year as well.

I would say, in the face of that, in order to have acceptable profitability, you need to index even more than you might normally on high quality underwriting, and the disciplined underwriting and a willingness to reshape portfolios and walk away from business. And so, in effect, our response to the market conditions is and has been exactly that. And so, we, I would say, in the light of the results in the third quarter last year and into the fourth quarter, started a programme of significant pricing and underwriting action across our UK business, and you've seen this year some of the evidence of that in the earlier quarters in terms of walking away from business and reducing the premium line as we work through the renewal cycles.

Clearly when you do re-underwrite books, it can take one to two years to do it, firstly, because a renewal cycle lasts over a whole year, and secondly, you don't always get everything the first time around and so sometimes you have to go back again in the light of experience. And so, you can take it that we will continue to be aggressive pricers of business that is not working for us and be reshaping our portfolios in an effort to trim the worst areas if we can't correct them from a price standpoint. And that action,

which is already underway, I believe is partly responsible for the fact that large losses in the UK are lower than they were last year but still not where they need to be, and we will continue those actions through into next year. For commercial lines underwriting, 01.01 is quite a big renewal date, so that allows you to make quite a big dent at the beginning of the year, which clearly, we'll be planning to do. So, that's one form of response.

In addition to that, we have made a series of management changes in our UK business in commercial lines. Our commercial lines business is divided into two divisions, both of them have new heads in January and February of this year and the large commercial line business, the new head came from Swiss Re, came externally; in the smaller and mid-sized business, it was internal promotion. And we have also just appointed in the last week a new Chief Underwriting Officer in the UK sourced from Zurich, who will make some good additions and changes. And of course there are other changes going on in the team.

So, in addition to underwriting and portfolio action, there has been management action, and then there are very many other actions to tool up our underwriters, to increase training and to try to bear down on the volatility element and on the quality of our underwriting. It's not clear to us that the quality of underwriting is particularly worse than that of others, but we want it to be better, and so all of these are no-regrets actions. The consequence of all of that is that we believe that not only is some of the performance in the third quarter volatility, but we believe that we can improve the underlying performance and reshape the portfolios in order, as Scott mentioned, to produce sharply better UK results next year and into the future.

It is clear that the UK is proving the most difficult of our territories to get towards the best-in-class levels. In fact, all of the other territories are getting very close already, albeit we think that there is plenty more we can do in those businesses, and the UK is not very close at the moment and it will take us longer, but we're equally determined to do it. We think we're doing the right things and unfortunately those things take some time to show through. But be under no illusions, we're pretty determined to press ahead and do all the things we can do to make the performance as good as it can be.

So, with that, let me hand over to Q&A.

## Q&A

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### Operator

Thank you. Ladies and gentlemen, if you wish to ask a question, please could you press 0 and then 1 on your phone keypad now in order to enter the queue, and then after I announce you, simply ask that question. And if you find that question has been answered before it's your turn to speak, please press 0 and then 2 to cancel. And there'll be a brief pause while the questions are being registered.

Okay, our first question is over the line of Jonny Urwin at UBS. Please go ahead. Your line is now open.

### Jonny Urwin

Hi, good morning. Good morning everyone. Just two questions from me please. So, firstly, on the London market business, I guess the obvious question from this update today and last year is, do you think RSA is the right owner of the London market wholesale business longer term? I mean, I appreciate we're in a soft market and conditions are tough. But I guess, is bringing unwelcome volatility to the book, which even if pricing is more adequate, that would still be true to some extent. So, any comments there would be much appreciated.

And then on the UK motor book, you're flagging higher attritional claims due to capacity issues in repair centres. I wonder, could you give us some more detail on that? Is that just a function of you guys being a bit smaller in that book and perhaps not having as much clout, or is it something else?

And then, I guess, the other area is, are attritional claims just rising because we've seen a bit of weak pricing as well? Thank you.

### Stephen Hester

Terrific. Thank you very much. On the first, what I'd say is the following, that we have absolutely no, if you like, emotional and irrational attachment to any area of our portfolio. And if we can't see the ability to compete successfully, we're going to stop doing things, and we've shown that quite a lot in the last few years and we'll do it again. And so, give an example of that, we have

something called a wholesale international portfolio that was particularly badly hit last year in the hurricanes, obviously not nearly as badly as lots of other people but nevertheless, and we have, I think, taken something like 60% out of that portfolio in the last 12 months.

And I can assure you the marine book, which is the primary source of the headaches in the third quarter, is going to be getting very significant treatment in the next few months and year to ensure that those areas that are performing badly are cut out of the book or comprehensively re-underwritten and re-priced. I think that on – and as a result of that, it may well be that our participation in the London market business shrinks. But all of that said, there are areas of London market, where we have over many years been very successful and where we have made good money. Of course, there are cycles to it, and indeed, in the – that was also true in the year-to-date.

And the issue with corporate business, I understand that about 60% of our UK business is corporate business, that there is a continuum that on which there isn't a completely clear stopping point between small, mid, large and international corporates. And if you want to have a large UK corporate business, then you have to service some of those corporations internationally. You serve them internationally, then there is other business you do alongside it to go alongside the same specialities. You do develop certain speciality niches, one of ours that, for example continues to be very profitable and where we're a world leader, is renewable energy and particularly in wind. And so, I think it's not a black and white issue of participation or not participation, but it is certainly the case that we need to be selective in our London market and international participation, and I think in the light of some of these, we will become more selective.

With respect to your second question on UK motor, I think that there – as best we can see, there is an element of attritional step-out that came from the tougher winter, more frequency of car damage car clogging up car shops and leading to longer car hire periods, so there is an element which I would expect to be market-wide but also time limited, because it rose out of bad weather. And I think there is also an element, as I've said many times before, where we are currently not tooled up to be as successful in the personal lines motor market in the UK as some of the mono-line and quasi-mono-line competitors. And it's for that reason, not just for motor but across all the personal lines, that we're in the middle of a very major tooling-up process – multi-year tooling-up process, of which the new platform was launched with Nationwide at the beginning of the year. Motor is going on it as we speak, and the other personal lines will roll out over the next couple of years, and we also are putting in a new claims platform, authorised over the summer and will go in again over the next two or three years. And that tooling-up process will allow us to compete with a fuller deck of cards relative to the people who are winning in that market than we currently can.

In the meantime, some of the restructuring that we're doing in our operations in the UK causes short-term disruption and can weaken us in the short term. And I think there was an element in motor, for example, in motor claims, we brought five sites of motor claims into one in the last 12 months, and I think some element of the attritional step-up was, if you like, the inexperience of some of the new handlers in the new centre. And, having lost some experienced handlers, over the long-term, it's clearly better to have all of our expertise in one centre, and that will serve us well in the future, but in the short term, it's cost us.

So, as I say, on the motor I think there is a little bit of market stuff, although I don't think that's long-term, long-lasting – it's probably weather-related, and there is a bit of self-administered pain as well.

**Jonny Urwin**

Very useful. Thank you.

**Operator**

We're now over to the line of Andrew Crean at Autonomous. Please go ahead.

**Andrew Crean**

Good morning everyone. It's Andrew Crean. Two questions and a request. On the London market, is there anything you can do to reduce volatility through greater levels of reinsurance, and is that under consideration?

The other question was on the overseas businesses, whether the improvement in the Q3 in Scandinavia and Canada relative to the first half was seasonal or whether it's underlying?

And then the request: given the relatively low level of confidence I think the market has in your London market businesses, would it be possible to publish the results, the premiums underwriting and combined ratios to the London market business separately,

so that we can get a sense as to whether they are underperforming because of one-off factors or whether it is a longer-term issue?

### Stephen Hester

Terrific. Thank you, Andrew. I think on your last point, I think, you know, it is sensible for us – I think the time to do that will be with the full-year results when we have, you know, obviously better disclosures and numbers to unpack, in disclosure terms, the London market and international component of the UK results more. And so, we'll try and respond to your request positively in that regard.

### Andrew Crean

Great, thanks.

### Stephen Hester

In terms of your other two questions, on reinsurance, I think the short answer is yes. Now is the time when we are actively considering what reinsurance to purchase at the end of the year, in terms of the year-end purchase. Clearly, three years ago, when we started the – purchasing the group aggregate cover, which provides protection against losses over £10 million, that was our first response to this, and that obviously captures both weather and large losses. And as Scott mentioned, that will – for example, this year – provide us substantial protection in the fourth quarter, since we've used up the full-year cover in the first three quarters. So, I think for £10 million and above, although we can still get significant monthly and quarterly volatility, the full year volatility is covered.

What we need to consider is whether, for losses that lie below £10 million where you can have full-year volatility, although historically seems to be less, but you certainly can have, whether we should do an aggregate cover or whether we should buy down into more areas, and that is an active part of our year-end preparations. And obviously, we'll update you with our year-end results as to whether we've found anything that we thought was good value for money in doing that.

And then, on your last – on your second question about the improvement in Scandinavia and Canada, I would say if we take Canada first of all, the main improvement was just the weather wasn't as bad, because actually Canada was fine in the first half on all of the controllables but had a horrible winter. And so, in that sense, I don't think it was per se seasonal, but it was just that the weather performed in a seasonally normal way in the third quarter and it hasn't done in the first half. And the other trends, you know, continue to be good. There was actually a bit of negative large loss volatility in Canada as well in the third quarter, and that will in turn be protected by an aggregate in the fourth quarter at a lower level.

In Scandinavia, where you don't really have significant weather trends normally, I think that the improvement was that large losses were better than they were in the first half, and the rest of the lines, you know, behaved themselves and, you know, and so that's – I don't think that's particularly seasonal either, but Scandinavia is less seasonal than other markets in any event.

### Andrew Crean

Great, thanks.

### Operator

Okay. We now go to the line of Thomas Seidl at Bernstein. Please go ahead. Your line is now open.

### Thomas Seidl

Good morning. A first question on UK. Again, you say that the main driver of the performance there was marine. But as I understand it, in marine, your net retention is between £5 and £10 million, so in order to get to a £70 million loss there, it must have been a quite large number of marine losses. Maybe you can confirm that this is the main driver, a very large frequency, rather than super-sized marine losses?

Secondly on attritional, you say at the group level, it's broadly consistent. Would that mean slightly up, because otherwise I would have expected you to write it's slightly improving. So broadly consistent, does it mean it's slightly up?

And finally, on the dividend, and with this weak quarter with you because as you say, this is in your view maybe abnormal volatility. Look through the numbers here, we just simply apply to typically pay-out ratio for the dividend.

### Stephen Hester

I think on marine, we do have coverage down to about £10 million for individual losses, not £5 million, and we did have about four individual marine losses that were just under the £10 million number. And so yes, that was an unusual frequency of those losses.

### Thomas Seidl

And where does the other £30 million then come from?

### Stephen Hester

Well, as we said, on the – the £70 million loss in the UK, about £30 million was weather that was worse than expected which divides about half – a third May flood carryover, a third subsidence and a third marine loss which was tornado in – hitting a cargo in Iowa. And so that was £30 million. Large overall was about £35 million over our expectations, and a couple of those were marine and couple were UK domestic, the large ones, and then there was some attritional step out both in marine and in motor, as mentioned.

On your question on attritional loss ratios, if I'm understanding you correctly, it was our ambition that attritional loss ratios be better this year than last year, and at the moment they're not. So, in that sense, they're worse than we thought they would be, even though they're not absolutely worse.

And your last question on the dividend, you know, clearly, we'll make dividend decisions in February of next year in light of the full year results and we're not making them now, but I think it would be reasonable to expect us to not be treating the dividend as a completely fixed mathematical function of profit and to take consideration of short-term volatility and not flex the dividend as much as short-term volatility would flex.

### Thomas Seidl

Thank you, very helpful.

### Operator

Okay. We're now over to the line of Greig Paterson of KBW. Please go ahead, Greig. Your line is now open.

### Greig Paterson

Good morning gentlemen. A lot of my questions were asked. But three sort of maybe numerical ones. In terms of motor, I wonder if you could just talk about your current run rate for net premium that you're achieving. I know it's premium minus inflation. Specifically, I'm interested because you're telematics-focused; I'm just trying to see how that relates back to the market.

And then in terms of home, if you could just enlighten whether you've currently got positive or negative draws in terms of rate. Those two would be useful. Thank you.

### Scott Egan

Hi, Greig. So, picking your first one – It's Scott here. Picking your first one, which is really on home, I think we described before that we are sort of – our household we can sort of different by distribution channel and different by scheme, etc. But I would say as a rough proxy, you know, sort of 7% to 10% would be the rate that we're carrying at home. That's no different to what we said at half year, and we will continue with that action until we believe that the book is actually rectified accordingly.

### Stephen Hester

There is positive draws, i.e., the attritional loss ratio of household has come down.

### Scott Egan

Yeah. And that action, to Stephen's point, which is why I mentioned that it in my script, the actions we're taking are feeding through. You know, a two or three-point improvement in household claims ratio would indicate that the actions we're taking are having the desired effect.

Can I just be clear on motor, Greig? Could you just repeat the question...?

### Greig Paterson

Well, it's basically to say – I mean, obviously you've got a quirky book in that you focus on – you're spending a lot of time focusing on telematics. So, it's basically the same question as home. What sort of – you know, what sort of net rate are you getting through, net of claims inflation there?

### Scott Egan

So, we're cutting around 3% or 4% on our motor book up to sort of Q3, Greig. Obviously we'll revisit that in light of performance and try and see through what Stephen described as short-term issues versus longer-term issues. What I would say is that if we believe we need to carry more rate, then we will. I don't think there's any particular quirk between, for example, our telematics book or our [inaudible] book. I think we are sort of seeing similar dynamics in both. So, that would be my answer to your motor question.

### Greig Paterson

So, when you say you're going three to four, that's a year-on-year positive, right? But you say you actually got negative draws because you said you need to carry a bit more –

### Stephen Hester

Correct, yes, yes. The attritional loss ratios got worse in motor, yeah.

### Greig Paterson

Cool. By how many points, is it one or two or very – a lot?

### Scott Egan

It's probably one on motor book. It's really probably about three points, Greig. We've seen a sort of step-out relative to the end of the year.

### Greig Paterson

Perfect. Thank you.

### Operator

Okay. We are now over to Ben Cohen at Investec. Please go ahead, Ben. Your line is now open.

### Ben Cohen

Thanks very much. There were two things I wanted to ask, please. Firstly, on the marine underwriting, I was just wondering – or re-underwriting – if you could put it into the context of the actions that you took after the large losses of the second half of the year. I mean, are there particular things in your portfolio that you think that you've missed, if you like, that needs to be, you know, materially addressed? And I guess as part of that, you're already putting through, I think it was a 7% rate in the first half. Can you give any indication in terms of how much more rate you think you need there?

And the second question was on the UK personal motor, you referred to, I suppose, just maybe being less good at competing against some of the best-in-class companies at the moment. Can you just remind us how quickly do you think you will get to that point where you have that confidence? And in the meantime, you know, how much further do you need to shrink the portfolio to sort of support profitability?

### Stephen Hester

On marine, I think rating information on a portfolio like marine in some ways isn't very helpful because, if you lapse business, it doesn't show up as rate, and yet that might be even better than rate. And if you increase rates, maybe you're doing the wrong thing, maybe you should lapse it altogether. And so, I don't actually have the latest data to hand but I'm not sure how helpful it is.

And in terms of which bits of marine we're going to reshape, obviously, in the light of the third-quarter performance, that's intensive that's going on now in order to have our strategy in place for 01.01 renewal season. So, I think it's better for us to



update you properly at the year-end than to go off at half cock. But, you know, there's certainly – the marine market, whilst a very large one, is actually many, many, many diverse small segments. And I think that our preliminary conclusion is that we are in too many small segments, and it'll be better to be in less and to cut out some of the smaller segments where we have less depth of expertise. But it's a better question for us to answer I think at the full year.

And in terms of motor, it's not a sort of on-off black-and-white switch as to when our competencies will be at the desired level. But looked at today, I would say 2020 would be the first year that I would expect us to feel confident about expanding the motor book. Now, that depends of course on market conditions whether we even then want to expand it or not. But I would think we'll be trying to consolidate over the – for another 12 months or so. And whether the book goes up or down in the next 12 months will be a function of whether the market gives us what we need in the near term rather than us thinking we're now ready to go out and play with the big boys.

### Ben Cohen

Right, thank you very much. Thanks.

### Operator

We're now over to the line of Dhruv Gahlaut at HSBC. Go ahead, your line is now open.

### Dhruv Gahlaut

Good morning. Thanks for taking my question and apologies if the signal is bad. I just had a couple of questions. Firstly, listening to the commentary in terms of rates in Canada and Scandinavia, in terms of good momentum on pricing, I appreciate that through the cycle, you could still be at the current indication level on the combined ratio, but is it possible that you might do a better result for the short term? Number one.

Following on the UK, given what you've seen in terms of results today, would you say that the – as in would you change the 94% ambition you have for UK or would you delay when you achieve that ambition?

And lastly, if I could just follow up on UK as well, you gave in terms of what you're carrying as rates in home business of between 7% to 10%. Could you update what you're carrying for the other lines as well in terms of pet, etc., just to get an idea of where the book is? Thanks.

### Stephen Hester

I'll ask Scott to take your last one but on your first two, I don't think there's anything particular going on in Scandi in rates that's unusual. So, in that sense, I don't see any – you know, I mean, obviously, everyone knows our objective in Scandi is a combined ratio of better than 85. Clearly, we got that. We didn't get that in the first half. We got that in the third quarter. My guess is our ambition will be to be there or thereabouts next year, although I don't yet have a plan for next year in a formal sense because that kind of happens in the first quarter. But I don't see – and clearly, you have, you know, natural volatility that could take you above or below that whether that's weather, large or PYD.

In Canada, the market is hardening quite nicely as everyone responds to challenges, not just in the motor lines but on the property line and even in commercial. And that is allowing us to rate harder without losing volume in the way that we are doing in the UK. And so, looked at today, I would say that our attritional loss ratios in Canada next year as a result of that rating are likely to be better than we had originally thought.

However, we're also likely to assign a higher weather loading in Canada than we originally thought, which is the reason we're rating harder. And so, I'm not sure that we would expect our Canadian profitability to be better. But hopefully, we are – the market is allowing us to rate hard enough to absorb a higher weather loading. Now, whether we'll need a higher weather loading or not, who knows, but we are not feeling that we can assume that this year was a complete one-off in that regard.

On your second question on our combined ratio ambition, I mean, you know, the better than 94 for the time being seems to us to be a best-in-class number when you look across commercial and personal lines. Obviously, there are different players in different places. And so, if we can perform at levels equivalent to a composite best-in-class, you know, Aviva, we're somewhere close to that, although to be fair, they don't allocate all their costs into their UK business, so it's slightly flattened. But I think that that's the right ambition. But I would say – as I have said at the half-year and last year, that it seems likely that the UK will be the last of our territories to get to best in class, assuming we do anywhere as it were, but in our ambition, and I think we would be, you

know, a few years out from that goal in the UK. Scott.

### Scott Egan

Yeah, Dhruv, I think your last question was around sort of UK rates beyond which I've talked about. I think we're really talking about some of the more general commercial lines. I think my comment would be we continue to carry on average low mid-single-digit, obviously recognising that the commercial markets remain competitive and tough, I don't think just for us but for everyone. Obviously, my caveat is always, where we need to carry higher rate, we will. And as always, specific segments and specific areas, we will carry more. But I think as a general, it would be low mid-single-digits which is what we said at half year.

### Dhruv Gahlaut

Thanks. Thank you.

### Operator

Okay. We are now over to the line of Frederic [inaudible] of Chilton. Please go ahead. Your line is now open.

### Frederic

Hi, sorry if you might have answered partly the questions, but could you give the breakdown of the underwriting losses by segments, like higher weather, large losses and attritional claims, just so that we can put numbers on what is exceptional and what has been an underwriting – or underlying, I should say, change of trend within the UK and London.

### Stephen Hester

Well, yeah, we have partly said it before, but I'll try again. I'll give you the breakdown then one can debate what's repeatable and what isn't. So, weather in the third quarter in the UK was about £30 million higher than our plan. Large losses was about – we're about £35 million higher than our plan. Then attritional losses would've been £10 million to £15 million worse than our plans, and as it happens PYD was £10 million worse than our plan as well. Now that adds up to more than £70 million because obviously we normally would have expected to make a profit in the third quarter, and we made a £70 million loss. And so, the actual swing, relative to what we expected, is probably more like, you know, £90 million or so pre-tax or £80 million post-tax, you know, 8p a share kind of thing.

Now, of those elements, the – what is recurring depends on whether one thinks that any part of weather and large losses is a trend rather than volatility. We think the overwhelming majority is volatility but, you know, we don't want to be complacent, and so we're certainly going to take some actions. I think the actions are less going to impact weather but there's some actions to try to improve our luck in terms of volatility in large losses. So, will our large loss plan for next year be substantially lower than this year? Yes. Might it be slightly higher than it might otherwise have done? It might be. We're not yet able to say that.

And then on the attritional I think a chunk of the attritional – some of the attritional is one-off in nature. Some of it we will capture in accelerated management actions, whether pricing or portfolio action. But some of it will be through into next year because that's the way the earn patterns work. So, I can't give you a really good number for next year and not least obviously it's important for us to go through the fourth quarter which will give us more information on whether there are trends that we've seen the beginning of or whether we've seen random volatility. So, you know, we just can't be as precise as we'd like inevitably. Of course, insurance, you know, is a volatile business in some regards and that's a challenge that one will always have.

### Frederic

Thank you.

### Operator

Okay, we're now over to the line of Oliver Steel at Deutsche Bank. Please do go ahead.

### Oliver Steel

Morning. Actually, I was going to ask a similar question about the combined ratio breakdowns. So, I just wonder if you could then comment first of all on the expense ratio in the UK.

And then you're coming back to the reserve releases being worse than expected. Okay, only £10 million, but you said right at the start that in the last week you've been carrying out a reserve review, and you sort of seemed to imply that that was part of the

reason for the poor third quarter result. So, that's the second question.

And then the third question is, how much of the – will all of the UK and International loss be applicable to get a tax offset from your tax losses?

### Stephen Hester

I'll ask Scott to answer both your questions, but on the reserve, there always is quarterly volatility on PYD. So, we said the Group as a whole had PYD in the third quarter in line with the first-half trends. And so, at a Group level, there was no particular surprises in PYD. Indeed, the first-half trends were higher than we planned, and the third quarter was higher than we planned. But in the specific regions, the UK was weaker. However, if we took the UK as a whole, we're on plan for PYD year-to-date in the UK, it's just this quarterly variance which one doesn't know until the end of each quarter.

Scott, do you want to take the other two?

### Scott Egan

Yes. Two other things, Oliver, just on your cost programme, obviously at an aggregate level, our cost programmes continue to target a controllable cost ratio of less than 20%. I think quarter-on-quarter, you know, various movements, but broadly stable in the UK specifically quarter-on-quarter, albeit with an ambition to continue to target further expense pounds cuts.

With regard to your tax losses, yes, they're qualifying and so, yes, they'll count. I'd prefer profits to be able to use them.

### Stephen Hester

And obviously the bad news is that our UK tax rate is the lowest in the Group, so you don't get as much shelter as we would do if it was somewhere else.

### Scott Egan

As I say, I would prefer the profits, Oliver, to be able to start using those tax losses.

### Oliver Steel

Sure, thank you.

### Operator

Okay, before going on to Iain Pearce at Berenberg, if anyone has any further questions at this stage please do press 0 and then 1 on your phone keypad now. And while waiting for any final questions, I'm over to you.

### Iain Pearce

Thank you, morning everyone. Just two questions from me. Firstly, on the subsidence claims, could you just give us a bit of a view on the sort of timing of these claims? Are they imagine – I'd imagine they're sort of more back-end loaded in the quarter. And what the risks are going into Q4 of that trend continuing? And also, if there's any reinsurance protection you have in relation to subsidence in particular.

And then on the pricing environment at Lloyd's. There's been quite a lot of noise about, you know, increasing discipline and management trying to put a lot of pressure on the worst-performing lines and the worst-performing syndicates. I'm just wondering what your view is on that and if you think that will support you getting some of the rate through that you're trying to achieve without losing the volumes. Thank you.

### Stephen Hester

On your second – on your second question, we hope so, but we won't hold our breath. And Scott, do you want to deal with the first?

### Scott Egan

Yes, just on the subsidence point, Iain. I think, look, by a generalism, subsidence claims always take longer to come through in general anyway. Obviously, you know, spotting a crack appearing in your home is somewhat different to walking home and spotting a burst pipe. So, the tail on them is always slightly longer, and that's really why I was making the point that we would

expect to see a tail in those going into – going into Q4. Being very specific, it doesn't count for our Group aggregate cover in terms of reinsurance, i.e. it's not defined as a weather event.

### Iain Pearce

Okay, that's great. Thank you.

### Operator

Okay, the ultimate question for today is back to the line of Ben Cohen at Investec. Back to you, Ben, your line's now open.

### Ben Cohen

Hi, thanks very much. It was actually just to follow up on the subsidence. Could you maybe just put, sort of, this summer into a longer-term context to give us a sense of, if you like, how much of that – of that weather loss is, sort of, you know, bad luck against a long-term average? And I suppose the other part of that is, you know, how much repricing do you need to do for subsidence, if any? Thanks.

### Stephen Hester

I think the last bad subsidence year was more than a decade ago in the UK. And so, I doubt that we will see a pricing impact from it.

### Scott Egan

And I would categorise, and I would caveat it slightly on what we've seen so far, is it's not categorised, Ben, as a major subsidence year, but what we're seeing is some subsidence, yes. And so, I completely support what Stephen said. It's not, in my view, at this stage, a pricing event. It would sit within our normal expectations.

### Ben Cohen

Right. Thanks very much. Thank you.

### Operator

So, I do apologise, we do have another final question. That's finally over to Will Hardcastle at Citadel. Please do go ahead.

### Will Hardcastle

Morning guys. Just on the GVC cover, I mean, this is to a degree why people buy these protections. Just what would be the normal level of large losses that you'd expect to bear on your own balance sheet in a fourth quarter that should in theory now just be passed through to – via this protection?

### Stephen Hester

It varies between zero and £70 million in the last four years.

### Will Hardcastle

Thank you.

### Operator

Okay, as that was the final question, may I please pass it back to you for any closing comments at this stage?

### Stephen Hester

Well, thank you very much for bearing with us. Again, sorry to spring a Friday morning call on you. Hopefully we've given you the information that we're able to. As I say, I believe that most of the bag to prize[?] is volatility, but there certainly is stuff we have to work on. It certainly is taking us longer to improve that part of our business. On the other hand, the great majority of our business seems to be in pretty good shape, which is our international businesses, and we'll plug on in all parts trying to get better. Thanks for listening.

### Operator

This now concludes today's call, so thank you all very much for attending, and you may now disconnect your lines.