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RSA

2018 Preliminary Results Presentation
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RSA

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Business Review

Stephen Hester, Group Chief Executive
Good morning. Thank you very much for joining us all. The format of this morning will be exactly as normal. I will go through a few things. Scott will go through the numbers and then we'll do Q&A.

A number of my colleagues, as always, are here, mostly on the front row. And I'd like to pick out in particular Charlotte Jones who you will have read is becoming our new CFO. We've managed to get an upgrade in my view [Laughter] and so she's here to see what she can improve upon next time. Welcome Charlotte.

So just running through the headlines, which most of you will have already seen. At the headline levels are pre-tax profits are up 7%, our dividends are up 7%.

But the underlying results are down for the first time since 2013, driven essentially by higher weather costs and by large loss challenges in our Commercial Lines businesses. And so that gave the underlying earnings per share of 34p and the underlying return on tangible equity of 12.6%.

I know lots of financial institutions that would die to have a 12.6% return on tangible equity but obviously we aspire to do better and intend to do better.

Capital positon is in good shape which we'll talk more about. Both in relation to Solvency II and the pension settlement and we continue to have an impressive record of improving competiveness in cost terms.

We also are today, hopefully not surprisingly, reaffirming all of our key targets. We, notwithstanding the disappointments of last year, believe that our business is capable of doing exactly the performance that we believe it was capable of doing in the past; we've just got to make that happen of course.

And it's worth saying, although we'll spend most of our time today on the things that we need to particularly improve, that right across the Group there are many, many things going on that are making us a better company, a more competitive company and capable of higher performance in the areas that we've talked about before relating to customers, underwriting and cost.

We will talk about the results in part regionally but in part also drawing a distinction between Personal Lines and Commercial Lines. And our Personal Lines businesses are in pretty good shape although of course they did take a weather knock last year but fundamentally in pretty good shape.

The principle issues for us in terms of last year's performance that we need sharp corrections to, were the Commercial Lines which you can see had a negative combined ratio overall.

We have taken a lot of action, we've announced a lot of action and we'll go through that with you. And two of the, if you like, the headline pieces of that action, the exits that we've announced in our London Market business and some new reinsurance programmes we'd taken out. Had those been in place a year ago, of course they weren't, our earnings per share would have been 42p, which is about the same as last year, if you adjust for FX. And that's despite the rest of our business being hit by weather and large losses away from the exit portfolio. So I think it gives us a platform to build higher from.

Let's just then run through if you like in more detail some of those elements. And as I said I think the key feature from our standpoint was disappointing underwriting results last year. And as I mentioned that was partly weather above its normal trends and partly Commercial Lines and especially London Market losses. Which of course is a market wide phenomenon, not just us; we were hit maybe harder than some because of our concentration with in the London Market on Marine which was probably the worst area but be that as it may.

Away from those two issues which we'll come back to, we believe that the overall strategy is valid. Both when we look at our own operating plan and we look at the best in class competitors in each of our markets we believe that both of those things support our targets and our ambitions.

And we also would note, and you'll see it in the slides, that if you go back over the last five years, in what I'd call repeatable competitiveness both in terms of expense ratios and attritional loss ratio we have improved the fundamental competitiveness by 7 or 8 points of combined ratio. Which is, I think a really, really important platform from which we need to build and get a better job done in terms of our volatile items.

And so in response to the challenges, what are our responses? Our basic response is we're sticking to our road map, we're sticking to our plan and our strategy and we intend to keep improving the company.

But we are on top of that taking specific action, have taken specific action to address the areas of particular weakness that we saw last year. That's around portfolio exits, additional reinsurance purchases we'll talk about, we've made management changes. If we take the UK obviously there's Scott who will now run the UK but we also have new heads in the last year of both our Commercial Lines businesses and a new underwriting director in the UK.

And then in the rest of the company, because Commercial Lines underperformance was not just London Market, although it was mostly London Market, there's a whole bunch of other things happening on repricing and re-underwriting, what you might call an intense business as usual manner.

I won't dwell on the next two slides, but simply to repeat, this is our strategy and this is the basis on which we are trying to build our performance.

And it remains the case, clearly the slides don't change by very much year on year, that RSA has got a well-balanced business; roughly 60% Personal Lines, 40% Commercial Lines. Well balanced by geography, clearly Scandinavia likely to be, over the medium term, half or so of our profits and by distribution channel.

And as I also mentioned this slide is again one we show every year, but simply because while it may not be eye catching there is a permanent amount of intense activity throughout our company trying to improve what we do. Bucketed around customer service, underwriting and cost efficiency and that continues apace.

So now walking through if you like some of the key indicators in those three areas, on customer what I would say is as follows. When we are happy with the P&L we have shown the ability of making our customers happy too and growing our business. When we're not happy with the P&L we've also shown the determination to reprice, re-underwrite and exit which has the opposite effect in terms of customer volumes. But we think that that's the right orientation.

And so you'll see by and large we enjoyed customer growth in volume terms and also in retention terms in the Personal Lines areas where the P&L was good. The one exception being the UK where we were repricing mostly in household for attritional weather losses last year, with some success.

And in Commercial Lines where we've been struggling, we've been taking action in reflection of that struggling and you'll see that in the volumes.

So I think we are comfortable that when we want to appeal to customers, by and large we do appeal to customers and they do like doing business with us. And we do enjoy very good relationships and good qualitative ones as well as quantitative ones.

It remains the case that cost is a fundamental and repeatable driver. And I think we continue to do a good job on that and you can see that track record has continued into 2018.

The bumps in the road tend to be when the top line adjusts faster than the cost line. That obviously happened in the UK last year and indeed will happen through the London Market exits next year in the UK. But fundamentally I think that we are closing in on, and capable of, getting to our targets on cost, and that's a really important element.

The attritional loss ratio broadly now has been flat for the last two or three years, having improved dramatically from the levels of 2013 and before. That's not bad, and indeed I think the potential in order to get to our best in class level for attritional loss ratio is not huge from here. But I do believe that there's something like 1% to go for on attritional loss ratios, whether we get all of that next year or whether it takes us a couple of years but it's that sort of order.

And you can see in particular last year, although we had a broadly flat level in total, Personal Lines came down and Commercial Lines went up. And that was part of the underperformance of Commercial Lines that showed itself more in large losses and weather but some in attritional. And so in particular we need to correct that element.

So just moving, as I say, into just showing you a cut by type of business and then we'll move into the regions later. Our Personal Lines businesses are about 60% of the Group. You'll see the geographic spread here, and I would say best in class performance levels would translate to about a 90% COR given our makeup. You'll see, in fact we did 90% in 2017, it was higher last year, that's entirely a weather matter. If we get normal weather patterns I think we can get back to 90% or thereabouts.

Beneath the covers of course there are more complex stories away from those big generalisations. But I'm pleased to note overall we grew 5% in Personal Lines and that growth was driven by our most profitable areas, particularly in Scandinavia and our direct business in Canada, Johnson.

There are challenges in Personal Lines, Motor is a challenge for most places in Personal Lines in terms of claims inflation, and of course weather has produced challenges; in particular in Canada. Therefore where needed we continue to rate and in particular in Canada. Canada is probably the hardest of the markets that we participate in, everyone is rating up and we're doing so too.

I think it's worth noting, I suspect we will be the second best performer in Canada this year even though our performance is down. Intact will be the best I would imagine. If we look at the Auto line which they've talked about, Intact's combined ratio in Auto was 100 last year, ours was 99. They will probably improve a bit faster than us this year. I think we should be better than 99 but not in our target level.

We are more Property weighted than they are, they are more Auto than us, which is why in a bad weather year we tend to go down by more than them and in a good weather year we will go up by more than them. But they represent the gold standard that we would aspire to in Canada.

Commercial Lines obviously as we've discussed is where we had our headaches last year. And you'll see the geographic breakdown on the left and of course a chunk of our Commercial Lines businesses is what we would call, international business, even though we badge it under the UK and International division. And there you'll see the combined ratio of 102. That was driven year on year by large losses but given that 2017 had a very heavy weather penalty, weather didn't get any better from 2017. So relative to what you'd normally expect, there was also a big weather component, you'll know that last year I think was the fourth worst year on record for what we call global weather events, you know hurricanes and so on. And we've seen that in the international bits of all other reporters.

So a lot of this was market orientated but nevertheless gave us more volatility that we wanted to have. And so we've taken a bunch of action, we'll go through those actions in terms of portfolio exits and reinsurance and away from those are lots of BAU action which I've mentioned in terms of pricing, re-underwriting business and management changes and so on and so forth.

And you'll see there the proforma COR which is just proforma for exits, I hope we can do significantly better in COR from our other actions as well.

So going through the big actions portfolio exits, we've put here the London Market business which was £300m if you like when we started the surgery, should end up about half that level. I say about half because with Scott having just come into the UK he obviously has a right to decide whether he wants to draw the line precisely where it was otherwise going to be drawn. And so we'll report back at the half year if that changes.

But broadly at the moment the plan is to halve the size of our London Market presence and you'll see broadly the areas that, that is taking place in. And you'll also see the impact that would have made on the combined ratio, of course even after those exits last year would have been a loss making year in the London Market reflecting the overall international environment. Although it may be that we can make underwriting improvements that would do better than that, that are not exit portfolios but are capability improvements.

Away from those exits, the main exits in the London Market, there's a few other exits. We have over the last three or four years been eliminating, what we call, generalist MGA schemes in the UK. There was about £80m done over the years ’14 to ’17, another £65m to complete that process going through in ’18 and ’19. And for the purpose of the proformas those exits, those generalist exits, we’ve added up to the London Market ones to give you the pro forma.

In addition to that we are exiting an element of our renewable energy business booked through Codan in Denmark, which is our ‘Interconnector’ Business Lines which lost us £34m last year which is why Scandi had a poor second half. We will exit those, we won’t write any more business in those. We’re not including that in our proformas just for the sake of record so you can decide if you want to include it or not.

And then there’s a bunch of other things that we’re exiting in our European branches, again we haven’t put those in the proformas because those are, if you like more surgical and individual in nature. But we announced yesterday for example exiting Germany which is a relatively small business for us anyway.

On top of the portfolio exits we have made some changes to reinsurance. The change that we made a few years ago, the Group Volatility Cover, has served us well and in the last two years we’ve indeed called upon it.

But what we experienced last year was an unusual amount of volatility in losses that fall above £1m and below £10m and the GVC has protected us above £10m. Normally those have evened themselves out and they probably will normally but they didn’t last year. And so we felt motivated to buy some more insurance in the below £10m and so in each one of our three regions we now have aggregate covers, you can read the detail at your leisure, which should dampen volatility in the sub £10m and would have saved us net of the premiums we were paying to get it, about £30m last year. Although in a normal year we wouldn’t expect them to kick in because we’d expect our larger weather experience to be better.

So moving away if you like from that lens, let me just update on a regional lens. And clearly Scott will do this more thoroughly in terms of the year’s financials.

Scandinavia remains, in my view, a jewel in our crown. Although the combined ratio was worse than 2017, it’s still strong. If you average ’17 and ’18 you get results that are in line with best in class in Scandinavia. And importantly, what I'll call the fundamental improvement of our competitiveness which has been driven dramatically by the controllable expense ratio continues to march very pleasingly in the right direction.

And so, the powerhouse of our Scandinavian business, as indeed, other people's Scandinavian businesses' Personal Lines, that had an excellent year last year both in terms of growth and profitability.

What held us back last year was Commercial Lines. We've talked about the exits. There was one fire we talked about in the first half which, I think, is the first ‘more than £10m loss’ we've had in the last five years which we think is random volatility, and we've got a reinsurance aggregate cover.

So, our view is that our combined ratio ambitions for Scandinavia, that Scandinavia is there or thereabouts, and, in normal years, should be operating at or around our combined ratio ambitions, touch wood, of course.

In Canada, again, clearly a disappointing year in financial terms, and I think you'll see that in all Canadian results.

The aggregate cover, which we didn't have last year but we'll have going forward, would have saved us roughly 1% of combined ratio as you'll see. But, basically, by far the biggest delta year-on-year was that it was a bad weather year in Canada, and we are a little bit more weighted to Property and a bit less weighted to Auto, as I mentioned earlier on, which accentuated the relative movement for us versus, for example, Intact.

I think that we are making very good progress. You saw good growth in Canada. We're very pleased with the Scotiabank deal which has started writing business in a small way, but we'll start ramping up in the second quarter.

Cost continues to be an outstanding achievement in Canada, as you can see there. And so, I would say our main issues in Canada are to take advantage of the hard market and make sure we are rating hard. Part of that is because we want to get motor combined better, as everyone does that's constrained by regulatory pricing, but, nevertheless, good price increases are going through. Part of it is because, on Property lines, we want to be able to absorb higher weather charges. In other words, our planning assumption going forward for weather is higher than in the past and, therefore, we're trying make room on the attritional loss ratio line to fund some of that.

And then, in Commercial Lines, although there aren't, if you like, segment exits, there is very aggressive re-underwriting activity going on in certain bits of the Commercial Lines area, not just us, I think market-wide, which I believe will produce improvements.

So, again, I think our view of Canada is that we are maybe not as comfortably at or around our best in class potential as we are in Scandinavia, but we're pretty close to it provided that the bounce back that we're expecting this year happens. Obviously, we don't control the weather but, certainly, in Commercial Lines, we need to see evidence, and we need the pricing increases to help us out on the attritional lines, which we believe they will.

And then, finally, the UK and International. Of course, the headline on the slide on the left will show you actually that we have, contrary to sometimes the way we feel about it, improved the business but not as much as we expected to do. And the business really - and, obviously, Scott can speak to this in Q&A a little later to the extent that we want to delve into it - about 75% of the business is domestic, which, actually, made a small profit, underwriting profit last year, and the underwriting losses all came from the International component that we book in there, although some bits of the International Component, Ireland and the Middle East, had exceptionally strong results and, hopefully, illustrates the progress that we made particularly relative to Ireland in recent years.

Personal Lines was held back by weather, something like 4.5 points held back, but the key things that we were trying to achieve last year in terms of pricing to get over the escape of water issues and household attritional and, indeed, similar for pet, those attritional loss ratios have improved at least as much as we hoped. I think may improve further this year as that action feeds through still into this year. And so, our primary headache is Motor which, fortunately, is the smallest of our businesses in financial terms in Personal Lines, and, obviously, we need to keep working on that.

Commercial Lines, even away from the London Market, although the domestic Commercial Lines business was nicely in profit, not at our targets, it doesn't require huge amounts of pricing action, but it does require selected underwriting actions which are going through.

I think costs would have fine were it not for the top line shrinkage. And so, over the next two or three years, we need to figure out how to catch costs up with the top line, but there will definitely be a lag, and we have, needless to say, high hopes of Scott to help us in all of these areas.

And so, when I, if you like, sum up all the three regions, we have left our combined ratio ambitions intact, in part because the markets suggest that those are, indeed, best in class performance ambitions, in part because our own assessment of either where we are or where we can get supports those ambitions. But, just as I said a year ago, we think we're pretty close in Scandi and Canada, and we're less close in UK and International in terms of the likely timescales for accomplishment of those things. And, obviously, all of this is subject to the normal caveats around volatile items which we don't control.

So, with that, Scott, over to you.

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Financial Review

Scott Egan, Group Chief Financial Officer
Thanks, Stephen.

Good morning, everyone. I hope you can put up with me one more time because, as Stephen said, you get an upgrade to Charlotte. So I will try and do my best and, obviously, be best in class on my last ever presentation as CFO.

So, before we dive in, at headline level, we're obviously reporting today EPS up 21%, dividend up 7%, and a return on tangible equity of 12.6%.

However, as Stephen has said, beneath the headlines, underwriting profit, reduced by a third, and, while half of this was down to adverse weather, we're disappointed to be reporting the first down year since 2013.

This translated to a reduction in underlying earnings per share from 43.5p in 2017 to just over 34p in 2018, with sterling strength presenting a headwind of around 4% year-on-year.

Our Personal Lines businesses were performing strongly overall, and premiums are growing in the most profitable lines. They represent nearly 60% of the Group's premiums, and delivered an excellent combined ratio of 92.4% despite an increase in weather losses year-on-year of £88m, or nearly 2.5 points.

Commercial Lines across all regions had a challenging year, partly due to higher large and weather losses, but also where we could have underwritten better. Our top line is contracting, as you've seen, as we take the remediating actions.

So, in terms of the normal slides, I'll start with an overview of the numbers before going through the P&L and capital in a bit more detail.

Group Net Written Premiums are up 1% on an underlying basis, with growth across our Personal Lines businesses, partly offset by lower premiums across Commercial.

I've mentioned that underwriting profit of £250m was down 33%, or £127m, at constant FX. This was due to around £76m of adverse weather and higher large losses in Commercial Lines.

On a proforma basis, adjusting for UK portfolio exits and 2019 reinsurance changes, underwriting profit was £344m. This gives a sense of the scale of the actions we've already taken to address the UK challenges in particular.

Operating profit of £517m was down 19% at contact FX due to the lower underwriting profit and a slight decrease in investment income due to the continuing low yield environment.

Profit after tax was up 16% due to the absence of restructuring charges, lower interest costs and a lower effective tax rate translating to the 21% increase in headline EPS with underlying EPS down 19% at constant FX. On a pro forma basis, this would have been circa 42 pence and in line with 2017 at constant FX.

A return on tangible equity at 12.6% is slightly below our target range of 13% to 17%.

And, finally, TNAV was up 4% with profit after tax, partly offset by fair value mark to market movements, investments in intangible assets and, of course, dividends.

I'll now go through some of the areas in a bit more detail, starting with premiums.

As we did at half year, we prepared this slide excluding the impact of the 2018 reinsurance changes, allowing you to compare on a like-for-like basis.

Total premiums were up 1% at constant FX, and we're pleased to report top line growth in all regions in Personal Lines, while Commercial lines, as I've said, is down largely in response to underwriting and pricing actions. In other words, we're up where we're most profitable and we're down where we're taking action.

Briefly walking through each in turn, and starting with Scandinavia, the positive trends in Personal Lines have continued, with premiums up 6% at constant FX. Retention remains strong at 82% despite rate being ahead of both last year and our plans.

Personal Lines premiums in Sweden, our most profitable business, we're up 8%, while policy count grew 2%.

In Denmark, motor premiums were up 4%, and policy counts grew 2%. And, in Commercial Lines, premium and volumes were down as we rated ahead of last year. And, specifically in Denmark, premiums contracted by 2% as we took underwriting actions, mainly in our Property and Technical lines.

Turning to Canada, Personal Lines premiums were up 6% in 2018, with Johnson delivering organic growth of 4%. Retention remained at best in class levels, with Johnson and Personal Broker at 90% and 89% respectively.

In both Auto and Household, we carried rate above our plans and last year, however, recognising there is more to do on Auto.

In 2019, we're targeting somewhere between 6% and 9% of rate across our Auto business, varying, of course, by province.

Commercial Lines premiums grew by 3%, and we carried rate of circa 5% in a currently hardening market, particularly in the more recent months.

And, finally, Personal Lines premiums in the UK were up 4%, with policy counts up 2%.

Household premiums grew 16%, driven by our partnership with Nationwide, which generated premiums of around £170m in its first full year of trading.

Top line contracted on the wider Household book as we rated to mitigate the escape of water issues which we presented in H2 last year. Along with our claims management actions, this reduced the attritional loss ratio by more than four points in 2018, and we expect further gains in 2019. We, therefore, now expect a return rate to more normal levels.

In Motor, premiums were down 10% as double-digit rate impacted retention and new business in a competitive market.

And, finally, on Commercial Lines, premiums were down 6%, mainly due to our exit from the remaining generalist MGA schemes, underwriting decisions on some large individual risks and the start of the Speciality and Wholesale exits we announced in November. This has been well-covered by Stephen in his slides, so I'll now turn to the underwriting results.

The Group combined ratio was 96.2% for 2018, up just over two points. Volatile items were around two points worse than last year, with weather accounting for half of this. On a pro forma basis, the combined ratio was 94.6% despite the weather challenges and large loss volatility in the Commercial Lines portfolios.

The attritional loss ratio was broadly flat when adjusted for 2018 reinsurance changes.

Increases in Scandinavia and Canada were broadly offset by improvements in the UK and International region.

All regions are targeting attritional loss ratio improvements in 2019.

Quickly looking at the headline underwriting performance in each of our regions; in Scandinavia, the combined ratio increased by just under four points to 86.8%, Personal Lines reported an excellent 78.9% despite lower prior year development, while Commercial Lines increased by around seven points to 97.9% due to higher large losses, which I'll cover in the next slide.

The combined ratio in Canada was up around three and a half points to 97.6% net of GVC recoveries driven by significant weather experience and elevated large losses, partly offset by further progress on expenses. When we proforma for the new 2019 reinsurance, the combined ratio reduces further to 96.7%.

And, finally, the UK and International combined ratio improved slightly to 101.4%, or 97.4% or a proforma basis. UK Personal Lines was up just under three points to 102%, driven by weather, which was just over four points higher than 2017, and partly offset by an improved attritional loss ratio.

While UK Commercial Lines improved by two and a half points to 105.7%, losses remain elevated in our London Market business.

And, finally, Ireland and Middle East reported excellent results again, with combined ratios of 90% and 83% respectively.

Now, taking a closer look at the loss ratio movements - In Scandinavia, the loss ratio was just over four points higher than last year. Large losses were almost 9% compared to a five year average of just over 6%. This was dominated by a specific segment in our Technical Lines business, which we are exiting, and a single large Commercial Property fire loss, which I flagged at Half Year.

We expect more normal large loss trends in 2019.

The attritional ratio increased in Commercial Property and in Norway generally, but it improved in Personal Lines in both Sweden and Denmark.

The loss ratio was up about six points in Canada. Adverse weather was responsible for half of this, and industry estimates put insured damage for the severe weather events of 2018 at just under $2bn, which would be the fourth higher loss yet on record.

Higher large loss, particularly in Property classes, contributed 1.7 points to the loss ratio.

And, finally, the attritional loss ratio increased by just over a point, and reflected mid-size losses in household and commercial auto claims inflation.

Lastly, the UK and International loss ratio was just over one point better than 2017. The attritional ratio improved with UK Household down more than four points. Large losses also reduced, although they remain elevated, as I've said, in the London Market business.

These improvements were partly offset by adverse weather. The UK and Ireland, if you remember, experienced the Beast from the East at a cost of around £50m, and the hot and dry summer weather in the UK produced an increase in subsidence claims.

Very briefly turning to the volatile items - I've mentioned that they impacted us negatively by just over two points. I've covered most of the items in this slide so I won't repeat them again, but just a quick comment on prior year development, at 2.6%, it was broadly in line with last year, and, as usual, was widely spread across accident years and lines of business.

We continue to plan on PYD at roughly half this level, although, as always, I'm very happy to accept when it that turns out to be conservative.

Turning to costs, we continue to report excellent progress in costs, beating our target of more than £450m in savings since 2013, a year early.

Controllable costs reduced by 4% compared to last year, gross of inflation, with the controllable expense ratio now down by over four points since 2013. Our target remains to get this below 20% for each region.

Two specific regional comments - Firstly, in Canada, an already low cost ratio improved again as savings in staff costs, linked to productivity improvements, more than offset higher software amortisation costs.

While the controllable cost ratio is expected to remain below our target level of 20%, these higher software amortisation charges, linked to our investment in Guidewire, will increase it slightly in 2019.

Second, as flagged at Half Year and Q3, the UK and International controllable cost ratio increased. This was as a consequence of premium contraction as we take pricing and underwriting action to improve performance. For these reasons, we expect the ratio to increase again in 2019, and for that to modestly increase the Group ratio as well.

We remain focused on right-sizing the business and catching up with progress in the coming years.

As I've said on here before, our focus and mind-set for costs across all regions is now on continuous productivity improvement.

On investment income, no change to our investment strategy. The portfolio remains dominated by high quality fixed income, with around 90% of our bonds A-rated or above. An investment income of £322m was below 2017, but slightly higher than our guided range.

The average income yield was 2.3%, while the average reinvestment rate and the bond portfolio of 1.6% was marginally up on last year.

Based on current forward yields and FX, we're forecasting investment income in the range of £285m to £300m in 2019, up slightly on the projections we made a year ago. 2020 and 2021 are also included in the slide for your information.

And a final word on pull-to-par - you'll see from this slide that we expect the pull-to-par element and unrealised gains to largely unwind by the end of 2020, with a capital impact of around £60m in 2019, completely consistent with our previous guidance.

Moving onto non-operating items - no new news here. Interest costs almost halved following the debt restructuring actions of the last two years. Other non-operating items largely fell away as planned, so earnings flowed more cleanly to the bottom line.

And, finally, the effect of tax rate reduced to 23%, reflecting, really, the profit mix, and our guidance remains unchanged with underlying tax rate of around 20%.

Turning now to capital and pensions, and starting with pensions - We're pleased to have successfully concluded our triennial evaluation process for our UK schemes. The Group has committed to continue paying contributions of £65m per annual with a further £10m per annum top-up subject to our capital ratios. We expect to continue paying at this level until the schemes are fully-funded on a lower risk basis.

In addition to the regular contributions, the Group made an additional one-off payment over December and January of around £65m, with the majority of it being paid in December.

All else being equal, these additional payments would bring the deficit level to around £400m.

Turning to capital, our Solvency II coverage ratio of 170% at year end is a record, and up 7% from the end of 2017.

On an IAS 19 basis, which we use, of course, for accounting and capital ratios, the £88m pension deficit at the start of the year become £182m surplus by year end. This was mainly due to spread movements, longevity improvements and, of course, contributions.

We generated 22 points of capital from earnings during the year. Net capital expenditure and bond pull-to-par accounted for eight points, while dividends accounted for 12 points.

Market movements drove five points of the increase in our coverage, which, although in our favour, should always be seen as more volatile. This was driven in large part by widening credit spreads improving the pension positions, as I've already noted.

And, as a reminder, Solvency II dictates that you can only include pension scheme surpluses up to their marginal share of the SCR. Beyond this, we cannot include them in the ratio, but they are there, effectively, as a shock absorber for future market movements before impacting the ratio.

At year end, one of our UK pension schemes was at its cap, and the other was close to it.

This is also important from a rating agency capital perspective, from which all surpluses are excluded.

And, finally, you can see that our capital quality has improved, with a Core Tier 1 coverage increasing by nine points to 107%. This is important because, as you know, we regard the Tier 3 capital category as lower quality.

And, finally, on dividends, we've announced today, a proposed final dividend of 13.7 pence, which gives a total dividend for 2018 of 21 pence, and represents an increase of 7% from 2017.

This represents a 62% payout of underlying EPS, and a 50% payout of pro forma EPS.

Our dividend policy is unchanged, targeting 40% to 50% normal payout levels, with additional payouts possible where prudent to do so, and supported by real capital generation.

If we decide to payout above the 40% to 50% range, other than in response to volatility, we would expect that to be decided at the end of a year and executed either through stock buybacks or a special dividend.

So, to conclude, our Personal Lines businesses are performing strongly overall, and premiums are growing in the most profitable lines. Commercial Lines is a key focus with extensive action underway, particularly in the UK. Costs, as always, will be a focus, particularly in the areas where underwriting actions are reducing business volumes. And we're pleased to have reached agreement on a more stable long-term funding plan for the main UK pension schemes. All of this is underpinned by a strong balance sheet.

Our ambitions for the Group are high and unchanged, and we look forward to delivering good progress against them in 2019.

Thank for you for that. I'll hand back to Stephen.

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Questions and Answers

Stephen Hester, Group Chief Executive
Thank you very much, Scott.

So let's go straight into Q&A. And if could, obviously, wait for the mic to be delivered and then identify yourselves. We'll start up here.

. . . .

Andy Sinclair, Bank of America Merrill Lynch
Thanks. Three from me, if that's okay.

Scott, you're clearly moving from Group CFO to Head of the UK, just wondered if you could give us your thoughts on what you're looking at there?

. . . .

Stephen Hester, Group Chief Executive
This wasn't faked, by the way, but we were prepared for that question.

Laughter

But he'll talk to us in a second. Give us your own other two and then…

. . . .

Andy Sinclair, Bank of America Merrill Lynch
That's a little bit embarrassing on my account.

Secondly, okay, with your UK hat on, I wonder if you can talk a little bit specifically about London Market, its makeup and size. When does that become subscale? Are you the best owners of that operation going forward?

And, thirdly, just on the reinsurance protection increases, what's the P&L cost of those in a normal year? I realise it gives you the protection in volatile years.

. . . .

Stephen Hester, Group Chief Executive
I'll ask Scott to speak to the slide in a second, but just to pick up on the second two - I think, in terms of the London Market presence, I'm not sure I really think of it very clearly in scale terms because the London Market is made up of many hundreds of very narrow specialist portfolios, and your total size is completely irrelevant, which you can

see the relative success of some quite small syndicates in Lloyds and so on and so forth. It's really what are your specialities, and can you sustain the expertise?

And so that's why our London Market strategy was not to say - Let's cut everything by half - but it was to exit entirely sub-segments so that we could sustain the right level of underwriting expertise in a smaller business because the remaining portfolios aren't necessarily smaller, they're just a narrower range of specialities where we feel we can do it.

So, per se, I'm not worried about size, but it does remain the case that if it doesn't make money we should stop doing it. And, so, clearly, we have to prove that we can, or we have to make some more adjustments.

Can you remind me of your third question as well?

. . . .

Andy Sinclair, Bank of America Merrill Lynch
Reinsurance.

. . . .

Stephen Hester, Group Chief Executive
Reinsurance. Yeah. Reinsurance, I would say in a normal year…

Pause and Chat

Reinsurance will 'net' cost us nothing in a normal year because the extra expense of the aggregate programmes was broadly offset by savings in our main cap programmes where we actually reduced cost.

I'm sorry, not you. No, it's now Scott. Scott, over to you.

. . . .

Scott Egan, Group Chief Financial Officer
So, a little bit here is one we prepared earlier.

So, look, this is my disclaimer point - I'm two weeks into the role. Obviously, I know the business and I really have spent the first two weeks getting under the bonnet, as it were, as opposed to sitting on the roof rack, if that's not a bad analogy, to look.

So, number one, look, there are six areas really that I thought it would be worth touching on when I stood up here today; number one, there is no question, we have to restore credibility both within the organisation and externally on our ability to underwrite well.

And so, number one, number one and number one is to make sure that we deliver on our UK underwriting actions, our claims initiatives, etc, and, in addition to the exits, just to give you a sense of scale, that's well over £100m of actions that we're taking in that regard. And, as I stand here in sort of mid-Feb, we're doing well against that plan, we're running slightly ahead, and, if you remember, because of the way our P&L works…

Pause and Chat

Because of the way our P&L works, we've effectively already earned around 60% of that for 2019.

So, I'm not complacent, but we're absolute rigorously focused on making sure that we follow through and keep the focus on every single one of those actions that we've set out in our plans.

I think the second thing Stephen said, and, again, I don't want this to be dramatic in any way, but I do want to get my hands under the bonnet and have a good look at the sub-segments and stuff that we're in, and I want to make sure that we can align them with the capabilities we have, the outlooks for the market and to make sure that we can, in the end, make money.

I don't want to make any kneejerk decisions because if you remove yourself from a market then I think you have to accept to re-enter that market is much more difficult on the basis that you lose credibility and capability. But I will look to do that in the first few months that I'm here.

I think the third thing is, obviously, as we take top line out, you've seen it in the cost ratio in 2018, and I've alluded to it already, that I would expect the cost ratio to go up in 2019.

Please don’t think, for any second, that that doesn't mean we're not focused on taking cost out and improving productivity. And, you know, that is going to be a focus of the team.

I hope, as a sort of general management team across all of our regions, we've built a credibility and a track record for being able to do that. And so, you know, that's going to be a focus as we right-size the business. But, I think, there's no way it keeps pace with the top line, it's just the way it is.

The fourth thing is I don't want to lose sight - Middle East and Ireland have delivered fantastic underwriting results, and it wasn't too long ago that we were standing up talking about Ireland and the need to improve it. So, I think, two things; one, we've proved we can, it's the second year in a row it's delivered really strong underwriting results, and what I want to make sure is that we don't lose focus on any of those parts of the business while we try and address the more problem areas.

And then the fifth thing is really one of probably culture, mindset, which is I really want to make sure that the UK business is really known for, and respected for, a quality of execution, a focus, an agility and then a pace. The one thing, as I stand here, that I know already is I won't hit the plans for 2019 in the way that I thought because something will happen, there will be something that comes along, and I'm determined, along with the Management Team, to have a mindset of acting quickly and making sure that we can manoeuvre round some of those bumps. And that's really something that I want to be able to stand up here in 12 or 18 months' time and, hopefully, you can feel and see a difference in how the UK goes about its task.

And then, finally, look I'm targeting 96% to 97% combined ratio in 2019. As I stand here, that's not easy. It's going to take a lot of hard work, but I'm absolutely determined with the Leadership Team to achieve it. I think, if we do that, then we establish a platform for 2020, and I think the last part in the slide is I think it gets a credibility, once again, to the commitment to the best in class ambitions of 94%.

So, two and a half weeks in, from the roof rack to the engine, those are the areas. Of course, as we go through any decision-making processes, we'll update you, but that's where I'm at at the moment.

. . . .

Stephen Hester, Group Chief Executive
Fantastic. Thank you.

So, yeah, here at the front.

. . . .

Fahad Changazi, Mediobanca
Good morning. Apologies if I've missed the detail in this somewhere maybe – Thank you for giving the proforma numbers if you exited the business. Can you give an idea about the five year average profitability of the businesses you've exited, or the large loss load?

. . . .

Stephen Hester, Group Chief Executive
In the slide I gave earlier on, I showed the three year impact.

. . . .

Fahad Changazi, Mediobanca
Okay. And the final thing is, could you give an update on your EPS starting with a five, please?

. . . .

Stephen Hester, Group Chief Executive
As soon as possible.

Laughter

I think, you know, as I've said, we haven't budged our ambition, our combined ratio ambitions at all, and so it continues to be the case that I think our business is capable of EPS in the five and then beginning with a six, but what is just a statement of fact is our credibility is less good on that today than it was two years ago. And so we need to make sure that re-establish that credibility, and you can't do that by talking about it. You have to do it by delivering.

So, I think it's most unlikely to begin with a five in 2019 unless we have, you know, luck coming our way, but I think that we're on that trajectory very soon, if not immediately thereafter.

Let's see, at the back there.

. . . .

Andres Van Embden, Peel Hunt
Thank you.

I was intrigued by your slide, number 17 and 16, where you sort of gave a focus of both the underwriting lines, the Commercial Lines and the Personal Lines separately. I just wondered what would be the hurdle of managing all the international Commercial Lines businesses as an integrated division under RSA with a separate management team, and a clear focus per underwriting class it were rather than a focus on the regions? Thanks.

. . . .

Stephen Hester, Group Chief Executive
Thank you for that question. I know you wrote a report with that thesis.

I think the first thing I'd say is that, from an underwriting standpoint, we do try to have a global as well as a regional form of management, and Nathan Williams, who's here in the front, is our Group Underwriting Director, and has a staff of people centrally in a network globally, and all of the underwriters around the world have a dual line of reporting to Nathan as well as to their regional management structure. And that is so that, in those areas where there is commonality, it might be commonality of types of risk or commonality of standards of underwriting and training and things like that, we can do it in the same way.

That said, I believe the inherent strength of our business is that we are rooted in regional markets and, therefore, not exposed to the full blast of competition from the, you know, Allianz's, AIG's, Zurich's of this world who operate, if you like, in the global wholesale lines. And, indeed, maybe one of the reasons why we've done less well in that small part of our business, the London Market business that is exposed to those lines, is exactly that.

And so, when we're writing SME business, or mid-market business in each of our regions, those respond to regional knowledge, trends, client relationships, not to global management. And I think we would actually lose more than we gained if we moved the matrix, but there is a matrix that operates. Thank you.

So, just down here.

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Greig Paterson, KBW
Good morning. Three questions. One is just in terms of your reserving, given the issues you had with the third quarter, I'm wondering to what extent you've done some kitchen sinking in the reserving at the end of the year.

Second question, just in terms of the UK Motor and Telematics, I wonder if you could just talk a bit about - it's problematic about what sort of rate you're getting through, what sort of inflation, sort of, a bit of colour there?

And the third thing it's just - maybe it's my confusion, in terms of the London Market, am I correct in understanding that you're going to take one half, i.e. £150m out, and then you mention the £150m of additional actions. Are you talking about cost savings etc, etc. I'm getting a bit confused. Could you just give us some more colour exactly what you're saying?

. . . .

Stephen Hester, Group Chief Executive
Let me take the first one and then I'll ask Scott to take your next two.

So, we haven't knowingly kitchen sinked anything. We never knowingly kitchen sink it. And so, you know, only the passage of time will know whether the reserves run off positively or negatively, but there certainly hasn't, you know, we haven't made any change whatsoever to reserving practice.

. . . .

Scott Egan, Group Chief Financial Officer
Yeah, so Telematics, Greig, we're putting through double-digit rating increases in Telematics. I think that in direct response to claims inflation that we're seeing. It's why we're seeing a drop-off in some of the volume in our Motor book.

And, in the London Market space, the number I was referring to was in addition to the exits. We're taking a number of actions on putting normal rate through the books. In other words, you know, rate of Commercial Lines and Personal Lines, we're taking underwriting actions, that could be case specific rather than exit if you like, and then we would do a number of what I'd call claims initiatives to try and mitigate the impact of claims inflation because, of course, all of that is gross. There's always an element of claims inflation that you have to sort of mitigate in every year.

So it's that basket of additional measures that we're pushing very hard on, and, effectively, for every single one of them, we've got really detailed plans by line of business, because it varies greatly in that regard.

. . . .

Greig Paterson, KBW
Is that in addition to the profits ...?

. . . .

Scott Egan, Group Chief Financial Officer
Well, you have inflation, of course, and then you have to earn it through. So I think you have to - you know, there's a complicated formula by which you'll then see it in the numbers. But I think what is true, which you've seen from what I've said already, our ambition is to improve the UK combined ration from where it is now to something in the 90s, this is part of that path.

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Stephen Hester, Group Chief Executive
Thank you.

In the middle, here.

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Ivan Bokhmat, Barclays
Hi. I've got two questions. So the first one on the new reinsurance protection that you've bought, how should we think about the normalised weather and large losses going forward, because, presumably, it's coming down?

And, secondly, it's on the pension fund deficit. I think the previous number in 2015 was around £360m on the funding basis, so you've paid about £160m into that and it's grown to £400m, could you just explain why the number went the wrong way and whether the trajectory of these extra top-ups, you know, £65m or £75m, should be kind of flat, or we should expect another step up later?

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Stephen Hester, Group Chief Executive
Sure. On your reinsurance, or I guess your volatile items, I would say if we get the large losses to where we think we can they should average around 9% on a Group-wide basis.

Now, clearly, it's very different percentages business line by business line, but 9% is the Group-wide number that would represent, for us, success. Whether we get there this year or not, we'll have to see, but that's roughly what we would aim for.

On whether I would say, a Group-wide - the five year weather average, even taking account of last year's bad weather, is just over 3%, and so, at the moment, am I smarter than the five year average? I'm probably not. So I would say just over 3% would be a normalised kind of a number. But, obviously, both of those will have volatility around them that is natural as well as volatility around them that may be man-made in the sense of what we do and don't underwrite.

In terms of your pension question, the key thing, and you'll see it in every single UK pension scheme reporter, is real interest rates dropped significantly from 2015 to 2018 in the UK, and real interest rates are, by far, the biggest driver of funding deficits. And so you'll see every reporter with a triennial review last year with a substantially bigger, if you like, underlying funding deficit against which there are two things that have gone the right, one, contributions, and the second is there have now been two years of longevity improvements, probably '19 will show some more again. So those tend to be the moving parts on a funding basis as opposed to on the accounting basis.

So, right at the back.

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Dhruv Gahlaut, HSBC
Three questions. Just following on the reserve margin question, as in you used to disclose it was about 5%. Has that number changed?

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Stephen Hester, Group Chief Executive
It's disclosed again at about 5%.

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Dhruv Gahlaut, HSBC
Secondly, can I just move to Canada, actually? So, Johnson had a good 6% growth. What percentage of Canadian premiums and earnings come from Johnson today?

And I wonder if you'd comment around the sustainability of the growth coming from Johnson '19/'20? How do you see that?

. . . .

Stephen Hester, Group Chief Executive
It's 40% of premiums, and what it is of earnings depends on the year. Last year it was 100% of earnings plus.

You know, I think Johnson can operate at 90, or just above, in combined ratio terms in a normal year. Last year it was 94, a change, but that was obviously weather hit. So, it would be, by far - in the same way that Personal Lines and Scandi disproportionately drives our Scandi results, Johnson disproportionately drives…

And there's a reasons for both of those which is that if we are writing direct with customers, intermediaries aren't taking 20% commissions out of the middle, and so that helps customers get a better deal and helps our profitability, and so those markets with bigger direct writing tend to be more profitable.

. . . .

Dhruv Gahlaut, HSBC
Can I ask you on Norway as well as in – It was a challenging year last year, premiums have gone down and there's been higher losses last year on underwriting. What's the future of Norway, as in is it still core? Is still core for you guys?

. . . .

Stephen Hester, Group Chief Executive
Yeah. Bear in mind, look, Norway's 2% of our business, so I think everyone had a really tough time in Norway, we're a minnow, but the big guys did. You saw in Gjensidige's results, certainly stripped of PYD, and so there was some specific things going on in Norway, both weather and especially auto claims inflation.

We need to get our business in better shape. There's a complete renewal of the technology platform. We need, off the back of that, to be able to compete more strongly. And so, I would say, it's not material to our results, and we're trying to get it to the point where we can compete successfully, but we're not yet there.

Middle, yeah. There we go.

. . . .

James Shuck, Citi
Thank you. Two questions from me. Firstly, how close were you to actually doing a special dividend or a buyback at this stage? You have the variable band of 20% to 35%, and the pull-to-par of that was 20, so, at the midpoint there should have been some

scope, and clearly you've got visibility that the pull-to-par impact will decline quite materially in 2019.

Second question is around the solvency position. So, if I remember correctly, you were previously targeting to be at the top end of the target range, and there's a comment now that you want to be above the top end of that range. So, just clarify whether I remember that correctly or whether there has been a change or not on that approach.

And kind of related to that, could you just update us on a full buyout cost of the pension scheme? And, if you were transact at current prices, what would be the impact on your solvency ratio, please?

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Stephen Hester, Group Chief Executive
We haven't updated the buyout ourselves, so I don't know, but I've no reason to believe it would be materially better than it was the last time we disclosed it a few years ago.

I think there's all sort of grey areas in the middle, but a full risk transfer, you know, would be a long way north of £1bn I would expect, although we haven't updated it.

In terms of the capital ratio, the issue is really as Scott laid out, that we disregard, for internal purposes, the deferred tax element of that. And so, if you include the deferred tax asset element, i.e. the Tier 3 element, then we do want to operate above the top of the range because we think, really, that puts us in our range when we disregard that, which we do internally. So that was what Scott was getting at.

And then, on your first question on dividends, I would say that we knew that we were likely to have the financial ability to distribute more than 50% of our earnings, even had last year been, let's call it, a normal year for us, and in our plans was that facility. The question that we would have faced, had we been in that position, is what amount of extra distribution is worth it?

In order words, at what point is a special dividend or a stock buyback too silly in its amount of money and you're better aggregating it with larger and what not? As it happened, we never got to make that decision because the volatility, in the sense, took up the room that we otherwise were planning, but that was, sort of, the only debate around it.

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Jonny Urwin, UBS
Thanks. I've got one question. What was the confidence level on that 96%, 97% combined ratio in the UK, and how much pressure do you guys feel under to get there?

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Scott Egan, Group Chief Financial Officer
You're probably going to get a different answer.

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Stephen Hester, Group Chief Executive
I think it would - I mean, we can't have confidence in it in the sense – by which I don't mean that we don’t have confidence in our actions, I believe we will take our actions, but we're not masters of our own destiny entirely. The market can throw weather and large loss challenges that we don’t - and our competitors can throw things, so it would be absurd to say that that is entirely under our control. And also we have a poor track record in the last two years. And so that's what we're aiming for.

We're trying as hard as we can to carry out the actions that should give rise to that outcome, but I can't really, to be honest, say more than that.

As to pressure, we want to win. You know, this entire company is being managed with the objective of winning, winning for our customers and winning for our shareholders, and when we don’t win as well as we'd like we're disappointed and we try to do something about it, which I hope you can see we are trying to do.

Andrew.

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Andrew Crean, Autonomous
Thanks. Can I ask three questions around, firstly, what have you done on Ogden? Are you still at minus 0.75 or have you moved?

Secondly, what is your view as to your vulnerability on front book, back book issues within the UK, particularly related to bank and building society orientated household business?

And, thirdly, you talked about thinking about a long-term average of 9% of large losses, which I assume is a function of your five year averages. To what extent should you worry that, actually, large loss activity is getting increasingly worse, and that the five year average is understating the potential?

. . . .

Stephen Hester, Group Chief Executive
Let me ask Scott to take the first two. I'll take your last one if I may.

We use the five year average when we're talking to you to try and, if you like, have a simple expression. In fact, what happens, in addition to simple top down analysis, there is an enormous amount of bottom up portfolio-by-portfolio analysis and completely different time periods taken.

So, for example, on something like a liability portfolio, we might take a longer period than five years because of the pattern of emergence of liability claims and their settling. On something like a short tail property portfolio we might take a two year period and, indeed, give higher weighting to the nearer periods within that two year. And so, the actual, the underlying build-up of our large loss projections is much more granular than just a five year average. And the places we've been getting volatility, we weight our forecasts on more recent experience.

Now, that's not completely answering your question because it's possible that things worsen from even more recent experience, and that you chase your tail a bit, which is also possible of weather, so there are those risks, but we try to, you know - we don't manage simply on looking back five years.

Scott, do you want to take the other two?

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Scott Egan, Group Chief Financial Officer
Yeah two things. I think I've said this before on Ogden Andrew but basically if you remember for us it wasn’t obviously as big a number as for many of our competitors, that’s the first thing. The second thing, since it came in we’ve actually been settling claims along the way. They’ve certainly been settling inside the Ogden estimate as it was originally and I think that was probably borne out of an expectation that it wasn’t going to stay there.

I think if you look across our book we’re probably not far away from zero in terms of an assumption, but obviously we want to be careful and thoughtful and not get ahead of our skis in terms of it becoming legislative in that respect. So that’s kind of where we’re at. But for us as I say it’s not really that big a number.

I think in terms of the front book, back book pricing, I mean look this is a really important issue in the market. I think firstly it’s a market behaviour, it’s not something that’s new or unique, it’s existed in insurance for many, many years in terms of new business pricing being discounted at renewal. I don’t think we’re the only industry. I'm not trying to justify it in anyway, that’s just the market behaviour and it’s the customer behaviour alongside that, but I think you also see it in banking, I think you see it in mobile phones etc. as well.

We try and do the right things by our customers. So we have a set of pricing rules that wrap around front book, back book pricing to make sure that we don’t push to extremes. I think we also take lenses on things like vulnerable customers etc. which I think we absolutely should. And I think when we write to our customers at renewal we’re also very explicit with them about their renewal premiums and what their renewal premium was last year and what it is this year. And as part of that literature we’re also clear that the market environment means that if they shop around they may be likely to find a cheaper premium.

So I think lots of things in there that we try and do the right thing by the customer but I think the starting point is the market has behaved in that way for many years and the customers behave within that market in that way.

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Stephen Hester, Group Chief Executive
And I think it’s worth saying that the phenomenon is massively less marked in our international territories, in other words although everywhere you get some level of new business discount, the difference between new business and renewal prices is much, much lower everywhere else. So it is very much a UK consumer market phenomenon, not even particularly a UK insurance phenomenon.

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Barrie Cornes, Panmure Gordon
Couple of questions if I may. First of all just looking at London market and UK Commercial, just trying to dig a bit deeper. Do you think - it's a wider question but do you think maybe the pressure, short term pressure on costs has resulted in some of the perhaps more experienced, relatively more expensive underwriters leaving the company over the last five, ten years, which has resulted ultimately in what's happened on the London market result today?

. . . .

Stephen Hester, Group Chief Executive
Well that wouldn't be a cost issue. If it were true that wouldn't be a cost issue because the costs don't lie in a handful of people sitting on a floor down here dealing with London market underwriters, the costs lie with the thousands of people you employ to process and answer phones and shuffle paper and all the different things which productivity is allowing us to streamline.

I think you should note that the UK Commercial Lines performance has been disappointing for at least a decade. So I'm not sure we're very proud of that but I'm not sure the evidence is that it's getting worse, it's just generally been disappointing with some volatility around that. And that's why by and large we're shrinking.

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Barrie Cornes, Panmure Gordon
Okay thank you. And the other question I had was in respect of UK Motor. Can you just go into a bit more detail what's going on there and maybe split between say Personal and Commercial fleet if there is a difference?

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Scott Egan, Group Chief Financial Officer
I don't think there is Barrie in one sense in that the things that are driving it are the kind of parts inflation, it's sort of the bodily end of the inflation, it's the usual things. And I think whether you're in a commercial vehicle or a personal vehicle I think it's the same. I mean obviously we're not a mainstream Motor player so our sort of mainstream personal Motor book isn't that large. Our segment that we're obviously a market leader in is the young driver but I wouldn't specifically highlight anything different.

I think what we've seen is that things like Telematics technology which can be employed in commercial vehicles and in the young driver segment in the personal space that we're in can be really good influencers of driving behaviour. And I think I've said before you know an interesting stat in the young drivers space is that where we interact with the driver on the behaviour, whether it be driving too fast, braking too heavily etc, we see a 90% response, i.e. an improvement in driving behaviour as a consequence of that. And I think that opportunity exists in the fleet space as well where the commercial vehicles have that technology or some of them have that technology as well. And I think those are helpful aids to try and influence what is a rising claims cost, but I don't think you can fight the underlying drivers of that inflation.

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Edward Morris, JP Morgan
Two questions please. The first just on the outlook for premium in the UK. Obviously there's a few different reasons why premium will come down, London market, the rating action you're taking elsewhere and also the reinsurance changes. Could you help us a little bit with what the proforma outlook might be for premium and what might be required for you deliver the 96 to 97?

And the second question is just coming back to the pension. If you could just clarify what the threshold is to make the additional £10m contribution per year? And also the one off £65m that you paid, was this a choice on behalf of RSA or if you could just explain the rationale for why that payment was made? Thank you.

. . . .

Stephen Hester, Group Chief Executive
Sure. I'll ask Scott to do your first but on the pension the - I expect us to pay £75m a year because I don't expect our capital position to be so weak that - you know the opposite, I expect our capital position to be strong. So if you're wanting to pencil something in you should pencil in 75 a year.

Now obviously the 75 - whatever we pay only costs us capital in Solvency II terms once we're above the caps which we might be. But even if we were above the caps we would count that as shadow capital because it's a loss absorbing buffer for pension volatility before you get to Solvency II. And so in a sense we'll be looking through some of that impact. And that's really the answer on the 65, it made the overall pension negotiation easier and didn't cost us anything in a ratio sense, and so that's why we did it.

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Scott Egan, Group Chief Financial Officer
So premium, can I break it into three parts because it might be more helpful. So I think look in Personal Lines, and I was trying to allude to it when I said it, I think on our household book which is the main driver of the Personal Lines premium, I am hoping that the core Household book will now start to stabilise now that we're coming off what I'd call higher rate and action and returning to more normal levels. Obviously I need to keep alive because if something happens in claims inflation then we'll react again, but I'm hoping to see that kind of volume shortfall start to stabilise without being exact because I don't know, and I'm recognising it's a competitive market.

I think in the Commercial space I'd split it into two parts. One, on the kind of non-domestic side I'm obviously still having a look so there's nothing more I can say in that at the moment. I think though on the domestic side and it's really what Stephen was alluding to, we made good profits on our domestic UK Commercial business. And obviously given my background that's a market I know really well. I was part of it for many years in my career and so I think we've got really good relationships with brokers and that's something that I'm looking to kind of build on and cement. So again I'm not highlighting it as a problem area as I sit here today given that it made money in 2018, but don't read anything - any words of complacency in that because there's none. I'm all over everything with the team to make sure that we don't go backwards as well on stuff that did make us money.

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James Pearse, RBC
Thanks for taking my question. Just one from me. On the UK exits is there any reason why you can't go and make any further exits going forward to accelerate your ambition?

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Stephen Hester, Group Chief Executive
No, there's no reason why we can't other than if we want to.

Laughter

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Dominic O'Mahony, Exane BNP Paribas
So two specific questions and one sort of broader question. The first specific question Stephen you mentioned you think there might be a point to go on the attritional ratio for the Group. I'm just wondering if that's sort of a like for like number or a sort of reported number? And the reason for that question is clearly you're shrinking your Commercial relative to your Personal. Commercial has a much lower attritional -

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Stephen Hester, Group Chief Executive
It's the other way round actually. Personal has a higher attritional -

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Dominic O'Mahony, Exane BNP Paribas
Sorry I thought that's what I said, yes indeed.

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Stephen Hester, Group Chief Executive
So if we're shrinking Commercial that would hurt us, yeah.

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Dominic O'Mahony, Exane BNP Paribas
Yeah exactly, so does that mean actually the ambition is in a way greater than one point on a sort of a like for like basis?

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Stephen Hester, Group Chief Executive
It gets a bit lost in the noise. You know it's not like we're halving the size of Commercial. If Commercial is 40% of the business in round numbers and we're taking let's say £200m of premium out of it or something like that, it just doesn't move the percentages by that much.

So is it - the 1% isn't a precise number and the mix isn't a precise number, it's an observation of if you said to me we're operating at best in class levels in each of our three regional markets, what attritional loss ratio would represent that, it's about 1% better than where we are. And then we need to have a better performance on the volatile - well actually the three volatile items. We have over performed in PYD, we have - weather is volatile and you can't do much about it and we've underperformed in large. So in a sense hopefully if we look at 2019 as an example we'll have some gain on attritional, we'll have some gain in the tints of the pro forma exits, we'll have some gain on large although whether we'll get in the first year everything we want remains to be seen. Hopefully weather is better but that's random.

Then against that there'll be some headwinds as a bit of investment income headwind, there's some FX headwind, more depending how Brexit comes in which you have to watch out for. And we calculate there'll be some PYD headwind not because we know anything but just because we plan PYD at half the levels it's been. So those are sort of the ups and down for 2019 and going forward.

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Dominic O'Mahony, Exane BNP Paribas
And sorry that takes me onto the second question which is about PYD. So clearly you've done quite well there, you've continued to do particularly well in Canada and Canada has always performed, as long as you've had that disclosure, well above the guidance. There's no specific reason to think that we've had any one offs in '18 or '17 that I should be making sort of a material judgement difference?

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Stephen Hester, Group Chief Executive
No and that's why Scott said the PYD has spread across accident years and across regions, there's no sort of one huge item. But we do plan on it being lower. I think we've been - I think there will be a year when it is lower. I don't know whether it will be this year or not but we like to manage our business not relying on it as much as in fact we have in the last couple of years.

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Dominic O'Mahony, Exane BNP Paribas
My final question, a sort of broader question. What I think you've been trying to tell us thinking about the outer years there's sort of no change in ambition for the combined ratio and actually it's very helpful to have some timing around it. So in terms of our thinking for what the EPS numbers are going to be actually, and also because you've guided investment income, it must be a sort of a question about top line really for us.

And that I guess comes down to the question of the extent to which you're shrinking Commercial versus growing Personal, and actually it looks like Personal is growing quite fast across the markets.

And you've spoken a lot about the UK Commercial shrinkage. Looking at the other regions, and I really mean Scandinavia, what gives you the confidence that actually the sort of latest round of shrinkage of underwriting action re-pricing is sort of enough, or actually when we think about 2020, 2021 should we be also thinking actually this is not a market that we're going to be growing, if anything we might still be taking top line down a bit in order to get to those combined ratios?

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Stephen Hester, Group Chief Executive
Well I think what is true is in both Canada and Scandinavia in the Commercial Lines business we had bad results last year, and so this year I would expect our top line to modestly shrink in both of those areas in Commercial Lines, but I would expect our Personal Lines to expand. So I think Canada and Scandi taken as a whole will probably increase their premiums this year, but there'll be a dampening effect coming from Commercial Lines.

But I think hopefully that's a one year only recovery in terms of the pricing and underwriting changes that we want to make, and so I wouldn't necessarily project that forward for a long way. But of course it is - it's a management philosophy that we're inclined to take action as opposed to sit and accept inadequate profitability in the same as we're inclined to take action for other reasons.

I think frankly the thing that we don't know the answer to that you have to make a judgement and we'll find out over time, is not are our businesses is capable of X or Y performance we believe they are, but is do we get that performance out of them. And in 2016 we hit our ambitions in that year, in 2017 and 2018 we haven't hit overall. Some individual businesses have but not all. And so there's probably some level of credibility discount that we need to work our way out of as to whether and how fast we can restore performance. And so for me that's the thing that's more difficult to judge than where you could get a business if you work hard enough on it.

We might be running out of questions, any more?

Terrific, well you know where to find us. Thank you very much for joining us and look forward to seeing you in six months' time. Thank you.

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