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**RSA**

Half Year Results Presentation  
1st August 2019

**RSA**

**Stephen Hester, Group Chief Executive**

**Charlotte Jones, Chief Financial Officer**

**Scott Egan, Chief Executive Officer, UK&I**

**Questions From**

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**James Pearse, RBC**

**Ed Morris, JP Morgan**

**Ming Zhu, Panmure Gordon**

**Oliver Steel, Deutsche Bank**

**Dominic O'Mahony, Exane BNP Paribas**

**Sami Taipalus, Goldman Sachs**

**Ben Cohen, Investec**

**Jonny Urwin, UBS**

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**Abid Hussain, Credit Suisse**

**Philip Ross, Mediobanca**

**Business Review****Stephen Hester, Group Chief Executive**

Good morning everyone. Thank you very much for joining us and welcome obviously to RSA's 2019 half year results.

I'm delighted to be giving up my temporary role, extremely badly undertaken as CFO, to Charlotte Jones, who is one day formally into the job, although of course has been on our Board for more than a year and so Charlotte will be joining me in presenting this morning's numbers.

We will ask Scott Egan to do a brief cameo at the end since some of you will be interested in what he's been up to in our UK business in the first half and so we'll finish the presentation with that.

Obviously a number of my colleagues are here through the front rows, and I'm sure you've been talking to them already, and can do afterwards. And welcome as always to Martin Scicluna our Chairman who's on the front row and can answer any questions you have of him as well. But let's get started.

So I guess we're clearly using the adjective, solid, for our first half results. Personally I think we would be able to claim a more expansive adjective than that, but having had a couple of years where the second half didn't meet our expectations, we want to strike a cautious note in case that would happen again, although we're hoping it won't and we're not believing that it will.

But backing up the first half results, and I think most important as we look forward, is that we are able to report our best current year underwriting profit, possibly ever, but certainly in the last ten years. And that's without having any of the volatile items being better than our plans and so that's if you like based on solid underpinnings.

As you've seen from the headlines that has given us a first half (which is normally our seasonally weaker half; hurricane dependent) combined ratio of 94.3, 21p per share. And a 15% return on tangible equity which is right in the middle of our 13% to 17% range. And I think by financial services standards, a pretty decent level by the standards of our ambitions, not yet where we hope we can get it to.

Importantly we have all of the pricing and underwriting actions that we had scheduled to take in the first half of this year. In every region we are on, or ahead, of plan in the actions that we have taken. So obviously over the course of the next year or so we hope and believe those actions will continue to earn through our financial statements, and should do the things that we wanted them to do.

You can see some encouraging early news in attritional loss ratio which we will unpack. There are some headwinds in prior year and large losses which we'll also unpack. And clearly one of the particular proof points that we needed to produce better evidence on our UK and International division. And there we have actually an extraordinarily good combined ratio of 94 in the first half; I don't encourage you to annualise that.

But nevertheless, what we can say is it's a good start for the 'lucky general' who has gone into that business. And while there is lots more work to do, we're pleased to be starting on a positive footing. 3% up in dividend, designed to be entirely consistent with our policy. And of course a statutory profit lower than it would ordinarily be with some charges which we will also unpack for you.

So when I presented to you at the full year results we really set out in my view two priorities for 2019 for RSA.

The first was to make sure that the things that were going well, kept going well, because much of the company has been performing well, much of the things that we've wanted to do have been going well and we need to keep that going.

The second is we had to improve and fix some of the things that disappointed last year, which was the first and only year in the last five, where our underwriting profit declined. And so by way of brief update on those two objectives I think we believe we've made good progress against both of them.

In terms of keeping going what has been good, you'll see that our Personal Lines businesses, which are about 60% of the company, produced an exceptionally good first half result with a combined ratio under 90, and a strong underwriting profit (all current year driven) and with weather at or around its long term norms and so not particularly helped by that either; so we're really pleased with that.

The other thing that has gone well for us and been a big accomplishment in recent years was cost control, and again we extend our record on that cost very slightly down in absolute terms a bit, more down in real terms.

In terms of the fixes, I guess we'll put those into two buckets. There were things we needed to stop doing and then things we needed to improve.

The portfolio exits we said that we wanted to get out of £250m worth of business from the 2017 baseline. Obviously a bunch of that was done last year already and it has gone well so far and we are now 80% of the way through the run off of all that business. So the vast bulk of the exits are off our books already.

Related to that, and Scott will mention this later, with lower volume in our UK and International business, you'll see that the cost ratio has gone up and we will need an additional cost programme to correct that which we will be bringing forward in the second half.

Away from that, in our continuing businesses we had, and still have, lots of work to do in particular in our Commercial Lines businesses to improve.

An element of the improvement, of course, was putting in place hopefully some volatility dampeners in terms of reinsurance which we have looked at, at the half year. And we're nowhere close to being in GVC territory which is good. We probably will be protecting the second half in Commercial Lines well in Canada and in Denmark, by our Commercial

Lines aggregates, because that's where we haven't had such good experience in the first half.

As I mentioned right across the company we are at least on plan, and in some cases ahead of plan in every region on our repricing and re-underwriting actions. And you can see attritional loss ratios responding but H2 is important for us to see more of that come through.

What I've noticed interestingly in the vast majority of our competitors, particularly the international ones that have reported so far, is that almost every one is seeing lower prior year development this year. And in particular people are seeing, if you like, a follow through from the 2018 accident year and we have certainly experienced that.

As you'll see there's something like a £46m negative swing on PYD, that's driven by the 2018 accident year, mainly impacting Commercial Lines for us. And fundamentally it's because actuaries obviously work on smooth time periods of loss ratios. And so when you have a year that goes sharply to the negative, it's intuitive that they may not catch up with the exact damage of that year in the first go. And so it's proven with our case that, I don't believe there's anything there that's a long term drag.

Hopefully we've caught it all in the first half, could there be a little bit more in the second, it's possible, but I'm not worried about it long term. It just tells us that 2018 was a bit worse than we thought it was, not just for us, but you can see that across many of the other particularly the big Commercial Lines players which is where it is concentrated.

So our strategy remains unchanged, won't go over that and what we're trying to do unchanged, our targets all unchanged so it's just how well are we executing.

In terms of the customer report card, crudely in the areas where we're happy with profitability, we're able to serve customers well, we're able to retain them and able to get some modest growth. And in the areas where we have to take significant pricing and underwriting action that normally involves some sacrifice on volume. There are occasional exceptions to that, Canada would be one where the whole market is significantly hard but that's basically the rule.

Interestingly what you can therefore see is at a Group level retention, even at a Group level across everything has risen in the year, but has particularly risen in the Personal Lines businesses which have been doing very, very well. And in Commercial Lines, by and large, retention of volume has fallen which is bearing the brunt of the actions that we're needing to take.

There is a bit of a counter intuitive move in Scandinavia of increased retention in Commercial Lines. That was mainly Sweden driven; I think there are a couple of unusual renewals in there. Denmark, which is where we need to take the most action, would not have shown that and will not show it again at the end of the year either.

So broadly we're comfortable that our customers are right behind us and enjoying what we do for them in the areas that we're happy with it. And that the market is competitive

enough that when we do significant underwriting and pricing actions that are in any way different from the market, we obviously will give up some volume. We try to make sure it's the volume that is in shareholder's interests for us to give up.

Attritional loss ratios are of course a very important measure for us and although we've made huge progress over the last five years, that progress reversed a little bit last year. And I'm pleased to say that it has resumed.

I hope that it will look better than this at the year end because of course the worst period that we're comparing against was the second half of last year. These comparisons are for the first half, although we've put on the graph also the second half so you can see that comparison. And in both Personal Lines and Commercial Lines we have attritional loss ratio improvements; we have them in Canada and in the UK. Less pronounced in Scandinavia and that's partly because in Scandinavia, the key lines, the biggest lines, our Personal Lines area, is already exceptionally profitable, and we'd rather have volume than better attritional loss ratios at that level.

So the correction we have to make, which I'll come on to in Scandi, is in Denmark and there's more about large losses and only a bit about attritional.

Cost remains a key target for us and again we continue to do reasonably well on that. Scandinavia improving, Canada already at or below our targets, the UK, actually the costs were flat but of course the ratio went up with loss of volume. And as I mentioned we intend to take some corrective action there with a specific programme with Scott will talk about.

If we look at the business in Personal Lines and Commercial Lines first and then I'll give you a regional lens. As I mentioned I've taken in aggregate our Personal Lines businesses at 60% of the Group, continue to drive our profitability. And we are in aggregate very happy with them and particularly happy with the Direct businesses in each of our regions. And as you can see very strong profitability, significantly improved from last time and you can see the improvements across lots of different lines, attritional loss ratio.

Weather has improved from last year, although is roughly normal and there's a balance between terrible weather in Canada and good weather in the UK. And the two basically equal each other in terms of deviance from plan and so at the Group level was not a big deal one way or another.

I mentioned that the businesses where we're happy with profitability are also enjoying customer support. And so for example Johnson, our most important Canadian Direct business, good growth, both organic and with Scotiabank just beginning to come online and in Scandinavia, that's also true in Sweden and Denmark and also beginning to get a recovery in our UK Personal Lines businesses, particularly in the Pet and the Home areas. I would say that we still need to do some important work in the Motor in the UK which Scott will talk to.

Turning to Commercial Lines, which of course was our big headache last year, and still is a headache, as you can see still with an unsatisfactory combined ratio of 98.8. I think

it's important to note that a big amount of that was the swing on prior year developments. So our current year combined ratio improved very slightly, versus half one, and of course all of it is a lot better than half two of last year. But we have to get through half two of this year before we can feel comfortable we don't have another really bad third quarter.

When we look at early signals the attritional loss ratios in our commercial lines businesses has started to improve and we believe will improve further in the second half and into next year. The prior year development headwind, as I say I take to be a temporary thing.

The large losses have behaved themselves in the first half in our biggest Commercial Lines area which is the UK and International division. Indeed the London Market portfolios that remain, as opposed to the ones we've exited, were actually in the first half strongly profitable. Of course a half doesn't tell you too much so we'll see how the full year goes.

However, we have had worse than planned large losses in our Canadian Commercial Lines business and our Danish Commercial Lines businesses. We don't believe there's a particular thread or a particular trend or particular businesses that are leading to that. But it is important that the underwriting actions that we've taken take those large loss trends down as well and the second half will be an important proof point as the different actions that we've taken earn through and start being seen in the portfolio.

There's just a slide here, I won't take you through the numbers because you can read them afterwards. But allowing you to track all of the portfolios that we said we would exit, the amount of premium that we were coming out of, how far we have got now, what's left to do and where the first half losses were.

I think the key headline is that more than roughly 80% of the earned premium is behind us and therefore to the extent that has been a drag, it should be an increasingly minor drag and the vast majority of it should be done by the end of the year which is important to us.

We did say that we would update on, have we done enough, and I think the tentative conclusion is plus or minus we have. Of course there is always fiddling at the edges in terms of things that we may do more. But tentatively we think we've drawn it in the right place.

However, the important caveat to that is that in the remaining London market business that we have, which is largely Marine, we've halved the size of our Marine presence but we still have a meaningful Marine presence.

We need to make sure that the market continues its sharp improvement which is driven by rate and capacity reduction. If it were not to do, we would go further as well, but for the time being we feel that the market has responded by enough for us to retain the best bits of what we had. And so that's I would say a tentative conclusion to be relooked at again in the light of how the market trend as a whole continues.

So now giving a regional lens on how we have done. Scandinavia of course at a headline level our results are disappointing to us by being 11% down and going in the wrong direction relative to our ambition and relative to what we had expected.

That is entirely due to Danish Commercial lines, our combined ratio in the first half would have 82.9, ex Danish Commercial Lines and so Danish Commercial Lines made up all of the difference. That is a business which we believe can be good, we believe we have taken the right actions, we will be taking more.

The problem, the challenge with Danish Commercial Lines is more than 50% of it renews on 1:1 so you basically only get one shot every year to really change the portfolio. So we had a crack at the beginning of this year and we'll do a bit more at the end of this year or the beginning of next year and we're confident we'll get in the right place. But we haven't done yet and that in fact has held us back significantly in Scandinavia.

But the great majority of the Scandinavian business, Personal Lines businesses in fabulous shape, our Commercial Lines business in Sweden, best results for a very long time and in line with our target. And even Norway while the absolute levels aren't very good and it's a very small business, a very substantial improvement from last year. And importantly the expense ratio across the region continuing to improve.

So there's still some important work to do in Scandinavia but the headline I think is misleading as to how much work we have to do, it's very, very concentrated in part of one country's business.

Turning to Canada, on an absolute basis we are pleased that our Canadian profit doubled and we're upset that it's nowhere close to where we want it to be, and had planned it to be. I think it might prove to be actually the best result of any Canadian competitor in the first half. We saw Intact out yesterday with a combined ratio of 100 in Canada. And as you can see our combined ratio is 97.8, and it's unusual for us to be better than Intact and so we're rather pleased that we are, although it's only a six months period.

Of course so we've improved, terrific, what had held us back relative to our plans is overwhelmingly weather which was very bad in Canada. Although in our case offset by being good in the UK.

The Canadian market is what you would call a hard market with strong pricing and underwriting going on through all competitors. You're seeing that in the Property lines where broadly people are trying to price for worse weather trends going forward. And you're seeing it in the Auto Lines where the regulatory cycle is allowing us, and all of the competitors, to take a good rate and our Auto Lines are in aggregate back in profit as indeed Intact reported, although they had a big negative PYD on Auto which was larger than ours in the first half.

We are very pleased of course that attritionals have started to improve, reflecting that rating, although they should improve more as we go into the second half. Cost competitiveness continues to be in the right place. And the crown jewel, in the same way that Sweden is our crown jewel in Scandinavia, our crown jewel in Canada is our Direct Personal Lines business, Johnson, which is now up to something like 40% of our



business overall and continues to do very, very well both from a shareholder perspective and a customer perspective.

Our commercial Lines businesses as I've mentioned has had a poor first half, some of that is weather and just the luck of the draw, it got hit a bit more by weather actually than our Personal Lines business and some of it was large losses, which are not yet where they need to be.

And finally the UK and International, which as I mentioned Scott will talk a little bit more about when I have finished. Clearly the headline we're delighted with, best in class headline of 94 combined ratio. We don't expect to finish the year there but nevertheless really pleased to have it.

Within that it is very, very driven by current year underwriting improvements. And in fact would have been better had prior year not corrected as significantly as we talked about.

Ireland and the Middle East have very much driven the numbers, and both of them for different reasons, are likely to have worse second halves than first halves. So they're both in aggregate performing at good levels but this isn't a correct run rate in the first half, not least in Ireland they had no weather and very few large losses which helped a lot.

The UK standalone combined ratio was 96.5, you might recall a 97 to 98 ambition for this year, so slightly better than our ambition the first half and basically good weather offsetting bad PYD. But Scott will talk some more about it.

We're pleased with the start of improvements in attritional loss ratio and cost discipline has been okay, flat costs but we quite appreciate there's more to do. But as I say I won't say more about UK because Scott will have a go at that.

And then finally our ambitions slide. Ambitions unchanged, the eagle eyed among you will see that in Scandinavia and Canada, we at one stage thought it was possible that we could reach the combined ratio ambition this year. We had a '19 to '20 timeframe and you'll see we've put that back here. Why is that? It's because if you start behind the ball with the first half, you probably won't make that up in the second half. And in the case of Canada that's obviously a weather item and in the case of Scandinavia it's a Danish Commercial Lines item. We don't see any of those as, if you like long term issues around our ability to achieve the ambition but it probably means we won't achieve it this year.

So if I wrap up my overview we think that the results suggest that we are on track for the things that we wanted to do. We're particularly encouraged by the current year underwriting trends. We're very encouraged by the power houses that we have in our Personal Lines businesses. And we believe that the corrective actions that we're taking are showing early evidence, we think we're doing the right things but of course the proof will be in the pudding and the eating of the pudding, to sort of 'Boris Johnson-ise' this presentation. I think he was cake rather than pudding wasn't he. And so we need some time to see those go through.

We're very focussed on continuing the progress and having a decent second half.  
Charlotte, thank you.

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## **Financial Results**

### **Charlotte Jones, Chief Financial Officer**

Thank you Stephen. Good morning everyone. I'm delighted to be here to present the first half results. And whilst it is only my second day as CFO, my time as non-exec director means that I already know RSA relatively well.

As Stephen has said, we are pleased to report a solid set of numbers with underwriting actions on track and current year performance significantly improved. In terms of slides I will start with an overview of the numbers before walking through the P&L and capital in more detail.

Group net written premiums of £3.3bn were up 1% at constant FX, down 2% excluding changes in reinsurance.

We are pleased with Personal Lines growth in Scandinavia and Canada.

And while Commercial Lines across the group are down, this is largely in response to underwriting and pricing actions.

Group underwriting profit for the first half was £181m, excluding the exit portfolios, with a combined ratio of 94.3%.

Improvements in the attritional loss ratio underpin very good current year results. Our prior year development was positive, but lower than our planning assumption in the first half of 2018. As already said, the principle driver of this were refinements to loss estimates relating to the 2018 accident w1year.

Operating profit was £308m, excluding the exit portfolios and within this investment income decreased as bond yields fell further.

Statutory profit after tax of £183m was impacted by exits as well as non-operating charges. Underlying EPS at 20.9 and the underlying return on tangible equity of 15% was within our target range. And we are pleased to have declared an interim dividend of 7.5p, up 3% from last year and in line with our dividend policy.

Finally tangible equity increased by 2%, this was driven by profit after tax and fair value mark to market movements. These were partly offset by slightly lower pension surplus, investment into intangible assets and the impact of dividends.

I'll now go through some of the areas in more detail starting with premiums on slide 24.

Now we've prepared this slide excluding the impact of reinsurance changes to allow you to compare on a like for like basis.

As I just mentioned underlying premiums were down 2% at constant FX.

Positive trends in Personal Lines continued in Scandinavia where premiums were up 3% underlying to £567m.

We grew the business in our most attractive markets of Sweden and Denmark, with rate increases and better retention both contributing.

Swedish Personal Lines premiums grew 3%; Household, Motor and Personal Accident were all up.

In Commercial Lines across the Scandinavian business premiums also grew by 3% to £472m.

Rate action was ahead of our plans and last year in all lines of business. However, the impact on premiums was dampened by a 3% decrease in volumes.

We wrote less new business where we are taking the most action to improve performance, notably in Commercial Motor and Property.

Personal Lines in Canada grew 8% to £546m. We applied rate of about 7% in Auto and nearly 10% in Household. This is helping us to tackle ongoing and significant claims inflation. And it is starting to allow for the heavier weather losses expected as a result of climate change.

The hard market conditions Stephen mentioned meant that retention remained strong at 90% for Johnson and 85% for Personal Broker.

I'm also pleased to confirm that we started to write new business for Scotiabank in the second quarter. Commercial Line premiums in Canada decreased by 5% to £222m, where a 15% reduction in volumes was partly offset by rate of almost 10%. These lower volumes were in line with our plans and mainly driven by targeted lapses.

Now for the ongoing UK Personal Lines business in the UK premiums were down 10% in the first half to £488m.

Household was down 8%, importantly we've continued to achieve good rate in this business.

Motor and Pet also contracted and while retention improved, new business was impacted as we held our discipline on rate.

On the same basis Commercial Lines in the UK were up 2% to £648m. Rate was positive across all major lines. Marine achieved nearly 10% while Commercial Property achieved 6.

Now let's turn to underwriting results on slide 25. The Group combined ratio was 94.3% excluding the exit portfolios and we are pleased with the progress in the attritional loss ratio. While lower commission and more benign weather also contributed.

Against this the expense ratio increased slightly as expected and PYD reduced compared with 2018 and our planning assumption.

So looking at the headline underwriting performance in each of the regions. In Scandinavia the combined ratio increased by 1.5 points to 89.1.

Personal Lines remained excellent with a combined ratio of 79. This was despite higher weather losses and lower PYD.

Commercial Lines increased to just under 104%. Weather large and attritional losses all contributing to this. The deterioration was all in Denmark, with Sweden performing well.

The combined ratio in Canada improved by nearly 3 points to 97.8. Personal Lines improved by over 8 points to 94.5, despite another heavy weather period. Commercial Lines deteriorated to 105.6, due again to heavy weather, higher frequency of property, large losses and lower prior year development.

Finally the UK and International combined ratio was 96.1% or 94% on an ongoing basis. Within this the UK ongoing business reported COR of 96.5 and Ireland and Middle East reported excellent results again, with combined ratios of 83 and 82 respectively.

Now you should note that these ratios are expected to fall back somewhat while remaining better than target.

Now let's take a closer look at loss ratio movements by region on slide 26. In Scandinavia the loss ratio was about 2 points higher than the first half of last year at 71.9. The three volatile items each added nearly half a point.

Large losses were above the five year average, driven by Danish Commercial Lines. And while we saw some increase in loss frequency in Property and Tech Lines during the second quarter, our reviews concluded that the risks were well underwritten.

The attritional loss ratio is increased by 0.4 points, also driven by Danish Commercial, primarily in the Motor and Property books. Action plans are in place to improve both and these include repricing, re-underwriting and reducing capacity.

The loss ratio improved by about 1 point in Canada to 70.8, this is despite the volatile items costing just over a point.

Now while weather was nearly 3 points better than the prior year, it was again above the five year average. And as a backdrop to this in Canada insured Cat' losses for the industry were around \$600m for the first half with spring floods costing over a third of this.

The large loss ratio remained elevated, mainly in Commercial Property, positive PYD was lower than 2018 and our planning assumption.

We're very pleased to be reporting an improvement of 2 points in the attritional loss ratio, this was better across all major lines of business and it reflected the strong rate beginning to earn through. We will continue to push the rate in the second half subject to regulatory approval where that's needed.

And finally in the UK and International the loss ratio also improved to 59.9, excluding the exit portfolio. Weather was relatively benign and large losses were a little better than last year and our plans.

The attritional loss ratio was better with reductions in Pet, Household and Commercial Property partly offset by increases in Marine and Motor.

Household improved by 5 points, as strong rate earned through.

Prior year development reduced compared to the first half of 2018 as lost estimates for the 2187 accident year were refined. And while PYD was slightly adverse overall it was favourable for the ongoing business.

Now let's look at the impact of what we term volatile items on slide 27.

I've already covered most of the impacts of weather in large. So here I would just make a few additional comments on prior year development.

Overall PYD gave a 0.9 point benefit to the combined ratio excluding the exit portfolio, whereas for the first half of 2018 the benefit had been 3 points. At 1.2% the PYD for the second quarter was broadly in line with the planning assumptions which we communicated previously.

However, as you know we reported flat PYD for the first quarter which brings down the first half impact overall.

We saw a marginally positive development in each region excluding the impact of the exit portfolios and as I've already mentioned the lower PYD this year is driven primarily by the refined loss estimates for the 2018 accident year.

I think it's noteworthy that a number of our competitors have reported similar development, especially in International Commercial portfolios.

Now moving to costs on slide 28.

Group written controllable costs were down 2% in real terms in the first half and at earned controllable cost ratio was broadly flat at 21.3.

I will make two specific regional comments here. Firstly, in Canada an already low cost ratio improved to 17.6%, better than our plans. It is forecast to be increased in the second half as certain timing differences unwind. And we have previously guided that

while the cost ratio is expected to remain below our target level of 20%; higher software amortisation charges will increase it over time.

Secondly, we told you in February that the UK and International controllable cost ratio was expected to increase due to the premium contraction in the UK. We reported 22.8% for the first half which was an increase of 1.3 points. We're focussed on resuming progress towards our 20% target. And as Stephen has already mentioned a new cost programme is expected to begin before year end.

Now moving to investment income on slide 29.

Investment income at £154m was 4% lower than the first half of 2018 but broadly in line with guidance. There has been no change to our strategy, the portfolio remains dominated by high quality, fixed income. 91% of our bonds are A rated or above.

The average income yield on the bond portfolios was 2.2%, while the average reinvestment yield on the portfolio was 1.3.

Based on current forward yields and FX, we are forecasting investment income of between £285m and £295m in 2019. This is slightly down on the projections made six months ago.

Now we've included 2020 and 2021 on the slide for your information, these projections represent a more significant decrease in guidance as lower yields earn through.

Balance sheet unrealised gains increased by £181m during the first half. This was mainly driven by positive mark to market on bond holdings due to declining government yields and tightening credit spreads.

The higher opening balance together with flattening yield curves means that the predicted time for unrealised gains to unwind has increased. If yield curves stay as they are we now estimate the gains will take around 7 to 8 years to fully unwind. About 50% of this will be within the next three years.

The impact of pull to par on capital generation is forecast at about £40m for the second half and £70m for next year.

Now moving on to the non-operating items on slide 30.

I've only a few things to highlight here. Interest costs increased slightly in line with guidance, this reflects the adoption of IFRS 16 from the 1st of January this year. Other non-operating items include £17m for the completion of the UK legacy sale and £15m from a reduction in the discount rate on long term insurance liabilities in Denmark. Neither of these items negatively impact capital.

Finally, turning to capital on slide 31.

Our capital position and quality remains strong at the half year, with a coverage ratio of 167 and core tier one ratio of 104. We generated 13 points of capital from underlying earnings during the first half. Net capex and pensions absorbed 5 points of this.

Both major UK pension schemes were at their caps at the half year. This means that contributions were not fully eligible from a capital perspective. However, for each scheme the surplus over the cap acts as shock absorber for future market movements before there is an impact on our capital ratio.

The impact was exaggerated in the first half of 2019 due to the timing of the pension contributions. The exit portfolios and the impact on bond pull to par absorbed 4 points of capital generated, while market and other movements were neutral overall. You should note that the 7 point dividend impact show here represents a six month accrual for a full year notional dividend.

So to conclude, we are pleased with the solid set of numbers for the first half, particularly the current year underwriting results.

Our performance improvement actions are on track and their full power should earn through next year.

Our Personal Lines businesses are performing strongly overall and delivered a combined ratio of 90%. Premiums are growing in the most profitable lines.

Commercial Lines continue to be challenging, we still have much work ahead in all our regions before we can deliver at our ambition levels.

And costs have come under pressure in the UK as premiums have contracted which impacted the Group cost ratios. A new cost programme is expected to being before year end.

Financial markets continued to provide a headwind, this includes negative impacts from the translation of foreign earnings, lower bond yields and together credit spreads.

Of particular note is the increase in the FAS reserve and its expected impact of pull to par.

Finally our ambitions for the group remain high and unchanged and we are focussed on delivering good progress in the second half. And that concludes my run through of the numbers. I'll hand back to Stephen.

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**Stephen Hester, Group Chief Executive**

Thank you very much Charlotte, much appreciated. As mentioned I thought we would just give Scott five minutes to update on the UK before going broadly into Q&A which we'll do immediately after that.

Obviously Scott's only been in place for five months, six months I suppose given we're at the end of July. And so we're very conscious that the proof is in the pudding and it will take some years for us really to know what the efforts will add up to. But what I can say is from my perspective he's made a really good start, he's been decisive in terms of organisation and team. He's brought a pace and an incisiveness that we needed to our execution, so I'm hopeful but Scott why don't you speak for yourself.

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**UK Update**

**Scott Egan, Chief Executive Officer, UK&I**

Thanks Stephen. Good morning everyone. I've just had my half year appraisal I think in front of everyone in the room here.

So look I won't go back through the numbers because you've heard them all. But I guess I just wanted to give you my take on the UK and the progress that I think that we've made. I thought the best way of doing that is to put the same slide up that I used at full year, and the six priorities as I saw them then and give you a bit more colour behind each of them.

But I will reinforce what Stephen said. As I stand here I'm pleased with the progress, I'm actually really pleased with how the team in UK&I are reacting to the change. I think you have a number of people right across our businesses who are working incredibly hard to make sure they can get the UK business back to where we believe it can be, which is amongst the best in class in our marketplace. But at the moment it's about building momentum in that business and that's what I hope I can share with you as we go through the priorities.

So if I start with the first one which is about our underwriting actions and claims initiatives. For me the bedrock, no excuses, this is the area that we have to push hardest on and hopefully you will see the most improvement from it's what we do.

And at the end of the half year our rating is ahead of plan, our claims initiatives and savings are ahead of plan and the underwriting actions that we set ourselves beyond rate are 95% complete around the half year.

So I would an incredibly good performance from the team in terms of delivering those outcomes. In terms of the rate and the underwriting actions, the reason I want to highlight them is I don't want you to think that we're just hammering rate through, there's sophistication to what we're trying to do below the surface. And I think that's best evidenced by things like the retention rate etc that Stephen put up, which hasn't collapsed as we've gone through our changes.

That's not to say everything's perfect, Stephen highlighted it, I think in the first half if I had to highlight a couple of areas, the one I would highlight most would be Motor where I think we've found the Motor market tough.



I think in terms of claims inflation across the market we're seeing around between 5% and 6% covering both PD and BI. And for us as a Group particularly in our More Than business, in what I would call core Motor, non-telematics business, we haven't got the strategic scale that I think we genuinely need to help build our More Than business for the future. And that is something myself and the team will be working on in the second half of the year.

In terms of the second priority, the portfolio review, look I think we're broadly done with the big moving parts but they'll never be a day in the UK where we're not looking at segments, where we're not looking at products, where we're not looking at areas where we will continually take actions. But I think the actions that we outlined at the end of the year of that sort of magnitude; I think those are behind us for now.

But I will caveat and say things like the areas that have hurt us in the past, things like Marine and things like the London Market, I have to be honest and say they will remain under continue vigilance in the second half of the year and beyond.

But I think they've done a sterling job in the first half of the year. To give you a sense of the London Market, combined ratio improved 20 points year over year at H1. So a good job but too early to declare success.

You've heard a lot this morning on our third priority around cost improvements; it's something I've been very open about within the business. The UK cannot survive with a cost ratio of 23%. The Group has a regional target of 20% or below and the UK can be no exception to that.

Therefore I with the team are targeting structural cost opportunities of around 2% of our combined ratio and we hope to achieve full run rate on them by 2021. It's an area that we're working on in terms of the details so I'm not going to say more on that as I stand here now. But suffice to say the team are working incredibly hard on that detail and as and when we're ready to communicate both internally and externally then we will.

The performance of Middle East and Ireland has been exceptional in the first half year. I think you've heard from both Charlotte and Stephen, that was driven by strong PYD and benign weather. A more normalised combined ratio for those businesses would be around 90% for Middle East and perhaps low 90s for Ireland, recognising that at any point in time it could be higher or lower than that.

But again these are strong combined ratios even on a normalised basis. And there's quite exciting things going on in both businesses, particularly around the digital platforms which go from strength to strength.

The fifth one which is really about improving the quality of execution focus, agility and pace, I think we're at the start of that journey across the UK.

A few examples to the right hand side, one of the first things that I did on taking on the role was to refresh the exec team. As a reminder we appointed a new IT director, a new COO, a new head of Personal Lines, a new finance director and a new HR director. And all of those appointments were a mixture of both external and internal moves. That

teams is performing well, I'm really pleased with how we're tackling things, both culturally and operationally.

The second point is around attritionals and I think if I stood back at half year, I think the improvement that we've seen in attritionals across the UK business is providing good momentum, not only into the second half of 2019, but into 2020, improvements of between 2% and 3% if you compare it to the second half 2019.

And as I say that is really the evidence point of the rating ahead of plan, the claims savings and the underwriting actions.

We're starting to see some early beginnings of growth and I wanted to put that up there because I do not want to create an impression that the UK is shrinking to greatness, it really isn't. Very early days and I would not badge it is any more than that.

But just to give you a couple of examples. In More Than Home whilst if you compare it to last year it is down, More Than Home policy count actually grew in June for the first time in two years, year on year which is a really important evidence point of some of the actions that we're doing.

Predominantly that was driven by new business which is up 180% since the beginning of the year. So again some really good evidence that the team are really building on the pricing sophistication and the brand that we have in the marketplace.

And the intention is to refresh the More Than brand and relaunch towards the beginning of 2020 with the view that hopefully we can become the profit 'jewel in the crown' of the UK business, like we have in Scandinavia and like we have in Canada.

And on the Commercial side to give you one example, regional broker is a business which we run and which is a heartland of our UK Domestic Commercial. Again new business is up 18% year on year, retention as just below 90% and that's a business that enjoys combined ratios of low 90s. So I think we're growing where it makes sense to grow and we'll continue to build on that hopefully through the second half of 2019 and into 2020.

And then to end, which is a really important point, our staff engagement as you can see, at the heart of our business is our people, I keep saying it in every single location I go to. I keep hearing it from our customers and therefore I will always prioritise our staff and our engagement levels are actually up 4% since the turn of the year.

And if I jump across to the customer angle and look at our NPS scores in our Personal Lines business, they're up 5% from half 2 2018. So again small steps but hopefully small steps that can turn into bigger steps if we can keep the momentum going.

So to wrap it together I would badge it as no more than a promising start, it is a start, it's half year. I will keep everything crossed as well since I'm the lucky general and I hope in the second half of the year that luck will continue.

But for now I think it's a good start, we're hopefully building momentum and the aim from the team is to target the lower end of the combined ratio target that I set when I stood up here at full year results of around 96%. With that I'll hand back to Stephen.

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***Questions and Answers***

**Stephen Hester, Group Chief Executive**

Thank you very much Scott, much appreciated. Let's go to Q&A. Over here. Yeah, just over here.

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**Greig Paterson, KBW**

How are you doing? Three questions. One is your Solvency II ratio is above your range, I wonder if you could explain is that because of the rating agency constraint or is it to do with the credit spreads or credit situation, benign credit situation concerns there? And if it's not to do with either of those two, why don't you move the range, because it seems an oddity?

The second question is just the technical one on your credit spreads, there's a fair bit of sensitivity there. I was wondering how you treat the volatility adjuster and/or downgrades due within your spread assumption to make the scenario realistic?

And the third thing is I don't know if I misheard but when you were talking about the caps on the pension fund for Solvency II one of the comments was - we're at the caps. And then the next comments was - we have a buffer, which doesn't mean you're at the caps; you're well in the caps. I wonder if you could just explain the degree to which those caps are biting so we get a feel for the buffer?

.....

**Stephen Hester, Group Chief Executive**

Thank you for those, the precision of those questions. On our capital ratio as I've said I think many times before, we are really targeting a credit rating, we are not really targeting a capital ratio. And our credit rating is a mid-single 'A'. We'd like it like that. It's not under review either upwards or downwards by any agency and we think that that is the appropriate level for our Company. And I regard if you like, the nominal, the mathematical ratios beneath that as interesting but not terribly relevant compared to that central fact.

We've also said in relation to the Solvency II ratio that a feature of our ratio is that we have some deferred tax assets that are part of that. Personally I don't think that should be allowed under Solvency II. It is, but I don't think about it and if you were to extract those within the ranges that we've published we could move, you know, the ranges around. It just hasn't been a priority to do so.

I think on your second question which was about volatility adjustment, I'm not entirely sure I understood totally. We don't make use of the volatility adjustment element of Solvency II, which some other companies do. I think it's a bigger issue for life insurers than general insurers. We might one day if it ever became relevant; it's not worth a whole lot of money. But I think that was your question if I've understood that correctly.

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**Greig Paterson, KBW**

If you downgraded - I mean your sensitivities when you assume spreads open up, is there an assumption that X% of the portfolio downgrades or -

.....

**Stephen Hester, Group Chief Executive**

Yeah, so inherent in the Solvency II model are - and are therefore the capital requirement. Actually we use Moody's as the supplier of our volatility engines if I can put it like that, for the purpose of Solvency II, and so we use their black box. And in there is of course various assumptions about what happens in different scenarios in terms of downgrades and what have you. So we follow that and that's obviously signed off by all the regulators. I don't think we do anything different than other people do.

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**Greig Paterson, KBW**

But in sensitivity do you assume that there's - a series of downgrades in an actual scenario?

.....

**Stephen Hester, Group Chief Executive**

Well, now you're going well beyond my knowledge. If there is anyone who knows the answer to that that wants to pipe up. Why don't we come back to you on that?

And then your question on pension. Charlotte, do you want to have a go at that?

.....

**Charlotte Jones, Group Chief Financial Officer**

Yes, yes, I'll have a go at that. So on the caps ...

.....

**Stephen Hester, Group Chief Executive**

And by the way, if you know the answer on volatility, be my guest as well.

*Laughter*

.....

**Charlotte Jones, Group Chief Financial Officer**

I might pass on that one.

.....

**Stephen Hester, Group Chief Executive**

I told you I'd give you the nasty ones, didn't I?

.....

**Charlotte Jones, Group Chief Financial Officer**

So, you calculate it by each pension scheme as to its - and you'd look at the contribution to SCR and then that works out the cap per scheme.

At the year end, we were below those caps. At the half year we're above them. So we're now into that shock absorber phase for both of the main UK schemes. So sort of ...

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**Stephen Hester, Group Chief Executive**

So you're right. When Charlotte said - at the cap, she really meant slightly above it.

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**Charlotte Jones, Group Chief Financial Officer**

Well through it.

.....

**Greig Paterson, KBW**

So slightly above or was it ...

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**Stephen Hester, Group Chief Executive**

It was 2% above, over half year.

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**Charlotte Jones, Group Chief Financial Officer**

Yeah.

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**Stephen Hester, Group Chief Executive**

So in other words ...

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**Greig Paterson, KBW**

Two points.

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**Stephen Hester, Group Chief Executive**

Yeah, two points. So in other words our capital ratio would have been 169 had it been all eligible.

.....

**Charlotte Jones, Group Chief Financial Officer**

Yeah.

.....

**Stephen Hester, Group Chief Executive**

By the way, as of the end of July I think that 2% is down about half a percent because there's been some market movement in July. So it bobbles around all over the place. Next question, back here.

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**James Pearse, RBC**

Morning all. Thanks for taking my questions. So the first one is just on reinsurance, so can you quantify how far through the aggregates you are on your regional reinsurance programmes?

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**Stephen Hester, Group Chief Executive**

I can. It's in the press release.

.....

**James Pearse, RBC**

Okay.

.....

**Stephen Hester, Group Chief Executive**

So you can look it up there. It's not completely in my head, but it's all written down in the press release.

.....

**James Pearse, RBC**

Fine, okay. And then the second one was on the best in class ambition. So I know that you said you pushed back the kind of the range in terms of timeframe by a year, because of the current run rate I think you said in Scandinavia and Canada. On a normalised basis would you expect to still hit that ambition?

.....

**Stephen Hester, Group Chief Executive**

I worry about normalised because that requires me to be certain about what normal is. And so, you know, Canada is a really good example that what we have historically assumed as normal weather, we are moving our assumption.

And so I would expect us to do significantly better than a 94 combined ratio in Canada normalised for old weather. But lots of the pricing increase we're putting through is to assume worse weather going forward. And so it's just a tricky answer.

Generally, my expectation would be in normal weather for more recent years in Canada we would be operating once the current pricing earns through. So that's why I thought next year, if next year was a new normal year, Canada has a very good chance of hitting the 94 combined ratio.

Obviously, that requires some significant improvements. A chunk of that is weather but a chunk of that is really a very substantial rate just earning its way through the books, which obviously is true of the whole industry.

And then as I say, in terms of Scandinavia although there's lot of things we want to improve, really the thing that has to change is Danish Commercial Lines to get us into our target. And so again, hopefully the second half will be better. Hopefully next year will be better still.

And I think also in Scandinavia our costs still have another two points to fall, which I don't think by the way will happen next, but we can easily where we get to our ambitions in those two territories. Whether we get there faster or slower is partly how we execute and partly down to what the outside world throws at us.

In the UK we can see how to do it, we just know it's going to take us longer than in some of the other markets in part because of it's technology dependent, and it's also about rebuild of certain competencies and so on and so forth.

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**James Pearse, RBC**

Thank you.

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**Stephen Hester, Group Chief Executive**

So let's, see. Let's go over here.

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**Andy Sinclair, Bank of America Merrill Lynch**

Thanks. Three for me if that's okay. So firstly and secondly, a couple of questions on the UK. Scott, you mentioned the UK core Motor business maybe not having scale. Is that something you'd consider an exit or what can you do to build scale of that business in a tougher market?

Secondly, staying on the UK you mentioned the two points of expense ratio improvement. How much of that is attributed to the exit books just getting rid of the costs related to those versus the rest of the portfolio?

And thirdly, just on Denmark Commercial. Just any colour that could be given on the attritional creep that we've had in Danish Commercial, particularly given the comments about dependence on 1:1 renewals?



.....

**Stephen Hester, Group Chief Executive**

Yeah, I'll ask Scott to answer the first two. But just on Denmark, as I say the big issue in Denmark was really large losses. But beneath that we have had attritionals move out in two portfolios, Property but really concentrated in Real Estate, which is basically condominiums and things like that, and in Commercial Auto.

It's interesting actually; Real Estate has hurt us all around the world. I think there's a trend, things like of escape of water and so on, for what I'd commercially managed housing to have crappy loss ratios from an insurer's standpoint. And so actually in that segment we're having to take action in lots of different places.

But so those are the two places where we need to take some action related to the attritional loss ratio. And then related to the large loss ratio there are two segments that have been disproportionately hurting us. One is the feed through of some of the sub-segments of the Renewable Energy book that hurt us last year, which we've said we're exiting that sub-segment, but we haven't badged that in the exit portfolio so that's still in the ongoing. And then our Municipal area in Denmark, which is primarily around hospitals, has had some crappy large loss experience, and so we're going to get out of that. But again, we're not badging those exits.

But Scott, do you want to take the UK?

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**Scott Egan, Chief Executive Officer, UK&I**

Yeah. Two things, so just if I answer the second one first, and the 2% is on continued. Okay? So, and the fixed cost drag on our exited business is reasonably immaterial.

If I come back to Motor, my ambition is to actually build a Motor capability and sort of overall proposition that I think works for the UK.

If you remember a big part of new investment in technology has been about building a sort of core technology platform that we can then digitise, which in turn I think allows to at least have some of the tools to compete in the UK marketplace.

I think having a wider product base in a direct space is actually strategically really important to allow cross sale and leverage across the different products. So my ambition at the moment is to work out a strategy where we can align our capabilities, because we have to build them. We're not at the same level of capability as some of the more sophisticated players, and really leverage that carefully off the back of some of the investments we've already made. And that's what myself and the team will be working through in the second half of this year.

.....

**Stephen Hester, Group Chief Executive**

Sorry, one thing I should just say because we didn't mention it in our presentation on the subject of Motor, the Ogden chain, which obviously doesn't hit us so much because UK Motor isn't a big bit, but it will hit us probably £14m/£15m after tax, and that will be booked in the third quarter. And that was what I meant by PYD headwind in my statement.

.....

**Ed Morris, JP Morgan**

Thank you. Two questions. Just on that UK point, can you just clarify is this something that you would be looking to do organically or is acquisition ...

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**Stephen Hester, Group Chief Executive**

Yes. Yes, organically.

.....

**Ed Morris, JP Morgan**

Okay, organic. And the second question is around some of the below the line items. Really thinking about this with reference to how you think about capital management, I appreciate it's a little early in the year to set our expectations on special dividend, but just when you think about that pay-out range and you think about how you manage capital are you thinking about it with reference to underlying EPS or statutory EPS? Thank you.

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**Stephen Hester, Group Chief Executive**

Thank you for the question. So, what I would call our regular dividend, we think about in relation to underlying earnings, so in the first half that would be 21p. And so things that happen beneath the line would not normally impact our thinking of regular dividends.

When we think of the ability to pay more than regular dividends, whether that be in stock buybacks or any other form then obviously we look at the total capital picture and that would include some things below the line.

Now of course in the first half two of the three things that sat below the lines don't have a capital impact, so the only thing in the first half that was below the line did have a capital impact was exits. I think that will be a much smaller number in the second half, touch wood.

Not appearing in the income statement that has an income as pensions, pensions it all happens in the first quarter, so the first half you'd have to annualise so its impact across the year will not be any higher than we guided at the beginning. And then obviously we've given our data guidance on pull-to-par.

Pensions is sort of - we're not quite sure how to treat because pensions may optically burden Solvency II calculation. But if it does then it creates a buffer above Solvency II which is available to absorb a negative. So I think pension sits in a grey zone is how we really think about it.

We don't intend any of this to be strictly mathematical and so, you know, it remains our ambition to have the capacity in the coming years to do more than just ordinary dividends. But I do think that the market has continued to want to bully us on it and I'm not going to be bullied. And so we will continue to disappoint the bulls in this regard but to stay within our policy. You can have one supplementary in there.

*Laughter*

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**Ed Morris, JP Morgan**

Sorry, just a brief follow-up. When you the actions for the UK on cost would you expect that to also come with some exceptional costs?

.....

**Stephen Hester, Group Chief Executive**

Yes, I do expect there to be some costs for the cost programme. We haven't finalised the cost programme yet, so we don't know how much. If you asked me to guess, it would be spread this year and next year so it would be in two bites. And I don't, you know, if I completely invented a number of £20m this year, you know, it's not going to be 50 and it's not going to be nothing, order of magnitude. Okay?

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**Ed Morris, JP Morgan**

Thank you.

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**Ming Zhu, Panmure Gordon**

Just two questions please. And the first is in the UK Household, the top line came down 13% year on year, 4% is because of the sale of the Oak Home. Are the remaining 9% all from the rate increase? I'm trying to get a sense in terms of your top line sensitivity to the rate increase and what's your guidance going forward please?

And my second question is Scandinavia. Norway is very small for RSA, but the underwriting still made a loss even though the loss has halved. What's your strategy in Norway going forward? Would you consider to exit that place, or maybe do an acquisition? Because if you do a bolt-on acquisition presumably the PEs are pretty high in that region. Thank you.

.....

**Stephen Hester, Group Chief Executive**

Thank you very much for your question. Just on the UK, we significantly lost Household volume in 2017 by pricing well ahead of the market mainly in reaction to escape of water.

That has had the desired affect and our attritional loss ratios in Household have come down very substantially and have now allowed us to be profitable and competitive in the new business market, which is why Scott has said that our new business is now significantly above where it was before and is starting to outweigh the drag.

However, when you lose volume on the back book it feeds through for a little bit before your new business can outweigh the renewal gap that you had and so you know, I would hope that we would in total grow in Household next year over this year.

We don't have a firm plan yet, but I would hope that that would be where we would be. But obviously, you know, because the UK Personal Lines market is so dominated by price comparison websites it is one of those hair trigger markets that you can put on a lot of volume if you want to drop prices, and you can lose a lot of volume if you don't want to drop prices. And predicting what's going to happen for us given that we want to be disciplined on profitability requires you predict the rest of the market, and obviously that's slightly less easy to do.

On your topic of Norway, you're absolutely right to make the observation. We are completely re-platforming our Norwegian business to, in Scandinavian terms you know, the most up to date technology, that process will be done by halfway through next year. We're about halfway done now.

And we believe that that will do two things. It will one, allow us to start substantially reducing our costs and our loss ratio is in line with competitors in Norway. The thing that makes our results not in line is entirely costs. And so that intervention will allow us to significantly improve costs, albeit not until starting the second half of next year. And secondly, it will give us a greater agility and digital capability than the norm in the Norwegian market, which should allow us to be more commercially competitive.

So those things I think should give us a platform to improve. Are we subscale anyway? Yes, we are. Is there an easy way out of that? No. If there were bolt-ons that made sense post the re-platforming, we'd look at them, but our strategy isn't based on it.

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**Oliver Steel, Deutsche Bank**

So, two questions. The first is, you talked about raising your estimates for where the loss is going forwards in Canada. And obviously you've also done an awful lot of reinsurance programmes in Canada, in Denmark, you mentioned in the UK, but I don't see any updated guidance for large losses, weather losses even at the Group level, so I'm just wondering if you wanted to sort of comment on that relative to the numbers that you historically show on the five year average? So that's question one.

Question two is sort of 'similarish' I suppose, specifically on Canada. You're getting very strong rate increases. Are those running ahead of claims inflation in its sort of broadest form, recognising obviously that future claims will be volatile?

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**Stephen Hester, Group Chief Executive**

Thank you for that question. I would say on large losses at the moment we have no reason to change our long term guidance because we don't think there's inherently a trend in that that we've spotted, and so our planning assumptions remain the same. Obviously, at a Group level they can change as the business mix changes, but the underlying we haven't particularly changed anything.

In terms of weather I would say we also haven't changed any weather assumption outside Canada. In other words, the weather trends away from Canada, even if climate change is happening, are not pronounced enough for us at this stage to feel that we need to change anything.

In Canada truthfully, we don't know what to change it to, because obviously the inherent in year volatility dwarfs the ability to draw a trend line. And so basically what we're doing is putting through the maximum rate in Property Lines we can without losing stupid amounts of volume and seeing where that gets us. So I wish I could give you a more scientific answer than that, but that's the answer that I'm giving you.

And now I've slightly forgotten if there was another nuance to your second part of your question about Canada. Can you remind me what your second part was?

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**Oliver Steel, Deutsche Bank**

Yes. The second question was, are rate increases in Canada running ahead of your ...

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**Stephen Hester, Group Chief Executive**

Yeah. So the first answer is, yes. In other words for example, we have a two point improvement in the attritional loss ratio in Canada already, and that's with plenty more to earn through. What I don't know is how much of that improvement we're going to spend in higher weather trends going forward, that's a guess truthfully. Andrew?

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**Andrew Crean, Autonomous**

Good morning. A couple of questions. Firstly, Charlotte I think said that the UK combined ratio would be worse in the second half but better than the target of 96/7. And then Scott said he wanted it to be at the bottom end of the target in 96. So I don't know whether they could have a conflag.

.....

**Stephen Hester, Group Chief Executive**

We've got a market making process, there's a bid and an offer here.

*Laughter*

.....

**Andrew Crean, Autonomous**

Okay. The second question, if I go back two or three years the investment income guidance was some £60m, £50m/60m per annum higher than it is now, and that's when you set the combined ratios. If you're not changing your combined ratio targets, that implies that your return on equity targets are coming down. Is that fair and what is the quantum of that?

.....

**Stephen Hester, Group Chief Executive**

Important second point, our combined ratio targets are set relative to the, what I'll call our best in class ambition. In other words, they're set at the level that we think that would put us in the upper quarter on the performance in each of our markets. So they're not set in relation to return on equity target, they're set in relation to what would we achieve if we got our relative performance to the levels to which we aspire at now.

And therefore if over time all competitors were to say, lower interest rates means in need more underwriting income, therefore I'm going to rate harder, therefore I'm going to have a lower combined ratio, then you'd see the market improving its performance and you'd see us move those targets. But that would be where our targets in combined ratio terms would be calibrated.

Of course our current target of 13% to 17% return on equity is massively in excess of cost of capital and our ambitions imply that at least the top end of that target even with a lower investment income, and so I don't think our targets are at threat. But you are of course mathematically correct, if it were to be that the world in perpetuity has the

interest rates, we see now then all insurers will have lower investment income. And unless they do something in terms of profitability of underwriting, we'll have a lower ROE, even though you'd much rather have an insurance ROE than a banking ROE in that scenario.

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**Dominic O'Mahony, Exane BNP Paribas**

Thank you. Just one question left. In Canada the market looks very hard, as you say and the commentary from Intact is very positive through the rest of the year. I'm just trying to think about what could bring that to an end. In the past the Canada Government and particularly the Ontario Government has been quite active in legislating to at least reduce claims and thereby reduce rates.

What do you see as the outlet there? And I think there is chatter about whether there might be something to come there. I'd be interested in your thoughts on that. Thank you.

.....

**Stephen Hester, Group Chief Executive**

Yeah, I think we should probably divide Canada rate into regulated rate and unregulated rate, so the regulated rate is in the Domestic Auto markets, which of course is the biggest of the markets. And there, while each province has its own formula, it's basically linked to return on capital. And so the rate hardening cycle will end once the insurers are earning an adequate return on capital on the Motor books.

Now, my guess would be most of us plan to be in that position at some point next year. Some earlier, some later, some may not get there. But our rate filings are, that I could see, by the time they've all earned through would give us that sort of run rate next year, call it mid 90s combined for our Auto portfolios.

And so the thing that would see it slow down basically is industry profitability. There are, as you say, from time to time regulatory changes that happen that change claims patterns. But then with some lags you get an equal and opposite, if you like, change in regulation in terms of the rate you could have, and so that creates leads and lags but it doesn't change the basic formula. And although there is discussion, there's discussion in all provinces of water reform in different ways. There is discussion in Ontario. In Ontario the discussion would be oriented towards lower claims and therefore lower prices. But I don't really care, you know, so long as the margin between claims and prices is adequate. But I'm not holding my breath for anything in that regard.

Away from the regulated element and obviously the majority of our premiums are unregulated, because all of our Commercial premiums are unregulated and all of Household premiums are unregulated, and all of our Travel books and so on are unregulated. You know, there clearly the issue is what does the market bear? And that is much more driven at the moment by, you know, weather and weather pricing.

But again, who knows? Let's see. I think the level of pricing should get us into a good place as we go into next year as an industry. Or maybe not as we go into next year, but as we earn through next year. But it's all dependent on continuing to watch the weather line and hope that there are some years where volatility goes in both directions, not just in one.

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**Sami Taipalus, Goldman Sachs**

The first one really is from Scott on the UK; you talked about More Than as a potential 'jewel in crown' in the future. But how would you think about the UK Commercial Lines business? You know, do you think that could be a 'jewel in the crown' as well or are there some structural reasons for why it couldn't?

And the second question is more broadly on capex across the Group. You know, we're seeing some of your competitors investing quite heavily in their businesses at the moment. Do you think there's a need for further investments within RSA as well? I guess, you know, the UK would be on potential area for such, but more broadly across the Group as well? Thank you.

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**Stephen Hester, Group Chief Executive**

Thank you. I'll ask Scott in a second to answer your first question. On your second, capex for us, the only area we really spend capex is of course on technology. And our working assumption is that every single year for as long as we can see into the future we will try and have less people and more computers.

And therefore that means that we will aspire for one to offset the other as it were. So in other words, to have competitive cost ratios and ideally even better cost ratios in that process. But fundamentally I would expect us to spend more on technology than our amortisation every year for the foreseeable.

The constraint is not really a spending constraint. It is a significant bottleneck that all companies have of how much can you do at once whilst keeping business as usual going in a satisfactory way.

And so if we took this year for example, my guess is we'll spend about £30m at a Group level more than depreciation. It's some number within £10m of that anyway. And if you took a range of £20m to £50m more than depreciation in the coming years, and that's why in our dividend guidance we say, you know, assume that up to 25% of our profits are retained for a combination of pensions and capex. In no year will it be precisely 25%, but that's the thinking.

Scott, do you want to take the first ...

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**Scott Egan, Chief Executive Officer, UK&I**



Yeah, I'll take that first. Sorry, I should have turned around and kind of waved. Where was the question? Perfect, right. Thank you.

So, just to be really clear of what I said. I said, the profit 'jewel in the crown'. Okay? So, there are many parts of the UK business which I think are 'jewels in the crown', but like most direct businesses the reason they're the profit 'jewel in the crown' is because there's just less people in the chain in terms of the distribution channel.

So, I do think we can have and do have jewels in the crown in our Commercial portfolio. I tried to give one example which was our regional book where, you know, I talked about higher retention, growing new business, etc, and good combined ratios. But there are many other portfolios in that book as well. And actually an interesting one is Marine, and our regional broker is a really profitable book for us and has been for many years. So there are 'jewels in the crown' but the More Than direct thing is really a profit jewel just because the distribution channel advantage.

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**Stephen Hester, Group Chief Executive**

But inherent in our ambition for the UK, you can debate whether we'll hit it or how long it'll take us to hit it, but you know, inherent in that is combined ratios in the lower end of the 90s, let's call it the 94 target, in Commercial as well as in Personal.

Okay, the next one along.

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**Ben Cohen, Investec**

Hi. I just had a question on the negative PYD on the Commercial from 2018. Could you give a bit more colour as to where that came from? And I suppose I'm interested in your confidence that you've sort of fully adjusted for those trends. And I suppose then that the last part of that question is, looking into 2019 and where you're setting your initial loss picks, how have those changed because of you're learning from these reserve increases? Thank you.

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**Stephen Hester, Group Chief Executive**

Thank you for that question. And I'm going to answer it with a degree of humility because obviously the job of actuaries, has some mathematical complexities to it but ultimately what they're trying to do is say does the past give you clues in terms of data to the future. And though sometimes it does, also sometimes it doesn't and that's what PYD is an unforecastable line, truthfully speaking and why we try not to rely on it very much.

The negative PYD from 2018 actually was very broadly spread, and of itself had all kinds of diverse reasons. So for example, UK subsidence, it was hard to know how much to put aside for subsidence from last summer's hot weather. We ended up having, and subsidence can show through a lot later when people make claims because they don't

realise it until six months or twelve months afterwards, and so we've had a bigger tail of subsidence into this year from last year's hot summer than before.

To pick a different example, in Canada there was some storms in the last two days of December which we thought we'd captured adequately in terms of losses, but they turned out to cost us a bit more, which hurt us in the first quarter.

In our Marine books and in our Construction and Engineering books in Europe we had a bunch of late reported claims, which often happens in those and particularly happens on follow lines which were more than the actuarial assumption. So, in Denmark there was some stuff on Commercial.

So, there was no pattern as to these things except the, if you like, what I regard as the common pattern, is that how actuaries fundamentally work is that they take rolling averages of losses by line. Short tail lines is a shorter rolling average, long tail lines is a longer roller average. And therefore your latest year is never given 100% weighting, and that means you will tend to lead and lag market improvements and market dis-improvements.

Now some companies mask that through playing around with risk margins and hidden reserves, which we don't do. And so some companies will show us - move a picture. But I promise you the underlying isn't smooth because of this is just how the actuaries work.

The second bit of your question is the important one. Okay, if you're having to strengthen 2018 in a bunch of different places, and many of our competitors are doing the same as I mentioned, what's the feed through of that into 2019? And so a number of those assumptions have meant that we started by the eight ball in 2019, and lost picks.

However, the strength of our actions and our rating actions has meant that we have managed to overcome that disadvantage and end up with attritional loss ratios that nevertheless improved in the first half relative to the first half of last year. And so thank God we took the actions we did, otherwise we might not have had that to report.

As to confidence going forward, you know, I can't give you any confidence because none of us can know what the future is and whether the first half patterns are now outweighing last year.

We can take encouragement from the fact that it was the first quarter where we really experienced the 2018 true ups and our second quarter PYD was in line with our plans. And so my working assumption is either we've caught it, or we've caught most of it, but I can't give you that promise.

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**Jonny Urwin, UBS**

Hi there. Two quick ones please. So UK Home, where is pricing running versus claims inflation?

And secondly on capital, could you give us some indication of excess capital on a rating agency basis please? Thank you.

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**Stephen Hester, Group Chief Executive**

On a rating agency basis again, the rating agencies in my view don't work like that. In other words they have a whole series of criteria for rating you, only one of which is a capital model. And the capital model is substantially outweighed by the qualitative models of risk management, franchise and so on.

And so, on the capital model we are in line with a stable Single 'A'. There's obviously a band to that, so we're in a comfortable position on the capital element of it, but that doesn't tell you anything much I think because the capital element, you know, you could be below par for capital if you're above par in the others and vice versa.

Scott, do you want to take the Household?

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**Scott Egan, Chief Executive Officer, UK&I**

The Home to be exact science, because it differs by peril, etc. But we probably see inflation running sort of around the 4'ish% rate in the first half year. On our Personal Lines Home book it's running roughly around 5% or 6%.

So again, back to what Stephen said earlier on, we've taken a lot of the corrective action and therefore what we're trying to do now is toggle between what we think are reasonably good loss ratios, top line volumes, sophistication and segmentation. That's the game that we're trying to play at the moment.

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**Stephen Hester, Group Chief Executive**

Over here.

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**Andreas Van Embden, Peel Hunt**

Thank you. Just a question around your Commercial Lines business. When I think the premium split outside of the London Market business, could you give sort of a premium exposure to large corporates versus the SMEs across the Group?

And when you think about underwriting in the next three years, are you emphasising large corporates more or less than SMEs when you think about improving your combined ratio?

The second question is about MGAs and distribution. What proportion of your premiums is MGA driven and how do the underwriting controls work there from a Group level?

And my final question is, I understand a lot of the underwriting decisions are made regionally, you know, the UK, Scandinavia, Canada, but I just wondered whether there is a separate Chief Underwriting Officer sitting on top of that and making sort of strategic decisions about risk appetite, business mix and how you want to allocate capital purely across the Commercial lines business? Thank you.

.....

**Stephen Hester, Group Chief Executive**

Thank you for those questions. The answer to your last one is there is. He's sitting here between Scott and the Chairman. His office is next to mine and Charlotte's office is on the other side of mine. So you can see where our priorities sit.

And so we have centrally a whole group of people under Nathan, both for underwriting and claims. We badge the two together because there's, if you like, the technical disciplines who are setting underwriting standards, who are monitoring portfolio, who are monitoring underwriting quality and who provide training to everyone in the Group on a central basis.

So we have centralised standards and set the appetites and so on and so forth. And this is a very important role because while the conditions in each of our markets is different and while our markets are overwhelmingly regionally driven, and therefore we think it's right to decentralise decision making at least in expertise and underwriting standards you need to have an important central overlay, which we do have.

As to your first two questions, I'm sorry to say I don't have at my fingertips the statistic and we'll be happy to try and get it to you afterwards. But the statistic also has enormous complexity to it for both of the questions you asked, because obviously the move from small to large corporate has got many grey areas inside it. And normally in fact we have SME business, mid-market businesses and then high end businesses.

And I would say the great majority of our business in Canada and in Scandinavia are either small or mid, just simply because there aren't that many big companies in the markets, but there are some, and renewable energy would be an example in Denmark. And in the UK there's a bigger element of large companies, although that was where we took quite an axe in terms of the London Market, but I'm afraid I don't have the precise number.

In terms of emphasis I would say our emphasis is on the regional business. It's not on the ocean going large corporate business where we do that, if you like, as an accommodation to make sure we don't get eroded in our ability to serve mid-market and small.

Mid-market, we like. Small, depends on the country. Small has attractive retention characteristics normally and you know, is a large segment. But it also normally has an extremely high cost to serve because the premium sizes are about the same as individual. But it's not as automated as individual insurance because it has more

complexity and it tends to still be broker distributed, which puts a huge, if you like, commission cost in the middle.

And so, in some places small is very attractive to us. Scandinavia is the best example where the great majority of small is done direct, so we don't have the commission drag. It's becoming more and more automated and we make really good money. And we're emphasising that like mad.

In Canada it's in transition, still doesn't make good money although it has to be said, Intact do, we don't, but we're automating like mad.

And in the UK, you know, we're automating but we're I would say furthest behind in getting small profitable in the UK. But it's really a cost to serve issue as it relates to small.

And I think that your - what was your middle question? It was about MGAs. It's almost the same answer on MGAs because there is a massive range of flavour of delegated. So MGAs is a particularly badge, but the way I think about it is whenever you give any element of your pen away, and there are many, many different flavours of delegation of authority to people, you have a distribution arrangement that you're not completely in control of. And we have hundreds across the Group of different kinds of delegated arrangements as so does every Commercial insurer. And some of it is Personal Lines ranging from quite a lot of delegation to not very much at all.

Our experience has been that - and we have departments and policies whose existence is to make sure that that is controlled partly from an underwriting standpoint, but also from a regulatory standpoint. And that's particularly important for example, in the UK nowadays that you make sure people are not doing something under your authority that, you know, you wouldn't like, whether that be sanctions or any other thing. And so we have all sorts of restrictions and audits around that and things like that.

What our experience has been is when you really give the pen away in a sort of open way; you do badly because the pen is abused. And when you can focus it narrowly on a particular segment which you otherwise wouldn't reach. I don't know, motorcycle owners in British Columbia or something like that, you can get very good results because you're very, very narrow, very specialised in hitting some in a way that you wouldn't hit through generalised distribution.

So that's why we have been shifting our delegated arrangements to specialty and why 65 million of our exit total was trying to exit what are called 'generalised' MGAs, which is largely complete.

Over here.

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**Abid Hussain, Credit Suisse**

Hi, morning. Just one question from me please on the Solvency II ratio. Is it possible to translate the Solvency II target range into financial strength rating? So at what point for

example might the Solvency II ratio lead to a Single A rating to an A+ rating or a Single A to a -A rating?

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**Stephen Hester, Group Chief Executive**

It's really hard because the calculations are done differently. I think nowhere within ten points. I think our Solvency II ratio could be 10 or 15 points either side of where it is and not mean anything for our credit rating. There's that kind of tolerance in it. You know, if we were 180, you know, we'd probably be pushing an upgrade. I'm not saying 180 rather than 175 or any number, but I'm just trying to give you a sense. We're in a zone which is probably a 20 point wide zone, which would translate to where our current credit ratings are. But it is a deeply imperfect translation.

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**Philip Ross, Mediobanca**

Hi. Just coming back on that last point about the solvency range. You have target of 130 to 160 but prefer to operate above it. Is there a chance in future that if the business performs well, more reliably or becomes less volatile you might be in the target range or is it the point that that range is obviously linked to the credit ratings and other such metrics?

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**Stephen Hester, Group Chief Executive**

Yeah, I think that the credit rating is the only thing we care about. So if we got upgraded to 'A+' I would think we had too much capital if that was the reason we were being upgraded. As long as we're at Single 'A' then we're going to think we've got the right amount.

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**Philip Ross, Mediobanca**

Okay so if that's separate to Solvency range you could see yourself in between ...

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**Stephen Hester, Group Chief Executive**

Yeah, so if there was some divergence of the methodology such that you had to have either a lot higher or a lot lower solvency for a given credit rating then the solvency would go up or down because it's the credit rating we're targeting. It's just that's got so many subjective elements to it that it's hard to have a conversation about it if you see what I mean.

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**Philip Ross, Mediobanca**

Thank you.

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**Stephen Hester, Group Chief Executive**

Right, we're running out. How are we doing? Any more for anymore? Great.

We'll look, thank you for joining us. Obviously, you know where to find our teams for follow up questions.

As I said, I think we believe that we've made a promising start to this year. We believe that we are motoring well in the majority of our business, that it's strong. We believe we've taken the right actions for the things we needed to correct. We need to see that feed through.

We've got fingers crossed in the second half. So we don't want anyone to get carried away, but we do think this company is capable of more and we intend to get it out of the company.

Thank you for joining us.

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