Operating review

Motor

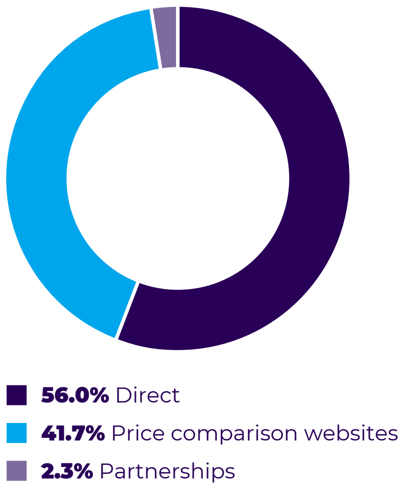
Motor: performance summary

Own brand in-force policies reduced by 2.9%, with an overall reduction in in-force policies of 3.4% to 3.8 million.

Own brand gross written premium reduced by 7.7%, overall gross written premium reduced by 8.2%.

Operating loss of £77.2 million, reflecting heightened claims inflation, an increase in claims frequency, and lower prior-year reserve releases.

Gross written premium by channel



	2022 £m	2021 £m
In-force policies (thousands)	**3,836**	3,971
Of which:		
Direct own brands[1]	**3,756**	3,869
Partnerships	**80**	102
Gross written premium	**1,432.7**	1,560.8
Of which:		
Direct own brands[1]	**1,398.5**	1,515.2
Partnerships	**34.2**	45.6
Operating (loss)/profit[2]	**(77.2)**	314.8
Loss ratio[2]	**86.2%**	64.3%
Commission ratio[2]	**3.4%**	3.3%
Expense ratio[2]	**25.1%**	24.8%
Combined operating ratio[2]	**114.7%**	92.4%
Current-year attritional loss ratio[2]	**90.9%**	72.9%

Market overview

The combination of the implementation of the FCA's PPR regulations, and the impact of elevated inflation, created a challenging motor market backdrop during 2022.

The FCA's PPR regulations reduced new business shopping and increased retention levels across the market. The increasingly competitive trading environment was exacerbated by market premiums not keeping pace with heightened claims inflation.

The increase in claims inflation was driven by the cost of second-hand vehicles, as well as supply chain disruption, which led to longer repair times. Claims frequency also increased compared to 2021, which saw lower driving levels during lockdowns.

Market premiums increased by mid-single digit percentage points at the start of the year with the introduction of the FCA's PPR regulations, followed by significant increases during the second half of the year.

Performance

In-force policies and gross written premium

Motor in-force policies reduced by 3.4% in 2022, with own brands falling 2.9%. The majority of this reduction was in Q3 as we increased premiums to reflect higher inflation trends and saw a reduction in new business volumes.

Retention remained strong on average over the year at 81.6%, although reduced across the year as renewal rate increases from higher claims inflation started to offset premium reductions from the introduction of the FCA's PPR regulations.

Motor direct own brand gross written premium was 7.7% lower in 2022. Average premiums fell 2.8% during 2022, reflecting the impact of the FCA's PPR regulations on renewal average premiums, as well as a greater mix of renewing business which tends to have lower average premium. Furthermore, changes to the Group's risk pricing models in H2 reduced risk mix and therefore average premium.

Motability Operations: Delivering an exceptional claims service

In H2 2023, we will welcome 600,000 new customers as part of our 10-year partnership with Motability Operations. We were chosen to partner with Motability Operations because of our excellent customer service record, our modern and innovative digital systems, and our ability to provide efficient vehicle repairs through an integrated, aligned and effectively managed supply chain. The partnership will help us to gain further insight into their fleet of modern vehicles and build additional scale in our expert claims management service.

In H2 2023, we welcome our new partnership with Motability Operations, which is expected to provide around £500 million of gross written premium per annum from 2024, of which 80% is reinsured.

Underwriting

Claims inflation accelerated over the course of the year. Entering 2022, we expected claims severity inflation would track slightly above our medium-term 3% to 5% expectation. Supply chain disruption, partly in response to the war in Ukraine and resource constraints across the market, drove an elongation in car repair cycle times, therefore increasing average repair costs as well as leading to longer credit hire durations. Furthermore, used car prices, which rose strongly in 2021, remained high throughout the year, particularly for relatively new cars.

Whilst we continue to believe we are outperforming the industry on the cost of claims we manage through both DLG Auto Services and our managed network, claims inflation arising from third-party managed claims was higher than expectations and pricing. Overall, we estimate claims inflation for 2022 was around 14%.

The combination of lower renewal premium arising from the FCA's PPR regulations, as well as higher than priced-for claims inflation and the non-repeat of 2021 Covid-related frequency benefits, resulted in a 18.0 percentage point increase in the current-year attritional loss ratio to 90.9%. Prior-year reserve releases were £60.7 million lower, resulting from delayed settlements of large claims and higher claims inflation on third-party claims. These factors combined resulted in an overall loss ratio of 86.2% (2021: 64.3%).

Combined operating ratio and (loss)/profit

The combined operating ratio was 114.7% (2021: 92.4%), primarily as a result of the higher loss ratio. The expense and commission ratios were broadly stable at 25.1% and 3.4% respectively.

Instalment income was £4.7 million lower than prior year due to lower Motor premiums while other operating income increased a little due to higher salvage recoveries.

Overall, Motor reported an operating loss of £77.2 million compared with a profit of £314.8 million in 2021.

Notes:
1. Direct own brands include in-force policies under the Direct Line, Churchill, Darwin and Privilege brands.
2. See glossary on pages 251 to 253 for definitions and appendix A – Alternative Performance Measures on pages 254 to 257 for reconciliation to financial statement line items.

Home

Home: performance summary

Total in-force policies 6.2% lower at 2.5 million. Own brand policies were 7.8% lower at 1.7 million, reflecting a reduction in new business sales volumes.

Total gross written premium was 10.3% lower at £518.1 million. Own brand gross written premium was 8.4% lower at 381.5 million.

Total operating loss of £8.7 million, primarily driven by several significant weather events and lower prior-year releases.

Gross written premium by channel

- **56.4%** Direct
- **18.1%** Price comparison websites
- **25.5%** Partnerships

	2022 £m	2021 £m
In-force policies (thousands)	**2,501**	2,667
Of which:		
Direct own brands[1]	**1,732**	1,879
Partnerships	**769**	788
Gross written premium	**518.1**	577.8
Of which:		
Direct own brands[1]	**381.5**	416.7
Partnerships	**136.6**	161.1
Operating (loss)/profit[2]	**(8.7)**	141.8
Loss ratio[2]	**80.2%**	50.7%
Commission ratio[2]	**5.1%**	6.9%
Expense ratio[2]	**21.6%**	22.5%
Combined operating ratio[2]	**106.9%**	80.1%
Current-year attritional loss ratio[2]	**60.9%**	55.7%
Normalised combined operating ratio[2]	**94.7%**	85.2%

Market overview

In 2022, the implementation of the FCA's PPR regulations had a more material impact on the Home market than Motor, whilst claims inflation increased at a more modest rate.

There were significantly fewer customers shopping for insurance quotes as more customers chose to stay with their existing insurer.

Customers that were shopping for insurance benefited from a wider choice of policies as the reforms drove more product diversification including "essential" style policies at a lower price point.

Following new business market premiums increasing at the start of the year on implementation of the FCA's PPR regulations, they remained broadly level throughout much of the year despite higher claims inflation.

In February 2022, the UK experienced three significant storms, Dudley, Eunice and Franklin. The extremely high temperatures in the summer of 2022 led to a rise in subsidence claims, and in December most of the UK experienced a freeze weather event which left many households with burst pipes.

Performance

In-force policies and gross written premium

The implementation of the FCA's PPR regulations in January 2022 resulted in lower premiums across the market, with fewer customers shopping and higher customer retention rates.

Against this backdrop, we focused on maintaining margins and therefore saw a reduction in new business sales volumes, in line with the broader market. Home in-force policies fell by 6.2% to 2.5 million while direct own brands fell by 7.8% to 1.7 million.

NatWest Group: Home contract extension

We extended our longstanding partnership with NatWest Group, continuing to provide home insurance to close to half a million of their customers until 2027. We were recognised for our ability to deliver excellent service and easy, digital-first journeys, making use of a new platform that improves the experience for customers, pre-populating their data and introducing our home product to Natwest Group's banking app, giving them access to simple and flexible products.

Direct own brands average premiums were stable year-on-year as pricing increases for new business were offset by renewal decreases and risk mix changes.

Overall, Home direct own brands gross written premium of £381.5 million was 8.4% lower than 2021.

Underwriting

Claims inflation remained elevated above the Group's long-term average and was estimated to be around 7.5% for 2022. This was consistent with the Group's pricing assumptions.

Home also saw several weather events during 2022, with floods, subsidence and freeze events totalling £119.1 million, well above our 2022 annual assumption of £52 million. Our weather-related claims assumption for Home for 2023 is £54 million. The freeze event in December was Home's most costly event since the Group listed over a decade ago.

Home's loss ratio increased by 29.5 percentage points in 2022 to 80.2%, predominantly due to higher weather costs, which increased 19.8 percentage points. The current-year attritional loss ratio increased by 5.2 percentage points following pricing action on the implementation of the FCA's PPR regulations and the non-repeat of positive claims experience in 2021. Prior-year reserve releases were £26.2 million lower following elevated releases in 2021 and the impact of inflation on subsidence claims costs from older years.

Combined operating ratios and (loss)/profit

Home's focus on protecting the value of the book enabled it to deliver a combined operating ratio normalised for weather of 94.7%.

An improvement in the expense ratio and a lower commission ratio helped mitigate some of the loss ratio deterioration and, overall, Home delivered an underwriting loss of £35.6 million (2021: profit £110.0 million) and a headline combined operating ratio of 106.9%.

The underwriting loss was partially offset by instalment and investment returns, leading to an operating loss of £8.7 million (2021: £141.8 million profit).

Notes:
1. Direct own brands include in-force policies under the Direct Line, Churchill and Privilege brands.
2. See glossary on pages 251 to 253 for definitions and appendix A – Alternative Performance Measures on pages 254 to 257 for reconciliation to financial statement line items.

Rescue and other personal lines

Rescue and other personal lines: performance summary[1]

Rescue in-force policies reduced by 3.9% to 2.2 million, driven by lower new business sales volumes in Green Flag direct and reduced linked opportunities from lower sales in Motor.

Total in-force policies and adjusted gross written premium reduced by 3.2% and 2.6% respectively, reflecting lower premium from Rescue, partly offset by higher premium in Travel.

Total operating profit of £59.7 million includes £52.8 million profit for Rescue.

Adjusted gross written premium by product[1,2]

- **53.3%** Rescue
- **26.2%** Pet
- **20.5%** Other personal lines

Ongoing operations[1]	2022 £m	2021 £m
In-force policies (thousands)	**2,424**	2,505
Of which:		
Rescue – ongoing operations	**2,185**	2,273
Of which Green Flag direct	**1,106**	1,179
Pet	**128**	138
Other personal lines – ongoing operations	**111**	94
Adjusted gross written premium[2]	**273.9**	281.1
Of which:		
Rescue – ongoing operations	**143.7**	155.2
Of which Green Flag Direct	**88.2**	88.3
Pet	**70.8**	71.4
Other personal lines – ongoing operations	**59.4**	54.5
Operating profit[2]	**59.7**	73.3
Loss ratio[2]	**54.0%**	49.9%
Commission ratio[2]	**3.9%**	3.6%
Expense ratio[2]	**27.9%**	25.4%
Combined operating ratio[2]	**85.8%**	78.9%

Market overview

Rescue

The rescue market continued its post-pandemic recovery in 2022 as consumer searches for breakdown cover increased.

The high inflationary environment adversely affected rescue service providers' claims costs due to the higher cost of fuel and insurance.

Other personal lines

The travel insurance market grew back rapidly in 2022, following the lifting of travel restrictions early in the year, with volumes of international leisure travel only marginally below pre-pandemic levels during the summer peak. European travel proved popular, with long haul destinations recovering towards the end of the year.

2022 continued to see pet ownership grow in the UK with an estimated 34% of households now owning a dog and 28% owning a cat[3].

Performance

In-force policies and gross written premium

In-force policies from ongoing operations reduced by 3.2%, primarily as a result of lower Rescue in-force polices, which was partly offset by higher own brand Travel polices. Gross written premium from ongoing operations reduced by 2.6% and showed a similar trend to in-force policies. Total in-force policies including run-off partnerships were 4.6 million and total gross written premium was £398.3 million.

Rescue

Rescue's in-force policies and gross written premium from ongoing operations were lower in 2022 as a result of lower

Green Flag: Disrupting the rescue market

Our Green Flag brand continues to disrupt the rescue market. We're delighted that this year it has been ranked by the Institute of Customer Service Customer Satisfaction Index as one of the top 20 brands for customer service in the UK.[4]

In 2022, Green Flag, in addition to launching a new online shop, extended its new technology ecosystem and enhanced its pricing and renewal capabilities.

Green Flag has also diversified its product portfolio, offering accessories via the online shop, as well as giving customers the convenience of booking maintenance and repair services, or providing a competitive price to check a vehicle's history before deciding to make a purchase.

Motor policies, where Green Flag is sold alongside the Motor policy, and transition effects as it rolled out its new policy platform.

Heightened claims inflation during 2022 increased average claims costs by 14%, driven predominantly by higher fuel costs and resource constraints across our network of suppliers. Claims frequency remained broadly stable with 2021, albeit below pre-pandemic levels.

In January 2023, we launched our first Green Flag branded patrol vehicles with repairs completed by our own mechanics. This aims to help mitigate the impact of heightened inflation as well as offer new revenue opportunities.

Rescue's combined operating ratio from ongoing operations remained attractive at 76.7%. Rescue operating profit from ongoing operations was £52.8 million, compared to £62.0 million in 2021.

Other personal lines

Other personal lines is made up of Pet, Travel, creditor and mid- to high-net worth business. Pet accounts for the majority of other personal lines profit.

Pet in-force policy count was 7.2% lower but premiums were broadly flat and profit increased year-on-year due to lower claims volumes and lower than expected claims inflation.

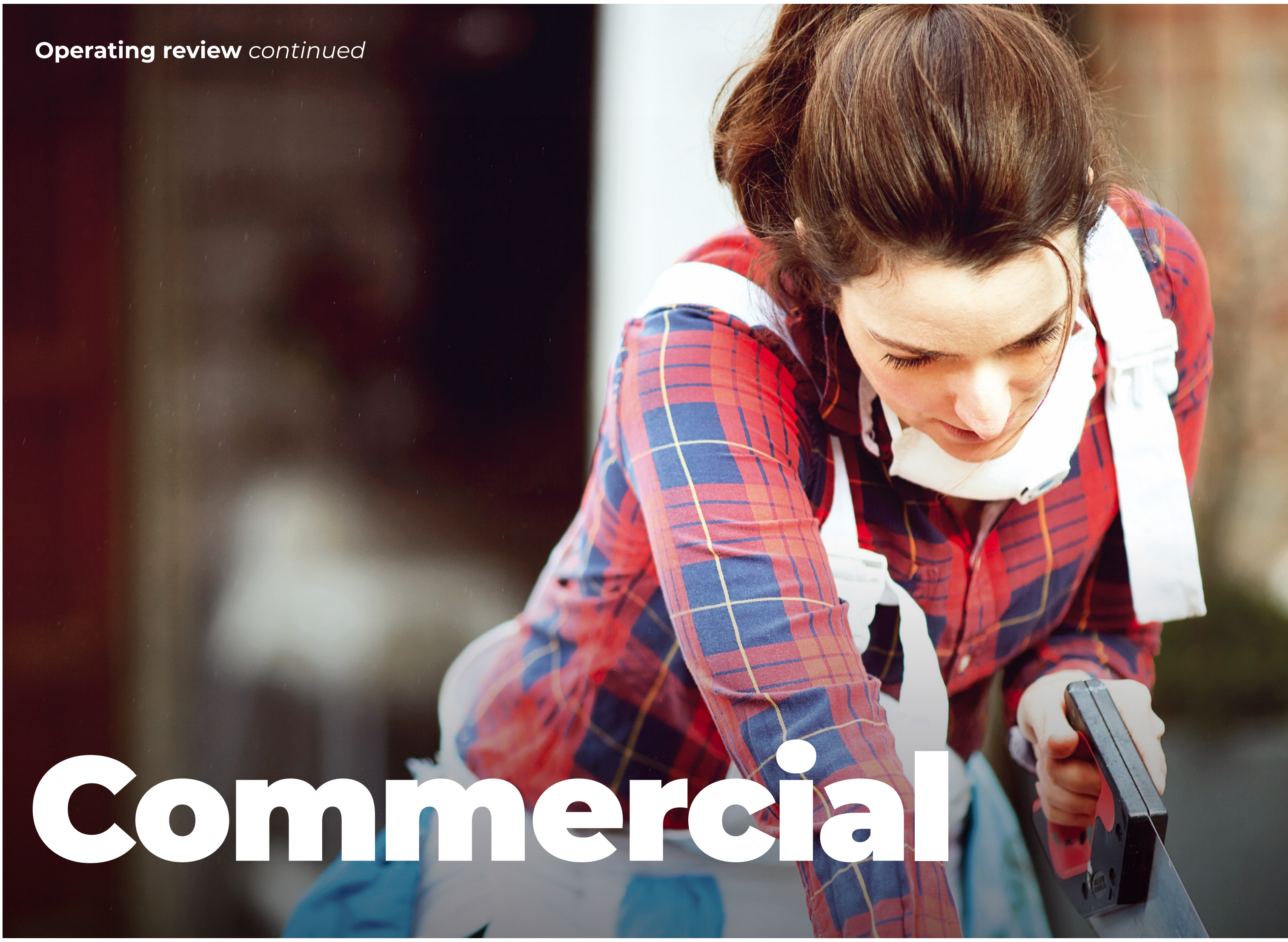
In Travel, the recovery seen across the industry in 2022 led to growth in premiums and in-force policy count.

The mid- to high-net worth business, Direct Line Select, reported an operating loss due primarily to weather-related claims.

Combined operating ratios and profit

Overall, the combined operating ratio from ongoing operations for Rescue and Other personal lines increased by 6.9 percentage points to 85.8%. Operating profit from ongoing operations was £59.7 million, a reduction of 18.6% and primarily related to higher Rescue claims.

Notes:
1. Ongoing operations – See glossary on pages 251 to 253 for definitions and appendix A – Alternative performance measures on pages 254 to 257 for reconciliation to financial statement line items.
2. See glossary on pages 251 to 253 for definitions and appendix A – Alternative performance measures on pages 254 to 257 for reconciliation to financial statement line items.
3. https://www.ukpetfood.org/information-centre/statistics/uk-pet-population.html
4. Customer Satisfaction Index.



Commercial

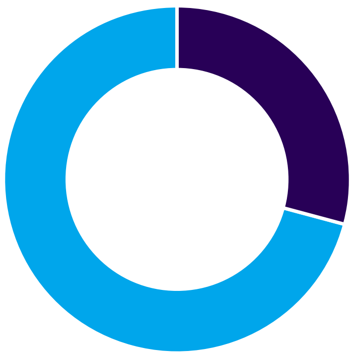
Commercial: performance summary

Total in-force policies grew 6.5%, with direct own brands and NIG and other growing 8.1% and 3.0% respectively.

Strong growth in gross written premium, increasing by 14.7% to £749.3 million, driven by growing in-force policies and higher average premiums.

Operating profit of £58.3 million was £2.1 million lower than 2021 due to higher weather event claims and lower prior-year releases.

Gross written premium by channel



- **29.2%** Direct
- **70.8%** NIG & other

	2022 £m	2021 £m
In-force policies (thousands)	**928**	871
Of which:		
Direct own brands[1]	**651**	602
NIG and other	**277**	269
Gross written premium	**749.3**	653.0
Of which:		
Direct own brands[1]	**218.9**	187.4
NIG and other	**530.4**	465.6
Operating profit[2]	**58.3**	60.4
Loss ratio[2]	**53.7%**	54.5%
Commission ratio[2]	**19.4%**	20.0%
Expense ratio[2]	**21.1%**	21.7%
Combined operating ratio[2]	**94.2%**	96.2%
Current-year attritional loss ratio[2]	**57.5%**	62.0%
Normalised combined operating ratio[2]	**92.8%**	96.3%

Market overview

Premiums remained high across the SME commercial market throughout 2022, supported by reduced capacity in this area. The introduction of the FCA's PPR regulations had a smaller impact on commercial insurance as opposed to personal lines.

However, the van segment saw fewer customers shopping in 2022. This was driven by a range of inflationary factors, including higher second-hand vehicle prices and higher premiums due to claims inflation.

There was considerable consolidation in the commercial broker sector, while the small and micro portion of the commercial sector continued to see a shift towards price comparison websites.

Performance

In-force policies and gross written premium

During 2022, Commercial continued to deliver strong in-force policy count growth and double digit premium growth. This reflected benefits of its transformation alongside a positive commercial market backdrop.

Gross written premium increased by 14.7% compared to 2021, with strong growth across both NIG and direct own brands. This was driven by growing in-force policies by 6.5% to 0.9 million whilst also increasing average premiums ahead of inflation.

Commercial growth

Our Commercial business delivered strong growth across all channels, continuing to realise the benefits of its transformation, improving margins, pricing sophistication and growing NIG's award-winning electronic trading platform. Over the last year:

- Our Risk Assist proposition, which helps business owners manage and reduce risks, has been enhanced with updated content and new tools;
- An 'Ask the Expert' app has been launched, supporting businesses to get tailored advice for their needs; and
- Our Motor and Mini Fleet coverage has been extended to include cables, batteries for EVs and charge points as we aim to increase our penetration into the growing EV segment.

Underwriting

Claims inflation remained elevated throughout 2022, and is estimated at approximately 7% across the portfolio. Pricing action was taken throughout the year with premiums on average increasing slightly ahead of claims inflation.

Commercial also experienced higher weather event-related claims in 2022, and these are currently estimated to cost £30.2 million, above our 2022 annual assumption of £21 million. Our weather-related claims assumption for Commercial for 2023 is £26 million. Prior-year reserve releases remained significant at £54.0 million, although a 12.1% reduction on 2021.

The earning through of higher average premium from 2021 led to a 4.5 percentage point improvement in the current-year attritional loss ratio, to 57.5%. The overall loss ratio was 0.8 percentage points better as an improvement in the attritional loss ratio was partially offset by higher weather event claims compared to 2021.

Combined operating ratios and profit

The expense and commission ratios improved slightly which, coupled with positive pricing, led to a combined operating ratio of 94.2%, 2.0 percentage points better than prior year. Normalised for weather, the combined operating ratio was 92.8%, an improvement of 3.5 percentage points.

Despite lower prior-year reserve releases and higher weather-related claims, underwriting profit increased by £15.7 million, to £37.1 million. Outside of underwriting, there was a £20.6 million reduction in the investment return, resulting in operating profit of £58.3 million, £2.1 million lower than 2021.

Notes:
1. Commercial direct own brands include in-force policies for Direct Line for Business and Churchill brands.
2. See glossary on pages 251 to 253 for definitions and appendix A – Alternative Performance Measures on pages 254 to 257 for reconciliation to financial statement line items.

Run-off partnerships[1]

In our H1 2022 results we disclosed that we planned to reduce our exposure to packaged bank accounts where they do not meet target levels of return and are no longer required for operational scale, in order to improve our capital efficiency. During the second half of the year, we have decided to exit all such partnerships and are presenting the results for this business as a separate segment.

Rescue packaged accounts

Our contract with NatWest Group ended in December 2022 and is due to run off by the end of 2023, albeit that claims may run off over a longer period. This partnership represented around 1.1 million in-force policies.

Travel packaged accounts

Our partnerships with NatWest Group and Nationwide Building Society are due to expire in 2024 and are expected to run off in early 2025. Together, these travel partnerships represent around 2.2 million in-force policies.

Underwriting

Gross written premium was £124.4 million (2021: £98.9 million). The operating loss relating to run-off partnerships in 2022 was £11.5 million (2021: £8.5 million).

	2022 £m	2021 £m
In-force policies (thousands)	**2,188**	4,551
Gross written premium	**124.4**	98.9
Operating loss	**(11.5)**	(8.5)
Loss ratio	**90.4%**	51.1%
Commission ratio	**1.8%**	33.5%
Expense ratio	**17.7%**	25.0%
Combined operating ratio	**109.9%**	109.6%

Notes:

1. Ongoing operations – See glossary on pages 251 to 253 for definitions and appendix A – Alternative performance measures on pages 254 to 257 for reconciliation to financial statement line items.