

DIRECT LINE INSURANCE GROUP PLC

PRELIMINARY RESULTS FOR THE YEAR ENDED 31 DECEMBER 2022 (UNAUDITED)

JON GREENWOOD, ACTING CEO OF DIRECT LINE GROUP, COMMENTED

"2022 was a tough year for Direct Line Group. Motor and Home market conditions were challenging, with high claims inflation and regulatory reforms creating substantial headwinds for the business, and we did not navigate these challenges as effectively as we would have wished. Exceptional weather and difficult investment markets also significantly impacted our results.

"Motor, in particular, was affected by high claims inflation, which remained ahead of our expectations throughout the year, as well as the impact of regulatory changes. We have taken pricing actions that will support restoration of margins in Motor and mitigate the impact of further claims inflation. We have also accelerated a range of other actions including deploying additional resources in Motor.

"All our other businesses performed broadly in line with our expectations, and within our target combined operating ratio, when normalised for weather claims. Adverse weather was a major factor in 2022, with storms and extremes of heat and cold resulting in the highest claims costs from large weather events since the Group listed over a decade ago.

"Since the year end we have taken action to begin to rebuild the resilience of our balance sheet, and we have further self-help options available, as well as organic capital generation to enhance our solvency ratio during 2023.

"Whilst our 2022 performance was disappointing, the fundamentals of our business remain strong and we are now fully focused on rebuilding our margins, further improving our capital strength and generating attractive sustainable returns for shareholders."

Results summary

	FY 2022 £m	FY 2021 £m	Change
In-force policies - ongoing operations ¹ (thousands)	9,689	10,014	(3.2%)
Of which: direct own brands ² (thousands)	7,245	7,529	(3.8%)
Adjusted gross written premium - ongoing operations ^{1,3}	2,974.0	3,072.7	(3.2%)
Of which: direct own brands ²	2,087.1	2,207.6	(5.5%)
Operating profit - ongoing operations ^{1,3}	32.1	590.3	(94.6%)
Combined operating ratio - ongoing operations ^{1,3,4}	105.8%	89.5%	(16.3pts)
Normalised combined operating ratio - ongoing operations ^{1,3}	103.3%	90.5%	(12.8pts)
(Loss)/profit before tax	(45.1)	446.0	(110.1%)
Return on tangible equity ³	(0.9%)	23.6%	(24.5pts)
Basic (loss)/earnings per share (pence)	(4.3)	24.5	(117.6%)
Dividend per share - total (pence)	7.6	22.7	(66.5%)
Solvency capital ratio ⁵	147%	176%	(29pts)
Solvency capital ratio (as above)/adjusted solvency capital ratio ^{3,5,6}	147%	160%	(13pts)

Financial summary

- Group operating profit from ongoing operations fell to £32.1 million (2021: £590.3 million) reflecting a volatile operating environment with elevated motor claims inflation, higher than expected weather event claims, new regulatory changes and challenging investment markets. Total Group operating profit was £20.6 million (2021: £581.8 million).
- Claims inflation was most acute in Motor, where severity inflation of around 14% was above the levels assumed in the Group's pricing. Alongside disruption to supply chains causing delays in third party claims, this led to a Motor combined operating ratio of 114.7% (2021: 92.4%). In our other businesses, pricing kept pace with claims inflation and combined operating ratios were broadly in line with expectations, when normalised for weather.
- 2022 saw the highest weather event costs since the Group listed over a decade ago with £149 million of claims, well above the 2022 £73 million budget assumption. The largest event was December's freeze, which delivered around £95 million of claims costs due to prolonged periods of sub-zero temperatures across Scotland and North West England.
- Group combined operating ratio for ongoing operations was 105.8% and 103.3% when normalised for weather. The Group's total combined operating ratio including run-off partnerships was 106.0%.
- Solvency capital ratio reduced during 2022 as a result of lower profit as well as unrealised losses on investments. A new 10% quota share reinsurance arrangement was agreed with effect from 1 January 2023 and, including the benefit from this, the solvency capital ratio was 147%. At the end of February the Group solvency ratio has further improved by approximately 5 percentage points due to positive credit movements on the bond portfolio and a reduction in ineligible capital on adoption of IFRS 17 'Insurance Contracts'.
- In line with the expectation previously disclosed, the Group is not proposing a final dividend for 2022, resulting in a total dividend for 2022 of 7.6 pence per share.

Business highlights

- Commercial delivered gross written premium growth of 14.7% at a combined operating ratio lower than 2021, driven by a strong customer focus across both the broker and direct-to-consumer brands, supported by Commercial's new platform.
- In Motor, we launched our new Churchill Essentials product into the price comparison website ("PCW") channel, designed to enhance our competitiveness in this market.
- The Group continues to review where it deploys capital to target the highest returns, consequently we are exiting some low margin packaged bank accounts. The new 10-year partnership with Motability Operations starts in the second half of 2023 and is expected to generate annual gross written premium of around £500 million, 80% of which will be reinsured.
- Home made good progress with its new technology platform, which remains on track for roll out in 2023.
- Green Flag started to roll out its own fleet of Green Flag patrol vehicles, designed to improve claims efficiency and to broaden the availability of products and services, such as batteries and tyres direct to customers at the roadside.
- Our Science-Based Targets were approved by the Science Based Targets initiative.

Dividend and outlook

The Group paid an interim dividend of 7.6 pence per share in 2022; however, given the year-end solvency ratio, as indicated at the January trading update, the Board is not recommending a final dividend. The Board understands the importance of dividends to shareholders and will update the dividend outlook at the half-year results.

2023 earnings are expected to be impacted by higher than assumed claims inflation on Motor business written during 2022 and in early 2023, alongside continued macroeconomic uncertainty.

With effect from the start of 2023, the Group has adopted IFRS 17 and moved from combined operating ratio to net insurance margin ("**NIM**") as a key performance indicator. The Group has an ambition over time to generate a NIM of above 10%, normalised for weather.

The Group continues to believe it has a fundamentally strong business and is pursuing a range of actions designed to both restore earnings and improve its solvency position.

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Notes:

1. Ongoing operations – the Group has excluded a number of Rescue and other personal lines partnerships from its ongoing operations results. The run-off partnerships relate to a Rescue partnership with NatWest Group that expired in December 2022 and Travel partnerships with NatWest Group and Nationwide Building Society which expire in 2024, and which the Group has already indicated that it will not be seeking to renew. Relevant prior-year data has been restated accordingly. See glossary on pages 56 to 58 for definitions and appendix A – Alternative Performance Measures on pages 60 to 63 for reconciliation to financial statement line items.
2. Direct own brands include in-force policies for Home and Motor under the Direct Line, Churchill, Darwin and Privilege brands, Rescue policies under the Green Flag brand and Commercial under the Direct Line for Business and Churchill brands.
3. See glossary on pages 56 to 58 for definitions and appendix A – Alternative Performance Measures on pages 60 to 63 for reconciliation to financial statement line items.
4. A reduction in the ratio represents an improvement as a proportion of net earned premium, while an increase in the ratio represents a deterioration. See glossary on pages 56 to 58 for definitions.
5. Estimates based on the Group's Solvency II partial internal model.
6. Adjusted solvency capital ratio as at 31 December 2021 excluded £250 million Tier 2 debt which was redeemed on 27 April 2022. See appendix A – Alternative Performance Measures on pages 60 to 63 for reconciliation to financial statement line items.

CEO REVIEW

2022 was a difficult year for the Group. Our performance in Motor fell well below our expectations and did not reflect our previous track record of delivering strong returns for shareholders. Rising claims inflation and new regulatory changes, along with severe weather events, resulted in a material fall in the Group operating profit and solvency ratio, and the Board's decision not to recommend a final dividend.

This is deeply disappointing and we have already taken and continue to take actions designed to strengthen our solvency position and improve our Motor pricing in this difficult trading environment. Enhancing how we price in the motor market will be a key focus for the Group throughout 2023.

All of our other businesses performed broadly in line with our expectations when normalised for weather.

Despite the setbacks in Motor in 2022, the long-term earnings potential of the Group remains robust. Our diversified business model and fundamental strengths remain a significant asset in the highly competitive UK insurance market. We have a strong franchise, some of the most recognisable insurance brands in the UK and strong customer service delivered by a high-quality workforce.

With a determination to enhance our pricing capability and better leverage the benefits of our integrated business model, I firmly believe that we can restore our performance in Motor, enabling the Group to get back to delivering attractive returns for shareholders.

Improving performance in Motor

Our main operational focus during 2023 will be on restoring performance in Motor, in order to drive profitability and build capital resilience, and we are pushing ahead in four main areas.

First, we have already taken pricing action to restore written margins based on our rebased inflation assumptions, and we will continue to prioritise maintaining margins over volume as we progress through 2023.

Secondly, we will focus on utilising our new pricing tools to their full potential and enhancing the sophistication of our risk pricing models. This will include deployment of substantial additional resource to ensure that Motor has the capability and capacity it needs to price with greater precision.

Thirdly, we will better leverage the wealth of claims insight that we have available through our vertically integrated model. We want to move from being an efficient claims processor and repairer, into a data-driven claims operation, utilising all our data to enhance our pricing capability.

Finally, we will align our model more closely to the PCW channel, which accounts for around 90% of new business motor sales in the market. We will do this through new propositions, such as our new 'Churchill Essentials' product, which has demonstrated how we can expand our PCW channel footprint and offer value to our customers.

Restoring the resilience of our balance sheet

In addition to the capital benefits from improving our Motor performance, we have a range of levers aimed at helping us build back our capital strength.

Reinsurance

We have always used reinsurance through our motor excess of loss reinsurance and our property catastrophe programmes to manage our risk profile.

We have now built on this with a new 10% quota share reinsurance arrangement effective from 1 January 2023. This not only strengthened our solvency position as at year-end 2022 by 6 percentage points, but it is also the foundation for an efficient long-term source of capital for the Group. We continue to explore further strategic reinsurance options.

Portfolio actions

At the 2022 half-year results we flagged our review of where we deploy our capital in order to deliver the highest returns. As a result we have decided to exit certain partnerships, reducing our exposure to low margin insurance within packaged bank accounts. In the second half of 2023 we plan to begin our new 10-year partnership with Motability Operations, which brings 600,000 new customers. We believe these changes to our portfolio will be positive from both a financial and strategic perspective.

Investment portfolio

With investment yields having increased substantially over the last 12 months, we are rebalancing our target asset allocations in order to deliver the correct balance between return and capital allocation. This should release further capital over time.

In addition to management actions, we expect the unrealised loss position on our investment-grade debt security portfolio to unwind due to the pull to par effect as bonds mature.

Organic capital generation

We believe the Group will be capital generative in 2023 supported by Home, Commercial and Rescue and other personal lines, although it will take some time to restore earnings in Motor.

Continuing to deliver for customers

Excluding Motor and elevated weather claims, all other business traded broadly in line with expectations.

Commercial delivered another strong performance, with the benefits of the technology transformation enhancing Commercial's already strong product and service offering and sophisticated pricing. In 2022, Commercial delivered double-digit growth across both its main businesses, NIG and Commercial direct own brands. Over the past 10 years this business has doubled in size and improved its combined operating ratio to 94.2% from over 100%.

Home successfully navigated the implementation of the FCA's Pricing Practices Review ("PPR") regulations and elevated inflation by focusing on maintaining margins and leveraging its diversified business model. Home also made progress with its new technology platform, which remains on track for roll out in 2023.

Green Flag successfully diversified its product portfolio, providing further value for customers by offering accessories via the Green Flag shop. This gives customers the convenience of booking maintenance and repair services, or providing a competitive price to check a vehicle's history before they decide to make a purchase. In January 2023, Green Flag patrol was launched, with its own network of recovery vehicles, in order to enhance network efficiency, improve customer experience and increase sales.

A key pillar of our strategy is reducing our carbon footprint and helping our customers make the green transition. Alongside expanding our electric vehicle propositions, in 2022 the Group became one of the first personal lines general insurers in the UK to have its Science-Based Targets approved by the Science Based Targets initiative.

Business performance

In 2022, there is a clear distinction between the results of Motor and those of the Group's other business lines.

	Gross written premium £m	Gross written premium %	Normalised combined operating ratio %
Motor	1,432.7	48.2	114.7
Home, Commercial, Rescue and other personal lines - ongoing operations	1,537.1	51.8	92.2
Total ongoing operations	2,969.8	100.0	103.3

Motor delivered a poor result, with a combined operating ratio of 114.7%. Claims inflation over the course of the year was greater than we expected, and not reflected in our pricing. This was compounded by higher claims frequency in the fourth quarter. This coincided with the introduction of the FCA's PPR regulations which reduced new business growth opportunities. Retention remained strong at 81.6%.

Our normalised combined operating ratio for ongoing operations across our Home, Commercial and Rescue and other personal lines was 92.2%. In Commercial, we combined strong growth with an improved current-year loss ratio following several years of pricing ahead of estimated claims inflation. We also priced ahead of claims inflation in Home, which saw a challenging new business market following the implementation of the FCA's PPR regulations. Rescue did not see the same growth as previous years but its margins remained strong.

Weather

During 2022, we experienced our highest level of weather-related claims since before our IPO in 2012, including our highest individual event from the freeze in December. Overall claims from weather-related events were £149 million, more than double our 2022 annual assumption of £73 million. This was made up of three events - storms in February, extremely dry weather over the summer which resulted in subsidence and the freeze in December. The freeze event was the most significant, with £95 million of claims costs across Home and Commercial following prolonged sub-zero temperatures, especially across Scotland and North West England. With relatively large shares of Home and Commercial insurance in Scotland, we experienced a significant number of large claims.

Implementation of IFRS 17 'Insurance Contracts' and IFRS 9 'Financial Instruments'

IFRS 17 and IFRS 9 are effective from 1 January 2023. These new accounting standards will improve alignment between IFRS earnings and capital generation under Solvency II and will not affect the economics of our business or its dividend paying capacity. Overall, we believe the new standards should improve comparability between companies.

We will change our headline key performance measure from combined operating ratio to net insurance margin ("NIM") under IFRS 17, which we believe is a better measure of how we run our business.

The key reconciling items when moving from a combined operating ratio to a NIM are the inclusion of instalment and other income within revenue, alongside the additional benefit from discounting more of our insurance liabilities. As a result the NIM is expected to be around 6 percentage points better than the margin implied by the equivalent combined operating ratio. For example, a 100% combined operating ratio, implying a 0% margin, under the previous accounting standard would translate into around a 6% NIM under IFRS 17.

Capital management

The Group's capital position was affected by the combination of significantly weaker levels of Motor profitability, adverse investment experience and well above average claims from major weather events. These factors reduced the Group's own funds during the year, whilst the weaker Motor outlook and higher inflation also contributed to an increased capital requirement, which was only partly offset by higher than expected investment income.

During H2 and into 2023, the Group took several actions which increased the Group's solvency capital ratio by 14 percentage points, including reducing the risk in the investment portfolio and agreeing a 10% whole account quota share reinsurance arrangement. As at the end of 2022, the Group's estimated solvency capital ratio was 147% which is within the Group's risk appetite range, albeit towards the bottom end of that range.

At the end of February 2023, the Group's solvency capital ratio has increased by approximately 5 percentage points due to the positive movements on the bond portfolio as well as a reduction in ineligible capital. We are pursuing a range of actions designed to bring the Group's solvency position back towards the middle of the range. The Group expects positive organic capital generation in 2023.

The Group paid an interim dividend of 7.6 pence per share in 2022; however, given the year-end solvency ratio, as indicated at the January trading update, the Board is not recommending a final dividend. The Board understands the importance of dividends to shareholders and will update the dividend outlook at the half-year results.

Outlook

Higher than expected claims inflation on business written during 2022 and in early 2023 will continue to affect Motor earnings during 2023. Furthermore, the outlook for claims inflation remains uncertain given, for example, capacity constraints in the repair industry, continued settlement delays in third party claims and potential care cost inflation.

In our other businesses, trading conditions in Commercial have remained favourable with continued growth in 2023 to date. In Home, market conditions in early 2023 have improved and Green Flag direct has continued to perform well.

The Group believes it continues to have a fundamentally strong business and has an ambition over time to generate a NIM of above 10%, normalised for weather.

JON GREENWOOD

ACTING CHIEF EXECUTIVE OFFICER

Group financial performance

		FY 2022	FY 2021	Change
Ongoing operations¹				
In-force policies (thousands)		9,689	10,014	(3.2%)
Of which: direct own brands (thousands) ²		7,245	7,529	(3.8%)
		FY 2022	FY 2021	Change
	Notes	£m	£m	
Ongoing operations¹				
Adjusted gross written premium ³		2,974.0	3,072.7	(3.2%)
Of which: direct own brands ²		2,087.1	2,207.6	(5.5%)
Net earned premium	3	2,844.4	2,860.2	(0.6%)
Underwriting (loss)/profit - ongoing operations¹	3	(166.6)	300.9	(155.4%)
Loss ratio ^{3,4}	3	74.7%	58.4%	(16.3pts)
Commission ratio ^{3,4}	3	7.3%	7.3%	0.0pts
Expense ratio ^{3,4}	3	23.8%	23.8%	0.0pts
Combined operating ratio ^{3,4}	3	105.8%	89.5%	(16.3pts)
Current-year attritional loss ratio ^{3,4}		74.4%	65.6%	(8.8pts)
Normalised combined operating ratio ^{3,4}		103.3%	90.5%	(12.8pts)
Instalment and other operating income	3	147.7	143.9	2.6%
Investment return	3	51.0	145.5	(64.9%)
Operating profit - ongoing operations^{1 3}	3	32.1	590.3	(94.6%)
Of which:				
Current-year operating (loss)/profit ³		(108.7)	347.2	(131.3%)
Prior-year reserve releases		140.8	243.1	(42.1%)
Restructuring and one-off costs	3	(45.3)	(101.5)	55.4%
Run-off partnerships ¹	3	(11.5)	(8.5)	(35.3%)
Operating (loss)/profit after restructuring and one-off costs³	3	(24.7)	480.3	(105.1%)
Finance costs	10	(20.4)	(34.3)	40.5%
(Loss)/profit before tax	3	(45.1)	446.0	(110.1%)
Tax credit/(charge)		5.6	(102.3)	105.5%
(Loss)/profit for the year attributable to the owners of the Company		(39.5)	343.7	(111.5%)
Profitability metrics				
Return on tangible equity ³		(0.9%)	23.6%	(24.5pts)
Basic (loss)/earnings per share (pence)	12	(4.3)	24.5	(117.6%)
Diluted (loss)/earnings per share (pence)	12	(4.3)	24.1	(117.8%)
Return on equity ³	13	(2.5%)	12.5%	(15.0pts)
Investments metrics				
Investment income yield ³		2.3%	1.9%	0.4pts
Net investment income yield ³		2.2%	1.7%	0.5pts
Investment return yield ³		1.0%	2.4%	(1.4pts)
Capital and returns metrics				
Net asset value per share (pence)		149.0	193.6	(23.0%)
Tangible net asset value per share (pence)		85.6	131.2	(34.8%)
Solvency capital ratio post dividend and share buyback ⁵		147%	176%	(29pts)
Solvency capital ratio (as above) / adjusted solvency capital ratio ^{3,5,6}		147%	160%	(13pts)

Notes:

1. Ongoing operations and run-off partnerships – See glossary on pages 56 to 58 for definitions and appendix A – Alternative Performance Measures on pages 60 to 63 for reconciliation to financial statement line items.
2. Direct own brands include in-force policies for Home and Motor under the Direct Line, Churchill, Darwin and Privilege brands, Rescue policies under the Green Flag brand and Commercial under the Direct Line for Business and Churchill brands.
3. See glossary on pages 56 to 58 for definitions and appendix A – Alternative Performance Measures on pages 60 to 63 for reconciliation to financial statement line items.
4. A reduction in the ratio represents an improvement as a proportion of net earned premium, while an increase in the ratio represents a deterioration. See glossary on pages 56 to 58 for definitions.
5. Estimates based on the Group's Solvency II partial internal model.
6. Adjusted solvency capital ratio - please refer to footnote 6 on page 2.

CHIEF FINANCIAL OFFICER REVIEW

Group financial performance

Ongoing operations ¹	31 Dec 2022	30 Sep 2022	30 Jun 2022	31 Mar 2022	31 Dec 2021	Year-on-year change
In-force policies (thousands) ²	9,689	9,771	9,911	9,952	10,014	(3.2%)
Of which direct own brands ³	7,245	7,304	7,417	7,459	7,529	(3.8%)
				FY 2022 £m	FY 2021 £m	Change
Adjusted gross written premium ²				2,974.0	3,072.7	(3.2%)
Of which direct own brands ³				2,087.1	2,207.6	(5.5%)
Underwriting (loss)/profit				(166.6)	300.9	(155.4%)
Instalment and other operating income				147.7	143.9	2.6%
Investment return				51.0	145.5	(64.9%)
Operating profit⁴				32.1	590.3	(94.6%)
Loss ratio ⁴				74.7%	58.4%	(16.3pts)
Commission ratio ⁴				7.3%	7.3%	0.0pts
Expense ratio ⁴				23.8%	23.8%	0.0pts
Combined operating ratio⁴				105.8%	89.5%	(16.3pts)
Current-year attritional loss ratio ⁴				74.4%	65.6%	(8.8pts)
Normalised combined operating ratio⁴				103.3%	90.5%	(12.8pts)

2022 was a challenging year for the Group. The aggregate effect of continued high inflation in Motor, regulatory change in personal lines, twice the assumed level of weather claims, as well as adverse investment conditions, reduced operating profit for ongoing operations by 94.6% to £32 million. Despite the headline reduction in profit, underlying underwriting performance in Home, Commercial and Rescue and other personal lines was broadly in line with expectations.

Ongoing operations and run-off partnerships

The Group has exited, or has initiated termination of three partnerships which will reduce its exposure to low margin packaged bank accounts so it can redeploy capital to higher return segments. The run-off partnerships relate to a Rescue partnership with NatWest Group that expired in December 2022 and Travel partnerships with NatWest Group and Nationwide Building Society which expire in 2024, and which the Group has indicated to the partner that it will not be seeking to renew.

The Group has excluded the results of these three run-off partnerships from its ongoing results and has restated all relevant comparatives across this review. Results relating to ongoing operations are clearly referenced. Note 3 (Segmental analysis) has also been amended to reflect the change. The operating loss relating to run-off partnerships in 2022 was £11.5 million (2021: £8.5 million).

In-force policies and adjusted gross written premium^{1,2}

In-force policies from ongoing operations were 9.7 million at the end of December, 3.2% lower than prior year with reductions across all segments except Commercial which continued to deliver strong growth. Adjusted gross written premium from ongoing operations experienced a similar reduction, falling by 3.2% to £2,974.0 million. Growth in Commercial was offset by reductions in Motor and Home arising from the combination of challenging market conditions together with the impact of regulatory change. Total Group in-force policies were 11.9 million and total adjusted gross written premium was £3,098.4 million.

Underwriting result¹

The Group made an underwriting loss from ongoing operations of £167 million (£179 million loss including run-off partnerships), a reduction of £468 million compared to 2021. This was predominately due to a £259 million reduction in current-year profitability in Motor, due to pricing not reflecting claims inflation, alongside £112 million higher weather costs in Home and Commercial. In Motor, 2022 did not see a repeat of low claims frequency experienced during the lockdowns in the first half of 2021, together with elevated claims inflation and the impact of regulatory reforms in 2022. Prior-year reserve releases from ongoing operations reduced from £243 million in 2021 to £141 million in 2022, with the reduction primarily driven by lower Motor and Home releases. Our claims reserves include specific allowance for inflation over the next few years to be higher than recently experienced for longer-tail lines of business.

The loss ratio from ongoing operations increased to 74.7% (2021: 58.4%) driven predominantly by Motor and weather events in Home and Commercial, although an improved current-year attritional loss ratio in Commercial offset an increased current-year attritional loss ratio in Home.

Weather-related claims in the year were £149 million, more than twice our 2022 annual assumption of £73 million and the highest since the Group's IPO in 2012. Our weather-related claims assumption for Home and Commercial combined for 2023 is £80 million.

The combined operating ratio from ongoing operations increased to 105.8% (2021: 89.5%) and 103.3%, when normalised for weather (2021: 90.5%).

The underwriting result including run-off partnerships was a loss of £179 million (2021: £292 million profit) and the combined operating ratio including run-off partnerships was 106.0% (2021: 90.1%).

Instalment and other operating income¹

	Note	FY 2022 £m	FY 2021 £m
Instalment income	3	92.4	97.3
Other operating income	3	55.3	46.6
Total instalment and other operating income - ongoing operations		147.7	143.9
Total instalment and other operating income - run-off partnerships		–	0.1

Instalment income from ongoing operations of £92.4 million was £4.9 million lower than 2021, largely reflecting lower volumes written in Motor and Home in 2022.

Other operating income from ongoing operations increased 18.7% to £55.3 million in 2022, primarily due to the introduction in 2022 of arrangement and administration fees in Rescue together with higher claims frequency in Motor, driving increased revenue from vehicle recovery and repair services and higher salvage income.

Investment return¹

	Note	FY 2022 £m	FY 2021 £m
Investment income		124.0	115.1
Hedging to a sterling floating rate basis		(5.9)	(13.2)
Net investment income		118.1	101.9
Net realised and unrealised (losses)/gains excluding hedging		(67.1)	43.6
Total investment return - ongoing operations	3	51.0	145.5
Total investment return - run-off partnerships		0.6	0.8
Total investment return		51.6	146.3

Investment yields

	FY 2022	FY 2021
Investment income yield ⁴	2.3%	1.9%
Net investment income yield ⁴	2.2%	1.7%
Investment return yield ⁴	1.0%	2.4%

Total investment return from ongoing operations decreased by £94.5 million to £51.0 million (2021: £145.5 million) primarily driven by realised and unrealised losses resulting from write-downs in fair value adjustments of commercial property (£39.1 million) and £24.9 million of realised losses from disposals of our debt securities holdings, predominantly relating to actions taken to reduce our longer duration USD credit holdings. The Group's investment return including run-off partnerships was £51.6 million (2021: £146.3 million).

Despite assets under management declining 16.1% year-on-year, investment income from ongoing operations was up £8.9 million, driven by a yield improvement in variable rate asset classes following eight UK base rate increases during 2022, when rates rose from 0.25% to 3.5%. This resulted in a net investment income yield improvement of 0.5 percentage points to 2.2%. The investment income yield is expected to increase to 3.2% in 2023 as maturing assets are invested at higher yields together with higher yields on floating assets. The total return yield for 2023 is expected to be around 4.0%, once pull to par effects are taken into account. Given this measure includes unrealised movements as well, the outcome will depend on market movements during the year.

Operating expenses before restructuring and one-off costs¹

	Note	FY 2022 £m	FY 2021 £m
Staff costs ⁵		232.9	246.7
IT and other operating expenses ^{5,6}		143.2	138.5
Marketing		93.5	112.0
Sub-total		469.6	497.2
Insurance levies		92.6	88.2
Depreciation, amortisation and impairment of intangible and fixed assets ⁷		115.7	96.6
Total operating expenses - ongoing operations	3	677.9	682.0
Operating expenses - run-off partnerships	3	21.6	24.3
Total operating expenses	3	699.5	706.3
Expense ratio - ongoing operations		23.8%	23.8%
Expense ratio - total Group		23.6%	23.9%

Operating expenses from ongoing operations in 2022 were £677.9 million (£699.5 million including run-off partnerships), in line with our target of around £700 million, and £4.1 million lower than 2021. This reflected a continued focus on improving efficiency and cost control. Despite inflationary pressures, controllable costs reduced by £27.6 million, more than offsetting a £23.5 million increase in amortisation, depreciation and levies.

The reduction in controllable costs was driven by a range of cost saving initiatives, including reducing the Group's office footprint, reducing technology run costs and increased customer adoption of digital and self-service channels.

The Group's full-time equivalent headcount reduced by 4.1% to 9,387 in 2022.

Looking ahead, the Group remains focused on driving cost efficiency, but is not immune to inflationary pressures in the market.

Reconciliation of operating profit to basic (loss)/earnings per share

	Note	FY 2022 £m	FY 2021 £m
Motor	3	(77.2)	314.8
Home	3	(8.7)	141.8
Rescue and other personal lines - ongoing operations ¹	3	59.7	73.3
Commercial	3	58.3	60.4
Operating profit - ongoing operations ¹	3	32.1	590.3
Operating loss - run-off partnerships ¹	3	(11.5)	(8.5)
Operating profit - total Group	3	20.6	581.8
Restructuring and one-off costs	9	(45.3)	(101.5)
Finance costs	10	(20.4)	(34.3)
Tax credit/(charge)		5.6	(102.3)
(Loss)/earnings attributable to the owners of the Company		(39.5)	343.7
Basic (loss)/earnings per share (pence)	12	(4.3)	24.5
Return on tangible equity⁴		(0.9%)	23.6%

Restructuring and one-off costs

The Group incurred £45.3 million of restructuring and one-off costs in 2022, principally due an impairment of an IT system of £15.2 million following the decision to exit Travel packaged bank account partnership business¹ and write-offs in relation to property fixtures and fittings. The majority of these restructuring costs are non-cash and therefore have no impact on the Group's solvency ratio.

Finance costs

Finance costs fell to £20.4 million (2021: £34.3 million) primarily as interest payments reduced following the redemption of the Group's £250 million 9.25% Tier 2 subordinated notes on 27 April 2022.

Effective corporation tax rate

The effective tax rate ("ETR"), which is calculated as total tax charge divided by profit/(loss) before tax was 12.4% for 2022 (2021: 22.9%). Unusually, due to the overall loss position the ETR is lower than the standard UK corporation tax rate of 19.0% (2021: 19.0%) as tax relief for the accounting loss is reduced by disallowable expenses which are only partly offset by tax relief for the Tier 1 coupon payments (which are accounted for as a distribution rather than expense), together with the tax effect of a property revaluation. Further details can be found in the tax reconciliation in Note 12 to the financial statements in the Group's Annual Report and Accounts.

Whilst the quantum of the disallowable expenses has returned to a more normalised level in 2022 following the one-off non-deductible Bromley lease payment in 2021, they have a greater impact on the ETR (calculated as tax charge divided by profit or (loss) before tax) as the denominator is much lower in 2022 compared with 2021. Ordinarily disallowable expenses would increase the ETR where there is an accounting profit (such as in 2021 and previous years), as more tax is paid than would be expected from applying the statutory tax rate to the accounting profit. However, in a loss making year, such as 2022, disallowable expenses lead to fewer tax losses than accounting losses, thereby leading to an overall reduction in the ETR.

Return on tangible equity⁴

Return on tangible equity decreased to (0.9)% (2021: 23.6%) due primarily to the reduction in the Group's operating profit.

(Loss)/earnings per share

Basic earnings per share decreased by 117.6% to a loss of 4.3 pence (2021: earnings of 24.5 pence). Diluted earnings per share decreased by 117.8% to a loss of 4.3 pence (2021: earnings of 24.1 pence), mainly reflecting the Group's loss after tax in 2022.

The financial performance of the Group is discussed in detail on pages 7 to 9. The calculation of (loss)/earnings per share is presented in note 12 on page 45.

Notes:

1. Ongoing operations and run-off partnerships – See glossary on pages 56 to 58 for definitions and appendix A – Alternative Performance Measures on pages 60 to 63 for reconciliation to financial statement line items.
2. See appendix B for additional data on in-force policies and adjusted gross written premium.
3. Direct own brands include in-force policies for Home and Motor under the Direct Line, Churchill, Darwin and Privilege brands, Rescue policies under the Green Flag brand and Commercial under the Direct Line for Business and Churchill brands.
4. See glossary on pages 56 to 58 for definitions and appendix A – Alternative performance measures on pages 60 to 63 for reconciliation to financial statement line items.
5. Staff costs and other operating expenses attributable to claims handling activities are allocated to the cost of insurance claims.
6. IT and other operating expenses include professional fees and property costs.
7. Includes right-of-use ("ROU") assets and property, plant and equipment. For the year ended 31 December 2022, there were impairment charges of £16.0 million which relate solely to impairment of intangible assets (2021: £2.6 million of which, £2.1 million relates to impairment of intangible assets and £0.5 million relates to ROU property assets).

Cash flow

	2022 £m	2021 £m
Net cash generated from operating activities	800.2	439.0
Of which:		
Operating cash flows before movements in working capital	(24.3)	435.9
Movements in working capital	8.2	(45.8)
Tax paid	(44.5)	(118.4)
Net cash generated from investment of insurance assets	860.5	167.2
Net cash used in investing activities	(100.8)	(138.7)
Net cash used in financing activities	(657.5)	(572.0)
Net increase/(decrease) in cash and cash equivalents	41.9	(271.7)
Cash and cash equivalents at 1 January	896.5	1,168.2
Cash and cash equivalents at 31 December	938.4	896.5

The Group's cash and cash equivalents increased by £41.9 million during the year (2021: £271.7 million reduction) to £938.4 million.

The Group had an operating cash outflow before movements in working capital of £24.3 million (2021: inflow £435.9 million), a reduction of £460.2 million due to the loss for the year compared to a profit in the prior year and an increase in adjustments for non-cash movements. After taking into account movements in working capital, the Group's cash outflow was £16.1 million (2021: inflow £390.1 million), a decrease of £406.2 million. The Group has considerable assets under management, the cash generated from these assets increased by £693.3 million to £860.5 million as proceeds from the disposal and maturity of available-for-sale ("AFS") debt securities exceeded purchases, in part due to actions taken to reduce the Group's longer duration USD credit holding, helping fund dividend payments and the redemption of £250 million of the Group's subordinated Tier 2 debt. Net cash generated from operating activities was £800.2 million (2021: £439.0 million).

Net cash used in investing activities of £100.8 million which reflected primarily the Group's continuing investment in its major IT programmes (2022: £108.4 million, 2021: £109.4 million).

Net cash used in financing activities of £657.5 million included £314.5 million (2021: £317.4 million) in dividends and Tier 1 capital coupon payments in the year, £50.1 million in share buybacks (2021: £101.0 million) and £8.9 million (2021: £101.9 million) lease principal payments. Also included in 2022 was the redemption of the remaining £250.0 million Tier 2 subordinated debt issued in 2012. Dividends paid in the year comprised the 7.6 pence interim dividend announced in the half-year results in 2022 and the 15.1 pence final dividend for 2021 announced in March 2022.

The £800.2 million the Group generated from operating activities more than offset net cash used in financing and investing activities and resulted in a net increase in cash and cash equivalents of £41.9 million (2021: £271.7 million reduction) to £938.4 million (2021: £896.5 million). The levels of cash and other highly liquid sources of funding that the Group holds to cover its claims obligations are continually monitored with the objective of ensuring that the levels remain within the Group's risk appetite.

Segmental Report

Motor

	31 Dec 2022	30 Sep 2022	30 Jun 2022	31 Mar 2022	31 Dec 2021	Year-on-year change
In-force policies (thousands)	3,836	3,854	3,944	3,954	3,971	(3.4%)
Of which:						
Direct own brands ¹	3,756	3,766	3,846	3,854	3,869	(2.9%)
Partnerships	80	88	98	100	102	(21.6%)
				FY 2022	FY 2021	Change
				£m	£m	
Gross written premium				1,432.7	1,560.8	(8.2%)
Of which:						
Direct own brands ¹				1,398.5	1,515.2	(7.7%)
Partnerships				34.2	45.6	(25.0%)
Operating (loss)/profit²				(77.2)	314.8	(124.5%)
Loss ratio ²				86.2%	64.3%	(21.9pts)
Commission ratio ²				3.4%	3.3%	(0.1pts)
Expense ratio ²				25.1%	24.8%	(0.3pts)
Combined operating ratio²				114.7%	92.4%	(22.3pts)
Current-year attritional loss ratio ²				90.9%	72.9%	(18.0pts)

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.

In H2, 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.

Home

	31 Dec 2022	30 Sep 2022	30 Jun 2022	31 Mar 2022	31 Dec 2021	Year-on-year change
In-force policies (thousands)	2,501	2,533	2,571	2,608	2,667	(6.2%)
Of which:						
Direct own brands ¹	1,732	1,758	1,792	1,825	1,879	(7.8%)
Partnerships	769	775	779	783	788	(2.4%)
				FY 2022	FY 2021	Change
				£m	£m	
Gross written premium				518.1	577.8	(10.3%)
Of which:						
Direct own brands ¹				381.5	416.7	(8.4%)
Partnerships				136.6	161.1	(15.2%)
Operating (loss)/profit²				(8.7)	141.8	(106.1%)
Loss ratio ²				80.2%	50.7%	(29.5pts)
Commission ratio ²				5.1%	6.9%	1.8pts
Expense ratio ²				21.6%	22.5%	0.9pts
Combined operating ratio²				106.9%	80.1%	(26.8pts)
Current-year attritional loss ratio ²				60.9%	55.7%	(5.2pts)
Normalised combined operating ratio ²				94.7%	85.2%	(9.5pts)

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 rate.

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.

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).

Rescue and other personal lines³

	31 Dec 2022	30 Sep 2022	30 Jun 2022	31 Mar 2022	31 Dec 2021	Year-on-year change
In-force policies (thousands)	2,424	2,472	2,512	2,512	2,505	(3.2%)
Of which:						
Rescue - ongoing operations	2,185	2,227	2,264	2,269	2,273	(3.9%)
Of which Green Flag direct	1,106	1,136	1,156	1,167	1,179	(6.2%)
Pet	128	130	133	135	138	(7.2%)
Other personal lines - ongoing operations	111	115	115	108	94	18.1%
				FY 2022	FY 2021	Change
				£m	£m	
Adjusted gross written premium ²				273.9	281.1	(2.6%)
Of which:						
Rescue - ongoing operations				143.7	155.2	(7.4%)
Of which Green Flag direct				88.2	88.3	(0.1%)
Pet				70.8	71.4	(0.8%)
Other personal lines - ongoing operations				59.4	54.5	9.0%
Operating profit²				59.7	73.3	(18.6%)
Loss ratio ²				54.0%	49.9%	(4.1pts)
Commission ratio ²				3.9%	3.6%	(0.3pts)
Expense ratio ²				27.9%	25.4%	(2.5pts)
Combined operating ratio²				85.8%	78.9%	(6.9pts)

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 policies, which was partly offset by higher own brand Travel policies. 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 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.

Commercial

	31 Dec 2022	30 Sep 2022	30 Jun 2022	31 Mar 2022	31 Dec 2021	Year-on-year change
In-force policies (thousands)	928	912	884	878	871	6.5%
Of which:						
Direct own brands ⁴	651	644	623	613	602	8.1%
NIG and other	277	268	261	265	269	3.0%
				FY 2022	FY 2021	Change
				£m	£m	
Gross written premium				749.3	653.0	14.7%
Of which:						
Direct own brands ⁴				218.9	187.4	16.8%
NIG and other				530.4	465.6	13.9%
Operating profit²				58.3	60.4	(3.5%)
Loss ratio ²				53.7%	54.5%	0.8pts
Commission ratio ²				19.4%	20.0%	0.6pts
Expense ratio ²				21.1%	21.7%	0.6pts
Combined operating ratio²				94.2%	96.2%	2.0pts
Current-year attritional loss ratio ²				57.5%	62.0%	4.5pts
Normalised combined operating ratio ²				92.8%	96.3%	3.5pts

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.

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.

Run-off partnerships

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).

Notes:

1. Direct own brands include in-force policies for Home and Motor under the Direct Line, Churchill, Darwin and Privilege brands.
2. See glossary on pages 56 to 58 for definitions and appendix A – Alternative Performance Measures on pages 60 to 63 for reconciliation to financial statement line items.
3. Ongoing operations and run-off partnerships – See glossary on pages 56 to 58 for definitions and appendix A – Alternative Performance Measures on pages 60 to 63 for reconciliation to financial statement line items.
4. Commercial direct own brands include in-force policies for Direct Line for Business and Churchill brands.

Balance sheet management

Capital management and dividend policy

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

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

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

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

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

In 2022, the Board announced an interim dividend of 7.6 pence per share. The Board is not recommending a final dividend and will update its dividend outlook at the 2023 half-year results.

In the Group's 2021 full year results, we announced a share buyback programme of up to £100 million, with an initial tranche of £50 million which was completed on 28 June 2022. The Board decided, when considering the half-year results to 30 June 2022, not to launch the second £50 million tranche of the £100 million buyback programme announced earlier in the year.

Capital analysis

The Group is regulated under Solvency II requirements by the PRA on both a Group basis and for the Group's principal underwriter, U K Insurance Limited. In its results, the Group has estimated its Solvency II own funds, SCR and solvency capital ratio as at 31 December 2022.

Capital position

At 31 December 2022, the Group held a Solvency II capital surplus of £0.57 billion above its regulatory capital requirements, which was equivalent to an estimated solvency capital ratio of 147%, after the interim dividend.

At 31 December	2022	2021
Solvency capital requirement (£ billion)	1.21	1.35
Capital surplus above solvency capital requirement (£ billion)	0.57	1.03
Solvency capital ratio post dividends and share buyback	147%	176%
Solvency capital ratio (as above)/adjusted solvency capital ratio ¹	147%	160%

Note:

1. Adjusted solvency capital ratio excluding Tier 2 debt which was redeemed in full on 27 April 2022.

Movement in capital surplus

	2022 £bn	2021 £bn
Capital surplus at 1 January	1.03	1.22
Capital (used)/generated excluding market movements	(0.06)	0.40
Market movements	(0.12)	(0.03)
Capital (used)/generated	(0.18)	0.37
Change in solvency capital requirement	0.14	(0.01)
Surplus (used)/generated	(0.04)	0.36
Capital expenditure	(0.12)	(0.12)
Repayment of subordinated Tier 2 notes	(0.25)	—
Interim dividend	(0.10)	(0.10)
Final dividend ¹	—	(0.20)
Share buyback	—	(0.10)
Removal of second tranche of share buyback	0.05	—
Increase in ineligible Tier 3 capital ²	—	(0.03)
Net surplus movement	(0.46)	(0.19)
Capital surplus at 31 December	0.57	1.03

Notes:

1. Foreseeable dividends included above are adjusted to exclude the expected dividend waivers in relation to shares held by the employee share trusts, which are held to meet obligations arising on the various share option awards.
2. At 31 December 2022, ineligible Tier 3 capital arose as the amount of Tier 3 capital permitted under the Solvency II regulations is 15% of the Group's SCR. At 31 December 2021, ineligible Tier 3 capital arose as the amount of Tier 2 and Tier 3 capital permitted under the Solvency II regulations is 50% of the Group's SCR.

During 2022, the Group repaid its then outstanding £250 million 9.25% subordinated Tier 2 notes. The Group used £0.18 billion of Solvency II capital after market movements and increased the surplus by £0.05 billion as the second £50 million tranche of the share buyback programme was not launched. Capital expenditure of £0.12 billion and the interim 2022 dividend of £0.10 billion reduced the capital surplus. Capital expenditure levels are expected to be broadly in line with 2022.

Change in solvency capital requirement

	2022 £bn
Solvency capital requirement at 1 January	1.35
Model and parameter changes	0.05
Exposure changes	(0.19)
Solvency capital requirement at 31 December	1.21

During 2022, the Group's SCR reduced by £0.14 billion to £1.21 billion. Exposure changes resulted in a £0.19 billion reduction partially offset by an increase of £0.05 billion relating to model and parameter changes. These changes were partly the result of management action to improve the Group's solvency ratio, including entering into a 10% whole account quota share reinsurance arrangement with effect from 1 January 2023 and reducing our longer duration USD credit holdings. The Group SCR also benefited from the impact of higher interest rates.

Scenario and sensitivity analysis¹

The following table shows the impact on the Group's estimated solvency capital ratio in the event of the following scenarios as at 31 December 2022. The impacts on the Group's solvency capital ratio arise from movements in both the Group's SCR and own funds.

At 31 December	Impact on solvency capital ratio	
	2022	2021 ²
Deterioration of small bodily injury motor claims equivalent to that experienced in 2008/09	(5pts)	(5pts)
One-off catastrophe loss equivalent to the 1990 storm "Daria"	(10pts)	(9pts)
One-off catastrophe loss based on extensive flooding of the River Thames	(10pts)	(9pts)
Increase in Solvency II inflation assumption for PPOs by 100 basis points ³	(10pts)	(9pts)
100bps increase in credit spreads ⁴	(5pts)	(8pts)
100bps decrease in interest rates with no change in the PPO real discount rate	1pt	(2pts)

Notes:

1. Sensitivities are calculated under the assumption full tax benefits can be realised.
2. 2021 figures exclude from own funds the value of the £250 million Tier 2 subordinated debt which was redeemed on 27 April 2022.
3. The periodic payment order ("PPO") inflation assumption used is an actuarial judgement which is reviewed annually based on a range of factors including the economic outlook for wage inflation relative to the PRA discount rate curve.
4. Includes only the impact on AFS assets (excludes assets held at amortised costs) and assumes no change to the SCR.

Own funds

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

At 31 December	2022	2021
	£bn	£bn
Tier 1 capital before foreseeable distributions	1.07	1.66
Foreseeable dividend and share buyback	–	(0.30)
Tier 1 capital – unrestricted	1.07	1.36
Tier 1 capital – restricted	0.32	0.36
Less reclassified restricted Tier 1 debt ¹	(0.05)	(0.02)
Eligible Tier 1 capital	1.34	1.70
Tier 2 capital – reclassified restricted Tier 1 debt and Tier 2 subordinated debt ¹	0.26	0.53
Tier 3 capital – deferred tax	0.21	0.18
Ineligible Tier 3 capital ²	(0.03)	(0.03)
Total eligible own funds	1.78	2.38

Notes:

1. As at 31 December 2022, £51 million (31 December 2021: £19 million) of the Group's restricted Tier 1 capital was reclassified as Tier 2 due to Solvency II tiering restrictions.
2. At 31 December 2022, ineligible Tier 3 capital arose as the amount of Tier 3 capital permitted under the Solvency II regulations is 15% of the Group's SCR. At 31 December 2021, ineligible Tier 3 capital arose as the combined amount of Tier 2 and Tier 3 capital permitted under the Solvency II regulations is 50% of the Group's SCR.

During 2022, the Group's eligible own funds reduced from £2.38 billion to £1.78 billion. Eligible Tier 1 capital after foreseeable distributions represents 75% of own funds and 111% of the estimated SCR. Tier 2 capital relates to the Group's £0.21 billion subordinated debt and £0.05 billion of ineligible Tier 1 capital. The maximum amount of Restricted Tier 1 capital permitted as a proportion of total Tier 1 capital under the Solvency II regulations is 20%. Restricted Tier 1 capital relates solely to the Tier 1 notes issued in 2017.

The amount of Tier 2 and Tier 3 capital permitted under the Solvency II regulations is 50% of the Group's SCR and the amount of Tier 3 alone is 15% of the Group's SCR. The Group has Tier 3 ineligible own funds of £0.03 billion.

Reconciliation of IFRS shareholders' equity to Solvency II eligible own funds

	2022	2021
At 31 December	£bn	£bn
Total shareholders' equity	1.93	2.55
Goodwill and intangible assets	(0.82)	(0.82)
Change in valuation of technical provisions	–	(0.01)
Other asset and liability adjustments	(0.04)	(0.06)
Foreseeable dividend and share buyback	–	(0.30)
Tier 1 capital – unrestricted	1.07	1.36
Tier 1 capital – restricted	0.32	0.36
Less reclassified restricted Tier 1 debt ¹	(0.05)	(0.02)
Eligible Tier 1 capital	1.34	1.70
Tier 2 capital – reclassified restricted Tier 1 debt and Tier 2 subordinated debt ¹	0.26	0.53
Tier 3 capital – deferred tax	0.21	0.18
Ineligible Tier 3 capital ²	(0.03)	(0.03)
Total eligible own funds	1.78	2.38

Notes:

1. As at 31 December 2022, £51 million (31 December 2021: £19 million) of the Group's restricted Tier 1 capital was reclassified as Tier 2 due to Solvency II tiering restrictions.
2. At 31 December 2022, the amount of Tier 3 capital permitted under the Solvency II regulations is 15% of the Group's SCR which resulted in ineligible capital of £33 million. At 31 December 2021, the amount of Tier 2 and Tier 3 capital permitted under the Solvency II regulations is 50% of the Group's SCR which resulted in ineligible capital of £31 million.

Investment portfolio

Our investment strategy aims to deliver several objectives, which are summarised below:

- to ensure there is sufficient liquidity available within the investment portfolio to meet stressed liquidity scenarios;
- to match PPOs and non-PPOs liabilities in an optimal manner; and
- to deliver a suitable risk-adjusted investment return commensurate with our risk appetite.

Asset and liability management

The following table summarises the Group's high-level approach to asset and liability management.

Liabilities	Assets	Characteristics
More than 10 years, for example PPOs	Property and infrastructure debt	Inflation linked or floating
Short and medium term - all other claims	Investment-grade credit	Fixed - key rate duration matched
Tier 1 equity	Investment-grade credit	Fixed
Tier 2 sub-debt (swapped fixed to floating)	Commercial real estate loans and cash	Floating
Tier 2 sub-debt fixed	Investment-grade credit and cash	Fixed or floating
Surplus - tangible equity	Investment-grade credit, short-term high yield, cash and government debt securities	Fixed or floating

Investment holdings

At 31 December	2022 £m	2021 £m
Investment-grade credit ¹	2,360.0	3,721.1
High yield	278.8	342.1
Private placements	98.2	91.2
Credit	2,737.0	4,154.4
Sovereign ¹	510.3	35.7
Total debt securities	3,247.3	4,190.1
Infrastructure debt	238.2	250.8
Commercial real estate loans	199.1	200.8
Other loans	1.9	—
Cash and cash equivalents ²	938.4	896.5
Investment property	278.5	317.0
Equity investments ³	13.6	6.2
Total investment holdings	4,917.0	5,861.4

Notes:

1. Asset allocation at 31 December 2022 includes investment portfolio derivatives, which have a mark-to-market asset value of £1.6 million which is split as an asset of £2.5 million included in investment grade credit and a liability of £0.9 million included in sovereign debt (31 December 2021: mark-to-market asset value of £14.2 million and £0.1 million respectively). This excludes non-investment derivatives that have been used to hedge operational cash flows.
2. Net of bank overdrafts: includes cash at bank and in hand and money market funds.
3. Equity investments consist of quoted shares and insurtech-focused equity funds. The insurtech-focused equity funds are valued based on external valuation reports received from a third-party fund manager.

At 31 December 2022, total investment holdings of £4,917.0 million were 16.1% lower than at the start of the year, reflecting adverse fair value movements in fixed rate debt securities, payment of the interim dividend, repayment of subordinated debt and share buy-back activity. Total debt securities were £3,247.3 million (31 December 2021: £4,190.1 million), of which 3.8% were rated as 'AAA' and a further 59.0% were rated as 'AA' or 'A'. The average duration at 31 December 2022 of total debt securities was 2.3 years (31 December 2021: 2.5 years).

At 31 December 2022, total unrealised losses, net of tax, on AFS investments were £194.7 million (31 December 2021: £9.0 million unrealised gains) as a result of higher credit spreads and increased interest rates.

Net asset value

At 31 December	Note	2022 £m	2021 £m
Net assets ¹	13	1,934.0	2,550.2
Goodwill and other intangible assets	13	(822.2)	(822.5)
Tangible net assets	13	1,111.8	1,727.7
Closing number of Ordinary Shares (millions)	13	1,298.2	1,317.3
Net asset value per share (pence)	13	149.0	193.6
Tangible net asset value per share (pence)	13	85.6	131.2

Note:

1. See glossary on pages 56 to 58 for definitions and appendix A – Alternative Performance Measures on pages 60 to 63 for reconciliation to financial statement line items.

Net assets at 31 December 2022 decreased by £616.2 million to £1,934.0 million (31 December 2021: £2,550.2 million) and tangible net assets decreased to £1,111.8 million (31 December 2021: £1,727.7 million) following adverse movements in the Group's AFS reserves and the reduction in profit for the year.

Leverage

The Group's financial leverage decreased by 1.4 percentage point to 23.8% (2021: 25.2%). The decrease was primarily due to a reduction in subordinated debt following the redemption of the Group's £250 million 9.25% Tier 2 notes on 27 April 2022, partially offset by a reduction in shareholders' equity, primarily due to dividends paid in the year and the share buyback, along with a reduction in the Group's AFS reserves.

At 31 December	2022 £m	2021 £m
Shareholders' equity	1,934.0	2,550.2
Tier 1 notes	346.5	346.5
Financial debt – subordinated debt	258.6	513.6
Total capital employed	2,539.1	3,410.3
Financial-leverage ratio¹	23.8%	25.2%

Note:

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

Credit ratings

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

Reserving

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

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

The most common method of settling bodily injury claims is by a lump sum. When this includes an element of indemnity for recurring costs, such as loss of earnings or ongoing medical care, the settlement calculations apply the statutory discount rate (known as the Ogden discount rate) to reflect the fact that payment is made on a one-off basis rather than periodically over time. The current Ogden discount rate is minus 0.25% for England and Wales, minus 0.75% in Scotland, and minus 1.5% in Northern Ireland.

We reserve our large bodily injury claims at the relevant discount rate for each jurisdiction, with the overwhelming majority now case reserved at minus 0.25% as most will be settled under the law of England and Wales. The Ogden discount rate will be reviewed again at the latest in 2024. There has been an ongoing reduction in large bodily injury exposures as a result of continued positive prior-year development of claims reserves, and a higher proportion of reserves being covered by reinsurance for the 2014 to 2020 underwriting years. Since 2021, we have reduced the level of Motor reinsurance purchased, resulting in higher net reserves for accident years 2021 and 2022. The 2023 Motor excess of loss ("XoL") reinsurance contract is in line with the 2022 Motor treaty, resulting in a similarly higher net retention for accident year 2023.

If the claimant prefers, large bodily injury claims can be settled using a PPO. This is an alternative way to provide an indemnity for recurring costs, making regular payments, usually for the rest of the claimant's life. These claims are reserved for using an internal discount rate, which is progressively unwound over time. As it is likely to take time to establish whether a claimant will prefer a PPO or a lump sum, until a settlement method is agreed we make assumptions about the likelihood that claimants will opt for a PPO. This is known as the PPO propensity. In 2022, the Group reviewed the estimates used to discount PPOs. Given the significant changes both in the current economic environment and the longer term outlook, the Group changed from flat rate inflation and discounting assumption to a yield curve approach, allowing for an increase in short-term inflation and higher long-term real returns. This resulted overall in the application of a real discount rate of 0.9% (2021: 0.0%), the combination of cash flow weighted inflation and discounting of 4.2% and 5.1% respectively, the latter driven by an expected increase in the long-term yield of the assets backing PPO liabilities.

Higher claims inflation remains a risk, given the continuing high level of consumer prices and wage inflation. In 2022, consumer prices inflation was at its highest level for the past decade and is not expected to normalise until 2024. Pressure is likely to remain strong on wages, with potential implications for the cost of care. Global supply chain issues remain problematic, resulting in a risk of price increases for products and components in short supply. A range of general and specific scenarios for excess inflation have been considered in the reserving process.

Prior-year reserve releases were £163.2 million (2021: £258.1 million) concentrated towards more recent accident years, with good experience across all categories.

Looking forward, the management best estimate will be replaced under IFRS 17 by the best estimate of liabilities ("BEL") and a risk adjustment. The BEL will be on a discounted basis and include an allowance for events not in data ("ENIDs"). The risk adjustment will be set around the 75th percentile.

Claims reserves net of reinsurance

	2022	2021
At 31 December	£m	£m
Motor	1,546.3	1,607.9
Home	409.2	297.8
Rescue and other personal lines (excluding run-off partnerships) ¹	55.2	53.5
Commercial	567.5	547.3
Total ongoing operations	2,578.2	2,506.5
Run-off partnerships ¹	30.0	41.9
Total	2,608.2	2,548.4

Note:

1. Ongoing operations and run-off partnerships – See glossary on pages 56 to 58 for definitions and appendix A – Alternative Performance Measures on pages 60 to 63 for reconciliation to financial statement line items.

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

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

	Increase/(decrease) in profit before tax ^{1,2}	
	2022	2021
At 31 December	£m	£m
PPOs³		
Impact of an increase in the discount rate used in the calculation of present values of 100 basis points	31.0	43.0
Impact of a decrease in the discount rate used in the calculation of present values of 100 basis points	(42.8)	(58.9)
Ogden discount rate⁴		
Impact of the Group reserving at a discount rate of 0.75% compared to minus 0.25% (2021: 0.75% compared to minus 0.25%)	46.7	42.5
Impact of the Group reserving at a discount rate of minus 1.25% compared to minus 0.25% (2021: minus 1.25% compared to minus 0.25%)	(64.2)	(59.4)
Claims inflation⁵		
Impact of a decrease in claims inflation by 200 basis points for two consecutive years	79.4	74.3
Impact of an increase in claims inflation by 200 basis points for two consecutive years	(80.5)	(75.5)

Notes:

- These sensitivities are net of reinsurance and exclude the impact of taxation.
- These sensitivities reflect one-off impacts at the balance sheet date and should not be interpreted as predictions.
- The sensitivities relating to an increase or decrease in the real discount rate used for PPOs illustrate a movement in the time value of money from the assumed level of 0.9% for reserving. The PPO sensitivity has been calculated on the direct impact of the change in the real internal discount rate with all other factors remaining unchanged.
- Ogden discount rate sensitivity has been calculated on the direct impact of a permanent change in the discount rate in England and Wales with all other factors remaining unchanged. The Group will consider the statutory discount rate when setting the reserves but not necessarily provide on this basis. This is intended to ensure that reserves are appropriate for current and potential future developments.
- We have updated this sensitivity, across 2021 and 2022, to a 200 basis point increase/decrease in inflation in acknowledgment of the current uncertain economic environment.

The PPO sensitivity above is calculated on the basis of a change in the internal discount rate used for the actuarial best estimate reserves as at 31 December 2022. It does not take into account any second order impacts such as changes in PPO propensity or reinsurance bad debt assumptions.

Tax management

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

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

Tax authorities

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

Tax policy and governance

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

For more information please see our published Group Tax policy on the Group's website at:

www.directlinegroup.co.uk/en/sustainability/reports-policies-and-statements.html

Total tax contribution

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

During 2022, the sum of taxes either paid or collected across the Group was £803.9 million. The composition of this between the various taxes borne and collected by the Group is shown below.

Total taxes borne

	2022
At 31 December	£m
Current-year Corporation Tax credit	(9.8)
Irrecoverable Value Added Tax incurred on overheads	79.9
Irrecoverable Value Added Tax embedded within claims spend	176.5
Employers' National Insurance contributions	44.8
Other taxes	5.9
Total	297.3

Total taxes collected

	2022
At 31 December	£m
Insurance Premium Tax	389.4
Value Added Tax	14.8
Employees' Pay As You Earn and National Insurance contributions	102.4
Total	506.6

NEIL MANSER

CHIEF FINANCIAL OFFICER

Principal risks and uncertainties

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

Our principal risks are under continuous review and assessment, and with the introductions of the FCA's PPR regulations and Consumer Duty, Conduct Risk is now deemed a principal risk to the Group. In addition, strategic and operational risks are seeing increasing trends, impacted by macro-economics changes putting pressure on strategy and the ongoing changes in technology systems, people, and processes.

Principal risks	Risk commentary
<p>Insurance risk is the risk of loss due to fluctuations in the timings, amount, frequency and severity of an insured event relative to the expectations at the time of underwriting.</p>	<p>Key drivers of the outlook for Insurance risk across the Group's strategic plan (the "Plan") include reserve, underwriting, distribution, pricing and reinsurance risks. Issues relating to claims inflation, the cost of living crisis, the impact of the FCA's PPR regulations and the global political situation, combined with supply/demand issues following Covid-19 and Brexit, have been key areas of focus for the Group in 2022 and have been the main drivers of the increasing trend in Insurance risk. This includes a slow-down in the processing of recoveries and liabilities with third party insurers which increases the estimation risk of these amounts.</p> <p>Unanticipated claims inflation, particularly in the motor market, has had a significant adverse impact on claims trends leading to uncertainty in claims reserving and pricing in 2022 and beyond.</p> <p>Key risk themes relating to this category include Macroeconomic Environment & Geopolitical Landscape, Organisational Resilience & Agility, and Sales Risk in a post FCA PPR regulations world.</p> <p>We have used scenario testing to understand the potential financial impacts of these risks and continue to monitor these risks closely.</p> <p>Finally, climate change presents a risk of more frequent extreme events and key risk indicators are being continually enhanced to monitor related risks across Home and Motor.</p>
<p>Market risk is the risk of loss resulting from fluctuations in the level and in the volatility of market prices of assets, liabilities and financial instruments.</p>	<p>Key drivers of market risk are the sensitivity of the values of our assets and investments to changes in credit spreads, our exposure to losses as a result of changes in interest rate term structure or volatility, and the key risk theme of Macroeconomic Environment & Geopolitical Landscape.</p> <p>Market risk remains at a heightened but stable level over the Plan due to recession risk, volatile markets and the risk of further property devaluations. Concerns about the risk of a prolonged recession and fiscal policy could affect equity and credit markets within the global economy leading to credit spread increases, foreign exchange rate volatility, interest rate changes and further devaluation of UK property assets.</p> <p>To seek to address this, we have an investment strategy which is approved by the Board and includes limiting exposure to individual asset classes and the amount of illiquid investments we hold. We also use risk reduction techniques such as hedging foreign currency exposures with forward contracts, and de-risking the investment portfolio during volatile periods.</p>

Principal risks	Risk commentary
<p>Operational risk is the risk of loss due to inadequate or failed internal processes or systems, human error or from external events.</p> <p>The key risks within this category relate to Cyber, Change, Partnerships, Model, Technology & Infrastructure, Business Interruption, and Material Outsourcing.</p>	<p>Operational risks can arise within all areas of the business and can manifest themselves as a result of inadequate or failed internal processes or systems, human error or because of external events.</p> <p>Key risk themes relating to this category include Organisational Resilience & Agility and People & Culture and our approach is to manage our operational risks proactively to mitigate potential customer harm, regulatory or legal censure, and financial or reputational impacts.</p> <p>The increasing trend in operational risk is driven mainly by increased risk in the control environment as the Group continued during 2022 and continues to implement and embed changes in its technology systems, data flows, pricing models, people, and processes, whilst operating within a more volatile external environment. The implementation and embedding of its motor platform and related matters coinciding with the volatile external environment in 2022 made the operating environment more challenging and increased the risk profile. We have in place operational processes and systems, including prevention and detection measures, that seek to ensure the Group is well placed to absorb and/or adapt to internal or external events that have the potential to have an adverse impact on our customer operations and the wider business more generally.</p> <p>With hybrid working well embedded across the business, large numbers of our people effectively continue to work from home. The business also remains on its journey to improve its use of data, pricing models, controls, processes and management information and the performance and resilience of its IT estate, focusing on delivering system stability, using new technologies to enhance contingency strategies, and seeking to optimise the use of tools and capability across the Group.</p> <p>Reviewing our target operating models across the Group, streamlining change implementation and ensuring we drive effective prioritisation in our investment decisions has remained a key area of management focus, to support the Group in achieving its strategic aims whilst also actively strengthening its controls to further mitigate the impact of potential risk events.</p> <p>Finally, the external threat landscape has continued to remain volatile globally, including the increase in state-sponsored cyber-attacks, more sophisticated ransomware attacks, disruptions to supply chains and the continued challenges associated to the cost of living crisis.</p> <p>The business has continued to monitor the external landscape closely, taking proactive measures to introduce new controls, strengthened existing ones, and enhanced our suite of automated monitoring and reporting, to enable us to respond to malicious and unintended threats from both internal and external entities.</p>
<p>Conduct risk describes the risk of failing to put the customer at the heart of our business, failing to deliver on our commitments and/or failing to ensure that fairness is a natural outcome of what we do and how we do it.</p>	<p>We have maintained a strong culture of delivering on our commitments to our customers.</p> <p>Pricing practices within the general insurance market have remained a key area of focus for the FCA and for the Group.</p> <p>Since the implementation of the FCA's PPR regulations, we have continued to carefully monitor with a view to ensuring that the right outcomes are being delivered to customers and we have maintained regular and close engagement and dialogue with the FCA throughout the year including concerning the requirements of the FCA's PPR regulations.</p> <p>The introduction of the Consumer Duty represents a significant shift in the FCA's expectations of firms and applies to all of the Group's regulated products. A comprehensive implementation plan has been put in place to address the requirements arising from the new Duty, which has been approved by the Board.</p> <p>Finally, the Group is aware of the impact of the rising cost of living on our customers and we are taking measures to help support customers during this period, including finalisation of the Vulnerable Customer Strategy and the launch of Churchill Motor Essentials to adapt to changing customer needs.</p>

Principal risks	Risk commentary
<p>Regulatory and compliance risk describes the risks leading to reputational damage, regulatory or legal censure, fines or prosecutions and other types of non-budgeted operational risk losses associated with the Group's conduct and activities.</p>	<p>The outlook for regulatory compliance risk is increasing as financial institutions respond to multiple regulatory change priorities, alongside a challenging external environment covered in strategic risk and insurance risk. Further, regulators are increasingly expecting financial institutions to play a broader role in resolving societal issues, such as income inequality, climate change and diversity and inclusion; creating challenges for insurers to balance commercial and societal outcomes in decision-making, as they seek to meet the needs of different stakeholders.</p> <p>We have maintained an open relationship with our regulators, and we have continued to engage with the regulators and HM Treasury regarding the future regulatory framework within the UK.</p> <p>We remain focused on the key areas of regulatory attention, including implementation of the FCA's PPR regulations, the Consumer Duty, FCA's 'Dear CEO' letter on cost of living and insurance, FCA guidance on the fair treatment of vulnerable customers, PRA 'Dear Chief Actuary' letter on reserving and capital modelling and inflation risk and the PRA's 'Dear CEO' letter on the PRA's supervision of climate related financial risk.</p> <p>We have also continued our focus upon operational resilience in accordance with the increased regulatory requirements introduced during the year.</p> <p>Finally, we have a governance and accountability framework in place as part of the Senior Managers and Certification Regime, and carry out an annual declaration process to ensure the ongoing fitness and propriety of the Group's Senior Managers and Certified Functions.</p>
<p>Credit risk is the risk of loss resulting from default in obligations due from and/or changes in the credit standing of issuers of securities, counterparties or any debtors to which the Group is exposed.</p>	<p>To manage credit risk, we set credit limits for each material counterparty and actively monitor credit exposures. In addition, we only purchase reinsurance from reinsurers with at least A- rating and, for liabilities with a relatively long period of time to settlement, this rating is at least A+. Finally, we also have well defined criteria to determine which customers are offered and granted credit.</p>
<p>Strategic risk is the risk of direct or indirect adverse effects resulting from strategies not being optimally chosen, implemented or adapted to changing conditions.</p>	<p>The trading updates issued in July 2022 and January 2023, the CEO stepping down also in January 2023 and response to the FCA's PPR regulations has led to an increasing strategic risk for the Group over the Plan period and a need to rebuild balance sheet resilience. A period of uncertainty in leadership continuity may restrict the Group's ability to progress with its strategic growth agenda. However, completing the Group's 10% quota share reinsurance contract has contributed to restoring capital resilience.</p> <p>Strategic risk is also influenced by internal and external developments, including the risk of the UK entering a recession, the worst cost of living crisis in decades, high levels of inflation, and the longer-term implications of the war in Ukraine and other geopolitical tensions that could crystallise.</p> <p>To allow for better recognition of internal and external drivers of climate-related risk and to provide a focal point for the reporting of risks relating to climate change, the Strategic risk category has been broadened to include Climate risk within Environmental, Social and Governance risk.</p> <p>The Group takes the following steps to manage its risks:</p> <ul style="list-style-type: none"> — we agree, monitor and manage performance against the Board-approved plan and targets; — the Board leads an annual strategy and five-year planning process which considers our performance, competitor positioning and strategic opportunities; — as part of the timetable for the Plan, the Risk Function carries out a risk review of the Plan which is documented in the Group's Own Risk and Solvency Assessment and presented to the Board; and — we identify and manage emerging risks using established governance processes and forums.

Effects of macroeconomic and trading environments on the Group

The UK is facing into a cost of living crisis and the potential of a UK recession, driven by the challenging macroeconomic environment. This, in conjunction with a challenging trading environment, could lead to or exacerbate existing risks for the Group and we remain alert to possible developments across our risk universe.

Emerging risks

Emerging risks are defined by the Group as newly developing or changing threats or opportunities, external to the Group, that are subject to a high degree of uncertainty but have the potential to materially impact the Group.

The Group has in place an emerging risks process designed to enable it to:

- have a proactive approach to emerging risk management;
- identify, manage and monitor a broad range of potential emerging risks; and
- mitigate the impact of emerging risks which could impact the delivery of the Plan.

The Group records emerging risks within an Emerging Risk Register. An update on emerging risks is presented to the Board Risk Committee annually and is supplemented by deep dives on selected emerging risks.

The most notable emerging risks currently being monitored via the emerging risks process are outlined below.

Climate change

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

During 2022, the Group has continued to embed further controls and targets around climate change including receiving approval of its emission targets from the Science Based Targets initiative, whilst the Climate Executive Steering Group has created a sub-group to provide expertise on the reporting and governance of targets.

We continue to monitor these risks closely and to develop our climate change modelling capability. Further details on our risk management approach to climate change are included in the Group's annual report, within the Task Force for Climate-related Disclosure ("TCFD") report.

Changing customer needs

As consumers face intense pressure on their finances and time, coupled with generational changes, this is expected to generate a rapid structural shift in customer demand, requiring the Group to innovate and adapt its product offerings in order to remain relevant.

In 2022, in response to this emerging risk, the business reviewed its new product approval processes to identify opportunities to streamline the approach and enable a faster, but still safe, route to market. It also developed an implementation plan to embed Consumer Duty principles.

Keeping up with digital advancements

Developments in technology and changes in market, regulatory and consumer trends are creating opportunities for new entrants to profitably exploit new distribution channels, business models and niches. Failure to keep up with such developments could lead the Group to fall behind. To mitigate this, the Group is delivering multiple programmes to provide the Group with the capabilities to enable future innovation at pace.

Geopolitical tension

Due to heightened tensions on the world stage, there is a risk that measures are implemented by governments that decrease political stability, erode countries' relationships and contribute to increasing protectionism. This could lead to multiple impacts including on investment performance and supply chains. The Group conducts ongoing analysis to monitor exposure to the developing geopolitical environment (for example, Russia/Ukraine), while maintaining a close eye on the political risk landscape.

Automotive technology

New car technology, such as autonomous vehicles and hydrogen power are in development which, once on UK roads, is expected to be transformative. Traditional motor policies may no longer serve the needs of customers, requiring changes to the Group's pricing models and policy wordings to remain relevant. The repair networks' capabilities will also need to be upgraded to serve this demand effectively. The Group will focus on launching new products that will better serve customer needs in the future while engaging with regulators to help shape policies and understand potential impacts for the Group.

Data ethics

Consumers are becoming more aware of their data rights and regulators more interested in how firms use customer data. The industry is also gathering more data than ever before and increasingly exploring more sophisticated processing capabilities, such as artificial intelligence ("AI") and machine-learning. These trends together could lead to data being used in ways that customers or regulators find unacceptable, or which result in unfair customer outcomes.

The Group is embedding the Data Ethics Framework within the Pricing & Underwriting team's policies and procedures, while providing guardrails to apply across the Group. As new data capabilities are introduced, our monitoring and oversight is designed to ensure adherence to the principles set out in the Framework.

CONSOLIDATED INCOME STATEMENT

For the year ended 31 December 2022

	Notes	2022 £m	2021 £m
Gross earned premium		3,132.2	3,168.0
Reinsurance premium		(165.7)	(210.6)
Net earned premium	4	2,966.5	2,957.4
Investment return	5	51.6	146.3
Instalment income		92.4	97.3
Other operating income	6	55.3	46.7
Total income		3,165.8	3,247.7
Insurance claims	7	(2,218.0)	(1,915.3)
Insurance claims (payable to)/recoverable from reinsurers	7	(16.6)	196.6
Net insurance claims	7	(2,234.6)	(1,718.7)
Commission expenses	8	(211.1)	(240.9)
Operating expenses (including restructuring and one-off costs)	9	(744.8)	(807.8)
Total expenses		(955.9)	(1,048.7)
Finance costs	10	(20.4)	(34.3)
(Loss)/profit before tax		(45.1)	446.0
Tax credit/(charge)		5.6	(102.3)
(Loss)/profit for the year attributable to the owners of the Company		(39.5)	343.7
(Loss)/earnings per share:			
Basic (pence)	12	(4.3)	24.5
Diluted (pence)	12	(4.3)	24.1

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2022

	2022	2021
	£m	£m
(Loss)/profit for the year attributable to the owners of the Company	(39.5)	343.7
Other comprehensive loss		
Items that will not be reclassified subsequently to the income statement:		
Remeasurement (loss)/gain on defined benefit pension scheme	(9.8)	3.8
Tax relating to items that will not be reclassified	2.5	(0.8)
	(7.3)	3.0
Items that may be reclassified subsequently to the income statement:		
Cash flow hedges	0.2	(0.3)
Fair value loss on AFS investments	(295.8)	(84.1)
Add: net loss/(gain) on AFS investments transferred to income statement on disposals	24.9	(7.9)
Tax relating to items that may be reclassified	67.2	17.1
	(203.5)	(75.2)
Other comprehensive loss for the year net of tax	(210.8)	(72.2)
Total comprehensive (loss)/income for the year attributable to the owners of the Company	(250.3)	271.5

CONSOLIDATED BALANCE SHEET

As at 31 December 2022

	Notes	2022 £m	2021 £m
Assets			
Goodwill and other intangible assets		822.2	822.5
Property, plant and equipment		83.7	113.8
Right-of-use assets		73.0	76.1
Investment property		278.5	317.0
Reinsurance assets	14	1,101.7	1,211.8
Current tax assets		71.9	14.4
Deferred tax assets		62.0	—
Deferred acquisition costs		188.3	186.6
Insurance and other receivables		791.6	762.8
Prepayments, accrued income and other assets		105.8	125.1
Derivative financial instruments		31.3	35.9
Retirement benefit asset		1.6	12.1
Financial investments	15	3,698.5	4,633.6
Cash and cash equivalents	16	1,003.6	955.7
Assets held for sale		40.9	41.2
Total assets		8,354.6	9,308.6
Equity			
Shareholders' equity		1,934.0	2,550.2
Tier 1 notes	18	346.5	346.5
Total equity		2,280.5	2,896.7
Liabilities			
Subordinated liabilities	19	258.6	513.6
Insurance liabilities	20	3,654.3	3,680.5
Unearned premium reserve	21	1,462.7	1,500.7
Borrowings	16	65.2	59.2
Derivative financial instruments		29.6	19.5
Provisions		64.3	96.4
Trade and other payables, including insurance payables		457.8	457.3
Lease liabilities		81.6	84.2
Deferred tax liabilities		—	0.5
Total liabilities		6,074.1	6,411.9
Total equity and liabilities		8,354.6	9,308.6

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2022

	Share capital (note 17) £m	Employee trust shares £m	Capital reserves £m	AFS revaluation reserve £m	Foreign exchange translation reserve £m	Retained earnings £m	Shareholders' equity £m	Tier 1 notes (note 18) £m	Total equity £m
Balance at 1 January 2021	148.9	(40.3)	1,451.1	83.9	—	1,056.1	2,699.7	346.5	3,046.2
Profit for the year	—	—	—	—	—	343.7	343.7	—	343.7
Other comprehensive (loss)/income	—	—	—	(74.9)	(0.3)	3.0	(72.2)	—	(72.2)
Total comprehensive (loss)/income for the year	—	—	—	(74.9)	(0.3)	346.7	271.5	—	271.5
Dividends and appropriations paid (note 11)	—	—	—	—	—	(317.4)	(317.4)	—	(317.4)
Shares acquired by employee trusts	—	(20.3)	—	—	—	—	(20.3)	—	(20.3)
Shares cancelled following buyback	(3.7)	—	3.7	—	—	(101.0)	(101.0)	—	(101.0)
Credit to equity for equity-settled share-based payments	—	—	—	—	—	17.0	17.0	—	17.0
Shares distributed by employee trusts	—	19.2	—	—	—	(19.2)	—	—	—
Tax on share-based payments	—	—	—	—	—	0.7	0.7	—	0.7
Total transactions with equity holders	(3.7)	(1.1)	3.7	—	—	(419.9)	(421.0)	—	(421.0)
Balance at 31 December 2021	145.2	(41.4)	1,454.8	9.0	(0.3)	982.9	2,550.2	346.5	2,896.7
Loss for the year	—	—	—	—	—	(39.5)	(39.5)	—	(39.5)
Other comprehensive (loss)/income	—	—	—	(203.7)	0.2	(7.3)	(210.8)	—	(210.8)
Total comprehensive (loss)/income for the year	—	—	—	(203.7)	0.2	(46.8)	(250.3)	—	(250.3)
Dividends and appropriations paid (note 11)	—	—	—	—	—	(314.5)	(314.5)	—	(314.5)
Shares acquired by employee trusts	—	(11.0)	—	—	—	—	(11.0)	—	(11.0)
Shares cancelled following buyback	(2.1)	—	2.1	—	—	(50.1)	(50.1)	—	(50.1)
Credit to equity for equity-settled share-based payments	—	—	—	—	—	9.5	9.5	—	9.5
Shares distributed by employee trusts	—	13.4	—	—	—	(13.4)	—	—	—
Tax on share-based payments	—	—	—	—	—	0.2	0.2	—	0.2
Total transactions with equity holders	(2.1)	2.4	2.1	—	—	(368.3)	(365.9)	—	(365.9)
Balance at 31 December 2022	143.1	(39.0)	1,456.9	(194.7)	(0.1)	567.8	1,934.0	346.5	2,280.5

CONSOLIDATED CASH FLOW STATEMENT

For the year ended 31 December 2022

	Notes	2022 £m	2021 £m
Net cash (used by)/generated from operating activities before investment of insurance assets		(60.3)	271.8
Cash generated from investment of insurance assets		860.5	167.2
Net cash generated from operating activities		800.2	439.0
Cash flows used in investing activities			
Purchases of goodwill and other intangible assets		(108.4)	(109.4)
Purchases of property, plant and equipment		(11.7)	(29.3)
Proceeds on disposals of assets held for sale		19.3	—
Net cash used in investing activities		(100.8)	(138.7)
Cash flows used in financing activities			
Dividends paid	11	(297.9)	(300.8)
Appropriations paid	11	(16.6)	(16.6)
Finance costs (including lease interest)		(23.0)	(31.4)
Principal element of lease payments		(8.9)	(101.9)
Purchase of employee trust shares		(11.0)	(20.3)
Redemption of subordinated Tier 2 notes		(250.0)	—
Shares purchased in buyback		(50.1)	(101.0)
Net cash used in financing activities		(657.5)	(572.0)
Net increase/(decrease) in cash and cash equivalents		41.9	(271.7)
Cash and cash equivalents at the beginning of the year	16	896.5	1,168.2
Cash and cash equivalents at the end of the year	16	938.4	896.5

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1. Accounting policies

1.1 Basis of preparation

The financial information included in this preliminary announcement has been prepared in accordance with the recognition and measurement criteria of International Financial Reporting Standards ("IFRS") as adopted by the UK. The financial information set out in the announcement does not constitute the Company's statutory accounts for the years ended 31 December 2022 or 2021. The financial information for the year ended 31 December 2021 is derived from the statutory accounts for that year which have been delivered to the Registrar of Companies. The auditors reported on those accounts: their report was unqualified, did not draw attention to any matters by way of emphasis and did not contain a statement under s498(2) or (3) of the Companies Act 2006. The audit of the statutory accounts for the year ended 31 December 2022 is not yet complete. These accounts will be finalised on the basis of the financial information presented by the Directors in this preliminary announcement and will be delivered to the Registrar of Companies following the Company's Annual General Meeting.

1.2 Going concern

The Directors believe that the Group has sufficient financial resources to meet its financial needs, including managing a mature portfolio of insurance risk. The Directors believe the Group is well positioned to manage its business risks successfully in the current economic climate. The trading update that was approved by the Board of Directors and announced to the stock market on 11 January 2023 in respect of the Group's trading for 2022 and outlook for 2023, set out the challenging conditions that the Group has faced, in particular with respect to the severe weather in December 2022 and further increases in motor claims inflation, as well as the impact on the Group's investment property portfolio valuation. The Finance Review describes the Group's capital management strategy, including the capital actions taken in the last 12 months designed to ensure the continued strength of the balance sheet and sets out management actions that the Group continues to pursue to improve capital strength. The Group's financial position is also covered in that section, including a commentary on cash and investment levels, reserves, currency management, insurance liability management, liquidity and borrowings. The financial disclosures relating to the Group's principal risks are set out in note 3 of the Group's 2022 Annual Report and Accounts. This covers insurance, market and credit risk; and the Group's approach to monitoring, managing and mitigating exposures to these risks.

The Directors have assessed the principal risks of the Group over the duration of the planning cycle, which runs until 2026. The Group's Risk Function has carried out an assessment of the risks to the strategic plan ("the Plan") and the dependencies for the success of the Plan. This included running adverse scenarios on the Plan to consider the downside risks to the Plan and subsequent impact on forecast profit. The key scenarios applied to the Plan were in relation to the impact of adverse claims inflation, delay in pricing actions, increase in operating expenses and a fall in asset values. The key judgements and assumptions applied in these scenarios were as follows:

- adverse claims inflation: the Group's Plan includes a scenario for inflation being higher than expected, leading to claims costs increasing by 3% with the Group and market response delayed by six months;
- delay in pricing: future initiatives deliver 50% of expected value;
- increase in operating expenses: there is a delay of 12 months to achieving benefits from 2023 expense reduction initiatives; and
- fall in asset values: an increase in credit spreads of 50 basis points in the UK and 25 basis points outside of the UK in 2023, with spreads remaining elevated.

In connection with the trading update released on 11 January 2023, a reforecast based on the Plan was prepared without delay.

The Risk Function has also carried out an assessment of the risks to the Group's capital position over 2023 and 2024. Two specific macroeconomic scenarios, a moderate and a severe, have been run to assess the possible impact on the Group's own funds in the period to 31 December 2023 and 31 December 2024. The macroeconomic assumptions for key parameters such as Consumer Price index, GDP and bank base rate for the moderate scenario reflect the adverse end of the Bank of England November Monetary Policy Committee forecast range. The severe scenario adopts the key parameters from the 2022 Bank of England Banking Stress Test, which is described as "severe but plausible".

A reverse stress test was also performed to identify a combination of stresses that would result in capital loss and thus threaten the viability of U K Insurance Limited, the Group's principal underwriter, i.e. a reduction of own funds to below the solvency capital requirement. The reverse stress test combines the severe macroeconomic stress with the impacts from a series of three natural catastrophes from the 2022 PRA Insurance Stress Test.

In the moderate and severe scenarios, it was concluded that the Group's and U K Insurance Limited's solvency capital requirement would not be breached following the implementation of management actions, such as de-risking the asset portfolio, the purchase of additional reinsurance cover, asset disposal or, if necessary, raising equity.

Further information in relation to the sensitivity of key factors on the Group's financial position are included in the Chief Financial Officer Review. This sets out the impact on profit before tax of an increase and a decrease in claims inflation of 200 basis points for two consecutive years. The market risk note in the 2022 Annual Report and Accounts sets out the impact on profit before tax and equity of a 100 basis points increase in spreads on financial investments and the impact of a 100 basis points increase in interest rates on financial investments and derivatives.

Therefore, having made due enquiries, the Directors reasonably expect that the Group has adequate resources to continue in operational existence for at least 12 months from 12 March 2023 (the date of approval of the consolidated financial statements). Accordingly, the Directors have adopted the going concern basis in preparing the consolidated financial statements.

1. Accounting policies continued

1.3 Adoption of new and revised standards

The Group has adopted the following new amendments to IFRSs and International Accounting Standards ("IASs") that became mandatorily effective for the Group for the first time during 2022. None of the changes have a material impact for the Group.

In May 2020, the IASB issued narrow-scope amendments to three standards:

- Amendments to IFRS 3 'Business Combinations' update a reference in IFRS 3 to the Conceptual Framework for Financial Reporting without changing the accounting requirements for business combinations;
- Amendments to IAS 16 'Property, Plant and Equipment' prohibit a company from deducting from the cost of property, plant and equipment amounts received from selling items produced while the company is preparing the asset for its intended use. Instead, a company will recognise such sales proceeds and related cost in profit or loss; and
- Amendments to IAS 37 'Provisions, Contingent Liabilities and Contingent Assets' specify which costs a company includes when assessing whether a contract will be loss-making.

Also, in May 2020, the IASB issued 'Annual Improvements to IFRS Standards 2018-2020' which makes minor amendments to:

- IFRS 1 'First-time Adoption of International Financial Reporting Standards' which simplifies the application of IFRS 1 for a subsidiary that becomes a first-time adopter of IFRS standards later than its parent;
- IFRS 9 'Financial Instruments' – this amendment clarifies that – for the purpose of performing the '10 per cent test' for derecognition of financial liabilities – in determining those fees paid net of fees received, a borrower includes only fees paid or received between the borrower and the lender, including fees paid or received by either the borrower or lender on the other's behalf; and
- IFRS 16 'Leases' which removes the illustration of payments from the lessor relating to leasehold improvements.

1.4 Accounting developments

Changes in accounting policies and disclosures

(a) Estimated impact of the transition to IFRS 17 'Insurance Contracts' and IFRS 9 'Financial Instruments'

The Group will apply IFRS 17 and IFRS 9 for the first time on 1 January 2023. IFRS 17 is expected to bring a significant change to how the Group accounts for its insurance contracts issued and reinsurance contracts held and is therefore expected to have a material financial impact on the Group's consolidated financial statements in the period of initial application. IFRS 9 has a limited impact. The table below summarises the expected financial impact:

Estimated reduction in the Group's total equity

	1 January 2022 £m
Adjustments due to the adoption of IFRS 17: Non-life contracts	(73.9)
Adjustments due to the adoption of IFRS 9: Impairment of financial assets	(4.1)
Current tax impacts	—
Deferred tax impacts	17.8
Estimated impact of adoption of IFRS 17 and 9 after tax on total equity	(60.2)

The following notes provide a summary of the main accounting policies that the Group will adopt on transition to IFRS 17 and IFRS 9, as well as the significant estimates and judgements that will be made.

(b) IFRS 17 – Significant accounting policies

Insurance and reinsurance contracts classification

Contract classification, as disclosed in policy note 1.3 of the Group's Annual Report and Accounts, remains unchanged on adoption of IFRS 17.

The Group has reinsurance treaties and other reinsurance contracts that transfer significant insurance risk. The Group cedes insurance risk by reinsurance in the normal course of business.

Insurance contracts accounting treatment

(i) Separating components from insurance and reinsurance contracts

The Group assesses its insurance contracts to determine whether they contain distinct components which must be accounted for under another IFRS instead of under IFRS 17. After separating any distinct components, the Group applies IFRS 17 to all remaining components of the (host) insurance contract. Currently, the Group's contracts do not include any distinct components that require separation.

1.4 Accounting developments continued

(ii) Level of aggregation

IFRS 17 requires that a level of aggregation is determined for applying its requirements. The level of aggregation is determined firstly by dividing the business written into portfolios. Portfolios comprise groups of contracts with similar risks which are managed together. IFRS 17 also requires that no group, for aggregation purposes, may contain contracts issued more than one year apart.

Hence, within each year of issue, portfolios of contracts are divided into three groups, as follows:

- a group of contracts that are onerous at initial recognition;
- a group of contracts that, at initial recognition, have no significant possibility of becoming onerous subsequently (if any); and
- a group of the remaining contracts in the portfolio.

(iii) Recognition

The Group recognises groups of insurance contracts it issues from the earliest of the following:

- the beginning of the coverage period of the group of contracts;
- the date when the first payment from a policyholder in the group is due or when the first payment is received if there is no due date; or
- for a group of onerous contracts, when facts and circumstances indicate that the group is onerous.

The Group recognises a group of reinsurance contracts held it has entered into from the earlier of the following:

- the beginning of the coverage period of the group of reinsurance contracts held. However, the Group delays the recognition of a group of reinsurance contracts held that provide proportionate coverage until the date any underlying insurance contract is initially recognised, if that date is later than the beginning of the coverage period of the group of reinsurance contracts held; and
- the date the Group recognises an onerous group of underlying insurance contracts if the Group entered into the related reinsurance contract held at or before that date.

(iv) Contract boundary

The Group includes in the measurement of a group of insurance contracts all the future cash flows within the boundary of each contract in the group. Cash flows are within the boundary of an insurance contract if they arise from substantive rights and obligations that exist during the reporting period in which the Group can compel the policyholder to pay the premiums, or in which the Group has a substantive obligation to provide the policyholder with insurance contract services.

A liability or asset relating to expected premiums or claims outside the boundary of the insurance contract is not recognised. Such amounts relate to future insurance contracts.

(v) Measurement – Premium Allocation Approach ("PAA")

The Group applies the PAA to all the insurance contracts that it issues and expects to apply it to reinsurance contracts that it holds, as:

- the coverage period of each contract in the group is one year or less, including insurance contract services arising from all premiums within the contract boundary; or
- for contracts longer than one year, the Group has modelled possible future scenarios and reasonably expects that the measurement of the liability for remaining coverage for the group containing those contracts under the PAA does not differ materially from the measurement that would be produced by applying the General Measurement Model. For insurance contracts, this is expected to equate to less than 2% of gross written premium under IFRS 4 on transition; for reinsurance contracts, this is primarily in respect of the Group's Motor excess of loss treaty and is also expected to apply to the Group's quota share reinsurance agreement.

Insurance contracts – initial measurement

For a group of contracts that is not onerous at initial recognition, the Group measures the liability for remaining coverage as:

- the premiums, if any, received at initial recognition; plus
- any other asset or liability previously recognised for cash flows related to the group of contracts that the Group pays or receives before the group of insurance contracts is recognised.

Where facts and circumstances indicate that contracts are onerous at initial recognition, the Group performs additional analysis to determine if a net outflow is expected from the contract. Such onerous contracts are separately grouped from other contracts and the Group recognises a loss in profit or loss for the net outflow, resulting in the carrying amount of the liability for the group being equal to the fulfilment cash flows. A loss component is established by the Group for the liability for remaining coverage for such onerous group depicting the losses recognised.

Reinsurance contracts held – initial measurement

The Group measures its reinsurance assets for a group of reinsurance contracts that it holds on the same basis as insurance contracts that it issues. However, they are adapted to reflect the features of reinsurance contracts held that differ from insurance contracts issued, for example the generation of expenses or reduction in expenses rather than revenue.

Where the Group recognises a loss on initial recognition of an onerous group of underlying insurance contracts or when further onerous underlying insurance contracts are added to a group, the Group establishes a loss-recovery component of the asset for remaining coverage for a group of reinsurance contracts held depicting the recovery of losses.

1.4 Accounting developments continued

Insurance contracts – subsequent measurement

The Group measures the carrying amount of the liability for remaining coverage at the end of each reporting period as:

- the liability for remaining coverage at the beginning of the period; plus
- premiums received in the period; minus
- the amount recognised as insurance revenue for the services provided in the period.

The Group estimates the liability for incurred claims as the fulfilment cash flows related to incurred claims. The fulfilment cash flows incorporate, in an unbiased way, all reasonable and supportable information available without undue cost or effort about the amount, timing and uncertainty of those future cash flows; they reflect current estimates from the perspective of the Group and include an explicit adjustment for non-financial risk (the risk adjustment). The Group adjusts the future cash flows for the time value of money and the effect of financial risk for the measurement of liability for incurred claims, including those that are expected to be paid within one year of being incurred.

Reinsurance contracts held – subsequent measurement

The subsequent measurement of reinsurance contracts held follows the same principles as those for insurance contracts issued and has been adapted to reflect the specific features of reinsurance held.

Insurance acquisition cash flows for insurance contracts issued

All insurance acquisition cash flows are expensed as incurred. This includes for a small number of contracts where the coverage period exceeds a period of twelve months (see above) and there are no material amounts of acquisition costs relating to these contracts. This differs to the Group's previous policy of deferring acquisition costs over a 12-month period.

Insurance contracts – modification and derecognition

The Group derecognises insurance contracts when:

- the rights and obligations relating to the contract are extinguished (i.e. discharged, cancelled or expired); or
- the contract is modified such that the modification results in a change in the measurement model or the applicable standard for measuring a component of the contract, substantially changes the contract boundary, or requires the modified contract to be included in a different group. In such cases, the Group derecognises the initial contract and recognises the modified contract as a new contract.

When a modification is not treated as a derecognition, the Group recognises amounts paid or received for the modification with the contract as an adjustment to the estimate of fulfilment cash flows.

(vi) Presentation

The Group presents separately, in the consolidated balance sheet, the carrying amount of portfolios of insurance contracts issued that are assets, portfolios of insurance contracts issued that are liabilities, portfolios of reinsurance contracts held that are assets and portfolios of reinsurance contracts held that are liabilities.

The Group disaggregates the total amount recognised in the income statement and insurance service result, comprising insurance revenue and insurance service expense and insurance finance income or expenses.

The Group does not disaggregate the change in risk adjustment for non-financial risk between a financial and non-financial portion and includes the entire change as part of the insurance service result.

The Group separately presents income or expenses from reinsurance contracts held from the expenses or income from insurance contracts issued.

Insurance revenue

The insurance revenue for the period is the amount of expected premium receipts (excluding any investment component) allocated to the period. The Group allocates the expected premium receipts to each period of insurance contract services on the basis of the passage of time. The liability for remaining coverage is not discounted.

Insurance finance income and expense

Insurance finance income or expenses comprise the change in the carrying amount of the group of insurance contracts in respect of incurred claims arising from:

- the effect of the time value of money and changes in the time value of money; and
- the effect of financial risk and changes in financial risk.

The Group does not disaggregate finance income and expenses because the related financial assets are managed on a fair value basis and measured at fair value through profit or loss ("FVTPL").

Net income or expense from reinsurance contracts held

The Group presents separately on the face of the income statement the amounts expected to be recovered from reinsurers, and an allocation of the reinsurance premiums paid. The Group treats reinsurance cash flows that are contingent on claims on the underlying contracts as part of the claims that are expected to be reimbursed under the reinsurance contract held and treats amounts not dependent on the underlying claims, such as ceding commissions, as a reduction in the premiums paid to the reinsurer. Additionally, the allocation of premiums paid will not be presented as a reduction on the face of the income statement.

(c) IFRS 17 – accounting judgements and sources of estimation uncertainty

It is expected that the Group will have additional accounting judgements and sources of estimation uncertainty on adoption of IFRS 17 as follows:

1.4 Accounting developments continued

Level of aggregation

Accounting judgement

The Group defines a portfolio as insurance contracts subject to similar risks and managed together. Contracts within the same product line are expected to be in the same portfolio as they have similar risks and are managed together. The assessment of which risks are similar and how contracts are managed requires the exercise of judgement.

Premium Allocation Approach

Accounting judgement

For a small number of insurance contracts, and reinsurance contracts, which have a coverage period that is greater than 12 months (as described in note 1.4 (b) (v)), the Group elects to apply the PAA if at the inception of the contract, the Group reasonably expects that it will provide a liability for remaining coverage that would not differ materially from the General Measurement Model. The Group exercises judgement in determining whether the PAA eligibility criteria are met at initial recognition.

Onerous contracts

Source of estimation uncertainty

The Group assumes that no contracts are onerous at initial recognition unless facts and circumstances indicate otherwise. This is based on an assessment of future cash flows, which may be uncertain due to their timing, size and/or probability. If at any time during the coverage period the facts and circumstances indicate that a group of insurance contracts is onerous, the Group establishes a loss component as the excess of the fulfilment cash flows that relate to the remaining coverage of the group over the carrying amount of the liability for remaining coverage of the group as determined above. Accordingly, by the end of the coverage period of the group of contracts the loss component will be zero. Where the Group recognises a loss on initial recognition of an onerous group of underlying insurance contracts, or when further onerous underlying insurance contracts are added to a group, and the Group has a corresponding reinsurance held contract, the Group establishes a loss-recovery component of the asset for remaining coverage for a group of reinsurance contracts held depicting the expected recovery of the losses.

Estimates of future cash flows

Source of estimation uncertainty

In estimating future cash flows, the Group will incorporate, in an unbiased way, all reasonable and supportable information that is available without undue cost or effort at the reporting date. This information includes both internal and external historical data about claims and other experience, updated to reflect current expectations of future events. The estimates of future cash flows will reflect the Group's view of current conditions at the reporting date, ensuring the estimates of any relevant market variables are consistent with observable market prices, however these cash flows are inherently uncertain in size, timing and are based on probability-weighted average expectations.

Discount rates

Accounting judgement

IFRS 17 requires entities to determine discount rates using either the 'bottom up' or 'top down' approach. The 'top down' approach involves using discount rate curves derived from a portfolio of reference assets adjusted to remove all characteristics of the assets that are not present in insurance contracts, but not requiring to eliminate the illiquidity premium. The Group selected to apply the 'bottom up' approach which requires the use of risk-free rate curves and adding the illiquidity premium. The standard does not specify how to derive the illiquidity premium.

The Group will generally determine risk-free discount rates using the Solvency II risk-free rates sourced from the Bank of England. For cash flows that are not in respect of PPOs, a small illiquidity premium will be added to the risk-free rate, reflecting the short settlement tail. For PPOs, to reflect the different liquidity characteristics of the cash flows, the risk-free yield curves will be adjusted by a generally higher illiquidity premium. The illiquidity premium will be determined by using a fundamental spread approach by deducting the risk-free rate and credit risk premium from corresponding corporate bond reference portfolios. For non-PPOs, the reference portfolio is A-rated bonds with terms of 1 to 3 years and for PPOs, the reference portfolio is BBB-rated bonds with a remaining term of 15 or more years. Judgement is applied when determining the illiquidity premium with respect to allowances for past and future trends, considering changes in the economic environment. Under IFRS 4, the Group does not currently discount future cash flows, except in respect of PPOs, which are discounted at a rate that is consistent with the expected return backing these long-term liabilities.

Risk adjustment

Source of estimation uncertainty

A risk adjustment for non-financial risk will be determined to reflect the compensation that the Group would require for bearing non-financial risk and its degree of risk aversion. It will be determined at Group level and allocated to groups of contracts based on the size of their reserves. The risk adjustment for non-financial risk will be determined using a confidence level technique.

The Group will estimate the probability distribution of the expected present value of the future cash flows from the contracts at each reporting date and calculate the risk adjustment for non-financial risk as the excess of the value at risk at the target confidence level over the expected present value of the future cash flows allowing for the associated risks over all future years. The target confidence level will be at the 75th percentile for liabilities for incurred claims. The risk adjustment is derived using the reserve risk distribution calculated in the Internal Economic Capital Model and consequently, is subject to model and parameter uncertainty.

1.4 Accounting developments continued

(d) IFRS 9 – Significant accounting policies

IFRS 9 'Financial Instruments' addresses the classification, measurement, recognition and derecognition of financial assets and financial liabilities, introduces new rules for hedge accounting and a new impairment model for financial assets.

The Group will apply the new rules retrospectively from 1 January 2023 and comparatives for 2022 will be restated. The Group has reviewed its financial assets and liabilities and is expecting the following impact from the adoption of the new standard on 1 January 2023.

The Group's debt instruments of £4,084.6 million, that are currently classified as AFS under IAS 39 'Financial Instruments: Recognition and Measurement', as at 1 January 2022 (the opening date of the comparative reporting period) will satisfy the conditions for classification as 'held to collect and sell' under IFRS 9 to be measured at fair value through other comprehensive income ("**FVOCI**"). However, the Group will apply the IFRS 9 option to designate debt instruments, that would otherwise be categorised as FVOCI, as FVTPL to reduce the accounting mismatch that would arise from measuring debt instruments at FVOCI and insurance liabilities at FVTPL and recognising insurance finance income or expense in profit or loss. The AFS reserve of £7.5 million will be transferred to retained earnings on 1 January 2022.

There are no other reclassifications as a result of applying IFRS 9 as:

- assets currently classified as HTM and loans and receivables satisfy the IFRS 9 condition to be classified as 'held to collect' and measured at amortised cost as they are debt instruments with contractual terms that give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding and sales are infrequent or insignificant;
- derivatives will continue to be measured at FVTPL;
- equity investments will continue to be valued at either FVOCI when designated as such at initial recognition or FVTPL; and
- financial liabilities will continue to be measured at amortised cost.

The Group's current fair value designated hedge relationships will no longer be required. The Group will continue to have a small number of immaterial designated cash flow hedges; the Group will apply the IFRS 9 hedging requirements to these cash flow hedges.

The new impairment model requires the recognition of impairment provisions based on expected credit losses ("**ECL**") rather than incurred credit losses as is the case under IAS 39. The Group has established a default probability model for its debt securities held at amortised cost and loans & receivables. As the majority of the Group's debt securities will be held at FVTPL, for which no ECL calculations are required, ECL provisions are expected to be in the region of £2.9 million on 1 January 2023.

ECLs for other receivables will be based on a probability matrix and are expected to be similar to the level of existing bad debt provisions.

(e) IFRS 9 – accounting judgements and sources of estimation uncertainty

The critical estimates and judgement disclosure for impairment of financial assets will be updated for ECL calculations. The key areas of estimation relate to:

- determining when there has been a significant increase in credit risk since initial recognition;
- inputs and assumptions used in preparing a range of unbiased and probability-weighted scenarios; and
- weightings to be applied to these different scenarios.

As the majority of financial instruments of the Group are held at FVTPL, with fair value movements included in the income statement immediately, the ECL provision is not expected to be material.

2. Critical accounting judgements and key sources of estimation uncertainty

Full details of critical accounting judgements and key sources of estimation uncertainty used in applying the Group's accounting policies are outlined on pages 190 to 191 of the Annual Report & Accounts 2021. There have been no significant changes to the principles or assumptions of these critical accounting judgements and key sources of estimation uncertainty in the period ended 31 December 2022 except as described in note 2.3 in respect of the discount rate applied to PPOs. However, in the light of the uncertain economic environment, an update is provided below.

2.1. Impairment provisions – financial assets

The Group's financial assets are classified as AFS or held-to-maturity ("**HTM**") debt securities, FVTPL equity or loans and receivables. Excluding those assets held at FVTPL, the Group makes a judgement that financial assets are impaired when there is objective evidence that an event or events have occurred since initial recognition that have adversely affected the amount or timing of future cash flows from the asset. The determination of which events could have adversely affected the amount or timing of future cash flows from the asset requires judgement. In making this judgement, the Group evaluates, among other factors: the normal price volatility of the financial asset; the financial health of the investee; industry and sector performance; changes in technology or operational and financing cash flow; and whether there has been a significant or prolonged decline in the fair value of the asset below its cost. Impairment may be appropriate when there is evidence of deterioration in these factors.

2. Critical accounting judgements and key sources of estimation uncertainty continued

The majority of the Group's financial assets are classified as AFS debt securities (31 December 2022: £3,147.5 million; 31 December 2021: £4,084.6 million). Impairment losses and exchange differences arising from translating the amortised cost of foreign currency monetary AFS financial assets are recognised in the income statement. Other changes in fair value are recognised in a separate component of equity. No impairments have been recognised in the AFS portfolio. Had all the declines in AFS debt securities asset values met the criteria above at 31 December 2022, the Group would have suffered a loss of £262.9 million (2021: £24.8 million), being the transfer of the total AFS reserve for unrealised losses to the income statement. However, these movements represent mark-to-market movements and, as there was no objective evidence of any loss events that could affect future cash flows, no impairments have been recorded.

The Group has a small portfolio of investments classified as HTM (31 December 2022: £98.2 million; 31 December 2021: £91.2 million). These assets are measured at amortised cost and there have been no impairment losses (2021: £nil).

The Group has a portfolio of investments classified as loans and receivables, primarily comprising infrastructure debt and commercial real estate loans (total 31 December 2022: £439.2 million; 31 December 2021: £451.6 million). There was an impairment of £1.8 million within the loans and receivables portfolio in the year ended 31 December 2022 (2021: £2.1 million).

2.2. Fair value of investment properties

The Group holds a portfolio of investment properties, with a fair value at 31 December 2022 of £278.5 million (2021: £317.0 million). Where quoted market prices are not available, valuation techniques are used to value these properties. The fair value was determined using a methodology based on recent market transactions for similar properties, which have been adjusted for the specific characteristics of each property within the portfolio. The valuation in the financial statements is based on valuations by independent registered valuers and the techniques used include some unobservable inputs. The valuations used for investment properties are classified in the level 3 category of the fair value hierarchy (see note 22).

2.3. General insurance: outstanding claims provisions and related reinsurance recoveries

General insurance claims provisions are £3,654.3 million at 31 December 2022 (31 December 2021: £3,680.5 million) and reinsurance recoverables are £1,046.1 million at 31 December 2022 (31 December 2021: £1,132.1 million). The Group's reserves are exposed to the risk of changes in claims development patterns and claims inflation.

The Group settles some large bodily injury claims as PPOs rather than lump sum payments. The Group has estimated the likelihood of large bodily injury claims settling as PPOs. Anticipated PPOs consist of both existing large loss case reserves including allowances for development and claims yet to be reported to the Group. Reinsurance is applied at claim level and the net cash flows are discounted for the time value of money. The discount rate is consistent with the expected return on the assets backing these long-term liabilities. In 2022, the Group reviewed the estimates used to discount PPOs. Given the significant changes both in the current economic environment and the longer term outlook, the Group changed from flat rate inflation and discounting assumption to a yield curve approach, allowing for an increase in short-term inflation and higher long-term real returns. This resulted overall in the application of a real discount rate of 0.9% (2021: 0.0%), the combination of cash flow weighted inflation and discounting of 4.2% and 5.1% respectively, the latter driven by an expected increase in the long-term yield of the assets backing PPO liabilities.

Higher claims inflation remains a risk, given the continuing high level of consumer prices and wage inflation. In 2022, the CPI was at its highest level for the past decade and is not expected to normalise until 2024. Pressure is likely to remain strong on wages, with potential implications for the cost of care. Global supply chain issues remain problematic, resulting in a risk of price increases for products and components in short supply. A range of general and specific scenarios for excess inflation have been considered in the reserving process. The percentages applied range from 2% to 5% and for future periods of up to 5 years, depending on the class of business and claim type and allowing for the level of inflation included in the best estimate. The Group has observed a slow-down in the processing of recoveries and liabilities with third party insurers which increases the estimation risk of these amounts. A range of data types and methods are used with historical comparators to assess the underlying position separate from the timing effects to mitigate the uncertainty.

Changes in the climate can impact both frequency and severity of losses, particularly for wind storm and flood events. This is taken into account in the planning process, pricing and through our capital model; the impact on reserves is only seen when major loss events occur.

Changes in claims frequency present greater uncertainty for the unearned part of the business, whereas uncertainty over the level of claims severity has a greater impact on both the earned and unearned claims reserves. Claims severity risk is particularly acute with respect to care costs for large bodily injury claims as well as input costs and replacement costs for damage claims, in particular increased second-hand car costs in Motor. The sensitivity analysis in the Chief Financial Officer Review looks at a 200 basis point change in the claims inflation assumed in the actuarial best estimate over the next two years and therefore continues to remain relevant and is within the Group's booked reserve margin. The risk of material adjustments to the Group's estimates which could affect the carrying value in 2023 is highest in relation to long tail classes where inflation has been less evident to date. The Group therefore reserves for the risk of excess inflation on these classes within the management margin.

There have been no other significant changes to the principles or assumptions of these critical accounting judgements and key sources of estimation uncertainty for the year ended 31 December 2022.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

3. Segmental analysis

The table below analyses the Group's revenue and results by reportable segment for the year ended 31 December 2022.

	Motor £m	Home £m	Rescue and other personal lines ¹ £m	Commercial £m	Total Group - ongoing operations ¹ £m	Run-off partnerships ¹ £m	Total Group £m
Gross written premium	1,432.7	518.1	269.7	749.3	2,969.8	124.4	3,094.2
Gross earned premium	1,489.9	543.7	275.1	700.7	3,009.4	122.8	3,132.2
Reinsurance premium	(77.3)	(26.4)	(2.3)	(59.0)	(165.0)	(0.7)	(165.7)
Net earned premium	1,412.6	517.3	272.8	641.7	2,844.4	122.1	2,966.5
Investment return	28.9	9.9	2.5	9.7	51.0	0.6	51.6
Instalment income	64.7	16.5	2.7	8.5	92.4	—	92.4
Other operating income	36.2	0.5	15.6	3.0	55.3	—	55.3
Total income	1,542.4	544.2	293.6	662.9	3,043.1	122.7	3,165.8
Insurance claims	(1,197.6)	(417.3)	(147.5)	(345.1)	(2,107.5)	(110.5)	(2,218.0)
Insurance claims (payable to)/ recoverable from reinsurers	(19.8)	2.6	0.3	0.2	(16.7)	0.1	(16.6)
Net insurance claims	(1,217.4)	(414.7)	(147.2)	(344.9)	(2,124.2)	(110.4)	(2,234.6)
Of which:							
Current-year attritional	1,283.8	315.2	148.0	368.7	2,115.7	132.8	2,248.5
Prior-year reserve releases	(66.4)	(19.6)	(0.8)	(54.0)	(140.8)	(22.4)	(163.2)
Major weather events	n/a	119.1	n/a	30.2	149.3	n/a	149.3
Commission expenses	(47.4)	(26.3)	(10.7)	(124.5)	(208.9)	(2.2)	(211.1)
Operating expenses before restructuring and one-off costs	(354.8)	(111.9)	(76.0)	(135.2)	(677.9)	(21.6)	(699.5)
Total expenses	(402.2)	(138.2)	(86.7)	(259.7)	(886.8)	(23.8)	(910.6)
Operating (loss)/profit	(77.2)	(8.7)	59.7	58.3	32.1	(11.5)	20.6
Restructuring and one-off costs ²							(45.3)
Finance costs							(20.4)
Loss before tax							(45.1)
Underwriting (loss)/profit	(207.0)	(35.6)	38.9	37.1	(166.6)		(178.7)
Loss ratio	86.2%	80.2%	54.0%	53.7%	74.7%		75.3%
Of which:							
Current-year attritional	90.9%	60.9%	54.3%	57.5%	74.4%		75.8%
Prior-year reserve releases	(4.7%)	(3.8%)	(0.3%)	(8.4%)	(5.0%)		(5.5%)
Major weather events	n/a	23.1%	n/a	4.6%	5.3%		5.0%
Commission ratio	3.4%	5.1%	3.9%	19.4%	7.3%		7.1%
Expense ratio	25.1%	21.6%	27.9%	21.1%	23.8%		23.6%
Combined operating ratio	114.7%	106.9%	85.8%	94.2%	105.8%		106.0%
Current-year combined operating ratio	119.4%	110.7%	86.1%	102.6%	110.8%		111.5%

The table below analyses the Group's assets and liabilities by reportable segment for the year ended 31 December 2022³.

	Motor £m	Home £m	Rescue and other personal lines ¹ £m	Commercial £m	Total Group - ongoing operations ¹ £m	Run-off partnerships ¹ £m	Total Group £m
Goodwill	130.4	45.8	28.7	10.1	215.0	—	215.0
Assets held for sale	27.7	4.8	0.6	7.5	40.6	0.3	40.9
Other segment assets	5,517.4	931.8	150.7	1,434.1	8,034.0	64.7	8,098.7
Segment liabilities	(4,119.4)	(705.4)	(91.5)	(1,106.8)	(6,023.1)	(51.0)	(6,074.1)
Segment net assets	1,556.1	277.0	88.5	344.9	2,266.5	14.0	2,280.5

Notes:

1. Ongoing operations and run-off partnerships – See glossary on pages 56 to 58 for definitions and appendix A – Alternative performance measures on pages 60 to 63 for reconciliation to financial statement line items.
2. See glossary on page 57 for definitions.
3. This segmental analysis is prepared using a combination of asset and liability balances directly attributable to each operating segment and an apportionment of assets and liabilities managed at a Group-wide level. This does not represent the Group's view of the capital requirements for its operating segments.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

3. Segmental analysis continued

The table below analyses the Group's revenue and results by reportable segment for the year ended 31 December 2021.

	Motor £m	Home £m	Rescue and other personal lines ¹ £m	Commercial £m	Total Group - ongoing operations ¹ £m	Run-off partnerships ¹ £m	Total Group £m
Gross written premium	1,560.8	577.8	281.1	653.0	3,072.7	98.9	3,171.6
Gross earned premium	1,597.8	579.8	274.8	617.9	3,070.3	97.7	3,168.0
Reinsurance premium	(124.5)	(26.4)	(2.5)	(56.7)	(210.1)	(0.5)	(210.6)
Net earned premium	1,473.3	553.4	272.3	561.2	2,860.2	97.2	2,957.4
Investment return	99.8	12.5	2.9	30.3	145.5	0.8	146.3
Instalment income	69.4	18.3	3.0	6.6	97.3	—	97.3
Other operating income	33.9	1.0	9.6	2.1	46.6	0.1	46.7
Total income	1,676.4	585.2	287.8	600.2	3,149.6	98.1	3,247.7
Insurance claims	(1,086.8)	(287.7)	(135.6)	(363.6)	(1,873.7)	(41.6)	(1,915.3)
Insurance claims recoverable from/ (payable to) reinsurers	139.8	7.3	—	57.6	204.7	(8.1)	196.6
Net insurance claims	(947.0)	(280.4)	(135.6)	(306.0)	(1,669.0)	(49.7)	(1,718.7)
Of which:							
Current-year attritional	1,074.1	307.9	144.4	348.2	1,874.6	64.7	1,939.3
Prior-year reserve releases	(127.1)	(45.8)	(8.8)	(61.4)	(243.1)	(15.0)	(258.1)
Major weather events	n/a	18.3	n/a	19.2	37.5	n/a	37.5
Commission expenses	(48.2)	(38.1)	(9.7)	(112.3)	(208.3)	(32.6)	(240.9)
Operating expenses before restructuring and one-off costs	(366.4)	(124.9)	(69.2)	(121.5)	(682.0)	(24.3)	(706.3)
Total expenses	(414.6)	(163.0)	(78.9)	(233.8)	(890.3)	(56.9)	(947.2)
Operating profit	314.8	141.8	73.3	60.4	590.3	(8.5)	581.8
Restructuring and one-off costs ²							(101.5)
Finance costs							(34.3)
Profit before tax							446.0
Underwriting profit	111.7	110.0	57.8	21.4	300.9		291.5
Loss ratio	64.3%	50.7%	49.9%	54.5%	58.4%		58.1%
Of which:							
Current-year attritional	72.9%	55.7%	53.1%	62.0%	65.6%		65.5%
Prior-year reserve releases	(8.6%)	(8.3%)	(3.2%)	(10.9%)	(8.5%)		(8.7%)
Major weather events	n/a	3.3%	n/a	3.4%	1.3%		1.3%
Commission ratio	3.3%	6.9%	3.6%	20.0%	7.3%		8.1%
Expense ratio	24.8%	22.5%	25.4%	21.7%	23.8%		23.9%
Combined operating ratio	92.4%	80.1%	78.9%	96.2%	89.5%		90.1%
Current-year combined operating ratio	101.0%	88.4%	82.1%	107.1%	98.0%		98.8%

The table below analyses the Group's assets and liabilities by reportable segment for the year ended 31 December 2021³.

	Motor £m	Home £m	Rescue and other personal lines ¹ £m	Commercial £m	Total Group - ongoing operations ¹ £m	Run-off partnerships ¹ £m	Total Group £m
Goodwill	130.4	45.8	28.7	10.1	215.0	—	215.0
Assets held for sale	29.2	3.5	0.6	7.4	40.7	0.5	41.2
Other segment assets	6,467.2	750.1	152.2	1,566.7	8,936.2	116.2	9,052.4
Segment liabilities	(4,551.2)	(550.3)	(92.5)	(1,143.9)	(6,337.9)	(74.0)	(6,411.9)
Segment net assets	2,075.6	249.1	89.0	440.3	2,854.0	42.7	2,896.7

Notes:

1. Ongoing operations and run-off partnerships – See glossary on pages 56 to 58 for definitions and appendix A – Alternative performance measures on pages 60 to 63 for reconciliation to financial statement line items. Run-off partnerships was previously included in Rescue and other personal lines segment and the comparative data for year ended 31 December 2021 has been re-presented accordingly.
2. See glossary on page 57 for definitions.
3. This segmental analysis is prepared using a combination of asset and liability balances directly attributable to each operating segment and an apportionment of assets and liabilities managed at a Group-wide level. This does not represent the Group's view of the capital requirements for its operating segments.

4. Net earned premium

	2022	2021
	£m	£m
Gross earned premium:		
Gross written premium	3,094.2	3,171.6
Movement in unearned premium reserve	38.0	(3.6)
	3,132.2	3,168.0
Reinsurance premium paid and payable:		
Premium payable	(141.6)	(186.4)
Movement in reinsurance unearned premium reserve	(24.1)	(24.2)
	(165.7)	(210.6)
Total	2,966.5	2,957.4

5. Investment return

	2022	2021
	£m	£m
Investment income:		
Interest income from:		
Debt securities	78.7	90.9
Cash and cash equivalents	14.0	0.2
Infrastructure debt	7.9	4.4
Commercial real estate loans	8.8	6.0
Interest income	109.4	101.5
Rental income from investment property	15.6	14.5
	125.0	116.0
Net realised (losses)/gains:		
AFS debt securities	(24.9)	7.9
Hedging	(31.0)	(5.2)
Investment property	–	0.2
	(55.9)	2.9
Net unrealised (losses)/gains:		
Impairment of loans and receivables	(1.8)	(2.1)
Hedging	25.0	(8.1)
Investment property	(39.1)	37.6
Equity investments held at FVTPL	(1.6)	–
	(17.5)	27.4
Total	51.6	146.3

Total investment return decreased by £94.7 million to £51.6 million (2021: £146.3 million) primarily driven by realised and unrealised losses resulting from write downs in fair value adjustments of commercial property (£39.1 million) and £24.9 million of realised losses from disposals of Group debt security holdings, predominantly relating to actions taken to reduce the Group's longer duration US dollar credit holding.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

5. Investment return continued

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

	2022 £m	2021 £m
Foreign exchange hedging:		
Foreign exchange forward contracts ¹	(184.1)	(2.6)
Associated foreign exchange risk	188.0	1.9
Net gains/(losses) on foreign exchange hedging	3.9	(0.7)
Interest rate hedging:		
Gains/(losses) on interest rate swaps ¹ designated as hedge instruments	68.8	33.5
Change in fair value on designated hedge items	(78.5)	(35.1)
Interest rate hedging ineffectiveness	(9.7)	(1.6)
Undesignated interest rate hedging losses	(0.2)	(11.0)
Net losses on interest rate hedging	(9.9)	(12.6)
Total hedging losses	(6.0)	(13.3)

Note:

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

The Group holds fixed rate USD and EUR denominated bonds whose fair value is exposed to movements in interest rates. In order to economically hedge the interest rate risk of these bonds the Group enters into hedges paying a fixed rate and receiving floating interest rate swaps, which are subsequently designated as hedging instruments in a fair value hedge.

At 31 December 2022 the total USD and EUR denominated bonds was £916.4 million (2021: £1,574.2 million). The notional exposure of the interest rate swaps at 31 December 2022 was an asset of £240.4 million and a liability of £107.6 million (2021: asset of £901.0 million and a liability of £9.1 million). The hedged risk is the change in the fair value of the bonds which is attributable to changes in the SOFR and EURIBOR curves.

6. Other operating income

	2022 £m	2021 £m
Revenue from vehicle recovery and repair services	24.2	19.7
Vehicle replacement referral income	14.6	13.1
Legal services income	4.9	7.2
Other income ¹	11.6	6.7
Total	55.3	46.7

Note:

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

7. Net insurance claims

	Gross 2022 £m	Reinsurance 2022 £m	Net 2022 £m	Gross 2021 £m	Reinsurance 2021 £m	Net 2021 £m
Current accident year claims paid	1,355.3	(0.2)	1,355.1	1,058.6	(1.1)	1,057.5
Prior accident years claims paid	888.9	(69.2)	819.7	793.2	(88.7)	704.5
Movement in insurance liabilities	(26.2)	86.0	59.8	63.5	(106.8)	(43.3)
Total	2,218.0	16.6	2,234.6	1,915.3	(196.6)	1,718.7

Claims handling expenses for the year ended 31 December 2022 of £188.9 million (2021: £188.4 million) have been included in the claims figures above.

8. Commission expenses

	2022 £m	2021 £m
Commission expenses	207.5	201.2
Expenses incurred under profit participations	3.6	39.7
Total	211.1	240.9

9. Operating expenses

	2022 £m	2021 £m
Staff costs ¹	246.8	268.8
IT and other operating expenses ^{1,2}	180.1	157.0
Marketing	93.5	112.0
Insurance levies	93.4	89.0
Depreciation, amortisation and impairment of intangible and fixed assets ³	131.0	97.1
Loss on termination of property lease ⁴	–	83.9
Total other operating expenses (including restructuring and one-off costs)	744.8	807.8
Of which restructuring and one-off costs ^{4,5}	45.3	101.5
Total excluding restructuring and one-off costs	699.5	706.3

Notes:

- Staff costs and other operating expenses attributable to claims handling activities are allocated to the cost of insurance claims.
- IT and other operating expenses include professional fees and property costs.
- Includes right-of-use ("ROU") assets and property, plant and equipment. For the year ended 31 December 2022, there were impairment charges of £16.0 million which relate solely to impairment of intangible assets (2021: £2.6 million of which, £2.1 million relates to impairment of intangible assets and £0.5 million relates to ROU property assets).
- In 2021, U K Insurance Limited signed a contract in relation to its Bromley site to surrender the current lease and DL Insurance Services Limited signed a contract to purchase the head lease. The loss on termination of property lease, related to the Bromley site was allocated to restructuring and one-off costs. The value of the fixed asset capitalised was £19.8 million.
- Restructuring and one-off costs of £45.3 million (2021: £101.5 million) are included as follows: staff costs of £3.1 million (2021: £7.8 million), other operating expenses of £26.9 million (2021: £9.3 million), impairment charges of £15.2 million (2021: £nil) and depreciation of £nil (2021: £0.5 million). Restructuring and one-off costs primarily relate to the Group's decision to exit Travel packaged bank account partnership business and the continued reduction in the number of head office sites. It is expected that the Group will incur £2.0 million of additional restructuring and one-off costs in 2023 in relation to head office sites.

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

	At 31 December		Average for the year	
	2022	2021	2022	2021
Insurance operations	6,523	6,976	6,828	7,502
Repair centre operations	1,508	1,408	1,433	1,432
Support	1,356	1,402	1,407	1,382
Total	9,387	9,786	9,668	10,316

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

	2022 £m	2021 £m
Wages and salaries	391.6	392.8
Social security costs	43.9	42.6
Pension costs	26.5	26.1
Share-based payments	8.2	18.4
Total	470.2	479.9

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

10. Finance costs

	2022	2021
	£m	£m
Interest expense on subordinated liabilities	17.8	33.6
Net interest received on interest rate swap ¹	(2.2)	(5.3)
Unrealised losses on interest rate swap ¹	2.4	5.8
Amortisation of arrangement costs, discount on issue and fair value hedging adjustment of subordinated liabilities	(0.8)	(3.0)
Interest expense on lease liabilities	3.1	3.2
Other interest expense	0.1	—
Total	20.4	34.3

Note:

- As described in note 19, on 27 April 2012 the Group issued subordinated guaranteed dated Tier 2 notes with a nominal value of £500 million at a fixed rate of 9.25%. On the same date, the Group also entered into a 10-year interest rate swap to exchange the fixed rate of interest on the notes for a floating rate. This was treated as a designated hedging instrument. On 8 December 2017, the Group redeemed £250 million nominal value of the notes and the hedging instrument was redesignated accordingly. On 31 July 2020, the Group identified that the hedge no longer met the criteria of hedge effectiveness under IAS 39 and, under the rules of the standard, the accumulated hedging adjustment was amortised to the income statement from the date of the last successful hedge effectiveness test over the remaining life of the subordinated debt using an effective interest rate calculation. The remaining notes, with a nominal value of £250 million, were redeemed in full on 27 April 2022.

11. Dividends and appropriations

	2022	2021
	£m	£m
Amounts recognised as distributions to equity holders in the period:		
2022 interim dividend of 7.6 pence per share paid on 9 September 2022	99.0	—
2021 final dividend of 15.1 pence per share paid on 17 May 2022	198.9	—
2021 interim dividend of 7.6 pence per share paid on 3 September 2021	—	101.9
2020 final dividend of 14.7 pence per share paid on 20 May 2021	—	198.9
	297.9	300.8
Coupon payments in respect of Tier 1 notes ¹	16.6	16.6
	314.5	317.4
Proposed dividends:		
2021 final dividend of 15.1 pence per share	—	199.4

Note:

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

The trustees of the employee share trusts waived their entitlement to dividends on shares held to meet obligations arising on the Long-Term Incentive Plan, Deferred Annual Incentive Plan and Restricted Share Plan awards, which reduced the total dividends paid for the year ended 31 December 2022 by £2.0 million (2021: £1.7 million).

12. (Loss)/earnings per share

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

Basic

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

Diluted

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

12. (Loss)/earnings per share continued

	2022 £m	2021 £m
(Loss)/earnings attributable to the owners of the Company	(39.5)	343.7
Coupon payments in respect of Tier 1 notes	(16.6)	(16.6)
(Loss)/profit for the calculation of earnings per share	(56.1)	327.1
Weighted average number of Ordinary Shares for the purpose of basic earnings per share (millions)	1,304.3	1,335.8
Effect of dilutive potential of share options and contingently issuable shares (millions)	15.0	20.8
Weighted average number of Ordinary Shares for the purpose of diluted earnings per share (millions)	1,319.3	1,356.6
Basic (loss)/earnings per share (pence)	(4.3)	24.5
Diluted (loss)/earnings per share (pence)	(4.3)	24.1

On 8 March 2022, the Group announced that the Board had approved a share buyback programme of Ordinary Shares for an aggregate purchase price of up to £100 million, for which an initial tranche of up to £50 million was completed in H1 2022. The Group repurchased 19,324,855 Ordinary Shares for an aggregate consideration of £50.1 million as reflected in retained earnings (including related transaction costs). On 18 July 2022, the Group announced in its H1 2022 trading update, that the Board had decided not to launch the second £50 million tranche of the £100 million share buyback programme announced earlier in the year.

On 8 March 2021, the Group announced a share buyback programme of Ordinary Shares for an aggregate purchase price of up to £100 million, which was completed on 15 November 2021 in accordance with its terms. Across the programme, the Group repurchased and cancelled 33,838,593 ordinary shares for an aggregate consideration of £101.0 million (including related transaction costs).

After each share buyback, the shares were subsequently cancelled giving rise to a capital redemption reserve of an equivalent amount to their nominal value as required by the Companies Act 2006.

13. Net asset value per share and return on equity

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

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

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

	2022 £m	2021 £m
Net assets	1,934.0	2,550.2
Goodwill and other intangible assets ¹	(822.2)	(822.5)
Tangible net assets	1,111.8	1,727.7
Number of Ordinary Shares (millions)	1,311.4	1,330.7
Shares held by employee trusts (millions)	(13.2)	(13.4)
Closing number of Ordinary Shares (millions)	1,298.2	1,317.3
Net asset value per share (pence)	149.0	193.6
Tangible net asset value per share (pence)	85.6	131.2

Note:

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

Return on equity

The table below details the calculation of return on equity.

	2022 £m	2021 £m
(Loss)/earnings attributable to the owners of the Company	(39.5)	343.7
Coupon payments in respect of Tier 1 notes	(16.6)	(16.6)
(Loss)/profit for the calculation of return on equity	(56.1)	327.1
Opening shareholders' equity	2,550.2	2,699.7
Closing shareholders' equity	1,934.0	2,550.2
Average shareholders' equity	2,242.1	2,625.0
Return on equity	(2.5%)	12.5%

14. Reinsurance assets

	2022 £m	2021 £m
Reinsurers' share of general insurance liabilities	1,078.5	1,169.6
Impairment provision ¹	(32.4)	(37.5)
Total excluding reinsurers' unearned premium reserves	1,046.1	1,132.1
Reinsurers' unearned premium reserve	55.6	79.7
Total	1,101.7	1,211.8

Note:

1. Impairment provision relates to reinsurance debtors, allowing for the risk that reinsurance assets may not be collected, or where one or more reinsurers' credit rating has been significantly downgraded and it may have difficulty in meeting its obligations. Of this amount a total of £0.1 million is past due (2021: £6.7 million).

15. Financial investments

	2022 £m	2021 £m
AFS debt securities		
Corporate	2,605.1	4,006.9
Supranational	25.2	14.0
Local government	5.9	28.1
Sovereign	511.3	35.6
Total	3,147.5	4,084.6
HTM debt securities		
Corporate	98.2	91.2
Total debt securities	3,245.7	4,175.8
Total debt securities		
Fixed interest rate ¹	3,232.1	4,158.3
Floating interest rate	13.6	17.5
Total	3,245.7	4,175.8
Loans and receivables		
Infrastructure debt	238.2	250.8
Commercial real estate loans	199.1	200.8
Other loans	1.9	—
Total loans and receivables	439.2	451.6
Equity investments²	13.6	6.2
Total	3,698.5	4,633.6

Notes:

1. The Group swaps a fixed interest rate for a floating rate of interest on its US dollar and Euro corporate debt securities by entering into interest rate derivatives. The hedged amount at 31 December 2022 was £401.8 million (31 December 2021: £1,005.6 million).
2. Equity investments consist of quoted shares and insurtech-focused equity funds. The insurtech-focused equity funds are valued based on external valuation reports received from a third-party fund manager.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

16. Cash and cash equivalents and borrowings

	2022	2021
	£m	£m
Cash at bank and in hand	124.8	162.8
Short term deposits with credit institutions ¹	878.8	792.9
Cash and cash equivalents	1,003.6	955.7
Bank overdrafts ²	(65.2)	(59.2)
Cash and bank overdrafts³	938.4	896.5

Notes:

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

The effective interest rate on short-term deposits with credit institutions for the year ended 31 December 2022 was 1.46% (2021: 0.16%) and average maturity was 10 days (2021: 10 days).

17. Share capital

Issued and fully paid: equity shares	2022			2021		
	Number of shares	Share capital	Transfer to capital redemption reserve ⁴	Number of shares	Share capital	Transfer to capital redemption reserve ⁴
	millions	£m	£m	millions	£m	£m
Ordinary Shares of 10 10/11 pence each ¹						
At 1 January	1,330.7	145.2	4.8	1,364.6	148.9	1.1
Shares cancelled following buyback ^{2,3,4}	(19.3)	(2.1)	2.1	(33.9)	(3.7)	3.7
At 31 December	1,311.4	143.1	6.9	1,330.7	145.2	4.8

Notes:

1. The shares have full voting, dividend and capital distribution rights (including on wind-up) attached to them; these do not confer any rights of redemption.
2. On 8 March 2022, the Group announced that the Board had approved a share buyback programme of Ordinary Shares for an aggregate purchase price of up to £100 million, for which an initial tranche of up to £50 million was completed in H1 2022. The Group has repurchased 19,324,855 Ordinary Shares for an aggregate consideration of £50.1 million as reflected in retained earnings (including related transaction costs). On 18 July 2022, the Group announced in its H1 2022 trading update, that the Board had decided not to launch the second £50 million tranche of the £100 million share buyback programme announced earlier in the year.
3. On 8 March 2021, the Group announced a share buyback programme of Ordinary Shares for an aggregate purchase price of up to £100 million, which was completed on 15 November 2021 in accordance with its terms. Across the programme, the Group repurchased and cancelled 33,838,593 ordinary shares for an aggregate consideration of £101.0 million (including related transaction costs).
4. After each share buyback, the shares were subsequently cancelled giving rise to a capital redemption reserve of an equivalent amount to their nominal value as required by the Companies Act 2006.

Employee trust shares

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

At 31 December 2022, 13,214,811 Ordinary Shares (2021: 13,442,422 Ordinary Shares) were owned by the employee share trusts at a cost of £39.0 million (2021: £41.4 million). These Ordinary Shares are carried at cost and at 31 December 2022 had a market value of £29.2 million (2021: £37.5 million).

18. Tier 1 notes

	2022	2021
	£m	£m
Tier 1 notes	346.5	346.5

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

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

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

18. Tier 1 notes continued

The Group has the option to cancel the coupon payment. Cancellation becomes mandatory if the Solvency condition¹ is not met at the time of, or following, coupon payment; there is non-compliance with the SCR or the minimum capital requirement the Group has insufficient distributable reserves; or the relevant regulator requires the coupon payment to be cancelled.

Note:

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

19. Subordinated liabilities

	2022	2021
	£m	£m
£250 million 9.25% subordinated Tier 2 notes due 2042	–	255.2
£260 million 4.0% subordinated Tier 2 notes due 2032	258.6	258.4
Subordinated Tier 2 notes	258.6	513.6

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

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

£250 million 9.25% subordinated Tier 2 notes due 2042

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

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

During 2020, the Group identified that the hedge no longer met the criteria of hedge effectiveness under IAS 39 and, under the rules of the standard, the accumulated hedging adjustment was amortised to the income statement from the date of the last successful hedge effectiveness test over the remaining life of the subordinated debt using an effective interest rate calculation.

The remaining notes, with a nominal value of £250 million and accrued interest of £11.6 million, were redeemed in full on 27 April 2022 when the Group had its first option to repay. Associated transaction costs were £0.1 million. The interest rate swap hedging these notes expired on the same day.

£260 million 4.0% subordinated Tier 2 notes due 2032

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

20. Insurance liabilities

	2022	2021
	£m	£m
Insurance liabilities	3,654.3	3,680.5

Gross insurance liabilities

	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Accident year											
Estimate of ultimate gross claims costs:											
At end of accident year	2,184.0	2,094.5	2,118.1	2,157.7	2,217.3	2,300.1	2,110.4	1,847.3	1,955.8	2,294.1	
One year later	(117.6)	20.7	(30.0)	(86.7)	(116.2)	(62.3)	(67.2)	(116.8)	(52.5)		
Two years later	(153.0)	(38.4)	(143.5)	(53.3)	(103.1)	(52.0)	(56.1)	(34.4)			
Three years later	(21.0)	(144.9)	(62.4)	(82.8)	(42.4)	(9.5)	(14.0)				
Four years later	(102.1)	(50.2)	(22.9)	(46.1)	(21.0)	(15.4)					
Five years later	(50.8)	(51.6)	(22.0)	(16.7)	(12.8)						
Six years later	(27.4)	(33.6)	(9.0)	(27.0)							
Seven years later	(14.0)	(6.5)	(9.3)								
Eight years later	(0.3)	(17.4)									
Nine years later	(3.0)										
Current estimate of cumulative claims	1,694.8	1,772.6	1,819.0	1,845.1	1,921.8	2,160.9	1,973.1	1,696.1	1,903.3	2,294.1	
Cumulative payments to date	(1,686.7)	(1,715.3)	(1,732.9)	(1,772.1)	(1,799.4)	(1,913.3)	(1,669.7)	(1,326.3)	(1,351.3)	(1,208.7)	
Gross liability recognised in balance sheet	8.1	57.3	86.1	73.0	122.4	247.6	303.4	369.8	552.0	1,085.4	2,905.1
2012 and prior Claims handling provision											663.0
											86.2
Total											3,654.3

Net insurance liabilities

	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Accident year											
Estimate of ultimate net claims costs:											
At end of accident year	2,093.9	1,971.0	1,926.7	1,922.2	2,016.9	2,125.9	1,941.2	1,674.5	1,791.8	2,205.2	
One year later	(123.6)	(29.7)	(67.0)	(18.9)	(79.7)	(41.4)	(34.5)	(88.1)	(35.0)		
Two years later	(134.4)	(42.0)	(77.8)	(38.2)	(65.3)	(27.1)	(54.5)	(44.7)			
Three years later	(27.8)	(100.7)	(30.4)	(43.7)	(14.0)	(27.6)	(5.7)				
Four years later	(64.3)	(41.3)	(24.1)	(16.9)	(39.7)	(3.1)					
Five years later	(38.9)	(52.5)	(20.7)	(12.4)	(15.1)						
Six years later	(17.7)	(8.3)	(4.6)	(16.8)							
Seven years later	(10.6)	(8.0)	(7.4)								
Eight years later	0.4	(6.0)									
Nine years later	(2.7)										
Current estimate of cumulative claims	1,674.3	1,682.5	1,694.7	1,775.3	1,803.1	2,026.7	1,846.5	1,541.7	1,756.8	2,205.2	
Cumulative payments to date	(1,667.2)	(1,670.6)	(1,665.2)	(1,736.2)	(1,737.0)	(1,888.7)	(1,642.8)	(1,301.9)	(1,333.9)	(1,208.4)	
Net liability recognised in balance sheet	7.1	11.9	29.5	39.1	66.1	138.0	203.7	239.8	422.9	996.8	2,154.9
2012 and prior Claims handling provision											367.1
											86.2
Total											2,608.2

20. Insurance liabilities continued

Movements in gross and net insurance liabilities

	Gross £m	Reinsurance £m	Net £m
Claims reported	2,762.0	(842.8)	1,919.2
Incurred but not reported	777.0	(182.5)	594.5
Claims handling provision	78.0	—	78.0
At 1 January 2021	3,617.0	(1,025.3)	2,591.7
Cash paid for claims settled in the year	(1,851.8)	89.8	(1,762.0)
Increase/(decrease) in liabilities:			
Arising from current-year claims	2,142.9	(166.1)	1,976.8
Arising from prior-year claims	(227.6)	(30.5)	(258.1)
At 31 December 2021	3,680.5	(1,132.1)	2,548.4
Claims reported	2,840.0	(885.2)	1,954.8
Incurred but not reported	761.8	(246.9)	514.9
Claims handling provision	78.7	—	78.7
At 31 December 2021	3,680.5	(1,132.1)	2,548.4
Cash paid for claims settled in the year	(2,244.2)	69.4	(2,174.8)
Increase/(decrease) in liabilities:			
Arising from current-year claims	2,486.8	(89.0)	2,397.8
Arising from prior-year claims	(268.8)	105.6	(163.2)
At 31 December 2022	3,654.3	(1,046.1)	2,608.2
Claims reported	2,941.0	(835.7)	2,105.3
Incurred but not reported	627.1	(210.4)	416.7
Claims handling provision	86.2	—	86.2
At 31 December 2022	3,654.3	(1,046.1)	2,608.2

Movement in prior-year net claims liabilities by operating segment

	2022 £m	2021 £m
Motor	(66.4)	(127.1)
Home	(19.6)	(45.8)
Rescue and other personal lines - ongoing operations	(0.8)	(8.8)
Commercial	(54.0)	(61.4)
Total Group - ongoing operations	(140.8)	(243.1)
Run-off partnerships	(22.4)	(15.0)
Total Group	(163.2)	(258.1)

21. Unearned premium reserve

Movement in unearned premium reserve

	Gross £m	Reinsurance £m	Net £m
At 1 January 2021	1,497.1	(103.9)	1,393.2
Written in the period	3,171.6	(186.4)	2,985.2
Earned in the period	(3,168.0)	210.6	(2,957.4)
At 31 December 2021	1,500.7	(79.7)	1,421.0
Written in the period	3,094.2	(141.6)	2,952.6
Earned in the period	(3,132.2)	165.7	(2,966.5)
At 31 December 2022	1,462.7	(55.6)	1,407.1

22. Fair value

Fair value hierarchy

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, regardless of whether that price is directly observable or estimated using another valuation technique.

For disclosure purposes, fair value measurements are classified as level 1, 2 or 3 based on the degree to which fair value is observable:

- Level 1 financial assets are measured in whole or in part by reference to published quotes in an active market. In an active market quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency and those prices represent actual and regularly occurring market transactions on an arm's-length basis.
- Level 2 financial assets and liabilities are measured using a valuation technique based on assumptions that are supported by prices from observable current market transactions. These include AFS debt security assets for which pricing is obtained via pricing services, but where prices have not been determined in an active market, or financial assets with fair values based on broker quotes or assets that are valued using the Group's own models whereby the majority of assumptions are market-observable. Derivatives are valued using broker quotes or appropriate valuation models. Model inputs include a range of factors which are deemed to be observable, including current market and contractual prices for underlying instruments, period to maturity, correlations, yield curves and volatility of underlying instruments. Level 2 also includes quoted equity investments that the Group holds for which prices are available however, the market transactions upon which those prices are based are not considered to be regularly occurring.
- Level 3 fair value measurements used for investment properties, HTM debt securities, infrastructure debt, commercial real estate loans, and unquoted equity investments are those derived from a valuation technique that includes inputs for the asset that are unobservable. HTM debt securities are private placed securities which do not trade on active markets, these are valued using discounted cash flow models designed to appropriately reflect the credit and illiquidity of these instruments. The key unobservable input elements from the discount rate used across private debt securities is the credit spread which is based on the credit quality of the assets and the illiquidity premium. Infrastructure debt and commercial real estate are loans which do not trade on active markets. Valuations are derived from external asset managers' credit assessment and pricing models. These aim to take into account movements in broader credit spreads and are aligned to varying degrees with external credit rating equivalents. Unlisted equity investments are comprised of investments in private equity funds, which are valued at the proportion of the Group's holding of the net asset value reported by the investment vehicle. These are based on several unobservable inputs including market multiples and cash flow forecasts.

Comparison of carrying value to fair value of financial instruments and assets where fair value is disclosed

		Carrying value	Level 1	Level 2	Level 3	Fair value
At 31 December 2022	Notes	£m	£m	£m	£m	£m
Assets held at fair value:						
Investment property		278.5	—	—	278.5	278.5
Derivative assets		31.3	—	31.3	—	31.3
AFS debt securities	15	3,147.5	511.2	2,636.3	—	3,147.5
Equity investments	15	13.6	—	0.3	13.3	13.6
Other financial assets:						
HTM debt securities	15	98.2	—	28.6	61.0	89.6
Infrastructure debt	15	238.2	—	—	235.7	235.7
Commercial real estate loans	15	199.1	—	—	198.1	198.1
Other Loans	15	1.9	—	—	1.9	1.9
Total		4,008.3	511.2	2,696.5	788.5	3,996.2
Liabilities held at fair value:						
Derivative liabilities		29.6	—	29.6	—	29.6
Other financial liabilities:						
Subordinated liabilities	19	258.6	—	204.9	—	204.9
Total		288.2	—	234.5	—	234.5

22. Fair value continued

		Carrying value	Level 1	Level 2	Level 3	Fair value
	Notes	£m	£m	£m	£m	£m
At 31 December 2021						
Assets held at fair value:						
Investment property		317.0	—	—	317.0	317.0
Derivative assets		35.9	—	35.9	—	35.9
AFS debt securities	15	4,084.6	35.6	4,049.0	—	4,084.6
Equity investments	15	6.2	—	—	6.2	6.2
Other financial assets:						
HTM debt securities	15	91.2	—	24.3	69.1	93.4
Infrastructure debt	15	250.8	—	—	257.8	257.8
Commercial real estate loans	15	200.8	—	—	198.3	198.3
Total		4,986.5	35.6	4,109.2	848.4	4,993.2
Liabilities held at fair value:						
Derivative liabilities		19.5	—	19.5	—	19.5
Other financial liabilities:						
Subordinated liabilities	19	513.6	—	543.7	—	543.7
Total		533.1	—	563.2	—	563.2

Differences arise between carrying value and fair value where the measurement basis of the asset or liability is not fair value (for example; assets and liabilities carried at amortised cost). Fair values of the following assets and liabilities approximate their carrying values:

- cash and cash equivalents;
- borrowings; and
- trade and other payables, including insurance payables.

The movements in assets held at fair value and classified as level 3 in the fair value hierarchy relate to investment property and unquoted equity investments. A summary of realised and unrealised gains or losses in relation to investment property at fair value are presented in note 5.

There were no changes in the categorisation of assets between levels 1, 2 and 3 for assets and liabilities held by the Group since 31 December 2021. During 2021, there was one HTM debt security with fair value of £10.7 million transferred from level 3 to level 2 due to market-observable valuation inputs.

The table below shows the unobservable inputs used by the Group in the fair value measurement of its investment property.

At 31 December 2022	Fair value £m	Valuation technique	Unobservable input	Range (weighted average)
Investment property	278.5 ¹	Income capitalisation	Equivalent yield	4.23% - 7.61% (average 5.62%)
			Estimated rental value per square foot	£6.50 - £32.92 (average £13.59)

Note:

1. The methodology of valuation reflects commercial property held within U K Insurance Limited.

The table below analyses the movement in assets carried at fair value classified as level 3 in the fair value hierarchy.

	Note	Investment property £m	Unquoted equity investments £m
At 1 January 2022			
Additions ¹		317.0	6.2
(Reduction)/increase in fair value in the period	5	(39.1)	0.3
Foreign exchange movement		—	(0.9)
Capitalised expenditure		0.6	—
At 31 December 2022		278.5	13.3

Note:

1. Additions to unquoted equity investments are initially recognised at fair value plus directly related transaction costs.

23. Related parties

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

Subject to the preceding sentence, there were no sales or purchases of products and services to or from related parties in the year ended 31 December 2022 (2021: £nil).

Full details of the Group's related party transactions for the year ended 31 December 2021 are included on page 238 of the Annual Report & Accounts 2021.

24. Post balance sheet events

On 26 January 2023, the Group announced that its principal underwriter, U K Insurance Limited, had entered into strategic reinsurance agreements, that together comprise a 3-year structured 10% quota share arrangement. The contracts incept with effect from 1 January 2023.

On 1 March 2023, the Group's principal underwriter, U K Insurance Limited, and service company, DL Insurance Services Limited, entered into arrangements relating to Motability Operations and the motor insurance needs of approximately 600,000 of its customers.

Corporate information

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

Statutory accounts information

The Annual Report & Accounts 2021 were signed on 8 March 2022 and were delivered to the Registrar of Companies following the Annual General Meeting held on 10 May 2022. The Annual Report & Accounts 2021 is available at: www.directlinegroup.co.uk/content/dam/dlg/corporate/images-and-documents/investors/results-and-reports/2021/HandoverPack_2021_ARA_web-ready.zip.downloadasset.zip

At the time of the publishing of the Preliminary Results for 2022 the Annual Report & Accounts 2022 had not been published. Once published, the Annual Report & Accounts 2022 will be available on the Group's website at www.directlinegroup.co.uk

GLOSSARY

Term	Definition and explanation
Actuarial best estimate ("ABE")	The probability-weighted average of all future claims and cost scenarios. It is calculated using historical data, actuarial methods and judgement. A best estimate of reserves will therefore normally include no margin for optimism or, conversely, caution.
Adjusted gross written premium	An amended gross written premium number that identifies the impact of a contractual change to Green Flag premium such that a portion of income that was previously included in gross written premium is now included in service fee income.
Adjusted solvency capital ratio	The ratio of Solvency II own funds to the solvency capital requirement, excludes the Tier 2 subordinated debt which was redeemed on 27 April 2022.
Assets under management ("AUM")	This represents all assets managed or administered by or on behalf of the Group, including those assets managed by third parties.
Capital	The funds invested in the Group, including funds invested by shareholders and Tier 1 notes. In addition, the subordinated liabilities in the Group's balance sheet is classified as Tier 2 capital for Solvency II purposes.
Claims frequency	The number of claims divided by the number of policies per year.
Claims handling provision (provision for losses and loss-adjustment expense)	Funds set aside by the Group to meet the estimated cost of settling claims and related expenses that the Group considers it will ultimately need to pay.
Combined operating ratio	The sum of the loss, commission and expense ratios. The ratio measures the amount of claims costs, commission and operating expenses, compared to net earned premium generated. A ratio of less than 100% indicates profitable underwriting. Normalised combined operating ratio adjusts loss and commission ratios for weather and changes to the Ogden discount rate. Current-year combined operating ratio is calculated using the combined operating ratio less movement in prior-year reserves. (See page 60 - Alternative Performance Measures.)
Commission ratio	The ratio of commission expense divided by net earned premium. (See page 60 - Alternative Performance Measures.)
Current-year attritional loss ratio	The loss ratio for the current accident year, excluding the movement of claims reserves relating to previous accident years and claims relating to major weather events. (See page 60 - Alternative Performance Measures.)
Expense ratio	The ratio of operating expenses divided by net earned premium. (See page 60 - Alternative Performance Measures.)
Fair value through profit or loss ("FVTPL")	A financial asset or liability where at each balance sheet date the asset or liability is remeasured to fair value and any movement in that fair value is taken directly to the income statement.
Finance costs	The cost of servicing the Group's external borrowings and including the interest on right-of-use assets.
Financial leverage ratio	Tier 1 notes and financial debt (subordinated Tier 2 notes) as a percentage of total capital employed.
Gross written premium	The total premiums from insurance contracts that were inception during the period.
Incurred but not reported ("IBNR")	Funds set aside to meet the cost of claims for accidents that have occurred but have not yet been reported to the Group. This includes an element of uplift on the value of claims reported.
In-force policies	The number of policies on a given date that are active and against which the Group will pay, following a valid insurance claim.
Insurance liabilities	This comprises insurance claims reserves and claims handling provision, which the Group maintains to meet current and future claims.
Investment income yield	The income earned from the investment portfolio, recognised through the income statement during the period (excluding unrealised and realised gains and losses, impairments and fair value adjustments) divided by the average AUM. The average AUM derives from the period's opening and closing balances for the total Group. (See page 60 - Alternative Performance Measures.)
Investment return	The investment return earned from the investment portfolio, including unrealised and realised gains and losses, impairments and fair value adjustments.
Investment return yield	The investment return divided by the average AUM. The average AUM derives from the period's opening and closing balances. (See page 60 - Alternative Performance Measures.)
Loss ratio	Net insurance claims divided by net earned premium. (See page 60 - Alternative Performance Measures.)
Management's best estimate ("MBE")	These reserves are based on management's best estimate, which includes a prudence margin that exceeds the internal ABE.

GLOSSARY CONTINUED

Term	Definition and explanation
Minimum capital requirement ("MCR")	The minimum amount of capital that an insurer needs to hold to cover its risks under the Solvency II regulatory framework. If an insurer's capital falls below the MCR then authorisation will be withdrawn by the regulator unless the insurer is able to meet the MCR within a short period of time.
Net asset value	The difference between the Group's total assets and total liabilities, calculated by subtracting total liabilities (including Tier 1 notes) from total assets.
Net earned premium	The element of gross earned premium less reinsurance premium ceded for the period where insurance cover has already been provided.
Net insurance claims	The cost of claims incurred in the period less any claims costs recovered under reinsurance contracts. It includes claims payments and movements in claims reserves.
Net insurance margin ("NIM")	This is a proposed IFRS 17 key performance indicator based on the ratio of an insurance service return divided by a view of net insurance contract revenue. The definition of an insurance service return is the sum of the net insurance contract revenues, net insurance contract claims, acquisition costs and operating expenses, compared to the net insurance contract revenues generated. We will provide definitions of these terms reconciled to the statutory basis in future disclosures.
Net investment income yield	This is calculated in the same way as investment income yield but includes the cost of hedging. (See page 60 - Alternative Performance Measures.)
Ogden discount rate	The discount rate set by the Lord Chancellor and used by courts to calculate lump sum awards in bodily injury cases.
Ongoing operations	The Group's ongoing operations include Motor, Home, Rescue and other personal lines and Commercial segments and excludes the run-off partnerships segment. Please also refer to run-off partnerships . The use of the term ongoing operations is not considered equivalent to continuing operations as defined under IFRS 5 'Non-current Assets Held for Sale and Discontinued Operations' and run-off partnerships does not meet the criteria of a discontinued operation and has not been accounted for as such. (See page 61 - Alternative Performance Measures.)
Operating expenses	These are the expenses relating to business activities excluding restructuring and one-off costs. (See page 61 - Alternative Performance Measures.)
Operating profit	The pre-tax profit that the Group's activities generate, including insurance and investment activity, but excluding finance costs, restructuring and one-off costs.
Periodic payment order ("PPO")	These are claims payments as awarded under the Courts Act 2003. PPOs are used to settle certain large personal injury claims. They generally provide a lump-sum award plus inflation-linked annual payments to claimants who require long-term care.
Reserves	Funds that have been set aside to meet outstanding insurance claims and IBNR.
Restructuring and one-off costs	Restructuring costs are costs incurred in respect of those business activities which have a material effect on the nature and focus of the Group's operations. One-off costs are costs that are non-recurring in nature.
Return on equity	This is calculated by dividing the (loss)/profit attributable to the owners of the Company after deduction of the Tier 1 coupon payments by average shareholders' equity for the period.
Return on tangible equity ("RoTE")	This is adjusted (loss)/profit after tax divided by the Group's average shareholders' equity less goodwill and other intangible assets. Profit after tax is adjusted to exclude restructuring and one-off costs and to include the Tier 1 coupon payments. It is stated after charging tax using the UK standard rate of 19%. (See page 61 - Alternative Performance Measures.)
Run-off partnerships	The Group has exited, or has initiated termination of three partnerships which will reduce its exposure to low margin packaged bank accounts so it may redeploy capital to higher return segments. The run-off partnerships relate to a Rescue partnership with NatWest Group that expired in December 2022 and Travel partnerships with NatWest Group and Nationwide Building Society which expire in 2024, where the Group has indicated to the partner that it will not be seeking to renew. The term run-off partnerships does not meet the criteria of a discontinued operation as defined under IFRS 5 'Non-current Assets Held for Sale and Discontinued Operations' and has not been accounted for as such.
Science-Based Targets ("SBT")	Science-Based Targets are a set of goals developed by a business to provide it with a clear route to reduce greenhouse gas emissions. An emissions reduction target is defined as "science-based" if it is developed in line with the scale of reductions required to curb a global temperature rise to well below 2°C above pre-industrial levels and ideally to limit to a 1.5°C rise.
Solvency capital ratio	The ratio of Solvency II own funds to the solvency capital requirement.
Solvency capital requirement ("SCR")	The SCR is the amount of capital the regulator requires an insurer to hold to meet the requirements under the Solvency II regulatory framework. The Group uses a partial internal model to determine the SCR.

GLOSSARY CONTINUED

Term	Definition and explanation
Tangible equity	This shows the equity excluding Tier 1 notes and intangible assets (for comparability with companies which have not acquired businesses or capitalised intangible assets). (See page 61 - Alternative Performance Measures.)
Tangible net assets per share	This shows the amount of tangible equity allocated to each ordinary share (for comparability with companies which have not acquired businesses or capitalised intangible assets). (See page 61 - Alternative Performance Measures.)
Underwriting result	This is the profit or loss from operational insurance activities, excluding investment return and other operating income. It is calculated as net earned premium less net insurance claims and total expenses, excluding restructuring and one-off costs.

Forward-looking statements disclaimer

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

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

- United Kingdom ("**UK**") domestic and global economic business conditions;
- the direct and indirect impacts and implications of the coronavirus Covid-19 pandemic on the economy, nationally and internationally, on the Group, its operations and prospects, and on the Group's customers and their behaviours and expectations;
- the Trade and Cooperation Agreement between the UK and the European Union ("**EU**") regarding the terms of the trading relationships between the UK and the EU and its implementation, and any subsequent trading and other relationship arrangements between the UK and the EU and their implementation;
- the terms of trading and other relationships between the UK and other countries following Brexit;
- the impact of the FCA's PPR regulations and of responses by insurers, customers and other third parties and of interpretations of such rules by any relevant regulatory authority;
- market-related risks such as fluctuations in interest rates, exchange rates and credit spreads, including those created or exacerbated by the war in Ukraine following the Russian invasion;
- the policies and actions and/or new principles, rules and/or regulations, of regulatory authorities and bodies, and of changes to, or changes to interpretations of, principles, rules and/or regulations (including changes made directly or indirectly as a result of Brexit or related to capital and solvency requirements or related to the Ogden discount rates or made in response to the Covid-19 pandemic and its impact on the economy and customers) and of changes to law and/or understandings of law and/or legal interpretation following the decisions and judgements of courts;
- the impact of competition, currency changes, inflation and deflation;
- the timing, impact and other uncertainties of future acquisitions, disposals, partnership arrangements, joint ventures or combinations within relevant industries; and
- the impact of tax and other legislation and other regulation and of regulator expectations, interventions, enforcements, fines and requirements and of court, arbitration, regulatory or ombudsman decisions, judgements and awards (including in any of the foregoing in connection with the Covid-19 pandemic) in the jurisdictions in which the Group and its affiliates operate.

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

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

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

APPENDIX A – ALTERNATIVE PERFORMANCE MEASURES

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

Further information is presented below, defined in the glossary on pages 56 to 58 and reconciled to the most directly reconcilable line items in the financial statements and notes. Note 3 on page 40 of the consolidated financial statements presents a reconciliation of the Group's business activities on a segmental basis to the consolidated income statement. All note references in the table below are to the notes to the consolidated financial statements on pages 33 to 55.

Group APM	Closest equivalent IFRS measure	Definition and/or reconciliation	Rationale for APM
Adjusted gross written premium	Gross written premium	Adjusted gross written premium is defined in the glossary on page 56 and reconciled on page 62.	This measure identifies the impact of a contractual change to Green Flag Rescue premium such that a portion of income that was previously included in gross written premium is now included in service fee income. The measure supports comparability with prior period gross written premium. This measure was introduced with effect from 1 January 2022.
Adjusted solvency capital ratio	This measure is based on the Group's Solvency II balance sheet and therefore there is no IFRS equivalent	Adjusted solvency capital ratio is defined in the glossary on page 56 and reconciled on page 62.	This is a measure that shows the Group's solvency ratio at 31 December 2021 excluding the Tier 2 subordinated debt which was redeemed on 27 April 2022.
Combined operating ratio	Profit before tax	Combined operating ratio is defined in the glossary on page 56 and reconciled in note 3 on page 40.	This is a measure of underwriting profitability and excludes non-insurance income, whereby a ratio of less than 100% represents an underwriting profit and a ratio of more than 100% represents an underwriting loss.
Commission ratio	Commission expense	Commission ratio is defined in the glossary on page 56 and reconciled in note 3 on page 40.	Expresses commission expense, in relation to net earned premium.
Current-year attritional loss ratio	Net insurance claims	Current-year attritional loss ratio is defined in the glossary on page 56 and is reconciled to the loss ratio (discussed below) in note 3 on page 40.	Expresses claims performance in the current accident year in relation to net earned premium.
Current-year combined operating ratio	Profit before tax	Current-year combined operating ratio is defined in the glossary on page 56 and is reconciled in note 3 on page 40.	This is a measure of underwriting profitability, excluding the effect of prior-year reserve movements.
Expense ratio	Total expenses	Expense ratio is defined in the glossary on page 56 and reconciled in note 3 on page 40.	Expresses underwriting and policy expenses in relation to net earned premium. Note that restructuring and one-off costs are not considered as underwriting costs and are not included in expense ratio calculations.
Investment income yield	Investment income	Investment income yield is defined in the glossary on page 56 and is reconciled on page 62.	Expresses a relationship between the investment income and the associated opening and closing assets adjusted for portfolio hedging instruments.
Investment return yield	Investment return	Investment return yield is defined in the glossary on page 56 and is reconciled on page 62.	Expresses a relationship between the investment return and the associated opening and closing assets adjusted for portfolio hedging instruments.
Loss ratio	Net insurance claims	Loss ratio is defined in the glossary on page 56 and reconciled in note 3 on page 40.	Expresses claims performance in relation to net earned premium.
Net investment income yield	Investment income	Net investment income yield is defined in the glossary on page 57 and is reconciled on page 62.	Expresses a relationship between the net investment income and the associated opening and closing assets adjusted for portfolio hedging instruments.

APPENDIX A – ALTERNATIVE PERFORMANCE MEASURES CONTINUED

Group APM	Closest equivalent IFRS measure	Definition and/or reconciliation	Rationale for APM
Normalised combined operating ratio	Profit before tax	Combined operating ratio and normalised combined operating ratio are defined in the glossary on page 56 and reconciled on page 63.	This is a measure of underwriting profitability excluding the variances of actual weather costs from our assumptions, Ogden discount rate changes and restructuring and one-off costs. It also excludes non-insurance income. A ratio of less than 100% represents an underwriting profit and a ratio of more than 100% represents an underwriting loss.
Ongoing operations (see also run-off partnerships)	Multiple - rationale for APM	Ongoing operations and run-off partnerships are on page 57 and reconciled in note 3 on page 40.	As noted in the Acting CEO and CFO reviews, the Group has exited or has initiated termination of three low margin partnerships in order to be able to deploy its capital where it may obtain higher returns and has excluded this business from its ongoing results to give the reader a clearer view of the Group's ongoing activities and activities that it is seeking to exit from.
Operating expenses	Total expenses	Operating expenses are defined in the glossary on page 57 and reconciled in note 3 on page 40.	This shows the expenses relating to business activities excluding restructuring and one-off costs.
Operating profit	Profit before tax	Operating profit is defined in the glossary on page 57 and reconciled in note 3 on page 40.	This shows the underlying performance (before tax and excluding finance costs and restructuring and one-off costs) of the business activities.
Return on tangible equity	Return on equity	Return on tangible equity is defined in the glossary on page 57 and is reconciled on page 63.	This shows performance against a measure of equity that is more easily comparable to that of other companies.
Tangible equity	Equity	Tangible equity is defined in the glossary on page 58 and is reconciled on page 63.	This shows the equity excluding Tier 1 notes and intangible assets for comparability with companies which have not acquired businesses or capitalised intangible assets.
Tangible net asset value per share	Net asset value per share	Tangible net assets per share is defined in the glossary on page 58 and reconciled in note 13 on page 46.	This shows the equity excluding Tier 1 notes and intangible assets per share for comparability with companies which have not acquired businesses or capitalised intangible assets.
Underwriting result	(Loss)/profit before tax	Underwriting result is defined in the glossary on page 58 and is reconciled in note 3 on page 40.	This shows underwriting performance calculated as net earned premium less net claims and operating expenses, excluding restructuring and one-off costs.

APPENDIX A – ALTERNATIVE PERFORMANCE MEASURES CONTINUED

Investment income and return yields¹

	Notes ²	2022 £m	2021 £m
Investment income	5	125.0	116.0
Hedging to a sterling floating rate basis ³	5	(6.0)	(13.3)
Net investment income		119.0	102.7
Net realised and unrealised (losses)/gains excluding hedging		(67.4)	43.6
Total investment return	5	51.6	146.3
Opening investment property		317.0	292.1
Opening financial investments		4,633.6	4,681.4
Opening cash and cash equivalents		955.7	1,220.1
Opening borrowings		(59.2)	(51.9)
Opening derivatives asset ⁴		14.3	8.0
Opening investment holdings		5,861.4	6,149.7
Closing investment property		278.5	317.0
Closing financial investments	15	3,698.5	4,633.6
Closing cash and cash equivalents	16	1,003.6	955.7
Closing borrowings	16	(65.2)	(59.2)
Closing derivatives asset ⁴		1.6	14.3
Closing investment holdings		4,917.0	5,861.4
Average investment holdings ⁵		5,389.2	6,005.6
Investment income yield¹		2.3%	1.9%
Net investment income yield¹		2.2%	1.7%
Investment return yield¹		1.0%	2.4%

Notes:

1. See glossary on pages 56 and 57 for definitions.
2. See notes to the consolidated financial statements.
3. Includes net realised and unrealised gains/(losses) on derivatives in relation to AUM.
4. See footnote 1 on page 20 (Investment holdings table).
5. Mean average of opening and closing balances.

Adjusted gross written premium

	Rescue - ongoing operations £m	Of which: Green Flag direct £m	Total Rescue and other personal lines £m	Total Group - ongoing operations £m	Of which: direct own brands £m
FY 2022					
Gross written premium	139.5	84.0	269.7	2,969.8	2,082.9
Effect of service fees recognised as other income	4.2	4.2	4.2	4.2	4.2
Adjusted gross written premium	143.7	88.2	273.9	2,974.0	2,087.1

Adjusted solvency capital ratio¹

	2021 £bn
Total eligible own funds	2.38
Less: Tier 2 subordinated debt redeemed on 27 April 2022	(0.25)
Add back: ineligible Tier 3 capital	0.03
	2.16
Solvency capital requirement	1.35
Adjusted solvency capital ratio	160%

Note:

1. See glossary on page 56 for definition.

APPENDIX A – ALTERNATIVE PERFORMANCE MEASURES CONTINUED

Normalised combined operating ratio – ongoing operations^{1,2}

	Home 2022	Home 2021	Commercial 2022	Commercial 2021	Total 2022	Total 2021
Loss ratio	80.2%	50.7%	53.7%	54.5%	74.7%	58.4%
Commission ratio	5.1%	6.9%	19.4%	20.0%	7.3%	7.3%
Expense ratio	21.6%	22.5%	21.1%	21.7%	23.8%	23.8%
Combined operating ratio	106.9%	80.1%	94.2%	96.2%	105.8%	89.5%
Effect of weather						
Loss ratio	(13.0%)	5.5%	(1.3%)	0.1%	(2.7%)	1.1%
Commission ratio	0.8%	(0.4%)	(0.1%)	—	0.2%	(0.1%)
Combined operating ratio normalised for weather	94.7%	85.2%	92.8%	96.3%	103.3%	90.5%

Notes:

1. Ongoing operations – please refer to footnote 1 on page 2.
2. See glossary on page 57 for definition.

Operating expenses¹

	Note ²	2022 £m	2021 £m
Operating expenses (including restructuring and one-off costs)	9	744.8	807.8
Less: restructuring and one-off costs	9	(45.3)	(101.5)
Operating expenses	9	699.5	706.3

Notes:

1. See glossary on page 57 for definition.
2. See notes to the consolidated financial statements.

Return on tangible equity¹

	2022 £m	2021 £m
(Loss)/profit before tax	(45.1)	446.0
Add back restructuring and other one-off costs	45.3	101.5
Coupon payments in respect of Tier 1 notes	(16.6)	(16.6)
Adjusted (loss)/profit before tax	(16.4)	530.9
Tax credit/(charge) (2022 and 2021 UK standard tax rate of 19%)	3.1	(100.9)
Adjusted (loss)/profit after tax	(13.3)	430.0
Opening shareholders' equity	2,550.2	2,699.7
Opening goodwill and other intangible assets	(822.5)	(786.8)
Opening shareholders' tangible equity	1,727.7	1,912.9
Closing shareholders' equity	1,934.0	2,550.2
Closing goodwill and other intangible assets	(822.2)	(822.5)
Closing shareholders' tangible equity	1,111.8	1,727.7
Average shareholders' tangible equity ²	1,419.8	1,820.3
Return on tangible equity	(0.9%)	23.6%

Notes:

1. See glossary on page 57 for definition.
2. Mean average of opening and closing balances.

APPENDIX B – IN-FORCE POLICIES AND ADJUSTED GROSS WRITTEN PREMIUM

In-force policies (thousands)

At	31 Dec 2022	30 Sep 2022	30 Jun 2022	31 Mar 2022	31 Dec 2021
Direct own brands	3,756	3,766	3,846	3,854	3,869
Partnerships	80	88	98	100	102
Motor	3,836	3,854	3,944	3,954	3,971
Direct own brands	1,732	1,758	1,792	1,825	1,879
Partnerships	769	775	779	783	788
Home	2,501	2,533	2,571	2,608	2,667
Rescue - ongoing operations	2,185	2,227	2,264	2,269	2,273
Pet	128	130	133	135	138
Other personal lines - ongoing operations	111	115	115	108	94
Rescue and other personal lines - ongoing operations	2,424	2,472	2,512	2,512	2,505
Of which: Green Flag Direct	1,106	1,136	1,156	1,167	1,179
Direct own brands	651	644	623	613	602
NIG and other	277	268	261	265	269
Commercial	928	912	884	878	871
Total in-force policies - ongoing operations	9,689	9,771	9,911	9,952	10,014
Of which: direct own brands	7,245	7,304	7,417	7,459	7,529
Run-off partnerships	2,188	3,315	3,320	3,339	4,551
Total in-force policies	11,877	13,086	13,231	13,291	14,565

Adjusted gross written premium¹

	H2 2022 £m	H2 2021 £m	FY 2022 £m	FY 2021 £m
Direct own brands	709.7	781.9	1,398.5	1,515.2
Partnerships	16.2	23.3	34.2	45.6
Motor	725.9	805.2	1,432.7	1,560.8
Direct own brands	199.4	218.1	381.5	416.7
Partnerships	68.3	81.4	136.6	161.1
Home	267.7	299.5	518.1	577.8
Rescue - ongoing operations	73.4	80.9	143.7	155.2
Pet	35.1	36.3	70.8	71.4
Other personal lines - ongoing operations	29.9	29.4	59.4	54.5
Rescue and other personal lines - ongoing operations	138.4	146.6	273.9	281.1
Of which: Green Flag direct	47.7	47.4	88.2	88.3
Direct own brands	112.7	96.5	218.9	187.4
NIG and other	258.8	220.4	530.4	465.6
Commercial	371.5	316.9	749.3	653.0
Total adjusted gross written premium - ongoing operations	1,503.5	1,568.2	2,974.0	3,072.7
Of which: direct own brands	1,069.5	1,143.9	2,087.1	2,207.6
Run-off partnerships	71.8	46.9	124.4	98.9
Total adjusted gross written premium	1,575.3	1,615.1	3,098.4	3,171.6

Note:

1. See glossary on pages 56 to 58 for definitions and appendix A – Alternative Performance Measures on pages 60 to 63 for reconciliation to financial statement line items.

ADDITIONAL INFORMATION

We confirm that to the best of our knowledge:

1. the financial statements within the unaudited Annual Report & Accounts, from which the financial information within these Preliminary Results have been extracted, are prepared in accordance with the International Financial Reporting Standards, issued by the IASB as adopted by the UK and give a true and fair view of the assets, liabilities, financial position and profit or loss of the Group and the undertakings included in the consolidation taken as a whole; and
2. the management report within these Preliminary Results includes a fair review of the development and performance of the business and the position of the Group, and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties faced by the Group.

Signed on behalf of the Board

NEIL MANSER
CHIEF FINANCIAL OFFICER

12 March 2023

LEI: 213800FF2R23ALJQOP04