Q3 IMS 2013

ANALYSTS PRESENTATION

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FORWARD-LOOKING STATEMENTS

Presenters

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Presentation

Philip Hampton

Good morning, ladies and gentlemen, welcome to our Q3 results, of course we don't normally do an analyst presentation at Q3 but there's more to talk about today.

First of all I'd like to welcome our new, top executive team, Ross McEwan and Nathan Bostock. They've been in post now for just a month, it's been an extremely challenging month for both of them, but they don't need me to tell them that's the shape of things to come, so that's life at RBS. We've also got a new capital framework that we've been discussing extensively with PRA in recent weeks and Nathan will talk about that. And of course today, the Treasury has announced the conclusion of their report into the good bank/bad bank merits.

The main theme today, although it is Q3, is actually capital. The Board are very clear with the PRA that we do need to further strengthen our capital position. There are various reasons for that but they particularly include litigation and conduct costs, which are a feature of our results in Q3 and that of many other banks.

On the good bank/bad bank, the Board has discussed this many times actually, in recent years, and we've always thought it was a great idea in principle but very difficult to do in practice, in the interests of shareholders at least, and so we're unsurprised that the Treasury has reached the same conclusion. There is obviously a limit to what can be achieved in the alternative that is an Internal Bad Bank restructuring, although we ourselves have achieved, I think, an enormous amount, probably at world-class levels, in terms of our own Non-Core rundown in recent years. The key issue that Nathan will talk about is the level of acceleration effectively of the new reconstituted Non-Core or bad bank group of assets. And although a lot of what we're talking about is strategic and capital in nature this morning, I think it's important to emphasise that Ross and Nathan have only been in post for just 30 days, and Ross will have much more to say on strategy generally by the time we get to the February results.

But there's no doubt in the Board's mind and indeed in all of our minds about where the value is in this business, in RBS, and I think it's quite simply running the business better for both the customers and for shareholders rather than the major corporate financial changes which have been such a dominant feature of recent years. There's still quite a lot to do in relation to Citizens and other transactions but we believe, very strongly, that the value in this business, the shareholder value in this business, is basically stored in the operational performance that we need to improve and can improve quite significantly. Andrew Large's report into our SME lending touches on that today. We commissioned that report, we decided that it should be made public in this way. Elements of it, as Ross has already described, are uncomfortable for the bank. Whenever you get an outsider to identify some of your weaknesses, that is always going to be the case, but we do think it's important to confront them and to make sure that what are identified as weaknesses can be turned into opportunities. And that is where, as I say, I think it's extremely important that Ross and Nathan and the entire team focus their very considerable energies and talents in the months and years to come, in basically running a much, much better bank. Thank you very much.

Ross McEwan

Thanks very much Philip. Thanks also for joining us this morning. As Philip said we normally would just have an audio for a Q3 but there's a lot to be said today. When I took on the job I didn't realise we'd be doing so much in so little time. Today I just thought I would cover off on a few things, as I come into the job, as Philip said one month in, and these are some of my early priorities that I discussed with the Board. First off was to resolve the good/bad bank issue that had been in place for about four months, very key for me to actually get this resolved very quickly and I think we've done that, as you've seen today. The second one was to resolve the capital position of the bank with the PRA. The business had done magnificent work on rebuilding the capital from being broke to being at 9.1 fully loaded, but our view is we needed to get that up to a higher level to take that one off the table as something that people conversed with us. Nobody talks to us about liquidity now; it's just all around capital and a lot of uncertainty, so that was the next one. The third one was to reset the relationship with HMT, PRA, UKFI and the Chancellor. I mean, we needed to get a firm basis of understanding about this business so that we could all go forward and spend 90% of our time on the good parts of this business rather than talking about those pieces that really now make up about 10% of the bank.

We also wanted to make progress on the DAS and it's good to see that is progressing well. Really that's just a sign to me of a normal bank again when you can pay dividends. And the final one was to sharpen our focus on our customer-focused businesses, and I'm going to give you a good update on that in February when we give our full year results. So, lots to do but those were the things that were very clear in my mind as priorities that I had discussed with the Board.

It's very clear that RBS has made considerable progress over the last five years. You look through all of the activities that this bank has been involved in and the things that Stephen and the team have tidied up are absolutely remarkable on getting this bank back, sound again. It's got a robust balance sheet and a dramatic change in the actual scale and scope of this business. Now, round about 80% of this business is in the retail and commercial space, which wasn't the case before. Non-Core process, well, you've seen in the numbers, down from 257 to about 39, 37 billion, actually above, better than forecast. The exiting of some of the businesses that we just didn't see as core activities. And then the final one is just the reduction in the reliance on the government and its support, and again more news on that today. So, I think, an amazing five years of putting this bank back to being safe and secure again.

But if we're going to build a really good bank, I think we've got more work to do and that's what I've signalled to my senior team and to the staff at large, that we need to continue to restore the capital strength of this bank, we need to get ourselves into a fully-loaded core tier one ratio of 11% by 2015 and 12% by 2016, that's what we've set ourselves and we believe we can do it. We have seen the acceleration to achieve this, the acceleration of the divestiture and IPO of Citizens which was brought forward from 215 into 214, that's a key piece for us in this, and we also need to continue to relentlessly take down, or reduce the risks, and hence the RWAs and other parts of our business, and Nathan will talk to you about that particularly around the good and bad bank.

We want to further reduce or de-risk our legacy bad assets. There's just so much value in that and getting our business in far better shape than it is today and the creation of the Internal Bad Bank that Nathan will take you through the numbers on, is an absolutely key part of that. And then we need to sharpen the focus on our core businesses, we've got some really good businesses sitting inside this organisation and that's where our efforts need to be.

Just a brief mention of Citizens because it is crucial to our capital plan. It's a very good business, but it's got good positioning in the US, it's the ninth largest by branch distribution, it's the seventh largest by ATM distribution and the second largest in store franchise. So, it's a very good franchise business. It's positioned for growth and improvement with Bruce now running the business, but to be quite honest it's not essential for RBS to have that business. We would like to put that capital back into our core businesses here in the UK, we believe we'll get better returns out of it but also strengthen what is home-based for us in the UK.

It also has limited connectivity to the group and much of the advantages that we have can be maintained by staying and building relationships with that business, no matter what the ownership structure is. So, an IPO second half of 2014 and a plan to exit the business fully by the end of 2016 is what we've set ourselves, we see some advantages in doing so.

Nathan’s going to take you through the detail but there, in my mind, are some real advantages around the established model of an Internal Bad Bank. First off, why we’ve done it. Well, what we’ve done, we’ve worked very stringently with the government and HMT, UKFI over the last four months to have a good look at what these assets are across our business and which are the ones that we could identify for a faster run-off which would be advantage. We did explore a range, both internally ourselves, and I know the government did, of should we take these assets out, should we manage them a different way? And the best option at the end of the day was to actually create an internal operation that would remove these assets faster than we’d planned to do.

There’s a range there of about 37 to 39 billion, it just depends where we end up at the end of this year that will go into this business and our targeting, and I say targeting is to exit the majority of these assets by the end of 2016. We admit there will be a rump and we’re not going to put huge pressure on this business that is not value-seeking for our shareholders, but we do have an aspiration of removing the vast majority of these assets by 2016.

The reasons why are pretty obvious, it does increase our capital ratio, it normalises our credit costs and retail tail risk reduces the tail risk of this business. We do need to put ourselves, as I said, in a better capital position and this certainly helps and it improves our acceleration to profitability and our return on equity for our core businesses.

Today I’m signalling three things. One, is we are doing a strategic review of this business which we’ll launch out to everybody in February 2014. It will be a market, customer-led strategy. I think we’re looking at all of our parts of our business and saying, how can we focus these far more on the customer to get better returns for the business. The core franchises will be centred on the UK but we do have a critical international network that we need to work with and I believe there’s a lot of value to be had out of doing far better connectivity with these connections. As I said you’ll see the results of that in February 14.

The next one is around our customer service. We need to make this bank a much simpler and easier business for customers to deal with us. Today it is not the case. Five weeks to get an agricultural loan answer, should be five days. Weeks and weeks to get an account, should be a day or less. These are some of the things we need to focus on. We are looking at our operations and IT and how that connects with our business. We want to make it simpler for our employees to do business and we want to drive revenue growth out of our core businesses and that’s going to be our focus. It’s clear that we do need to address costs and efficiencies of this business, a cost to income ratio of 65% is just too high, it’s a legacy of a much, much bigger business that we now no longer have. And we are targeting a mid-50s cost to income ratio, but we'll be coming out with full detail on that in February.

That's all I wanted to say today and I'm going to hand over to Nathan Bostock who's going to take you through the Internal Bad Bank. So, I'm pretty sure you're going to be interested in those, and then we'll take questions after. Over to you Nathan.

Nathan Bostock

Thanks very much indeed Ross. So, good morning everybody. And I think really the way that I would look at this is what I'm trying to do today is to give you a good understanding about the approach we're going to be taking to risk reduction. We've talked about effectively Citizens, accelerating Citizens and there's some capital action there. We've talked about effectively changing our targets to 11% and 12% for the future. So, this is really, what is the strategic thinking about the risk reduction and the creation of the Internal Bad Bank.

So firstly, I think it's worth having a little reminder around Non-Core and the reason for this is also to clearly ensure that people understand ultimately the difference by the end as well, of Non-Core versus Internal Bad Bank. So, all of you will have travelled the journey that we've been on. We've had a very successful, in my opinion, approach to reducing risk. As you know we've gone from some 258 billion down to some 37 billion of assets at Q3, we're ahead of that target and that's been done, in my opinion, in an extremely professional way, and we have all of the team and the skills to be able to do that. So that's really a scene set. But I think it's crucial to understand what was Non-Core originally. Non-Core originally was very much focused on using five criteria to create the asset selection for that particular unit. And those were a mixture, they weren't just bad assets, they were non-strategic assets and indeed, often they were actually high quality assets but mispriced. So they'd been priced at the height of the margin compression when funding costs were misunderstood, and so they created effectively long maturity assets with a real drag on ROE, but they were perfectly good assets.

But before I do that I want to really take you through the strategic thinking of what we're doing here and this is very much a strategic approach and thinking forward in terms of where we want to be in three-years time and taking account of the future but acting now because if we act now, by the time we get there we'll be very well positioned against it. And really the world has changed very significantly, certainly for UK banks, since August, in my opinion. And the reason it has is because under the CRD4 transition arrangements basically you were going to transition with capital reductions coming in over a period of time. That was fine and we were all planning for that. CP5, and I appreciate it's a consultation document, but effectively it comes live on 1st January, doesn't leave a lot of consultation time for all of us, and so my view of this is we need to work on the principle that majoritively this is going to land in the way it's described.

So, what are the areas that really it looks at? Well, firstly, and this is shown on the right-hand side because this is where a diagram really does help, on the right-hand side you'll see what is the new capital stack approach, under CRD4 and CP5. Two elements that appear, firstly this pillar 2A, I'm not really going to talk about that because it is crucial because it's going to uplift capital and there'll be various debates around whether it should be 100% of equity, should pension costs be fully in there and the rest of it. The real element that I'm going to talk about is the buffer, the stress buffer, and why. Because if you look at the top right-hand side you'll see, certainly for the near term, the PRA buffer is going to be crucial to determining the capital ratio of UK banks. The reason it is because on the left-hand side it's going to take till 2016 before you start building the CRD4 buffers into the calculation, and they'll come in 1% and then another per cent, another per cent, by 2019 you'll be at four. So, post 2019, if your PRA buffer is above four, that's going to be effectively the ceiling that you have to achieve. Prior to that though, it's really going to be 100% the PRA buffer that is going to be driving the top level of your capital ratio.

The other thing of course is now you're going to have to take all the deductions upfront, so, you haven't got that period of time, you're going to have to deal with the deductions starting from January. And then there's another nuance and happens to be correlated, I don't think it's by chance, effectively we have a new stress testing regime that's coming in, my way of describing it would be it's a CCAR++. The way it will be run is very similar except for, in particular they're going to bring in an idiosyncratic stress and generally we use macroeconomic stresses, same across the industry, but with an idiosyncratic, of course, there is a high likelihood that that is going to be targeted at the particular items that drive stress in your particular organisation. In our case, clearly we have a number of assets which have higher intensity and therefore can drive that stress calculation.

So, a long explanation but really important because it's going to drive, effectively, higher capital requirements faster. And so, if you think of the world as being a numerator, a denominator, now think of the third leg which is going to be your stress buffer and these are going to be crucial for UK banks.

Turning to the Internal Bad Bank. Firstly, what have we done? Well, I raised the Non-Core specifically and how we'd done the asset selection for that because this is really the first part of the journey into the Internal Bad Bank. One of the things that happened when we were doing the review with HMT, clearly we've been very, very focused in driving all of the risk reduction in Non-Core and core businesses but it enabled us to step back and say, actually, can I think of the profile of the assets of this bank linked to the strategic thought process I was just talking about? And what that said was, well, Non-Core actually isn't all of your higher intensity assets for the very reason I gave you in the first place. If you actually look at the mix of assets in Non-Core, roughly about 16 billion of them, and this is based at June 13, roughly 16 billion of them figure under the profile I gave you before. Money good, lower returning, they're going to be around for a period of time. They should really sit in the core bank, and if Non-Core wasn't here, that's precisely where they would be.

On the other hand there's a set of assets in the core bank generally from our global restructuring group, some of them are coming naturally from the core part of Ulster, so a differentiation between core and Non-Core, all suffering within the same environment as we know, basically, Ireland, but also then generally, also your higher risk assets that typically also sit in your defaulted portfolio. If you do that, that's 17 billions worth of assets. The numbers are pretty coincidental in terms of 16 and 17 so we used filtration; we used a variety of tests to look at forward expected losses, several of them. The two probably that just give you a flavour of it is, basically these were assets that were sitting below BB-, in terms of asset quality, and/or, they were above 150% risk weighted, again, giving an element of definition around the risk.

What's interesting then is if you then look at the bottom part, this says, here's the capital we currently have consumed, tied up against this balance sheet, so just playing the numbers game, 5% of the group assets from a funded asset point of view and roughly 20% of the actual capital of the bank consumed in these assets.

So, moving on to the next slide. Two other things that are probably important, first of all, so, why is this firstly 38, 39 and not the 45 billion I've talked about? Ross eluded to that it's because we started in June but we worked with the government as well on a thought process that was actually forward-looking, so it was looking to the 31st December this year. Our estimation of the glide path of the assets that we're managing, by the end of the year we will be at around about 38 billion on that original pool of 46 billion.

The right-hand side is the most illustrative though and probably the most important in trying to understand the number movements that are going to be caused by this because although all the information is available that shows you the amount of capital we've got consumed against these assets, it's not the easiest thing in the world to actually see it, and the reason is because, as the chart shows on the right, circa 5 billion, almost 50% actually sits in capital deducts. So, we think of things here as RWAe's and in fact that's what you'll see in the IMS, we just sort of grossed them back up to give ourselves a ready reckoner, but in reality you can see by December we will still have circa 11 billion of capital tied up against these assets.

So, what's different? Well, let me just cover off the left-hand side Ross did originally. Our aim here is to strategically change the speed with which we manage these assets, again linking back to what I showed you in terms of timetables of regulatory change. So, our aim is to be somewhere between 55% and 70% by the end of 2015, that's what I've used for these modelling purposes, and our target is to have less than 15% left of these assets by the end of 2016. So, again, subject to market conditions, all the usual things that you would naturally apply to it.

What's fundamentally different? Have a look at the right-hand side, this is the best way and the simplest way of explaining what we're doing. If you look across the top horizontally where it says, previous plan, what this shows you is really the two techniques, main techniques that we've been using around the management of Non-Core and indeed, the management of higher risk assets. Generally, one and this is best for extracting capital, we effectively use forced refinancing at maturity, it's by far the best way, you get a 100% back, but you start early and you work hard with your clients effectively for the refinancing. It doesn't happen in all cases and clearly there will be some asset sales. But typically in that Non-Core picture we've actually been looking at assets that stretch out over a very long period of time, years potentially. So, it's not just a 2013-16 window, in terms of outlook, these assets could be 3, 5, 10, 15 years. And typically if we're going to use that maturity profile and we're going to use the forced refinancings, then you can see those things are going to happen over a long period of time.

What are we doing in the Internal Bad Bank? Well basically, we're going to continue to use the forced refinancing approach, for maturity profiles within the period. Again, it's by far the best technique for extracting the maximum amount of capital on those assets, but we're actually going to accelerate the exit of the remaining assets down to the level that we talked about. And so what that's going to do is effectively, that means those assets that were going to be around longer, effectively they're going to have a shortened life. So, that's a strategic change in the way that we manage them. What does that do? Well, what it does in terms is generate disposal losses, I'll talk about those in a second, but also it changes the period over which you calculate the collateral value for accounting purposes, and so that accelerates your impairment charge to being upfront.

How might you think of this? And, so, starting to get really to the numbers, well, firstly if you think about it, what I've said is, this is a period of time and you have to think about lifetime impairments.

So, again, if you're taking an accelerated number what you're really doing is you're accelerating impairments you expected to take. So, how do I give you a feel for the numbers? Well, first of all, the best way of probably thinking about this is go back to that expected loss minus provision. I'm going to tell you that I think that that's a pretty realistic type of number. I think it's a pretty realistic type of number for defaulted assets because actually our experience is showing it is the changes in capital models and all these types of things are reasonably trueing up these types of things. And in fact there's a couple of quotes in the BlackRock Solutions report where actually they support this and I'm very happy to read those out later, but they basically support this logic about the accuracy, in their mind, of our expected loss of forward projections.

So, what that says is we've got roughly, let's call it, the 5 billion tied up in that, we've also got some RWA capital because that's sitting there as well, and so again you can expect that there's an element of that that will convert into losses. Put those two together you get roughly 5 to 6 billion of potential credit costs. And again, you have to think holistically and term nature in all of this; roughly 50% to 60% of the impairments that we would be accelerating actually come outside of that 16 outlook period.

How do you get the incremental cost of disposal? Well, Rory here and Derek, they've been engaged in this. We've moved over about 90 odd billion of assets in Non-Core, so, we have a reasonable idea now of the way people think about these things and generally there's a clear look-through to the actual credit cost. So, most people have a very similar view of how they look at the credit and the risk in the credit. What's different of course is the acquirers weighted average cost of capital versus your own. And so that's where you generally get this incremental cost occurring, we believe that on these assets, under the profile we've talked about, etc., etc., it's roughly 1.5 to 2 billion.

Having said that, there's a couple of offsets against this in terms of that incremental cost because that would clearly be a straight hit to TNAV as well. Firstly, if we didn't do something with these assets, we would actually be holding these assets over the longer term, so effectively we would have a funding cost that you can offset effectively against the cost that the acquirer would have, and in our estimations we reckon that that's worth, again, circa 50% of that 1.5 to 2 billion number. So, although that's the number that appears as a disposal loss, you have to start thinking longer term and more holistically to realise that actually if you passed that point in time and kept those assets, there would be a cost to you as well.

On top of that, and this is where it really links back to the strategic view I gave you, there's actually going to be a stress cost, and remember that the selection criteria for these are: they're higher risk assets, they have a greater propensity to suffer under stress. So again, try to give you a flavour of the size of the types of numbers that go with this, first of all I said, around about 20% of our capital is consumed in these assets. It actually, though, generates between 40% and 50% of our overall stress losses. Now, if you want to convert that and say, okay, how reasonable is it to think therefore that in a stress buffer that that's at least 100 basis points of stress buffer? It may or may not be, could be more, could be less, but it's certainly not unreasonable to be thinking of it in terms of those sorts of magnitudes, or even larger. If it is, then clearly it converts to an actual cost for you as an organisation because as you pass out further than 16 with those remaining assets, imagine it was 1% for those remaining assets, roughly half the pool, sorry, 15%, sorry, going back to the original you would have had the longer term picture that I said, so 50% to 60% of your impairments.

If you actually look at that the way of thinking about it is that that's a, lets call it 5 billion, that 16 point, how much is 5 billion of capital going to cost you? Say, 500 million effectively in terms of its opportunity cost to take it and re-use it into core businesses, that clearly should be in the right growth phase at that point in time, and it would have declined, so it would have gone down as the asset profile went down. But if you just accumulatively add those things up, you play it against the 100 basis points or so, you can easily see that you will negate the remaining 50% of the 1.5 to 2 billion. So, on that logic, we believe overall, this is broadly economically neutral, possibly slightly positively; however, of course, the way the numbers will be described will be quite different. And I will come back to that in a minute. And the only reason for that is the various timings and the fact that you're now trying to look at lifetime type of cash flows and thought process versus a financial outlook period.

Right-hand side also gives us a fantastic situation in terms of what does it really do for us if we actually go through and execute? Well, it's not just that we're doing strategic management against our stress buffer, what it also does for us is effectively it's ROE accretive, and again, I'll drop down and show you some of the numbers in a minute. Our non-performing loan ratio, as you all know, are well out of sync with our peers, that'll take us down from the circa 9% to 10% down into the, call it the 3% there or thereabout, but it certainly will put us very much in line with them. Clearly the volatility of future stress massively declined. A conversation I've had with the PRA, they're very happy to actually say, we fundamentally agree with you in terms of materiality, we can't give you absolute numbers because of course life isn't as simple as that, be we certainly will agree with you about the materiality. And, the other thing is it simplifies us, fundamentally simplifies the ability to understand the earnings of the overall bank and take away some of the complexity.

So, now, if we're looking at it and thinking, crikey, I understand this big picture long term, what would it actually look like to click the camera at different points along this journey? Well, the first one is 2013, so that's the first big question, and so we talk about accelerating impairments, indeed that is what we're doing, we're accelerating between 4 and 4.5 billion of impairments. Again, remember I said these are sat there, so these aren't unknown impairments, they're unknown in financial outlook period but not as an entirety. The good news and good news from a capital perspective is that the EL minus P is very good and the EL minus P basically means that in that first instance you'd have around about a ten basis point hit. There's some subtlety as to why that is but it's basically just to do with part of the organisation and a trapping of an element of it, but, anyway, basically again, neutral.

14 to 16 you see a set of things; you will see impairments on the performing assets. So if you look above, what it says is, I've got my performing assets 60%, I've got my non-performing which are 40%, it's those that the change of strategy creates the upfront impairments for, not for your performing, that doesn't change. You're still using IFRS for those, you haven't changed the outlook on them, you haven't got an exit view on those that materialises in cash flow terms.

So, then you've got your disposal costs, you'll see that coming through in the years, and then naturally you've also got the general economics of those assets so you've got income, you've got the funding cost, you've got the operational cost, etc., and we believe that that's also around about 1.5 billion over the period. By the end of it, by 2016, you're releasing around about 2 billion of capital. 2017 onwards you get the various things I described in terms of the non-performing loans, etc. And of course, the impairments that you would have been incurring then for a long period of time, those actually have gone.

So, summing it all up before we come to questions, and I've tried to again look at this in terms of short term and medium term, I've used medium term because there's a slight difference for TNAV in the core equity tier one ratio between 2016 and the eventual number, so I'll explain that, versus just pure 2016. So the numbers at the bottom really reflect pure 2016, so, risk-weighted assets will be down by about 60 billion, so now this is managing the denominator as well. Capital reductions will have obviously decreased by the 5 billion. Return on tangible equity will go up between 90 and 120 basis points, that's on the remaining group. Stressed impairments will be down between 40% and 50%. I realise time will move forward and different economic situations and all the rest of it, but just from a pure today point of view. And on non-performing loans, which is clearly again a critical one that says, you are a simplified bank and you look normal, those will be down in the territory of others.

On the top two, TNAV and the core equity tier one ratio, have indeed given the 2016 number, but for the very logic that I described previously, those things actually will then trend towards each other over time. So, if you think about it, you take the TNAV hit up front, by 2016 it's roughly 1.5 to 2 billion, but if you look at that overall holistic picture that I said, that will then trend back down to basically a zero type impact, if not slightly positive, but it will only happen over time. You'll get the reverse impact on the core equity tier one that you've released, however you will have released 2 billion actually at the 2016 point in time.

That's probably where I was going to stop Ross and Philip, we'll take questions.

Philip Hampton

Okay. Thank you very much Nathan, thanks Ross. Let's move over to questions. Just one little thing, which I wouldn't normally say, but I will say this time. I think it's evident from Nathan's presentation that he in particular, Ross too, have spent a huge amount of time on this particular capital exercise in recent weeks. So, whilst you can ask any questions you like, I think you're more likely to get a better answer in relation to capital and planning and so on, rather than the Q3 results. But, as I say, we're open to any questions. We do have, I believe, around 300 people on the phone, so I'll move to them, and indeed there may be questions coming through on the webcast. But let's start first of all with the room. Who's going to shoot first?

Chirantan Barua – Bernstein

Hi there, this is Chira Barua from Bernstein. Just a quick one Nathan, a couple of questions around that. First, the 4-4.5bn, is there any tax treatment out there or straight away you say it's going to be a hit to the TNAV. Second, will this remain a volatile item, because it will be based on long dated macroeconomic assumptions. Should we look at it like a pension volatility stuff? And the third is, what kind of macroeconomic assumptions, especially around Ireland and the UK CRE do you have implied for, say, 2015, 16 in those numbers?

Nathan Bostock

So, I guess on the tax one, it's always good to start with tax isn't it. So, on the tax one we have worked through the tax position and of that 4 to 4.5 billion of impairments about 2.7 billion of it relates to Ireland. That's really where we haven't got an ability to use an effective tax shield and so we've taken a conservative view in our numbers and we haven't assumed a tax benefit on any of it.

In terms of the volatility, again, in all of these numbers, and it links almost to this macroeconomic one as well, we use multiple different profiles, so I haven't picked any particular one and assumed there's a particular one out at a point in time. I've tried to use this across a variety of ones and in fact, again, BlackRock themselves say that actually they think that our stress testing approach is actually conservative. So, I can tell you that I believe I've taken a reasonably conservative set of different scenarios, but I can't give you the particular, any particular one.

Philip Hampton

Okay. Why don't we go straight behind there?

Peter Toeman– HSBC

Peter Toeman from HSBC. I was expecting to hear something about the investment bank in today's announcement and maybe this is awaiting the strategic review, but, am I right in thinking that the investment bank will still be 20% of the group's capital in RWA terms and perhaps generate a profit of about 1 billion of PBT or has that, is that guidance going to change?

Ross McEwan

Do you want to take the guidance and then I'll talk about the (overtalking).

Nathan Bostock

Yes. There's no change to the guidance. I would think of it in terms of the RWAs that, including those elements, that are in the passive rates deduction element, and I think the way I would look at it is actually they've done incredibly well, they've actually hit their targets already. We've also got our IMM waiver approval, so again, that's another item to put in the case and shut the lid.

Ross McEwan

Yes, and the comment I was going to make just on Markets, it's performing better against RWAs already against the plan which was put forward some time ago, reasonably good quarter. Still a long way to go for them as you know the revenue comes down quicker than the expenses, and Peter and Suneel are working very hard on the expense base of that business to get its ROE back up, so good progress.

Philip Hampton

Why don't we come right to the front here?

Chris Wheeler – Mediobanca

Chris Wheeler from Mediobanca, A couple of questions if I may. The first one is just, can you perhaps talk about whether there's going to be any major change in the way you actually run the new Internal Bad Bank compared to the old Non-Core business? Because it seems to me there's some new disciplines you're going to want to employ in this unit perhaps to actually successfully go through the acceleration that you're laying down. That's the first question. And the second one, which is I know slightly tricky for you but on Citizens, clearly you're really keen to go down the IPO route but it's not difficult to see that has a lot more risk than trade sale just in terms of timing, what happens in the market and in terms of valuation, particularly given your issue with excess capital, which I think you're going to struggle to get out in the current environment. So, could you just confirm that obviously you will be doing a twin trade approach; I assume you will, in terms of saying, if the bid comes that you would consider it, certainly as opposed to just being absolutely committed to the IPO route.

Ross McEwan

First off on Citizens we are planning to take it down an IPO route just as we did with Direct Line Group. We showed absolute value and creation out of that. Look, if somebody does a preemptive on the thing they can come and talk, but our view is very focused 100% on the IPO route as the best value. And we have done examination of all those who are likely and the likes, but I think the IPO is probably the best value creation.

Nathan Bostock

In terms of, and it's a very good question, in terms of the disciplines, no, we have all of the disciplines actually that we need. Again, this is about the strategic mind-set of how you're looking to manage them rather than the skillset of the people. We've been employing all of these types of techniques and thought processes as we've gone, but we've now made the fundamental change across the asset pool as a whole.

Philip Hampton

We'll go to the lady there. Right in the middle, five down, six down.

Claire Kane – Royal Bank of Canada

Hi there, it's Claire Kane from Royal Bank of Canada. Just a quick question on slide 15, you talk about the lifetime losses 5 to 6 billion and you say that the decision the account allows you to take upfront losses. Can I ask why you don't take more impairments now, given you expect to record losses on disposal going forward, and is that decision perhaps due to the capital deduction impact and that you only want a near term deduction from your core tier one ratio ten basis points at this time?

Nathan Bostock

Sorry, probably I haven't necessarily fully explained it enough. The impairments that we're accelerating are the impairments that you would be taking over the life on these assets. The accounting, it's not an accounting change, it's just that when you actually have to value them you value a set of cash flows. Instead of expecting these cash flows over a number of different years right the way out, you're actually going to have to truncate them and therefore that effectively accelerates the impairments through to now. But it's really just a cash flow representation of the outcome. So, that's why when you do the disposal losses it's roughly, those are roughly neutral except for the incremental cost, i.e., the differential between you and the person buying it. So actually you're not differing necessarily on what you would think is a pure value, you're differing really on the fact that the person buying it has to make a return on the asset and they're carrying a different weighted average cost of capital. So, they're going to build that into the price they offer you, the impairment takes it actually to the realisable value that you would see in the market.

Philip Hampton

We'll give you a test on that later, okay. Why don't you just move it to the side?

Mike Trippitt – Numis

Good morning. It's Mike Trippitt at Numis. Two questions. Just following up on that one, I'm just interested to understand the criteria around the scale of the assets that have been transferred over, and was that actually driven in a way by the impairment loss that you could withstand on day one, versus your expected loss deductions? And the second question is, I don't know, you've mentioned in the release that you're in advanced stage on the DAS discussions with Treasury, can you give any kind of guidance in terms of, are we still just looking at a one-time payment for exit from that or are there more interesting solutions? I think the current Treasury estimate is a billion and a half as a DAS exit; can you update us on that?

Ross McEwan

I'll take the latter one first. We are in pretty advanced discussions so I won't make any more comments on that but it will come to shareholders who will have to vote on it, at this stage, advanced stage, so we're confident about that.

Philip Hampton

It's another related party transaction so it's got to be agreed effectively by the minority, in due course.

Nathan Bostock

No correlation to the, in terms of the number. Again, just providing background, I mean when we did this we looked across the bank as a whole, in terms of the profile of the assets and the impact that they have, we actually took the whole balance sheet as it was, we used various filters, so think about it putting stuff into a hopper and actually that came down to around about 100 billion that we then again started looking at in more detail with more different tests. By the time we actually came down to it this was the actual asset pool size that made sense against the criteria of what we were trying to do, which is to manage both the, let's call it the stress losses, but also just the natural higher risk that these assets had. Because the other bit of it as well, you have to think of it, if you just did it on pure asset quality type of elements, obviously you'd also potentially could have some pools of retail assets in there. We haven't, we've focused this in the broader wholesale and I'll call it SME type arena. But we've also cut it off so that we're in a position where we've retained our clear natural ability to build our franchise in the B&C and SME markets. So again, a number of different filters we've put there but it wasn't driven by EL minus P.

Mike Trippitt – Numis

Can I, sorry, just ask a cheeky follow-up? Have you, it may be in the detail, but have you given any pro-formats on the gross leverage impact of this, or can you?

Nathan Bostock

I don't think we have, no, we haven't. No, certainly by the year-end we'll be giving full information in multiple different ways for people to help, but sorry no, not at this moment.

Philip Hampton

Okay. Why don't we go nearer the middle here?

Chintan Joshi – Nomura

Thank you. Chintan Joshi from Nomura. I will kick off with a soft one for Ross and with further detailed questions. You mentioned in your priorities, resetting relationships with regulators. What elements do you need resetting and how will your approach differ from your predecessors?

Ross McEwan

Well, I think we've just got to start with the realisation that the government owns 81% of the shares in this business and we need to be having good, firm conversations with them about their views but also we've got to run this bank. And I think what we've had over the last four months has been very constructive conversations with a wide ranging group from HMT through to the PRA as well which I think have actually brought us into this position of being very comfortable with what we're putting forward today. Those relationships have been strained and my aim has certainly been, in my first month, is to get the parties together to have good conversations about the future of this bank.

Chintan Joshi – Nomura

How do investors get comfort that politicians won't be calling any more shots at the bank?

Ross McEwan

The politicians haven't been calling the shots on this bank. The issue for us is we just start to need to have a good conversation and understand that strategy for this bank going forward is going to be quite different to what it has been for the last five years. The last five years has been putting it into a safe and secure position, we now need to actually grow a bank again and get rid of the distractions. I mean, this senior team unfortunately have had to deal with a lot of distractions and the moves we're making here, for me, are saying, that's 10% over to the side, let's get on with the 90. And I think that's got to be good for everybody.

Philip Hampton

The starting point, if I may add, is company law. Under company law the duty of the Board of Directors is to act in the interests of the company and shareholders taken as a whole. Those are our legal duties and we're very careful to discharge them in that way. Of course, there's a practical reality here, we have one gigantic shareholder who put in a huge amount of money to rescue the business and we need to take their views on board very carefully. And there are some areas, particularly the composition of the Board, where they have a direct legal lockers themselves. They can decide if they want us or they want us to go, pretty much at any time. So, there's no doubt that these are complex relationships to manage. Nobody would ever design a business with its ownership structure, we all know the reasons why we're here with this particular ownership structure, but we recognise, Ross recognises in particular, it's very important to make these relationships work.

Chintan Joshi – Nomura

Okay. A couple of details on, perhaps one for Nathan. If I think about the old plan versus your new plan, the old plan allowed you to spread losses over time and have you seen instances in the past, for example, RMBS where given time and recovery, you can get out with profits. So I wanted to understand the new mix of the Internal Bad Bank, is it those kinds of assets where fair value sits so much below book value that we need not worry about recovery after you've taken these impairments or is there any scope in the short horizon that you could still have something coming back to shareholders after having taken those losses up front?

Nathan Bostock

Well, again, this is based on the risk of the assets and their performance under stress. So, again, when we're looking at different assets you actually do also have to consider where is the asset today in terms of its value. So, we've looked at each of them, if we think that something remains a high risk asset, then it will be in there. If something actually doesn't fit in terms of our expectations of expected loss because it's already at a level where we feel it's a good value, then it won't necessarily fall under the same criteria, in other words, when you stress it you actually don't end up with a significant loss. So this has been driven from an overall move from here, expectation of losses.

Chintan Joshi – Nomura

Okay. And final one is, on slide 14 you give us 2 billion release of capital on the fully loaded Basel III number and you give us one and a half billion costs, so, I assume half a billion annualised, what does that 2 billion, really where is it coming from is DTAs and ELs, and on costs, should we expect that half a billion reduction, by what point should we assume that cost reduction?

Nathan Bostock

Sure. Yes. So firstly, the costs are in relation to the actual running of this operation, so there'll be a mixture, as I say, of income funding costs, etc., and also the operational nature of it. So, those again, will reflect what we do to manage these assets over time, manage the size of the unit that we're using. So, again, it won't be constant across the period.

If you think of the 2 billion, the easiest way probably of thinking of the 2 billion is to go back to the original 11 that you've got tied up and then build the stack that gets you to the two, and the stack that gets you to the two comes from the 4 to 4.5 billion of impairments upfront, the 1 billion of impairments that you incur over time, the incremental cost to dispose, the 1.5 to 2 billion and then these other costs. Take all of those, add them up, take them from the 11 and you'll get the approximately the 2.

Chintan Joshi – Nomura

That's the upfront capital accretion assumption effectively.

Nathan Bostock

No, that's the one that will come out at the end of 16. The upfront one is actually a very small ten basis point hit, which is the differential between the impairments you are taking upfront and the EL minus P changing, the offset. That's why, as I say, it's actually a very sensible thing from a risk perspective and a capital point of view.

Philip Hampton

Can we have both barrels back there; there are two gentlemen with obviously very, very good questions.

Tom Rayner – Exane BNP Paribas

Thank you. Super, super questions. I'm Tom Rayner, Exane BNP Paribas. First one please, Nathan, just a bit more colour on the assets transferred out of core into Non-Core. I'm just trying to get a sense of what the impairments on those assets would have been if they'd stayed in core, just trying to reconcile back to what the incremental costs of the accelerated run-down really is. And, I guess, supplementary to that, if the incremental costs are in the 1, 2, 3, billion area, how is that actually better for shareholders than just having the capital tied up unproductively even for a little bit longer? So, I'm just trying to understand that issue a bit better. And I have a second question on the new capital targets, please.

Nathan Bostock

So, can you just go back, sorry, I was just thinking of the answer to the first one?

Tom Rayner – Exane BNP Paribas

The impairment on the assets, which were in core to now be switched.

Nathan Bostock

Yes. Let me just do that one. Yes, if you look at it I think, again, we haven't broken out all of the guidance on this yet and we will do by the year-end. We have put the assets that are being transferred; there is a more detailed schedule in the IMS, near the front of it, which will explain that for you. I said roughly 50% to 60% of the impairments are out past three years and if you look at the split of the 13, 16 period, it's roughly two-thirds Non-Core, one-third core. So hopefully that covers that one. Sorry, the second one again?

Tom Rayner – Exane BNP Paribas

That was the supplementary to the first one actually. How is that better for shareholders than the original take a longer time? I understand your point on the stress test maybe but...

Nathan Bostock

Well, as I said, I think, again this is our calculation and of course there's a number of different assumptions built into them. But we believe, that broadly from a shareholder point of view, this is broadly neutral or slightly positive, that's in a pure just shareholder point of view. But the other benefits that this brings in terms of basically the clarity and simplification of the organisation, I see this as about strategic change that delivers capital strength, it delivers risk reduction and it drives massive simplification. Put those together and say that against a broadly neutral shareholder value, this to me has to be the right strategic decision.

Tom Rayner – Exane BNP Paribas

Okay, thank you. Just on the new 12% or higher capital ratio target, you're talking about the PRA consultation. Can I ask you firstly, what assumptions are you making in terms of a voluntary buffer over and above the minimum level, whatever level the enforced distribution restrictions cut in under? I'm just interested in what you think is appropriate for banks to build in over and above whatever the PRA says is the minimum. And just on the dividend access share, I hear what you say about discussions, but I'm not sure that meeting that 12% plus is going to leave any room for dividend payments anyway, so are those discussions really of any relevance? Is there a possibility of paying dividends I guess in the next few years, is my question?

Nathan Bostock

Do you want to pass the divvie one back and I'll just cover the first? I'll do the first and end bit because they're linked. Actually we said we'll target circa 12% at the end of 16, but what we've also said is that we would expect that it would increase beyond there. And one of the reasons, again, that it will is because obviously we are only really starting to get the final part of the Citizens IPO coming through at that point in time, so, our target is circa 12, we would expect it to go above that post at 12, that clearly then helps from your point of view in terms of the question about capacity.

In terms of buffer, that really has to be an individual company choice. Clearly you're going to want to operate with what you think is a sensible buffer not to fall below your target ratio and clearly given that the regulators these days have a variety of techniques now to intervene in the management of the organisation, my view would be you've got to run a sensible buffer.

Ross McEwan

Just on the DAS, we've been thinking about the timing, which relates to the dividend piece of, when do we take, have the DAS removed. Whilst I'm not going to give you any indication of when we're assuming dividends, we have had negotiations regarding the DAS thinking that it's going to be in an extended period of time before dividends are taken, so we don't consume capital in that time, but as I said, the negotiations are well and truly at a concluding stage and we'll be able to announce those, I think, sooner rather than later. Thank you very much.

Philip Hampton

If you pass it directly behind, but in the meantime can I ask the operator if there is anybody on the phone who wants to ask a question?

Operator

Thank you, Sir. We have a question on the line from Raul Sinha, JP Morgan Cazenove

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Raul Sinha – JP Morgan Cazenove

Hi, good morning everybody. Good morning gents, can you hear me?

Nathan Bostock

Yes, we can. Yes.

Raul Sinha – JP Morgan

Excellent. Can I have two areas of questioning please? The first one is, how much of your capital buffer within the 12% that you're talking about here, is down to litigation risk? I think the Chairman mentioned that in his opening comments.

Nathan Bostock

So again, what I've done in this, I'm not going to give any specific number, but what I have done is, my belief on this is, if you're going to set your targets, what you should be doing is modelling multiple scenarios that actually allow you to have a high degree of confidence that you will actually be at those. And so in the scenarios I've actually modelled a variety of outcomes.

Raul Sinha – JP Morgan

Okay. But is it fair to assume that you have used a certain higher amount of buffer because it looks like you're arguing your PRA buffer is above the summation of the capital funds duration and your G-SIFI buffer, and some of that is down to litigation risk, is that a right conclusion?

Nathan Bostock

No. I would say again, my target is 12. I've tried to illustrate why one would want to run at certain levels rather than try and insinuate that the 12% equals our ratio. And again, my view is that if you're going to do sensible capital planning and you're going to have a reasonably high degree of confidence, then it's true that litigation conduct and clearly reg change are three things that you ought to be doing a variety of modelling for.

Raul Sinha – JP Morgan

Okay. And the second one was just around Citizens again, and firstly, I just had a point of clarification on slide 15 where you outline the improvement in your return on tangible equity as a result, I think, purely of the IBB of 90 to 120bps. Can I just clarify that this does not include the dilutive impact of full disposal of Citizens?

Nathan Bostock

That's correct, this is just the IBB.

Raul Sinha – JP Morgan

So, my number is, most of this positive is more than offset by the negative from Citizens. And related to that I was wondering if I can ask Ross, just I'm really struggling to understand your decision to make no changes to your Markets division, which is a single digit ROE business, and dispose fully the Citizens business, the double digit ROE business to improve your capital. But just if you could just outline your thoughts on what we should expect in terms of group shape going forward.

Ross McEwan

First off, the business is in major transition today against a plan that was set 12 months ago and performance against that plan. So that's the first thing we're looking at. Secondly, all our business is under review for the February strategic review, which looks at all, parts of our business from a customer perspective. So, nobody escapes that one, including Markets. But we won't be coming out with any other announcements on that until the February time, as we work through each part of our business. So, that's the reason why, I mean, why go through major shocks of a business again and again, this team needs to actually get time to actually deliver the strategy which… and they're doing a very good job against it. And all businesses reviewed February.

Philip Hampton

Okay. Can I ask the operator, any more on the phone, and then we'll come back to the room.

Operator

No further questions at this time, Sir.

Philip Hampton

Okay. Thank you.

Alastair Ryan - Bank of America Merrill Lynch

Thank you, it's Alastair Ryan with the Bank of America Merrill Lynch. I'm just trying to reconcile slides 11 and 13 because it's quite rare that you do get companies saying their old strategy was to optimise cash recoveries on a portfolio. I mean, is this change driven by the fact that you'd have needed a 120 basis point higher capital number if you hadn't done this and you just couldn't get to it without these changes? So, actually we're pivoting back we're not pivoting back from, in effect, the pressure from an individual shareholder, we're pivoting back from where the regulators got to on the way that it's changed, the way that it looks at concentration risk and stress loss and so on.

Nathan Bostock

Yes, my point here is, I think the landscape for UK banks is changing and it's changing because stress and higher risk assets and the consequences of those under stress conditions, based off the fact that you didn't have an idiosyncratic stress, clearly is going to mean that those things are going to look even more capital consumptive in a go forward position, and if you are not taking forward action now over a two, three, four year period then by the time you get there it will be too late.

Ross McEwan

I think it also shows why I put forward one of the early priorities was to resolve our capital position with the PRA, because lots of change going on from a regulatory perspective and we needed to understand those as we were looking at the full capital position of this bank.

Philip Hampton

It is also one of the things that the Board was most focused on, what are the shareholder value implications of this accelerated run-down, and we specifically confirmed with the PRA that the judgements that Nathan's making, assumptions that Nathan's making on the stress buffers, are shared by them.

Alastair Long - Bank of America Merrill Lynch

Just to clarify the T NAV and the earnings impact of doing this are really secondary to the hard constraint that you face, which is, that there just wasn't enough capital in the bank under the new rules to run it as it was being run before. Is that…?

Ross McEwan

One of the biggest issues for me coming in was how do we strengthen our capital position so we just don't talk about it again? As I say, liquidity is not an issue, we don't talk about it, capital in the banking industry is a major issue and we need to resolve that, and from that we built our plan going forward. So, that's the starting point.

Nathan Bostock

I mean at the end of the day as well, once you get past that, when you get to that point in time, why would you want to be holding lots of capital tied up in these effectively defaulted and low ROE earning assets, you want to put it to work.

Philip Hampton

Why don’t you just move it along?

Michael Helsby - Bank of America Merrill Lynch

Thank you. It’s Michael Helsby from Bank of America Merrill Lynch. Just to come back on what you just said there Nathan, why would you want to hold a lot of capital? I mean, essentially what you’re telling is that you’re blowing up 9 billion of 11 anyway, so you’re giving away that future upside that may or may not have been there, so, I don’t really understand the point that you’re making, but that’s not the question. So, three questions, if I can?

The first question is, just on the 1.5 billion of costs, so I understand it correctly, so, that’s an after revenue, i.e., that’s a pre-provision number? Yes, okay. The second question is just to go back to this Markets point, just looking at the Treasury, what they’ve announced today, they’re talking about a further significant shrinking of Markets, so they’re almost pre-empting your February strategy. Are they talking about the old plan or are they exactly pre-empting what you’re saying in February? And if you could tell us how Greenwich, because that’s the US, obviously a big part of markets, profitable part, how that sits maybe within Citizens, whether there’s an opportunity to bundle that together. And finally, just to wrap back to litigation, if you could tell us what reserves you’ve got currently on the balance sheet for things like FHFA work that’s been very high profile in the press let’s say, recently, and other things like the EU LIBOR settlement or other things are clearly out there. Thank you.

Ross McEwan

I’ll start with Markets again, let’s be quite clear, it is being reduced now. That was the plan for that business. All other reviews of that business will be done while we review every part of our business in February. So, no other changes to our strategy around our Markets, strategy as you know about today and any change we will announce in February but it will be across the entire business that we look at it.

We’re also looking at the connectivity of all of our businesses, and how can we get them far more connected than they are today. It’s a bank that’s quite rightly had to run in silos, we need to think about how can this run for the betterment of customers in doing more business.

Philip Hampton

Yes, I think it's also true that the change in the Markets balance sheet is currently underway, it's not done.

Michael Helsby - Bank of America Merrill Lynch

I appreciate if there's anything incremental to…

Nathan Bostock

And in terms of provisioning then we're following an IFRS approach clearly on it and to the extent that we have clear line of sight of, let's call it, settlement or anything like that, then we've already put those through the accounts and we've talked about those. In terms of the Board and litigation, I think we've got no change to the guidance we gave previously which is, we're at a very early stage of discovery and we believe that there are elements of our situation that are different to others.

Michael Helsby - Bank of America Merrill Lynch

Okay. And just Greenwich, is there a chance to bundle that back into Citizens or is that something that you just never considered to do.

Ross McEwan

Part of the review for February.

Michael Helsby - Bank of America Merrill Lynch

Okay.

Philip Hampton

Good. Okay. We have one webcast question. Okay, so I'll come over there. Which is, can you please share your thoughts on the upcoming EBA stress test and how you expect RBS to perform. And can you please give an update on the CRE exposure in the core bank and the expectation for loan losses going forward.

Nathan Bostock

Well, again I think on the stress test last time under the EBA one, we performed certainly adequately. I think again, with the risk reduction that we've done and indeed the way that the EBA carried out their stress approach previously was penal for anybody who had, for instance, a large trading business that had incurred losses and you had gradually, shall we say, made that much better, because you unfortunately had to take the whole of that previous experience into the stress test, you couldn't actually look at the position you're in today and move it forward. So, my belief is, clearly, we've come a long way since the last test, we're carrying out even further action, so, my view is that from our perspective we should be fine under that. What was, sorry, the other one?

Philip Hampton

CRE exposure in the core bank and expectation for loan losses going forward.

Nathan Bostock

I don't have those.

Philip Hampton

We'll come back to you on that, if we may. Okay. Let's go over here then.

Huw Van Steenis – Morgan Stanley

Good morning. I'm Huw Van Steenis Morgan Stanley. Thanks for your clarity around the Non-Core bank. I'm interested though Ross and Nathan, in your vision for the core business three or four years out. I appreciate you can't give us the results of the strategic review now, but if you run the slide rule, what are the kind of targets or aspirations for ROE and for loan growth in the UK that you're hoping for as you're starting the review maybe, 2017, 2018. What's your vision of the bank that far out? Thanks.

Ross McEwan

These are core parts of our franchises, 70% plus of our revenues come out of the retail bank and our big corporate bank, they've got to be the big parts of our strategy going forward and they will be. We need to be producing far better return on equity on our core businesses. I mean, we've got our retail bank that's got a very high return on equity, but even then if you take out the conduct issues and things that are coming through, it pulls it down dramatically. And the same with our corporate bank, we're pulling apart every part of our business and looking at what is it doing today and what is it capable of, as part of our February review. We need to do better on our return on equity. That's a key driver for me and the team, but also we need to start growing these franchises. We're just starting to see some growth in the retail bank coming through now, which is good to see, so, we need to be going on or slightly above market, let's not blow this thing up again, but on or slightly above market because of our capability not because we're pricing or we're doing stupid things on credit, this is the driver for me. But those are our core franchises.

Philip Hampton

Okay. We're starting to thin out a bit. Should we go over there?

Joe Dickerson - Jefferies

Hi. It's Joe Dickerson from Jefferies. I have a quick question on Citizens, and I just want to confirm, to the extent that this bank can be floated at a premium to book value, would you be able to realise a gain at such time – number one. And then number two, Chris had asked a question about the excess capital in that division and what you plan to do with that, and if you could perhaps elaborate on that, that would be helpful.

Nathan Bostock

Well, in terms of the amount of capital that is currently tied up in Citizens, yes, we recognise that the level in there is higher than it appears and therefore it's operating with excess capital, and we're holding various discussions with the relevant parties to see what we can do about it.

Joe Dickerson - Jefferies

I suppose the first part of my question is more about the trading multiple of the business. If you look and say, I believe you carried Citizens at its book value, the comps trade roughly 1.3 to 1.5 times tangible books, if you were to float at, say, a multiple of 1.2 times, would you be able to write-up that gain at the first part of the IPO?

Nathan Bostock

Do you want to take that Richard?

Richard O'Connor

It depends on how you structure the transaction. It just really depends on how you do it.

Philip Hampton

So it might be a yes, or might be a no, depending on the price. Okay. But obviously the capital planning around Citizens will form a key part of the IPO preparations. That's really the issue that's underway. Shall we go there?

Rohith Chandra-Rajan

Again on Citizens, just following up on Raul’s question earlier about the ROE impact on Citizens, so, obviously depending on the price at which you sell, I guess Citizens adds probably about 200 basis points or so to the group core tier one ratio, so, in terms of your capital target, so the 12%, 12% plus, does that include any redeployment to the capital that’s freed up through the Citizens disposal? And a second one, just on the discussions with the government around the capital structure.

Nathan Bostock

No, it doesn’t assume a redeployment of that capital. What was the other one, sorry?

Philip Hampton

The B shares and other elements of the capital structure.

Rohith Chandra-Rajan

Yes. So along with the DAS comment, there’s also a comment about discussions on simplification of the capital structure. I was just wondering if you were able to give any more detail on that in terms of what’s going on over time?

Ross McEwan

No. Other than to say that we are trying to simplify it and normalise it as much as possible, all in the one discussion.

Rohith Chandra-Rajan

Thank you.

Philip Hampton

Smack in the middle.

Jason Napier - *Deutsche* Bank

Good morning. It's Jason Napier from Deutsche. Two please. The first, you, Nathan, spoke about CCAR++, obviously that's something that we have to look forward to next year and I just wonder in that regard whether you have any line of sight at all on what the hurdles are or indeed what your capital requirement would be under the CP today assuming it landed with the asset mix you have. Obviously the announcement today is a very significant change in outlook for charges in the next quarter, and they need to explain that I guess more broadly when the right-offs come through. I just wondered whether you're going to publish what you think your CT1 requirement would be under the CP, you're the only bank that's talking confidently about it landing in much this shape, so I wondered whether you could give us a sense as to what's at stake here.

Nathan Bostock

No, I mean we don't have a specific line of sight of the outcome of where the PRA will position themselves, but I can say that they're fully behind what we're doing and we've had very constructive conversations about it.

Jason Napier - Deutsche Bank

Perhaps put it another way then, the 12% that you're hoping to hit in a number of years time, are we right in interpreting that as a CP plus a buffer number, assuming you've de-risked in the way that you've envisaged in the plan?

Nathan Bostock

I think the way you should think of it is that our target is to be circa 12% at 2016.

Jason Napier - Deutsche Bank

Thanks very much. Next question…

Philip Hampton

Nate has been dealing with politicians.

Jason Napier - Deutsche Bank

Yes. Thank you. Second question for Ross. This week we've seen a large European bank face a very significant increase in capital client and operational risk, given your heritage in the retail business and the IT failure last year and the fact that you flag IT as one of the things you're reviewing, I just wonder whether you had any thoughts about core platform replacements and the investment that the firm might need over the next few years in that area. Thank you.

Ross McEwan

We are looking at that as part of our February review and it sounds like everything is going to February but that's a big part of the business of how do we connect our IT with our customer businesses. There's a lot of spend going on in the business at the moment to remediate from the IT failure that happened 15, 16 months ago. A lot of that is not just for resilience but also to give us some more capability and capacity inside those systems. Most businesses core systems are pretty sound for a long period of time, just like ours, but it's what you put on top of them that's more important and that's where we've been concentrating our efforts and I think will show benefits over the next two to three years. I'm not a great proponent of replacing a core system in a bank. You have to have lots of courage more than capital to do it, having done one at CBA, so, I think we're better off spending money elsewhere and fixing up some of the applications that are connecting and then, let's say, it's a far too complicated business which then puts risk into it.

Philip Hampton

This is a second bite.

Michael Helsby - Bank of America Merrill Lynch

It is yes, sorry, I just want to tie together a couple of things, answers that you've said. It's Michael Helsby from Bank of America Merrill Lynch. I'm just interested in, Nathan and Ross, on the Citizens piece and the FHFA piece because there's talk of surplus capital that's clearly there. Could you just clarify if the FHFA potential liability, does that sit with the Royal Bank of Scotland Group or is that in any way linked to Citizens, I think that would matter for an IPO?

Ross McEwan

It's not linked to Citizens, it's with RBS.

Michael Helsby - Bank of America Merrill Lynch

Okay. Thank you.

Philip Hampton

Okay. Shall we go into the middle? And then this is the last one I'm told.

Ian Gordon - Investec

It's Ian Gordon from Investec. You'll be glad to know they're two very soft and easy questions then. I'd just like a little bit of comment on the Large report and what near term scale and pace of change we should expect to see in balance sheet given the still challenging macro backdrop to that. And then in retail, you've already talked about your 2017, 2018 vision, understood you referenced that in Q3 we've got half a billion of customer loan growth but unsecured products are still shrinking. Again, just a little bit of context in terms of the near term scale and pace of change, also referencing mix and what that does to your near term margin expectations.

Ross McEwan

Let’s start with the retail piece first. I see reasonably good growth in the home lending market. You’re starting to see the economy start pushing some of that through. Our problem has been we haven’t had enough capability in the organisation to actually take up enough of that growth, we’re just starting to see it come through now. So certainly in the home mortgage market I would see a growth.

The lending review was again, just to reemphasise this, this was instigated by Chris and his team to actually say, how do we become a really good bank for SME lenders. It’s given us a very good focus on some of the things we need to do, some of them are already in train, some of them not, so we’ll take that report and we’ll build a plan up and it’s a key part of our business going forward and that’s what we should be focusing on. Both that and the retail bank lending, home lending, and also lending into that SME market, are core growth markets for our revenue in the future, but we do need to get them right.

Philip Hampton

Good. Okay. Well, thanks everybody for coming, particularly at such short notice, and I think if we can make this progress in 30 days, imagine what we’re going to get in February, it’s going to be terrific. Thank you all very much.
