



**NatWest Group plc**

**H1 2022 Results – Sell-Side Update**

**2<sup>nd</sup> August 2022**

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**Alexander Holcroft, NatWest (AH)**

Good morning and welcome to you all. Just one very quick point to make. I think what we will do is Katie will start with some introductory comments. We will then take some questions in the room and then we will take questions online after that.

**Katie Murray, NatWest (KM)**

Lovely Alexander, thank you very much. Good morning, everyone, and thank you for joining us today in the room and also on the calls. Joining me today is Donal, so thanks to him. I think he might be in Greece, but he might not be. Portugal. Yeah, I obviously didn't pay well enough attention to my staff holiday, sorry Donal. Matt Waymark who's familiar to you all as well, is joining us in his new role, he's a finance director for Commercial and Institutional business.

I must admit I thought I had Stuart Nimmo as well, but you may see his face appear as well. As you know he is the finance director for the Retail business as well. And of course, there he is, hi Stuart and I've got the IR team with me also, this morning, before we open up for questions, I should remind you of our updated guidance.

So first, revenues, we now expect 2022 income excluding notable items of around £12.5, up from 10.1bn in 2021. The year-on-year interest rate benefits through the managed margin and structural hedge adds around 1.9bn. You then need to consider the impact of lower mortgage margins, which will partially offset this. We also have additional net benefits of higher average lending volumes and higher non-interest income.

This guidance is underpinned by our assumptions that our UK base rate increases to 2% by the end of the year and stays there. UK stock rates remain broadly in line with where they were at the end of June and leading to net interest margin above 270 bps for the full year. Secondly, on costs, we expect other operating expenses to reduce by around 3% in 2022 and then to keep broadly stable in 2023, with positive jaws.

Thirdly, on impairments, we still expect to remain below, through the cycle level of 20 to 30 bps in 2023. And now expected to be below ten bps in 2022. Which compares to just one basis point for H1. And fourthly on capital we reconfirm our guidance, and as you saw on Friday, we've stepped up the pace towards our year end 2022 target of around 14% and expect to be within our 13 to 14% target by full year 2023.

Taking all of this together, we expect to deliver a group return on tangible equity between 14 and 16% in 2023. And with that, I will open for questions.

**Omar Keenan, Credit Suisse (OK)**

Hi. I just wanted to explore a little bit, I know we started to talk about it yesterday on the 14 to 16% RoTE range. Just wanted to hear in your words, what the difference is between the 14-16, can you do some, sort of back-up of the overload numbers, on what the income statement might look like and if the flex was of revenues, it looks like something like 13, 14. I was just wondering, what's the variability to deposit betas possibly to say another event assumption to get there.

**KM**

Yep sure, I think that was about 4 questions all rolled into one so if I get lost along the way, you can help me, I'm sure someone else can come back. I'm also going to start at the end and work my way kind of forward. So, if we look at the kind of 2023 income H2, 2022 implies an income of around 6.6

bn, which then implies kind of 13.2 bn annualised. What I would say as you look at that 13.2 bn, you need to think a little bit about the lending volumes, further run rate of interest rates changes that comes through in 2022. Clearly whatever happens in the second half the year, has an equal kind of impact as we go into 2023. Further structural hedge income growth, that would be, we suspect more from the roll off and roll back on. Last week you talked about the 35 to 40 bn was rolling off and it's at about 75 bps to be rolling on around 250 based on that kind of numbers today, we don't particularly envisage a great growth in the size of the hedge. I know we did a big upgrade upscale of the size in Q2, we don't really envisage that going forward unless we see really significant movements in deposits, which again, we don't really anticipate. And then as I say, a bit of headwind against the mortgage margin in terms of that piece. We've assumed that the rate gets a 2% and stays there. We think we could all make lots of demands, well that's quite conservative in debates, but that's big word in terms of our assumptions and for the 14 to 16% as we move through from there.

Now if you go to the 14 to 16% the variables, obviously, exactly where income kind of lands, is a key one. I think other things to think about is Ulster, we would hope that we would deal with most of that 9 bn of credit related RWA's this year.

We've said that most of it will be gone by the end of this year and dribble into, sort of 2023. So, the timing of that, will kind of move around a bit and then obviously there's the OP risk which we'll kind of go through in terms of that. In terms of any relative deductions, we're not expecting anything else, that you would have any particular impact on that side of things.

Impairments we have reconfirmed our guidance of the 20 to 30 and be below that number, that's clearly a variable that today we feel that's a good view. You know, let's wait and see, I do see we'll get into that a bit more as well.

**OK**

That's great, and the deposit be to assumption...

**KM**

Sorry, so the deposit to be, forgive me, so what we've always said is that as interest rates rise, you'll see more pass through, coming through. We've pass through about 15% of the 115 rise to date. But what you could see if you were to, kind of put down each of the rate rises to see what we've done on them, you can see that they have risen.

I talked to Q1 that we just led up to 40 bps pass through I think I freaked you all out, it was only on the last range, apologies for that. But you can see the next rate rise we did nothing sort of thing, but what we've kind of worked on that we think it will kind of start to rise and settle at that 50 bps and what will actually happen will vary a little bit on what's kind of happening elsewhere you needn't be surprised how little pressure we actually get on it as well from regulators and things like that.

There's a lot of liquidity in the in the system. So, our illustration is done on a 50% pass through.

**OK**

Thank you

**Perlie Mong, Keefe, Bruyette & Woods (PM)**

Heya, just two questions from me. One is on M&A, so obviously there is now...

**KM**

I am not going to buy Quilter...

**PM**

No, it's more broadly, now that you've done the special and you're obviously a lot closer.

**KM**

No, I mean, we've always been, we've been quite clear on what we want to do. We have our M&A team that is around the corner. I'm actually not sure how many of them there are because they come in on different days. But it's not a small team. There must be like 50 or I actually have no idea how many there are that's quite embarrassing. Anyway. We've got an M&A team around the corner. We do look at things, you know, regularly we really prefer things that are adding real capability that we don't have and we are adding things in volume. And if you look at what we've done, they've all been quite small in reality, but it was still really important to us. It was a very small acquisition, but it filled a gap and it allowed us to accelerate a piece of development we were doing internally by about a year. We've seen the real value of that.

So now we've got a pocket money solution which, you know, pissed me off quite a lot when my child was old enough to get pocket money I have to go and get GoHenry, because what we had internally was rubbish so thankfully we now have our Rooster card, so that sort of thing. So, I think that was really important. Or, we've done things like looking at mortgage books so we can consistently do that.

We do think that we we've got more space that we can grow in kind of unsecured and in wealth, but it's something we continue to look at, but I don't think what we've done in terms of our share distribution that's closed the doors on any of those kind of actions at this point, but we don't comment on press speculation.

**PM**

So can I ask you one more, so philosophically as more of a philosophical question, just speaking to clients it feels like a number of people in the market think that this is as good as it gets for banks if rates go up any more is going to be a credit cycle, if rates go down because recession fears that it might just get crushed again, but yet the share price is still where they are. Do you think this is as good as it gets? If not, where is the catalyst going to come from?

**KM**

Lex brought a really nice column I thought on Friday, and it was a little bit around how does NatWest make sure it has a good crisis? You know, I hate the word crisis I'm not sure if we're in a crisis or not or things are just a bit difficult, you know, and I think the thing about it, what we're really focussed on, we don't think rates are going to go down over the next year to eighteen months.

We think we've got 2% of flat and then you can see that everything starts to tail off 24, 25. Donal would tell me: Katie, we can't see that far, no one can see that far. You know, we do obviously see that it's going to go up a bit more, so we'd expect that to improve. I think we've been doing a lot of work to improve our loan investment income and non-interest income sorry.

So, I think that's something that we are structurally weaker in, I think we're all very aware of that, and actually how do you make sure that you've dealt with the issues of Ulster, NatWest Markets hopefully is kind of behind us as well, and that you're actually really focused on that non-interest income. So that's things like how to get tails and pate work in terms of some of those newer

products, we're doing quite a lot of work and wealth management, we've got some early successes, volatile markets make it hard to do work in that space. But if we look at our net cash flows coming in as a percentage of our AUMA, it's like 7.9%, that holds itself up pretty nicely against many of our peers. Small numbers, of course, but actually how do we make sure that we really get those things in so, we're really focussing on that non-interest income side of things so that as you see the interest rate coming off, which will do eventually.

I'm very aware that if we had this meeting about a year ago, we'd all be panicking about negative rates and actually, so things do change quickly in terms of that piece. But as you see it coming off that we've kind of built some of the non-interest income to kind of try to deal with that as we go through.

I don't think the economy's powering yet, so we are all very clear on that. So, if I think look at businesses investment and if I think of the conversations I've had almost since the Brexit vote, we're waiting for this to pass, we're waiting for this to pass... sort of thing. And we can see the companies are beginning to open up their lines, they're beginning to think about what to do next. We do think that climate is an extraordinary opportunity in terms of, sort of, renewal of lending facilities, and renewal of activities. So, I think those things do all kind of combine together.

**James Invine, Société Générale (JS)**

Katie, can you talk a little bit about credit demand on the retail side, please, so we can see your numbers that you reported. But you changed your underwriting standards that sort of made it tougher for people to get credit. And then in particular, on the mortgage side, what we've seen is mortgage rates move up quite a lot. What's the customer reaction to that? Are they just trying to set that to longer term mortgages or are they going for a small mortgage loan connected to income?

**KM**

I'm going to actually get Stuart to jump in and then Stuart I will add anything afterwards. But he's very much the call face of a lot of that activity.

**Stuart Nimmo, NatWest (ST)**

Yeah, of course, thanks. Excuse me. Thanks for the question. Yeah, so I guess if I put it in terms of what we've seen over the course of the first half, we've seen a very robust mortgage market. In Bank of England data shows on average £25 bn of completions in over the first six months of the year. We have seen a little bit of a tail off through July in CACI application data and as I look forward.

I think it's probably fair given the headwinds that some customers are facing around affordability, that we would see some softening in the mortgage market from here and likely a shift from purchase to new mortgage, in particular we've seen a little bit of that over the first half of the year in terms of underwriting standards. I mean, I would note yesterday that clearly the Bank of England or FPC required stress rates were formally removed.

And I'm not going to speak in detail on that, but we are in no rush to remove stress on the mortgage book at this stage, we have made some adjustments, but nothing dramatic to our underwriting standards from that affordability perspective remain. I would say robust and I think we've spoken about how we deal with affordability through the first half of this year.

But essentially, we have been uplifting, application applicants' expenditure in line with our ONS basket of expenditure depending on exactly what the demographic is in order to capture the impacts of anticipated inflation increases. Whilst not increasing their income. And of course, the book has

continued to be stressed from an interest rate affordability as it has been up to this point, given that the guidance was only removed yesterday. So, I think from an underwriting standards perspective, very, very safe, is that helpful?

**JS**

Yeah, great. Thank you.

**KM**

Thanks Stuart

Other questions in the room?

**Simon Adamson, Creditsights (SA)**

We all know that we're heading into quite a sharp economic downturn here, possibly a recession and rising inflation, rising rates, you and I think just about every other bank in Europe at the moment don't seem to be seeing any material signs of stress in the loan book. Do you think this is just because it's too early, or are your clients actually more protected than we might think from the economic downturn that we're going to see? Because at this stage I thought we might have been seeing, for example in stage two loans, more evidence of stress

**KM**

In fact, what you saw this time in our numbers was stage two going in the other direction. We bought back sort of, you know 568 million of associated ECL in that space, it's part of the whole kind of overall move so in the half. I think it's a few things at play. One, we're prime lender, so we've obviously made big losses in the past as well. So, I think we've reshaped our work a lot. I think over the years, particularly in the commercial space we're taking a lot of that down, though you can see if you go into the detail of the sensitivities where we split it out across mortgages and non-mortgages at property and non-property, you can see the property in the base case sorry the extreme downside does stress a bit worse than you'd expect that in terms of that piece. So, I think there's that. People have a lot of money, and a lot of deposits sitting on their accounts. You know one of the things I look at you know the BBL loans are obviously they have the guarantee behind them that process is working well the background, but I look at the associated lending on the BBLs a lot and there's a table in the accounts which kind of shows you what's happening on BBLs, in terms of moving into stage three, which is obviously covered by the guarantee but then what's happening on the associated lending and it's still really strong. So we know that BBLs they could, 24% of them could be repay them tomorrow if they chose to, in terms they've got all the cash sitting on their balance sheet, we can also see that people are still kind of they're still spending, but they're not spending on the real kind of.... They're not using their credit cards to pay for a lot of groceries, that spend is actually down, which, again, you would expect because we're always home so now we're not. You don't see electricity going up on credit cards, you don't see people taking cash out on credit cards something that we all kind of early signs. You know, we spend all time looking at who's going to be monitoring, who's going to roll in terms of those kind of special measures within the commercial space. That's just pretty low. So, we're seeing so little space. It's incredible. I think for us, we're not prime lender. People have got a lot of backing. I think also during COVID with people very worried about the financial situation, many of them learnt tight budget a bit better in terms of that side of things. But I also think we'll see it coming, which is why we then we also added into our own PMAs, we, we added been the way that I think I said this last week, but we released about 200 million of COVID provisions, we added about 260 million of cost of living and so supply chain as part of that

number for PMA's which didn't really move but there was a little movement going on in it within the within the background of it. So, it's but it does feel it will be it'll be harder. I think the thing, though, is unemployment is the most important factor for us. And in our accounts, we gave you a kind of what happens if you're the single unemployment factor and the impact that that would have on ordinary payments, and things.

It wasn't it wasn't significant either in terms of the numbers. But so I think what we see today and, you know, you read the papers, you listen to radio for when you wake up in the morning or Chevron station, I guess, and then you just hear, you know, your bills going up to this and that. And actually, there's a lot of fear saying what we're doing a lot is where we made, you know, donations to our partners Stepchange and I always get that wrong, I think is the Moneywise. And this is the Advice Bureau, which is basically have them and we know that they're really busy. I do a lot of work with the money pension scheme as well. We know that they're really busy in terms of all of their affiliated organisations.

So, people are worried. The people that are struggling though are not people we have lent to and that say they kind of reality. And because our credit cards are our own book, that also gives us a little bit of comfort as we move forward from here. Joe.

**Joseph Dickerson, Jefferies (JD)**

Thanks. Can I just ask just on our on a related point, because I think a lot of investors seem to think that they set it out for Q1. Next thing. And after Q2, we'll know by now people know what's happening with credit for most, most for most indicators, it's really about unemployment, as we said. Could you just discuss it seems to me like banks such as yourselves are far more proactive on the corporate side in terms of helping your clients to think through what's happening than, say, 15 years ago. And so maybe if you could discuss some of the things you do now versus then, it would be very useful because it just seems as having looked at companies, these kind of companies for a long time, it seems like the way that you are engaging in a fairly proactive way with the corporate customer is completely different and everybody wants to go back and look at prior cycles.

So, if you can just elaborate on what's different, how you engage with the customers where there might be signs of stress today or so, I don't mean on the consumer side, those are discrete portfolios. That's macro different. On the on the bottom-up corporate side, that would be, I think, incredibly helpful.

**KM**

You know, I think we have changed a lot, Matt, do you want to jump in on that question and then I can.

**Matt Waymark, NatWest (MW)**

So, I'd say probably the fundamental USP for our commercial bank and our business bank is that we have a really good, solid network of local relationship managers. You really know their businesses and that is where we get a huge amount of our knowledge from. But the thing that we have also done a lot recently is the huge data.

So, we use a huge amount of data and analytics to do a lot of predictive work with our customers and that's with our data and analytics team and so on. It's all about feeding into those relationship managers a good idea of what is the next best action for your customer. So yes, you go your customer really well, but actually if we take the sector wide learning.

So, if you're in the agriculture sector, that bit of a perfect storm of fertiliser prices going up, hugely hard to get people to work on your farm. You've got just transition. You are very carbon intensive sector. There's a huge amount of competing pressures on sectors like that. And so, we have some real good agriculture specialists who then feed across into the local areas and that really is what it comes down to here.

We've got customer hubs, we're very proactive with engagement and I think, as you say, we've learnt over the years that it's much better to be proactive upfront than it is to wait for our customers come to us. And we've done a lot of changes in the commercial bank over the years, but the thing we've always tried to reinforce is the power and the sort of value of those local relationship managers.

## **KM**

And I think that next best action is really important because it used to be the next best action would be left to you to work out what it was for your customer and actually what we do not towards touch feed you say in your sector, and we talk much more about what's the next best action. So, there's pressure on the relationship managers. I'm going to actually provide the next best answer. I can't sit there.

I also think if you go back a number of years ago, we all have our friends that we like. We all have people in the office that we chat to that we naturally just get to and we go to. What I think we have done with our relationship managers is that we know much more, as now we know exactly who they're talking to, how long they talk to them for the visiting, who they're not visiting, who they should be visiting, that they didn't visit and things like that. So, I think those things are much more part of it. And I just I think the whole coming up all the way from what we do with the accelerators at your brand, your department coming in, that kind of takes you through that journey is just it's much, much more active than it used to be in terms of that piece of the data, I don't think can be understated.

So, if I look at how we did the PMA piece and this time around, the PMA is split retail and commercial for retail, we looked at who did we think in terms of their outgoings would be hit by energy price increases in October, but then on the supply chain side, we could go through which sectors did we think we're going to be hit by

different movements in PDs and all that sort of stuff. And then you could go through in a lot more granular detail. I couldn't do that two or three years ago. I mean, that's been a massive change in the last that's all that we can actually go kind of sector by sector and actually stress them for different events happening to them.

It doesn't mean the data is perfect, but it is definitely directionally correct. So, we go to Guy on a phone and then we can go to Martin, will come back to you. Morning, Guy.

## **Guy Stebbings, BNP Paribas (GS)**

Morning. Katie, apologies I couldn't be there in person. I just want to stay on impairment question and ECLs because for a lot of investors, they really, really struggle with the idea that the net cost of risk is going to be below normalised this year and next, given sort of the macro outflow that we're looking at. I mean, if I look at the guidance in terms of the extreme downsides, I mean, from a macro perspective, it looks very conservative assumptions, but it spits out a less than 1bn uplift in ECL, which doesn't seem particularly large in historical context.



So, I just wanting to sort of focus on the corporate side, how you treat large corporates where a few tall trees to fall over, I presume we would blow through that number. So could you give us a flavour around that, how you think about if you were to embed movements into stage three, I presume you must run a range of scenarios which in extreme are plausible. What sort of numbers that would spit out any colour? That would be super helpful. Thank you.

**KM**

I think it's important I think you've clearly picked up on it so that extreme downside that the billion number that I give you the 969 is for stage one and stage two. I think if the whole thing moves to those at 100% to those is that is the base you would clearly be seeing stage three and the problem, we have there is it's is very hard to estimate stage three losses. You can go there at a speed in terms of those numbers. We don't have numbers that we give we give to you on that. We don't think that extreme downside is particularly likely. I guess the reason why we get relatively comfortable is because we look at where particularly those large corporates are, where they are on cash, where they are their other facilities. We then also look at actually we do have this PMA of close to sort of 600 million. So, you kind of go, well, it's not as pretty as this wouldn't work as well as this, but you go kind of 600 million against 969. So even if I got to stage one I can kind of deal with it wouldn't obviously have to be perfect mapping, which it would be, but you kind of get there and then you go, well, 20bps would cost us thinks about seven or 800 million of losses.

So, you kind of go even to be below that cycle. And I've got quite a lot of runway for some pretty big stage threes. When we look at our commercial customers, we can kind of work our way through, which I think is why when you take those kind of component parts and think what would a 20bps number be, we're obviously saying would be below 20-30 bps that is the forecast I have given you just to be very clear in terms of the numbers. But that's so you're thinking you've got quite a lot of run on those numbers and what would you do? Do you really get to that level of darkness of economics and that's not what anyone is predicting. We kind of it's almost like the economists argue whether it's a real recession or technical recession or any of those sorts of things or there is really good and pretty low unemployment that kind of helps push through. Tall trees are almost impossible to predict because if you're predicting was them as tall trees that you'd already have them in special measures kind of idea working with them sort of thing. And we don't have that. But as we looked at it, we did the scenarios we kind of felt there was no reason to change the guidance from what we had because I couldn't see anything that would be suggesting it was different from the guidance that we had given you.

**Martin Leitgeb, Goldman Sachs (ML)**

Yes. Just two questions. One, on credit cards, it seems like the flow share of NatWest credit card, new credit card lending is meaningfully higher compared to the stock share. And I was just wondering, is the kind of run rate seen in the second quarter is the one we should look at going forward or is it in the process? And secondly, just a follow up on the deposit beta and the 50% guidance. Is any reason to believe that this would be different across personal and commercial in terms of behaviour going forward or should they be broadly the same as to where so far?

**KM**

Yeah. So, I'll do that piece, and Stuart, I'll come to you on credit cards afterwards. So, as we look at retail and commercial, they've been quite different already. So, I mean retail is kind of so 20% pass through in commercial, I would say 9% or 10%. So, you kind of get to this combined piece the other thing is interesting on commercial is, you know, for the smaller businesses, there is a 35 day notice

that we have that pays 40 bps. No one's putting their money into it. They're keeping their cash with access. 35 days is not a long time at all. So, I think people are valuing, which I guess is another sign of the concern, but they're valuing the immediacy of their cash. We're not under particular pressure from the large corporates to actually change rates and things of that because we have a lot of liquidity. We're not chasing any of those rates. So, I do think it's been a bit differentiated year to date. I would imagine it would continue to be a bit differentiated. I think one of the things Donal and I want to be a law is at what point we're in, the percentages we think is a level above the 2% that we have in terms of base rate. They start to marry much more closely together in terms of that piece. But the data has been great and we're not seeing that leading to change in terms of you want to take the first one on credit cards?

**SN**

Yeah, sure. Thanks, Katie. Thanks for the question. So, you have seen in the slides that we had our best start of the year, best first half of the year in credit card trading since 2014 I think. So, we're very pleased with that. Our stock share actually ticked up last Friday, another few basis points with a 6.6% stock share in credit cards, up from 6.4 at the end of last year. Again, pleased with that. We are, you know, versus current account market share of around 15%. I think you said earlier unsecured and credit cards in particular is a book that we are very keen to grow. We're at 4.1 bn of balances. We only went to our own customers. So, we do have optionality in that regard ahead. So, I would expect us to continue trading at around what we're doing at the moment, which is about 20% by market share and flow. Also, as I say, a growth area for us. Hope that helps.

**Benjamin Toms, RBC (BT)**

I guess my question just on the deposit beta point, when you're thinking about excess liquidity and there's lots of stuff sloshing around at the moment. When you are pricing your deposits do you take into account excess liquidity. Would you also like to keep the liquidity on the basis that you see those deposits is driving your other income line going forward that a customer who has kind of deposit with you will spend in other ways with the bank? Or do you see that excess liquidity as something that you can point out without impacts on you other revenue lines.

**KM**

I will let Donal come in if I can just say a few words at the beginning as well. So, we're very aware that excess liquidity is very valuable to us. I think it would be quite an aggressive way, which just to kind of let it slip away. So, if we saw rates going up and we've been having you'd see us taking our rates up because it is to us and it's one of those things you don't really know the law of the unintended, that once you start to move, that we've got kind of moves to moves afterwards, but we do see people managing their money. So, I think what was interesting for me, the Central retail deposits grew. It grew at the smallest rate that they had done to date. And actually, one of the debates we have is that you're a little bit at a tipping point of that. So, I think be for me, that's what I'm really interested with Q3 to see what kind of happens there. And is that the point where Joseph talked about, so actually, are we going to start seeing something there as well. You still kind of got the growth on that piece, but , Donal, do you want to talk about how we look at liquidity. And I think also to look at some of the actions we've done to try to kind of get a bit of better return from some of the liquidity, which is important over the last the last couple of quarters as well.

**Donal Quaid, NatWest (DQ)**

Yeah, no, sure. And I thought you said I think probably one thing to start with, but we don't get credit for is the strength of our deposit franchise. And I think that's probably a key driver of the income upside that you're seeing feeding through as well. But the way I would look at it, we get asked by a number of investors, you know what would you do to optimise liquidity and reduce down to levels? We have, as I said, I've actually no desire whatsoever to reduce do the levels of liquidity, given the price that we're paying for it and the value it actually brings and what it does allow us to do really over the next few years is grow our core lending franchises, you know, at a very, very cheap cost for new perspective. We're already seeing a number. Our peer has been active in securities lending markets, looking ahead to, in effect, the refinancing of TFSA me over the next few years. One luxury we have is that we have no requirements. We do 12 bn, but we have no requirement to refinance debt at all. So, it puts us in a very, very strong position as we look forward. But as Katie said, you know, there are a number of options that we have with that excess equity to actually drive that even further upside. So, for example, we've grown our we've grown our reverse repo book, which is, again, very short dated, low risk lending that just adds further upside from that from an income perspective as well. So, there's a number of options we can take. But as I said, it's very valuable. I'm very happy to sit on excess liquidity for the for the next few years.

### **Aman Rakkar, Barclays (AR)**

And it's Aman from Barclays just to build on the deposit based discussion. So, I mean, it does look like your commercial deposit base is really where something feels unique about your commercial deposit base the fact that deposit rates are so, so low feels very surprising given a lot of our corporate clients can put money into money markets and I would have thought that there was some kind of contractual rate in some of the deposit base. So, is there anything that you can tell us about? What is it about your commercial deposit base that feels so different from some of your largest high street peer banks that mean that you can extract the beta of this card? Is it because of the prominence of the SME base or the product set or something that would be question one. Two would be just coming back to Ulster. And if you could just help us think about what is the drag from Ulster that you were expecting in 2013? So, I know you've got the €900 million exit cost guidance. I'm really struggling to work out how much you book so far in H1. So, if you could tell us what's left and I guess my specifically what's going to be fair in 23, I'm just trying to think about what the nonoperating drags are to ROTE.

### **KM**

Okay, I'll take that second one and then, I'll get Matt for first one. So let me do the second one. So, I said it Q1 in one of my Q&A, so it was about 1%, right? We trade very little to date and in reality, we know we've got some big bookings that are coming through. In terms of that, I think the 1% is not wrong, but it's not there's things it could the variables that could change that was decisions that we could make that would allow us to bring cost forward. There're delays that could happen that would push it through. So, the 1% doesn't have a huge amount of science to it. But it was what I had said in Q1 in terms of that number. What we know is that and as we hate discontinued because you just end up with accounts are horrible or anything else. But so, you can see we're moving more and more into discontinued and we've obviously got that large charge that will come through in Q3 and €350 million.

So, we expect clearly that will come through and that's because the revalue of the mortgage book to fair value. So, we know that happens on the 1st of July because the accountants tell you if you read happens in the previous quarter or the first day of the next quarter, you have to book the fair value movement. So, we've got so that's one of the first kind of big charges that will come through. What

we'll start to see as we go through the late part of this year, some more of the restructuring charges coming in as well as we start to serve notice on staff and things of that. So, I mean it most the majority of it will come through over 22, 2023 and then you'll see in 23 on the cost guidance we'd give you that would be 200 million lower. And in terms of that of the coastline and then that would drive it, it's 24 before that would kind of come off in terms of everybody expect most the cost to be incurred in 22 and 23. So given the amount that's coming through in terms of that fair value adjustment, that's obviously I think we're waiting to 22, than 23. We just need to see what kind of decisions we make a little bit at the end of the year as well, which is the thing where you could end up with a little bit variability to how those come through, which is why we're giving you slightly annoying guidance of till 23, because there are a few different levers that you depending where you are and what how things are going that you might you might see to kind of pull a little bit and Matt, do you want to take the first question?

**MW**

Yes, thank you Katie. So, on a spread, especially at the large corporate end, I'd say we look at deposit margins and rates. That's very much as part of the wider offering. So obviously got operational banking, managed margin books and then you've also got all the ancillary services of knock out products. So, we look at it as part of the package. We ensure we do remain competitive, and I would say versus our large high street peers. So, we have about 80bn of managed margin deposits in the commercial. But I'm talking about the ringfence, 90% of that is at 10 bps customer rate. And that 90% is very, very competitive itself is some of our peers are still at one basis point for exactly that. But we do see some obvious non-standard rates. I unpublished rates a little bit more than us, but we still believe we're very, very competitive. What I would say is, obviously, as we look forward, we will continue to monitor that competitive position of the dialogue. But in the round, we do believe we are. And as Katie mentioned, we've got about 5% of the book is on 35-day notice period. That has not moved, we believe that to 40 bps and that's the best you could get in the market for 35 days. It hasn't moved at all in six months. We've been a good 20 to 30 bps above our competitors and nobody has got to it. So that tells us that our customers are very much at this point in the cycle valuing access over yield on deposit margins. And obviously as we continue to monitor that and talk to our customers as we go forward, that may move to maybe we pass through slightly more than the 9% that we've done to date. But I would say that the overall dynamics of that market do mean that I don't think if I'm brutally honest, we are that different to our peers at this place.

**AH**

I think we bring Jonathan in on the line, please.

**Jonathan Pierce, Numis (JP)**

Yeah. Hello. Morning, everybody. Hello it's a quick question coming back to Donal's comments a few moments ago a few moments ago that the group has no desire to reduce liquidity for the time being. In a couple of days we'll hear, as you know, from the Bank of England on quantitative tightening and Bayley's sort of indicative range that he gave a few weeks ago is £50 to 100 bn drain in year one obviously all else equal that's going to push down on the systems cash balances at the Bank of England. I'm interested in how your respond to that, given the comments just made. It sounds like there may be a desire to maybe participate on the other side of this QE. So maybe buying some of the government bonds that the government will be sorry the Bank of England will be selling in this maintain the overall liquidity position of group. Am I picking up the right sort of sense on that from you there or am I completely wrong?

**KM**

Donal, are you going to start off and then I will add at the end.

**DQ**

Yes, I'm happy to take, so I suppose the way we look at liquidity jumping across level one, we're kind of indifferent of whether that's in cash or level one assets. So, when I say retained liquidity, I don't necessarily mean retaining those cash balances at the central bank, which I suppose probably are likely to reduce down as we see QT (Quantitative Tightening). But I think in terms of, I suppose, the question around gilts, you're probably seeing you can pull out the UK bank's holdings of gilts I think are at an all-time low post GFC and there's a number of reasons I think for that. One is actually they're just not very, very attractive on a capital adjusted return at the moment versus the levels that you get paid to hold cash in the Bank of England. But also then I think one key thing, if you look at the regulation in the UK, obviously there's a strip out some leverage for holding cash balances, but there isn't for gilts. So, because they become less attractive as an asset class for a lot of UK banks and so, I suppose we'd have to see the question is would we participate? It would depend I suppose, on the pricing and on the capital adjusted return on those yields versus the level that you're getting on cash at the central bank. At the moment it doesn't look like an attractive proposition. So, you know, I think QT can play out, as I said, in the fixed income call last Friday in a number of ways. And we just have to you know, we run a number of different internal scenarios. We just have to monitor who is the marginal buyer and then what impact that has on bank balance sheet.

**KM**

And sorry, Jonathan. I would add to that, one of the things that we we've done that all of the banks have done is to actually look at our balances to try to work out who do we believe the buyers are and do we have their cash on our balance sheet in terms of that and what are we paying to them today is as you could imagine is little, given those commercial rates so obviously it would be impact, but we don't think by the time you take those numbers and you spread them around, that it's a particularly meaningful impact at this stage. So, you had something else.

**JP**

No, that's really interesting. I mean, I guess I'm just trying to get a sense as to what the net impact of QT will be on the liquidity of the overall system, because it's clearly that liquidity that's enabling these enormous deposit margins we're seeing in the moment. And clearly the buyers of the gilts is the important component of what happens to the money supply as the Bank of England starts doing more active QT.

**KM**

And I think what was really interesting is when they first started talking about QT there was a different narrative we had internally over liquidity, and I was quite on the view that it will reduce it within the certain places that are in the buyers. And the way I always think about it is that QT got into our balance sheet in many, many different ways. And then in reality, as an addition of many, many different small amounts, whether it was through furlough or whether it was through bounce back loans or delaying of payments, all sorts of different ways. So, it came in through this kind of what was a spider of lots of different things coming into the balance sheet and into people's accounts. And that will definitely not be the way that it will be sucked back out again. So, therefore the exit is going to be quite different now will be interesting is how it goes that we are actively upgrading feeds, what they what they say and then who actually starts to make some of those

investments. But the extraction will be so different from the injection that its impact will be naturally very different as well. And, I think Chris has just come on the line, Chris, good morning. Good to see you and would you like to go ahead?

**Chris Cant, Autonomous (CC)**

Good morning. Thanks for taking my questions. If I could just come back to the provisioning and ECL please, so you talked about the 260 million PMA, one of your large domestic peers, I think combines the PMA portion in relation to cost of living with what's come through to the macro modelling in terms of the inflationary inputs. I was just wondering if you could give us a comparable figure, i.e., how much of your kind of ECL modelling charge or balance is a function of the worse inflation expectation and unemployment expectations you've come through since year end, please. And then you also have announced yesterday a few tenders of Tier two bonds that there's some quite chunky ones in there. Just wondering if you could give us a steer on what we should be expecting there. In terms of the NII impact, I presume this was all baked into your guidance, but obviously it has come after the quarter, so any colour that would be appreciated.

**KM**

Thank you. So, it certainly baked into guidance, Donal do you want to take the second one? So, if you take the second question, I could come back on the first.

**DQ**

Yeah. In terms of first with the tender, I suppose it's all going to depend on the take up with we've tendered a number of these tier two's before the take up hasn't been huge. And again, rationale behind that is that there are a couple of values volumes amortised obviously 20% per annum during the last five years to maturity.

So, they're actually quite inefficient from a couple of perspectives. Hence our launched assets try and buy some of them back. But in terms of the impacts they are built in already the guidance that was that was given based on our expected to take up. So, it's not going to be material anyway. And the payback period on these securities is quite short dated as well.

**KM**

So, we haven't given you that number and it's not one that's in the case. You'll be able to pick up on it a little bit. So, Chris, if I just give you a little bit of colour on it, so we've got PMAs of 583 and they were predominantly, but not exclusively in relation to Covid, there are some other portions within them as well.

We released 200 million of the Covid provisions so that still some Covid left. And that Covid that's left, it's in the commercial space and rather than in the retail space. And that's because we do think there is still some pain that will come through. And then we added 267 sorry in terms of supply chain and so cost of living crisis for the for the retail space. But you can see in the PMA table that there's more of this in commercial than there has been the case in retail. If I look through it ultimately as part of the write off, given that the PMAs relatively stable, we had some movements modelled PMAs into ECLs. So most write off this comes through probably some of the as a blend of passage of time on the impact on the economics. But the numbers were are not significant in terms of the economic update, which is why we have a kind of shared them. So, they're relatively muted because actually both of that most of the provision release is in relation to that ECLs. So, the passage

of time a bit more sideways, the kind of impact on economics would be how I would think about it. Thanks, Chris. Good to see you this morning, Ed.

**Ed Firth, Keefe, Bruyette & Woods (EF)**

Apologies if this question has already been asked because I missed the beginning of the meeting. So, apologies. But I'm getting a lot more questions at the moment about the potential for bank tax. And I guess that you can see why that might be given. You know, we were talking about cost of living crises, etc., and banks have managed to reprice all the assets pretty rapidly and yet really passed on nothing to depositors. So, and certainly if you look back in the past, those of us who are old enough can remember the last time we had steep yield curve, we had a bank tax. So, I don't really know how you can answer it because I guess if you were having discussions, you couldn't tell us. But I mean, how should we think about that sort of risk? And particularly when you're you know, you've still got, I think, what, 12 or 15 bn of subsidised funding, which seems quite surprising for a company that's targeting a 15% return on tangible. But how should we think about all the sort of you know, the fact still getting subsidies you possible we assets you haven't cost on the deposits and other utilities getting bank taxes is that something we should risk to be thinking about or should we just ignore it? Or what should be the general thought process?

**KM**

I mean, I guess I'm the way that I think about it is to remind people that we already do have two banking taxes in terms of the banking levy and the corporation tax surcharge, 8% falling to 3%. And so, I think it's important to remember and as you have your conversations, just keep reminding people there already are two banking taxes. That's probably the last attempt to make sure we don't get a third or that they get an increase. I think that's that that is a really important point in terms of that kind of piece. And look, let's see, we're not having kind of conversations, but clearly ask to risk in terms of if they were to do that, that would naturally impact our assumptions and our results. And it depends how big it is as to what it would then do to the guidance, we have given to you. And if they were to do I think we talk about that at that time. I think it's always important. Remember that we do have two already. I'd say I'll leave to the politicians to work out whether there should be a third.

**Ed Firth, Keefe, Bruyette & Woods (EF)**

As a management team, Katie, I mean, if you saw that 16% was actually 20%, is that something you'd be comfortable with? I mean, if you could see your margins being materially above where they were in 2019, would you say like Rate Bank or would you be saying, look, we're getting to a level where actually as a 20% market share player, we have to start thinking about balancing both sides of the balance sheet.

**KM**

So, I think we were spending a lot of time at the moment balancing both sides of the balance sheet. You know, if I look at that mortgage pain and the cost of commercial lending and what would you say deposits. It's that is you know, and I understand if you're as a consumer, what you feel is that your mortgages are going up significantly, you're not getting anything of deposits. And but actually, I think when we're sitting particularly back to some of Q1 kind of application margins and the completion margins we talked about into Q2, those are quite painful for the bank, which is why the deposit side is really important to kind of offset those pieces. So, we spending a lot of time doing

that. I think if we were to get something meaningful that would come in, we would obviously then have to live with the sensitivities in what does that mean in terms of what do we what do we do next in terms of how we how we deal with the impact of that? And, I guess the way I think about is for ROTE we talking about for 2023 is not outlandish. It's just surprising given where we've all been for the last decade. But in terms of it's not, I don't believe is that number that's improbable that that's sort the next issue should be only but let's see what happens.

**AH**

Questions back in the room please.

**Aman Rakkar, Barclays (AR)**

I just want to ask about your view of the market buyback going forward. And should we expect to see any special dividend with share consolidation as a preferred method of distribution? So, you do look like you are set to build those.

**KM**

We are very capital generative, in terms that piece. We like the special with the consolidation because it mimics the buy back in terms of that piece. It's definitely I always talk about arrows in my quiver and I kind of feel there's four and with the consolidation there maybe fifth in there. We do like buybacks, but the board and myself and Alison decided was we didn't want to take the ownership above 50%. So, you could see that we're just below 49%. That doesn't give you an awful lot of room for movement. But I guess what we're hoping is that this period gives us a chance to get a few percentage points down and then we'll kind of see what happens. I do strongly suspect the next few years you'll see issues, a combination of any one of those arrows. And I don't think I'd like to get to doing a lot of special, which I am always very open. They're not my favourite. I think doing it with the consolidation works, but to doing that as a kind of repeating event doesn't feel like quite the right thing. But I think let's wait to see it. I think you've got to think what's the best way to term capital at the moment. It's situation I find myself in at this moment and you know, we don't have complete control over it, over all of those things. So, I think there's, you know, four and a half arrows, let's see which one we want to pursue at that time. But we, like this one, seem to be in good sense at this time.

**Benjamin Toms, RBC (BT)**

Can I just ask on that 50%? What's the magic around that 50%? Is there a derating effect?

**KM**

No, it's one of those things. So, it's important for the I it was important for the organisation. Look they're very good shareholder, you know, they don't interfere, they don't do any of those kinds of things. But I think if I look at a lot, particularly some of the US funds, some of them took restrictions on shares because they don't own majority of banks, even though we know from corporate rules 50% isn't the number that makes a big difference. You're still a majority shareholder. So, I guess you don't want to do is slip above 50% lending all by itself while obviously focussed you also find yourself back up at 55 or 56, you know, and that's one of the things. So, we took it there was a big debate, which is a wrong decision, of actually did we want to make sure we stay below and ask things about your message and rather that you can't send the message out internally or go back where no longer or to go back every other year.



So, saying has to kind of observe. I think it's our kind of journey in terms of that piece. So, we'll go over to the sellers. Our job is to make sure they have a bank that has got the right equity story that there's buyers and then that makes it easier. So, we'll see how we go forward. So probably put it to an end and thank you very much for your support and challenges there. But if they are appreciated in equal measures and I look forward to chatting as we go through next quarter, I know I will probably speak to the number of you as well. And then also as we head towards Q3, we had my first Q3 meeting yesterday, so I kind of feel a little bit grateful, it must be said. Look forward to talking again more formally in October. Lovely, thanks very much. Take care and have a good summer.