



NatWest Group plc
Annual Results, Sell-side Update
26th February 2020

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0:00:03.7

Katie Murray (KM)

Thank you Dave, good morning everybody and thank you for joining us today. Joining me today is Donal Quaid (DQ) our Group Treasurer and before we open up for questions, I'll make a few comments on Income, RWAs and also Ulster.

We spoke on Friday about the outlook for income, we are targeting lending growth above the market rate in 2021 which we expect to be more than offset by 2 main headwinds.

0:00:26.4

The impact of the structural hedge where we expect income to be a little over £300Mn lower than in 2020 and the income reduction in Natwest Markets to £0.8-£1Bn versus the £1.2Bn in 2020.

As a result, we expect income excluding notable items to be slightly lower in 2021 than in 2020.

On RWAs we ended 2020 at £170Bn and we expect to be in the range of £185-195Bn by the end of 2021 including the regulatory impacts effective on January 1st 2022.

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The main factors in this are lending growth, we intend to grow above market rate in our UK and RBSi retail and commercial businesses. Procyclicality which to date has been incredibly low, and the timing of which of course remains uncertain, and regulation, the main impact to mortgages which we expect to be RWAs to be around £12Bn higher, equivalent to an average risk rate of around 15%.

And finally, the ongoing refocus of Natwest Markets.

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Looking to 2023, we expect ongoing loan growth to impact RWAs and we would have expected procyclicality to have peaked and to have started to recede but the timing of the impact of Ulster RWAs of course remains uncertain.

As such we think that the upper end of our 185-195Bn range remains appropriate for 2023.

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We announced on Friday the conclusion of our strategic review of Ulster Bank and our intention to begin a phased withdrawal from Ulster Banks Republic of Ireland business over the coming years.

It is early days, and we have said we expect it to be a multiyear process and it to be capital accretive.

We have signed an MOU with Allied Irish Bank for the sale of 4Bn euros of performing commercial loan book.

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And we are in discussions with other strategic counterparts for certain retail and SME assets and liabilities.

In terms of how this affects our guidance, you will have noted our target for loan growth above market rate excludes Ulster Bank. Our guidance on 4% annual cost reduction, also excludes the direct cost base of Ulster Bank.

However, our guidance of strategic costs for 2021 of around £800Mn does include Ulster Bank.

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As I mentioned, it's too early to know how Ulster will impact our RWAs in 2023, however we expect to manage the withdrawal such that it is supportive of our group ROTE targets of 9-10% by 2023.

Overall, we have delivered a resilient operating performance with growth and net interest income in the fourth quarter and continued progress on both cost and RWA reductions accompanied by a strong capital and liquidity build.

0:03:12.7

We will now open up to take questions. Thank you Dave.

Operator – Dave

Thank you very much. As a reminder, if you are dialled into the call, then you'll need press *9 to raise a hand on your phone and then it'll be a case of pressing *6 to unmute when prompted. We do encourage you to turn your camera on when you do raise a hand, to make sure we can keep the call as interactive as possible.

Our first question today comes from Benjamin Toms of RBC. Benjamin, please go ahead.

0:03:41.4

Benjamin Toms - RBC

Morning, can you hear me. Hi, thank you for taking my questions. The first is just on your guidance of income, excluding notable items being slightly lower in 2021 than 2020.

If you take the 10-basis base rate cut out of your assumptions, would you still get that declining income year over year?

And then secondly, you've noted an ambition to grow AUM's significantly over the next 3 years, could this be achieved inorganically as well as organically? Thank you.

0:04:12.0

KM

Sure, so if I look at the 10-basis piece, guidance would still be there, if I look at the 10-basis point, we had it coming in our plan in Q2 this year, I'm conscious that we've moved out to, the consensus has moved that out to Q2 of next year at the moment, but it is moving around a lot, but that was only worth about £70Mn of income, so it would obviously be a bit of a positive up but it wouldn't be enough to offset the £300Mn and the range around Natwest Markets.

0:04:45.9

But it would be obviously a small positive for us in there. In terms of AUM, and acquisitions, what we've always, we're focusing on it, I think at the moment looking organically, very much looking at our Natwest invest product as well as continuing the build that we have with Coutts, and I think if I

look at Natwest invest, it's a very nice little product that's been quite difficult to use over the years, we do quite a lot of investment within making it much more integrated and much simpler for our customers to use and for many of your mass customers actually it's a perfect little product to be using, rather than having money sitting in your deposit accounts, so we need to work on that.

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And I think that's got some really strong potential once it starts to build. In terms of inorganic opportunities, what we always say on inorganic, it's something to add volume, or to add capability. We're pretty comfortable on the AUM side that we've got capability, it's about how we get it out to the customer base, and I think we also, as we look at asset management type investments, I think they're very hard to make real value from to integrate them into a bank, so it's probably not something that we would look at specifically.

0:05:55.1

What I would say is we do look at things as they come up for offer, often from before they are more widely known that they are being looked at, so we wouldn't discount things, but it wouldn't be one, that capability wouldn't be one that would be top of our list in terms of being able to add value. Thank Ben.

0:06:11.3

Operator – Dave

Thank you very much. Our next question comes from Paul Fenner of Society General, Paul Fenner would you please unmute and go ahead.

Paul Fenner - Society General

Hi, sorry, actually my questions been answered.

KM

Okay perfect thanks very much Paul.

0:06:28.3

Operator – Dave

Thank you our next question in that case comes from Aman Raldcar of Barclays would you please unmute and go ahead.

Aman Raldcar – Barclays.

Hey Katie can you hear me?

KM

Yes, perfect good morning

Aman

Morning, I've got a, some questions on Ulster and then one on the possible buy back if possible.

So, just a quick one, first of all, is there any chance you could help us understand the income contribution from the AIB corporate loan, we might have partially addressed it on the call the other

day but could you confirm how much current income should we expect to drop out from that particular loan sale to AIB?

KM

I'm going to just put Alexander on notice, I'm going to come to him to confirm that because I can't confirm it for you easily off the top of my head, so that will give him time to look through his papers if we've given any of that disclosure. I think we have so what was your next question and then we'll move on to Alexander to give him a minute to get to that.

0:07:27.8

Aman

I just wanted a sense of Ulster's cost base, I think it's about £440Mn that you guys called out for year 20, that's a combination of direct and indirect costs, what is the, illustratively if you were to get rid of the entirety of Ulster, miraculously overnight, how much of that £440Mn would go, I'm trying to work out what's centrally allocated and perhaps it's just going to hover around the rest of the group, versus actually does directly relate to Ulster, so what's the cost if you were to take them out, that you'd point us to?

0:08:05.0

And third, final one on Ulster is just around capital. I guess I've got one eye on the Irish Banks Bank of Ireland and AIB that are trading at about 0.4 x tangible book, I think if you were to 'exit' Ulster at that kind of level, you'd be lucky to be neutral in terms of the impact on Natwest Group, so given where you are right now and I appreciate there's a ton of uncertainties and it's not going to be an easy exit, do you think you can get out above that level and do you think you can claw back the capital, and just the final one...

0:08:50.4

Its just on buybacks. Is there any idea or any sense that you can give us in terms of how well advanced your conversations are with UKGI, do you get a sense that there is a chance that we could get a buyback sometime soon or obviously you've got the budget next week, new treasury forecast, at the same time the share price is not what it was the last time we placed? Thank you.

0:09:14.4

KM

Great, Aman, I'm thinking it might be four questions I am going to struggle to answer for you in a way that you would like your answers, but I'll do my best. Look and Alexander sorry I have got it here.

So, the best way to look at what you've got on Ulster is to go into the financial supplement on page 29. So, there you can see the commercial income is 219 this year, 240 last year, Allied Irish are buying the bulk of that commercial book, they're certainly buying all the performing pieces which would be the major contributor to that, so that's probably a decent proxy.

0:09:49.6

Similarly, you can see the direct and the indirect. There's always an element of indirect costs that are allocations which go around the group a little bit as well. But what I would say is, I'm really

loathed to give you a percentage on it, in terms of, most of that indirect, you could imagine that we would be working on, how do we remove that in line with, as we need to close down Ulster. And that indirect would be made up of all manner of different things, where they rely on tech systems for the group, some of them will be very specific to Ulster.

0:10:31.1

Within finance I have a number of people who are completely dedicated to working on Ulster, so as it ultimately goes, accepting that finance is often the last person to lock the door and walk away, in terms of the tax team and things we provide a huge amount of the resources in there.

So, I am going to be a little bit unhelpful and not give you a particular help on guidance here but you can see the piece there. You would assume that ultimately the directs would go, but sadly it's something that never happens overnight.

0:10:58.0

Even if we sold everything next week, the tying up and the process and the transferring of people is still has got quite a lot of time that is attached to it.

I think that page probably gives you at least the base information, I mean you've probably found that already.

In terms of the capital, I think they're at 28.5% CET1, on their local basis, we have historically talked about, that we think that we've got excess capital of around 1Bn to 1.5Bn Euros in that business.

0:11:28.2

Which is a number we shared with you historically. When we're looking at the withdrawal of that, we're obviously going to preserve as much of that as we can in that space, so what we've said last week was it will be capital accretive, in terms of the capital accretion, it's very much the returning of the capital back to the group and I think we'll update you when we know more Aman so sorry, not a terribly helpful answer in that space, but not unrealistic given where we are in terms of the transaction.

0:11:55.1

Just having Alexander, is there anything you would add to that, I don't think there's any more that we would give?

Alexander Holcroft (AH)

No, just to say, the perimeters are not set yet so no I wouldn't add further to that.

0:12:09.1

KM

Lovely thanks very much Alexander.

And then, in terms of buybacks, I think what's really positive on the buyback front is that we've got the regulatory permission in place with the regulator to be able to do that, so it's up to £1.25Bn that we asked for and they agreed with us, obviously we can only buy 4% at any one time, so we're thinking today's prices that's probably, it's around about £1Bn, £1.1Bn something like that, so the UK GI has always been quite clear that they're guided by fair value, not by historical purchase prices, so,

they obviously don't give us any particular guidance on their range, that would obviously be inappropriate to do that, but what I would say is that the team makes sure that they are ready at any point if they were to get the call that we'd be able to transact on that trade, so I think the most important thing that Alison and I focus on is making sure that there is an equity story that would be appropriate for others that we'd want to buy into the stock as well.

0:13:34.4

Thanks Aman

Aman

Thanks Katie.

Operator – Dave

Thank you very much. Our next question comes from Alvero Solano of Morgan Stanley, if you could unmute and go ahead.

Alvero Solano – Morgan Stanley

Just a question on the 2023 and I realise we've touched on it already on the call but just want to make sure I understand that, that 9-10% ROTE, the delta feels like it's mostly revenue versus consensus, you've given, any commentary of what you think consensus differs from what you're seeing would be useful, but in particular, you've given the 10 bit rate capped, that you're assuming for Q2 and that you're not assuming the steepening of the curve for this year, but presumably that means you were in that budget, you were assuming the flat yield curve that we have until very recently, just wanted to confirm that's the case and related to that...

0:14:22.6

Your structural hedge, I mean it's grown, but it hasn't grown as much as your deposits, presumably that's, is that because some of those deposits you assume will go away? Or should we think there's room to grow your structural hedge and how that plays into your guidance or is it more about fees?

And relating to the fee question, is, one of your competitors was sized the loss of revenue, from the lockdowns, I don't know if you can share some thoughts on how you see the recovering playing out and size maybe the loss of business.

0:15:03.0

And the last one, on Natwest Markets, that £800Mn-£1Bn, if that's a more normalised runway going forward, am I right to think that you might make a profit in Natwest Markets which was not the original plan? thank you.

0:15:19.4

KM

Yeah sure, so as we look at that. So, in terms of the 9-10%, I think what we talked about on the call last week was, in terms of the guidance we have given you, I would have suggested, so revenue is certainly important but I don't think it's the sole contributor so, we think a little bit down in this year, we're obviously making some significant investments, we would hope some of that would come through in revenue as well as cost take out and we've talked about above market growth within there.

0:15:51.4

But I think, Jonathan I think it was your question, we sort of said, look I would encourage you to look at our guidance in terms of cost take out and the 4% in the per annum and also in terms of the impairments, so what we've said for 2021 is that we would be at, or below with our 30-40 basis points through the cycle guidance, one would think that, that would tighten a bit more as you get to 2023, so I'd have a little bit of a look at your impairments as well, its kind of a blend of all of those different things.

0:16:25.8

You're absolutely right in terms of the rate cut. That is assumed on with a flat yield curve from there. We see the growth of that coming up and it's pleasing to see, I think I'll be pleased come June if it's still sitting there, but I'll not necessarily get too excited at this point in terms of where it is. But I think if you want a guide as to what it might feel like, the structural hedge guidance that we give you on page 232 of the accounts, gives you very clear guidance on what a 25-basis point upward shift would mean, in years 1, 2 and 3, obviously the biggest impact comes through on the managed margin, so that requires the Bank of England to be making changes as well...

0:17:10.4

Rather than just the market rate moving. I would think to a large extent in terms of how that comes through, but that will give you a little bit of guidance.

And then in terms of the growth and deposits I'll pass that point onto Donal who's on the line as well, but before I come to him, let me just talk in terms of the lockdown, we've not really sized the loss of business and I won't do that today. I think the best way to look at it, is we give you some really good analysis of the quarter-by-quarter numbers, so look at what it is in Q1 and what happened in Q2 and how it's recovered into Q4, so I would say that we're not back there yet but that definitely gives you a flavour of what the lost income would be and how we might expect to see it recover.

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I would obviously in there remember that in 2021 guidance we've got the Natwest Markets income will go against there as well as the disposal losses which is obviously not in an underlying basis, with £300Mn there and then by Q3 last year we had got to the runway of most of the regulatory changes, remembering that, that was a £200Mn impact last year and only an additional £100Mn impact this year, so flex them into your thinking as well, but I think if you look at those shaped by quarter, you get a pretty good feel for it.

0:18:26.8

And then, on Natwest Markets, we do think that they will start to, we had talked about them breaking even. We think with the £800Mn - £1Bn that you could see them being small single digit ROE, which is why we're more comfortable around the 8% ROE that you would see across the commercial and the Natwest Markets book, so, pleased to see that, lets get the disposal losses out of the way, lets see what else we can do in terms of really making sure we can deliver that number consistently, but I think they've had a good year and we feel more confident than we did a year ago.

Donal can I just come to you about the shape of your hedge and have you room to grow?

0:19:07.5

Donal Quaid (DQ)

Yep, you can, so there is definitely room to grow in terms of the volumes, the way we look at it in terms that of deposit growth is on a 12-month rolling average basis, so obviously as we saw deposit growth all the way through full year 20 that will only feed through over time. Obviously, there is some work to be done there in terms of those deposits and whether we think they're as sticky as other deposits we've seen previously.

0:19:28.7

But expectations are that you should see an incremental increase in total structural hedge noticeable over the next 6-12 months. And probably just to add on the yield curve, you're right as well, I think if I look at the average 5-year swap rate that we have in our base case, is probably in the region of 25-40 basis points, so obviously we're trading 5-year swap will be about 45 basis points as of yesterday but as Katie said, we have seen move higher in rates have been retraced quite quickly as well so we'll just have to see how that pans out over the coming months.

0:20:03.6

Alvero

And Katie just to confirm for your 2023, you're not assuming any rate hikes or any, you're assuming the same curve as in 2021? Is that correct?

KM

So, yes absolutely, so we assume that it fell in Q2 2021 and it did not recover, so if there is a positive and it stays then there is great upside to those numbers.

Alvero

Thank you very much.

0:20:33.3

Operator – Dave

Our next question comes from Lee Street of City Global Markets, Lee please do unmute and go ahead.

Lee Street – Global City Markets

Hello, thanks for taking my questions. I've got one which is a bit similar to Alvero's one, and then... so, obviously we've had a big move in rates that we weren't necessarily expecting, if the curve was to keep the same shape, and we'll still to be in a similar position or marginally higher come the end of the second quarter, would that be sufficient for you to start thinking there could be upside to your 9-10% 2023 return targets?

0:21:06.7

And then, on funding, I think I saw a comment from Scott Forest on Bloomberg saying that the markets are about as good as we're going to get, does that mean I should be expecting you to bring forward and try and get all of your funding plans out done as soon as possible? And lastly, Natwest Markets, given the run down, should I be not really expecting to see much funding come out of them at all over the forthcoming few years, that would be my 3 questions, thank you.

0:21:33.5

KM

Lovely, thanks very much, I'll take the first one and I'll give the next two over to Donal.

So, if I look at it in terms of the upside, I'm not going to commit this morning that we'll be updating our guidance within 2 quarters. I think we've given you what it could mean if it really did stick, and I think we'll happily talk more about it as we feel more comfortable in terms of the stickiness of it. But you can see the maths there and I think to reassure you, the conversation I have internally is, guys I don't want to see us hitting this number because you've taken all this benefit from the upside and that's the way we get to the number, I need to see us hitting the number on the plans that we had.

0:22:09.2

So, I think that, that's the internal conversations that we're having to make sure that we don't use this to mask, anything else that's happening inside. Donal, do you want to take the funding questions?

0:22:22.4

DQ

I will yes, so in terms of Scott's comments, I think he was probably reflecting more in terms of the wide array of demand that we had for the bond, there was a huge amount of investor interest and quite large diversification of investors as well, so I think that was it, as opposed to a view on outright levels of spreads, or anything like that, so I wouldn't be counting that you should see us fill our full funding requirement over the next few weeks in terms of being out across the capital stack and MREL. We will do it over the 12-month period.

0:22:53.0

On Natwest Markets, expectations obviously very low, this year, just in terms of as they downsize and bring down their RWA they're very, very well-funded at present, however as we move forward into 2022 and 23 are expecting to be more active but probably not at the levels you have seen in previous years.

Lee

Okay thank you very much.

0:23:11.7

Operator – Dave

Our next question comes from Andrew Coombs of Citi, Andrew please do unmute and go ahead.

Andrew Coombs – Citi

Ah good morning.

KM

Hi Andrew, good to see you.

Andrew

Sorry to follow straight on from Lee, double Citi, two questions. One on structural hedge and one on management overlays embedded into the IRFS9 modelling.

0:23:37.0

So, first on the structural hedge. In the annual report, you talk about going from 0.6 – 1.1 of incremental net interest income, because of the structural hedge. Can you just provide the absolute number that you actually have from the structural hedge rather than the incremental number?

KM

Yeah sure, do you want to give me your next question and we'll do both of them at once. I'll get Donal to do the structural hedge question.

0:24:07.7

Andrew

And then, attached to that, what I'm struggling with is, you still have a 5-year maturity on the structural hedge I think, if I compare to Lloyds which is a 2.5-year maturity they're going to a £400Mn headwind, you're going to a £300Mn headwind, it seems like your number is a little bit high, now I don't expect you to comment on Lloyds but I'm just trying to triangulate how you get to your £300Mn.

0:24:33.8

And then, second question on the management overlay point, Barclays and Lloyds both drew this out specifically on their call, how much of an overlay they've maintained in that, what they've essentially done is have more favourable economic assumptions but have increased the overlay and therefore haven't released. Could you just comment specifically on what overlay you have and how that changed between Q3 and Q4?

0:24:59.7

KM

Happy to, Donal why don't you take the couple of structural hedge points.

DQ

Yeah sure, so, the total income from the structural hedge respective you'll see in the report, it's £1.688Bn as opposed to the incremental figure of 1.14, that incremental figure is just really driven by the average LIBOR rate that we saw, the role off or the actual yield on the structural hedge obviously moves a lot slower than average LIBOR, so £1.688Bn and then the £300Mn that Katie's referred to is of that total figure.

0:25:32.1

In terms of duration, we roll our structural hedge from a product perspective on a 5-year swap and the average life or duration is about 2.5 years, so it's not hugely dissimilar to what Lloyds have disclosed around the 2 year, so just to put that into perspective.

0:25:49.4

KM

Okay lovely and then in terms of the PMA, we talked about it as well, sorry if you missed it, but basically what we did was we added £878Mn and you can see on page 170 of the accounts the piece is in there. What you might recall Andrew is that at Q3, we didn't update our economics piece, so because we hadn't updated our economics piece, we were still holding actually, relatively higher provisions, so therefore we didn't really have this PMA, to any substantive amount at that time, so therefore I wouldn't go for a Q3/Q4 movement, but more actually that what we saw happening, is that we've had the release from the economics piece and then an increase to add on this element for economic uncertainty.

0:26:38.3

And when you look at that page in the accounts, you can see that there's 202 from last year, so last year end that was very much in relation to multiple economic uncertainties, principally related to Brexit and the uncertainty around Brexit, and then this year it's now increased up to 878 but that's very much as a consequence of the government interventions.

0:27:00.6

So, in terms of how that might unwind, I think what we need to start to see is actually businesses starting to move into default, or to actually start to reach to the end of those interventions. What we know is that people are holding a lot of cash, which is a direct benefit from a lot of those interventions, so the unwinding of that I think will be something that we will talk about throughout this year, and I wouldn't even be surprised if it carried on a little bit into the early part of next year. In terms of that piece, but that's the number that we've got there.

0:27:29.9

Andrew

Okay thank you.

KM

Lovely thanks Andrew.

Operator – Dave

Our next question comes from Forhed Comra of Redburn, would you please unmute and go ahead.

0:27:41.1

Forhed Comra of Redburn

Hi Katie, just one quick question. Just to follow up on Aman's questions on Ulster. When we've seen previous run downs before, there's been a bit of an operational risk rate overlay which takes a bit more time to come out, from memory it's kind of 10% of the risk rates normally take, an additional 2 or 3 years after the business has gone, do we have a similar situation in Ulster where there's a proportion of operational risk rate overlay which then takes more time to come out and if there is that, how much roughly as a percentage of risk rates, is that operation risk rate overlay, thank you.

0:28:14.9

KM

So, I don't think we're at the point of confirming that, or even necessarily calculating it, but I would say that I think that's a relatively safe assumption to say that there will be a little piece, which drags on longer, so they're sitting at 13.2Bn of risk related assets so a portion of that be something that takes us a bit longer just to get off at the end of it, we'll confirm what the percentage might be but I think the percentage you've seen in the past, is probably a good enough one to work with if you want to do any detailed modelling but at this stage I don't really have an updated number to share with you.

Forhed

That's fair enough. The second question I have, just on costs as well, your 4% per annum cost decline, is quite exceptional to be honest, in the European and a UK context going forward, how do you think about investment spend versus the continual costs take out that you're having, I mean obviously we're digitalising all this post COVID world, is there a risk that perhaps you're not investing it enough, how do you think about the quantum of net cost reductions versus that investment spend, thanks.

0:29:23.5

KM

It's a good question and I think we're comfortable that we are investing enough, we're investing about £3Bn over the 3 years and the ultimate impact of that in terms of capitalisation and amortisation is built into the other operating costs, and I don't think that, that capitalisation/amortisation is a big story because of what we've done to date. So, it works out relatively smoothly, not completely, but relatively smoothly in those numbers, so we're comfortable that we're investing enough. I think part of that investment is to help improve some of the income numbers, but also to take the cost base out so we are comfortable on that.

0:30:03.0

I think the thing that we, if I look at the investments today, I would say, so I'd look at cost take out today, historically to this point, I think there's been two main things that we've done as a bank, one was to divest of things, obviously big cost take out, there's been much less of that in the last few years, and then I think the other balance of cost take out is we're very kind of silo cost take out, so retail will do their bit, commercial would do their bit, finance would do their bit, risk would do their bit, so then you get to a decent enough number, but actually by doing that, what you're not tackling is where you've got duplication of activity...

0:30:34.4

Whether that's things around, how you onboard clients, how you communicate with clients, what you do with your paper and all those kind of things, so actually what, the absolute mantra you would hear, internally now is, what's the one bank view and how can we take things out that go across the horizontal rather than just up and down the vertical, so that's obviously the verticals over, but it means that there's a much greater focus on those costs which can often be duplicated across different silos to help deliver that 4% takeout.

0:31:05.0

Forhed

Perfect, that's great, and a last question on the hedge. Just obviously I think the numbers Donal gave, like a 55 bit net hedge, you're 40-45 bit steeper to the yield curve right now, at some point I'm assuming that hedge, if the yield curve carries on, you are running off the higher yielding stuff right now, I'm assuming the back end is lower yielding stuff, mathematic am I right in thinking, if everything stays as it is, you've got a drag for one year or two years and after that, the hedge just based on averaging starts to become a tail wind rather than a head wind? Thanks.

0:31:39.5

KM

Donal do you want to take that?

DQ

Yeah, yeah, happy to. Again, if I look at the average yield on our hedge that's in our disclosures, just over 1%, so again, that would include also our equity hedge which is a 10-year swap at average life of 5 years, so you can probably look into that, we would still need to see a decent steepening front year to be it to be a positive on the upside as opposed to a headwind.

KM

I know you're aware of this year, 3 basis point impact per quarter, will be affecting that £3Mn piece.

Forhed

That's great, thank you very much, cheers.

0:32:21.2

Operator - Dave

Thank you, our next question comes from Jonathan Pearce of Numis, Jonathan would you please unmute and go ahead.

KM

Hi Jonathan.

Jonathan Pearce – Numis

Yeah, hello everybody. Thanks for the questions, sorry my internet is terrible, it's not because I'm in my pyjamas I promise.

A couple of questions they're related actually. I'm interested in how, if these deposits prove quite sticky through 2021 and I guess at a system level they must do in fact, they'll probably go up further because of the QE that it's still seeing. What are the LCR benefits as the year goes on? So, will you have for instance some of these retail deposits, maybe sat in less stable buckets moving into stable buckets for lower ratings, so again, improvement in LCRs through the year if the deposits do prove sticky...even before any further deposit growth.

0:33:20.4

And then connected to that, liquidity within Natwest Holdings, is, its currently pretty good and I'm thinking here about mortgage spreads because the big rise in swaps, has essentially taken your spread to swap on lower LTV products that you're writing down to about 80 basis points, as I look at

rates and swaps today, and how should I think about this dynamic going forwards, because you've got more mortgages being written this year than you have structural hedges rolling off, so in theory this rise in the swap rate, if you don't go increasing your mortgage rates is going to be a negative, or else equal. Or are you just going to keep pricing at whatever level you need to deliver the shared growth of the net lending targets that you have in place, so interested about how you're thinking about mortgage spreads and not just the structural hedge side of things.

0:34:19.9

Yeah sure, Donal do you want to start on the structural hedge and the deposit point and then I'll scoop up anything that's left on mortgage pricing.

DQ

Yeah sure, so on the deposit piece, I think you're right. I think our expectation now is that a large, well a decent percentage of deposit inflows that we saw in 20 will be sticky to 21. We've seen QE of £310Bn in 2020 and as you said in terms of the government lending schemes, I forget the latest figures but I think it's in excess of about £60Bn in total across the UK banks. So, unless you were to see significant early repayment of those schemes, I think what we'll see is those deposits being sticky for the next couple of years.

0:35:01.9

In terms of impact LCR, we're not expecting any benefit from an LCR perspective over the next 12-18 months in terms of the composition of those deposits, because to see that you would actually need to see a move from commercial deposits into retail where you would get the benefits from an LCR perspective, and that's not something that we're really expecting to see over the next 12 months.

0:35:22.6

Jonathan

Sorry, just on that, in terms of the retail deposit growth, sorry Katie, in terms of the retail deposit growth, is not a disproportionate amount of that growth not buy into less stable parts to the higher ratings at the moment and there could be some migration there as well?

DQ

I think what you've seen in terms, in retail, it's just a build up in terms of current accounts, that's really a phenomenon that we've seen over the last couple of years with savings rates so low, is what you've seen, is people just build up that liquidity within their current accounts, so in affect from an LCR perspective, we're not expecting any change in how we would view that going forward.

Jonathan

Okay thanks.

0:36:04.1

KM

And then if I look to the mortgage piece there, so you're absolutely right so the reason why mortgage spreads were so positive last year was twofold, one because we all put our pricing up a little bit but also because the spread rate came down so much, that's clear, so naturally as it goes back up, you'll then have the impact. What I would say, it doesn't happen instantly overnight in

terms of that but it would come through this year, so I think when we're looking at mortgage spreads, we very much have the conversation internally around how do we balance volume versus rates and also where we're originating them from, because that can make a big difference to our own economics, we're trying to do more internal and a bit less brokered and I think we've maybe done, historically will have a positive impact on that, but what we're keen to do is not race to the bottom, so that we end up back at those very low levels of margins in there.

0:36:58.9

So, I think if next week the Chancellor does extend the stamp duty piece, I think that helps a little bit as well because that means that they, we were very worried about the amount that would just get pushed through in the next few weeks and then what that would mean afterwards in terms of what the rest of the flow would look like, so that's important in terms of how we take it through, and I also think, something we don't talk a lot about, but as an analyst community we always talk about new mortgages, I think that re-mortgaging is a really important part as well in terms of how we do that, because obviously that is, for us, is ultimately, can be more profitable because just the cost of acquisition are so much more diminished on that side of things.

0:37:43.6

But again, I do think that they will certainly come down from where they are today, I hope that they won't drop as far as the numbers that you suggested, we don't see that at this stage but I think we do have to keep an eye on what happens with the stickiness of that swap curve.

Jonathan

Okay thank you.

0:38:00.4

Operator – Dave

Our next question comes from Robin Down of HSBC, Robin, if you could please unmute and go ahead.

Robin Down – HSBC

Good morning, its lovely to see so much sunshine coming through people's windows!

KM

No, it is indeed, I've had to close my curtain otherwise I'd just turn into a big white ball.

0:38:21.4

Robin

I've got a couple of questions, I apologise Katie I suspect you're going to throw these straight to Donal, but...

KM

And I'm glad Donal's with me, is all I can say this morning, so it's not a problem at all!

Robin.

The first one is on the dreaded structural hedge. I appreciate that you've tried to be helpful with the disclosure in giving us this £37Mn impact on the structural hedge, but that's using a parallel upswing in the yield curve and of course, what we're actually seeing is a steepening of the yield curve, so that £37Mn presumably includes the impact of LIBOR going up as well which would obviously limit the impact on the structural hedge, I don't know if you've got the sensitivity, we can do our own analysis on this, but whether you have a sensitivity just for a steepening of the yield curve as we've currently seen because I think the numbers might be a lot larger than £37Mn.

0:39:19.1

And the second question's really coming back to the Jonathan question, but perhaps asking it a slightly different way, we've got these massive deposit inflows, I think a lot of the surveys suggest that consumers will be perhaps looking to keep some of that in terms of savings going forward rather than spending it as soon as lockdown ends. I just wondered how you're thinking about kind of behavioural modelling deposit light, whether or not you might be tempted to invest the structural hedge at longer durations than 5 years on the product side, because given the steepness of the yield curve at the moment, you could almost quash the structural hedge drag if you were to commit to a return swap, how are you thinking about that? thanks

KM

Thanks Robin, Donal, I'll pass straight to you, it's turning into a group one to one here.

0:40:11.4

DQ

So, I think probably the first thing to say on the structural hedge, we don't take rate positions to the structural hedge, so we've been very, very consistent in terms of our approach. Now, saying that, we do constantly review behaviourisation of our liabilities and we haven't seen anything in the last 6-12 months that would make us change our assumptions on that to extend durations by any significant amount, but that is something we do on a constant basis, so we keep that under review.

0:40:44.5

What I would say is, the questions that we have from analysts probably this time 6 or 7 months ago, is would you look to extend duration and you can see now, if you'd taken that decision 6 months ago, you would be not looking too good given the backup we've seen in yields over the last few weeks, so again, for me it does give us a lot of confidence that the approach we've taken in terms of not taking rate views through the structural hedge has worked out.

0:41:13.5

We haven't provided any other sensitivity on the structural hedge, but I suppose one way when you think about it, you're right, it is a parallel shift, I think if you look at what we've seen in terms of the structural hedge, as I've said, the product hedge is put on a rolling 5 year swap basis, the equity hedge on a rolling 10 year swap basis, what you've probably seen is, not far away from the 25 basis points move in swap rates across that 5 and 10 year part of the curve, so that £37Mn is probably not a bad reflection as of where we sit today, obviously we need to see how the yield curve then goes from here over the next few months.

0:41:52.1

But as Katie says, when you look at our rates sensitivity, the big benefit in year 1 you get is for managed margins and you would need to see a move in the base rate for us to actually lock any of that in, and even though we've seen a steepening of the curve, I think base rate hikes are still a long, long way away.

0:42:07.1

Robin

So, to come back to it, in terms of helping us with our own analysis here, yeah there's no particular lumpiness to the hedge, I think you tend to reinvest on a regular basis, so we should probably be looking about £30Bn or so, of rollovers this year and I assume, I can go back 5 years and look on the swap rate and see what the yields are rolling off...

0:42:35.7

DQ

Yeah that's completely correct, we do take a very, very consistent approach so it's very, very hard to give any further clarity because in affect if we're sitting here next month, swap rates could be down 20 basis points, so you do need to build that in, but from a product hedge perspective we break it down, we have about £140Bn notional, on a product hedge that you can split it then there, 160 of that is rolling on a monthly basis and as well we give disclosures on the total yield as that portfolio winds down as well, so it is very, very subject to what rates do between here and the end of the year.

Robin

Brilliant, thanks guys, have a good weekend.

KM

Thanks Robin.

0:43:15.6

Operator – Dave

Our next question comes from Christopher Cant of Autonomous, if you could please go ahead.

Christopher Cant of Autonomous

Good morning, thanks for taking my questions, I had a few scatter gun on the top that have already been discussing really, so, firstly on Ulster, in terms of how we should think about that wind down, generally yourselves, the other Irish Banks when NPL's have been sold in recent years, they've been cleared off around bookmarks, there's not really been any evidence that the books are mismarked and with you talking about selling performing books as well as your end piece here so, am I right in thinking that the cost to exit here is really more to do with the fact that, you're not doing a whole business sale in all likelihood, there's going to be a little bit of cherry picking in terms of what's an AIB or a PTSB or whoever else is willing to take off you and therefore you're left with stranded costs that you need to take out, it's more of a restructuring cost issue for the remaining costs rather than expecting any bookmarks...

0:44:21.0

And if there are bookmarks are, they factored into your cost of risk guidance for this year or would you expect that to be coming through as disposal loss, so I would assume it's in the provision line but clarity on that would be helpful.

On the mortgage spreads point, I think last year, you talked about 140 bit spreads as being something more sensible so at the time we were some way above that, in terms of where quoted rates were and you indicated you thought it would come down to 140 bits as a more rational level, I guess that was at a time when you and all of the other banks were expecting more pressure to be coming through from your structural hedges, so do you think that, that 140 still stands as a sensible level, or are you now more inclined to think that it's probably going to be a bit lower than that in terms of where things settle?

0:45:12.7

And then finally on IFRS9, in terms of your cost of risk gains, I know you give us a fully loaded numbers and I guess that's what matters more, but in terms of the transitional, how are you expecting that transitional unwind to come through, I'm curious to see how that fits together with your cost of risk guidance, are you basically expecting to be within that cost of risk guidance releasing some of your stage one, stage two but obviously that just comes out of the add back that you've currently got in your capital schedule, thank you.

0:45:44.5

KM

A scatter gun indeed Chris, let me try to help you there. So, I think in Ulster, we're at the early stage of the disposal, we clearly have done some work with the AIB as well as with PTSB, so I think in terms of the pricing all I would say is we didn't take any mark adjustments in UBIDAC accounts or in our group accounts at this point, so that would suggest we're feeling relatively comfortable at how they're marked but the reality is that's going to work it's way through in terms of negotiation, and I think we're at the very first stages of negotiation but I would say, you're absolutely right, it's more akin to a book sale, rather than a whole entity sale within there.

0:46:32.4

And ultimately you will see some stranded costs that we, do we need to deal with? We're comfortable that whatever we've got this year, is built into the guidance appropriately for this year and we'll update you as we know more on that side of things.

In terms of mortgage spreads, I think it's an absolutely great question, in terms of where we are, we're sitting, applications are still sitting at the 180 basis points, if this recovery and this swap curve is sustained, that's definitely going to have an impact on that, and I think then it will depend what happens in terms of, where we go on competition in terms of any other impacts on pricing.

0:47:09.7

I look at the book today and it's got the back books 147 basis points, we're competing around about 160, so you can see that over the year you'd certainly expect that 180 to drag itself down, I probably wouldn't give you any newer number at this stage, I think it's something we can talk more about probably at Q1 when we actually see how sticky has this revival been and we'll chat more about it at that time I think. Certainly, the conversation we have internally is very much how do we mix both volume and value to make sure that you can get the right balance of that.

0:47:46.1

You know, cost of risk, our 30-40 basis points guidance is obviously IFRS9 guidance so it's what's hitting into the income statement not what's hitting against capital but you're right, part of that, as that comes through to us, is going to be a mixture of movements from stage 1 to stage 2, as well as the stage 2 into stage 3 which we just haven't seen before, so as that stage 2 to stage 3 happens, that's where you'll see the wind down of the IFRS9 impact on that.

0:48:15.6

This year, it's still 100%, next year obviously it then degrades to 75%, so there's a decent adjustment on the 1st January on that piece but I think the 30-40 guidance is very much P&L and not trying to get to the capital bit and it will be the 2-3 movement that will impact that capital and I would say that we've been surprised at how little 2-3 movement there has been today, if I think back when we first set the number up, we would have said to you then, we'd have thought we'd have been unwinding far more, even by the end of this year, which it basically didn't unwind at all.

0:48:49.9

Chris

Okay, thank you.

Operator – Dave

Our next question comes from Guy Stebbings of Exane, Guy please go ahead.

Guy Stebbings of Exane

Hi, morning Katie, morning Donal, a couple of questions. The first question was on the commercial division, and just in terms of how to think about as activity levels, normalise over the course of this year, are there any pockets of that book where you'd say balances are artificially depressed if you like? And they should step back up quite quickly, perhaps asset finance or anywhere else and how we can think about that or quantify that, that would be very helpful.

0:49:26.3

And then the second question was on Brexit, it has happened now and I just wondered have there been any lessons from that, any surprises in terms of, incremental costs, extra capital restrictions with local regulators asking for more, I presume not but I just wondered if you have learnt anything or anything has surprised you there, thank you.

0:49:45.2

KM

Thanks very much for that question. So, I look at the commercial division, as we look at where growth will come next year in terms of traditional lending it will be in the mid-large courts where we know that they RCFs has been brought down quite significantly, they're also sitting on cash as well, but we also know that in terms of infrastructure projects and things like that, that, that will start to move. But I do think if we look at some of our specialised businesses within there, they have obviously been quite depressed in terms of, in things like invoice financing, it's just hardly happened all year, in reality because of the level of invoices in some of the trading.

0:50:29.7

It's probably stronger now than it was in the middle of the last year, but it has been more depressed and asset financing similarly hasn't been as strong, so I do think we'll see a little bit of strength coming back within there as we look to this year.

So, that's probably the pace to look at in terms of particular holding back of income and that side of things.

0:50:52.4

Brexit, no particular surprises, I would say, I mean from, certainly no additional costs that we're carrying at the moment. I think if you were to go into the bulbs of our NB accounts you would see that we do hold quite a lot of capital there already, but that's not a new piece of information, that's as it was established. I think what we have seen as, what we're doing in the Netherlands and then we've got a German branch as well, which is becoming a German, we're creating a German sub as well, is the desire to have in country presence of a lot of the support and control functions.

0:51:31.2

Probably adds a little bit of cost, not in a meaningful way, because they're very small entities, but that's probably, it's something that's not new but as we're just getting more bedding into it, you can see that, that in country presence rather than being serviced ex-country is more a thing, but at this stage there's not been any particular capital controls on that.

I think what's more interesting in Brexit, and we'll know more about it as we go through, is to actually say things like, what's really happening on trading, so we can see that a lot of our, that companies are holding back, we hear from some of the narratives that some companies are basically saying, I'm just going to pull back a little bit from the activity from within Europe just while things kind of settle down...

0:52:18.9

Let the complexity sort itself out, and it will sort itself out, the paperwork and everything will resolve itself, but it's certainly, it's been a bit more of a challenge. I don't think it's a coincidence that Boris Johnson is urging us all to eat British fish and that's because the British fish is not being exported as much as it should have been, and actually, so it's more of, exports, that will be clearly have an impact on us as well, because obviously we fund some of those customers, but it's a bit too early to say whether it's just real teething issues, or whether it's something that's more sustained.

Guy

Okay thank you.

0:52:55.2

Operator – Dave

We have time for one last question, and this comes from Raul Sinha of JP Morgan, Val please go ahead.

Raul Sinha - JP Morgan

A couple of questions maybe, one on Ulster, I was just trying to understand the process of repatriating capital, I think the last time you managed to get some kind of dividend out of Ulster, was last year, wasn't it, early last year, so I was wondering whether you expect to be able to pay a

dividend once the ECB restrictions expire post September or do you think we should be thinking about any sort of capital repatriation linked to the completion of the assets that, as you sell them, are you able to repatriate them along the way, or should we then think that actually all the capital repatriation comes at the end?

0:53:44.8

And then the second one, I was wondering if you could give us some sense of the real estate costs footprint within the group, relative to the total cost base, I don't know if you missed it somewhere but any sense of the scale of that, and I was just trying to understand, especially the size of the strategic costs relative to the cost base, look quite high, so I was trying to understand whether your 2021 guidance on strategic costs is trying to upfront a lot of the strategic costs that will come in future years and I was wondering if you could give us some sense of the trajectory off that, thanks.

0:54:23.3

KM

Yeah sure, so look, as we look at Ulster, I think what we've seen happen with Ulster over the last couple of years, is that obviously not in 2020 but in 2019 and in 2018 that they did pay out dividends up to us, we obviously haven't had those kind of detailed conversations yet with the regulators as to how this would go, I think that we'd hoped that as books were dealt with that we would get to a point that they would be distributing as we were going rather than saying, you must all wait till the end...

0:55:00.3

Its not a conversation that we've had with them yet, but what I would say is that, when we've asked to take dividends out the last 2 times, they've said yes, so given where we're sitting in terms of CED when we're told they would continue with that approach, but the reality is, that time will tell on that.

Raul

Am I right in thinking that legally they can't stop you from paying dividends anymore once the restrictions are off?

0:55:28.4

KM

So, I actually would need to check that, I think they can, I think the same way that we pay a dividend, when we pay dividends, they reapply to the PRA to get permission to do that, its a form I sign the day before results and now by the evening it's come through, so they've obviously said, this is what we're thinking, so they're not big conversations. It would be the same in Ulster I think, I think to move the money out in contravention of any movement with the regulator, it would mean it would be the last bit of money that we'd move out, I'm pretty sure they will stop us.

0:56:05.3

In terms of strategic costs in the property piece, it's not a number, I don't think it's a number that we're given the detail, I'm just going to just check what we publish there in terms of that, but what I can say, in terms of the, if you look you can see that in the accounts when you combine it with

premises and equipment it's about £998Mn, and then the property costs Alexander has just pinged me the answer, so if you look at page 88 of the ARA you can a bit there.

0:56:35.3

What I would say in terms of strategic costs, you know that during the year, we took a charge in relation to Regent's House in Islington, at the end of the year, in terms of strat costs there were 3 more properties that were included within there, one was in terms of a data centre, that we have another property in Bristol and another property as part of the RBSi network, so those are important costs to take, so part of our strat costs going forward will definitely be continue a property refining.

0:57:08.0

I think we've taken most of the big ones, there are still some bigger properties out there, but I think we've taken quite a lot, we've been quite aggressive on the managing of that portfolio over the last number of years, so you can see it come down, but the horrible reality is that property has horrible payback in terms of when you take the costs, it's generally, you're looking at a 10-year payback of the costs that you've taken. It makes sense ultimately, but at the point of taking them it is painful, but page 88 of the ARA will give you a bit more information in terms of what that shape is.

0:57:40.6

Raul

Right but I guess the question is also about the 2021 strategic costs, are they upfront in most of the strategic costs for the plan or, how do we think about the trajectory beyond 2021?

KM

Yeah, so what I would say there is what we've talked about is, we're 1.4 – 1.1 – 800 now, we can expect to continue to see those decreasing down as we go through. Historically we talked about getting to a £300Mn number, that's probably still something that we're keen on, if we make a big decision on a property when you're at that level, clearly that would have a material impact of that. There are some property costs in relation, in the strat costs this year there is definitely some property in there as well, but it's not the lion share of it, is what I would say, so it's not that we're trying to get a whole bunch of property done in anticipation of, in future years.

Raul

Thank you.

KM

Lovely thanks very much.

0:58:33.0

Operator – Dave

Thanks very much and Katie that was our last question we have time for, so we'll hand back to yourself.

KM

Lovely thanks very much Dave, so just as ever, thanks very much for joining this morning, thanks for the support and the questions, if you need anything further, always happy to meet on an individual

basis and obviously Claire and Alexander are there to help you as well so thanks very much and enjoy the reset of what appears to be a sunny day!