Non-core Investor Round Table
28th June - Live Webcast Transcript

Introduction
Richard O'Connor
Head of Investor Relations

Good afternoon everyone. Thanks very much for coming over to RBS on what is a hot day. I will introduce you to Nathan Bostock and his team. Nathan will make the introductions in a minute. We have a 30-35 Slide Presentation which we will run through quite quickly. Do interrupt if things are not clear or you want clarification on any points as we go through. But we do have plenty of time for questions at the end. So we may refer you to the end for some questions to give the team a chance to run through the slides. But with that I will hand over to Nathan.

Nathan Bostock
Head of Reconstruction and Risk

Thanks very much Richard. Well good afternoon and welcome to all of you here and those of you on the webcast. First of all can I just introduce the team. Rory Cullinan is the Head of Non-Core Division, Christine Palmer, is the Chief Risk Officer for Non-Core Division and Pam Kerr is the CFO, COO for Restructuring and Risk and reports to me in that capacity.

So with that I will kick off. First of all on slide 5, just a little recap really to start the Presentation. First of all I think the key point for me is that non-core is a central pillar of the overall RBS Group Strategic Plan. I think often people think of non-core and associate it as being just bad bank. That is not correct. What we have done is we have sort of reprinted the criteria in the appendix so that you can see the criteria that we used in order to determine whether something was put into non-core or whether it stayed in core. And you will see that round about 60% of the portfolios and businesses that are in non-core are basically just non strategic assets.

I think the other point I would make is that my belief is that we have made good progress to date. We have basically gone from a standing start. So whilst everybody sort of hears that non-core exists, suddenly it is flagged. You have the assets and you can see them from an external point of view. That is not the same as establishing the organisation internally. Everything runs vertically. You have to connect up across the organisation as a whole multi country, multi assets and create what is effectively an ongoing entity. So I think when you put all of that together and look at the on track nature, I think we have come a very long way in the last sort of 12 months.

In terms of the bigger picture, the sort of RBS Group Strategic Vision. I think the point here for me is the two, core and non-core sort of sit together. They are both the key elements to driving the sort of fundamental macro reshaping of the organisation. So that is driving towards a 2013 objective of being a AA credit rated organisation. And you can see that really it is about that macro risk reduction and reshaping in non-core along with the sort of sustainability, lower volatility of earnings, core franchises, changes to funding mix etc with core. Put those two together and it is the combination of those two travelling together that gets us to that 2013. And I will talk a bit more about the funding towards the end.

So with that we will move onto non-core specifically.

Rory Cullinan,
Head of Non-Core Division

Thanks Nathan. Good afternoon everybody and good morning to those on the webcast from the States. Just bringing sharp relief, the difference between core and non-core. Whilst may not be a bad bank, obviously not really fantastic results in the previous periods. And emphasising the point these are not strategic businesses for the Group, not per say, the bad businesses for the Group. And looking just for a sense of scale of this, this is still a business that has a £2.5 billion of costs inside it, it still has 40% of the bank's var and it had 60% of the Bank's impairments inside it last year. So there is a large amount of scale, obviously a large amount of risk embedded in those balance sheets, a disproportionate number of RWA's and you can see on this sheet here, the RWA's is a total of the two. And the two numbers being those inside APS and those not inside APS. The larger number being the ones not inside APS. And also point out the fact this franchise is basically unfunded and we will come to funding later on in the Presentation. And therefore has no deposits embedded inside it. And a large amount of market risk given the income from trading last year. So a lot of things going on inside that business. We are going to try and peel back a few of the layers in this over the next few slides.

Just going over to page 9. The composition of the Division from its onset. As Nathan said, the 5 tests are at the back. Those 5 tests were really around the issues of franchise, value, connectivity, profitability through a cycle, RoE, greater than 15% and its funding risks. And therefore per say you didn't have to have 1, 2 or 3 out of 5, to actually pass or fail. You could fail just on one of these things alone. So we had a few businesses that fell entirely on connectivity or franchise. Some retail assets. You will have businesses on the other end of the scale that fail in terms of either profit, ROE or funding. Those can be very long term asset intensive businesses. So we have the whole spectrum here. And just on the sure scale size, as somebody said earlier today, this bank had start up of more TPA funded assets than Standard Chartered Bank and this was set up from scratch in the middle of last year. And also in terms of geography we are across the world. So we are in every time zone in pretty much every product and a whole diverse set of clients.

On page 10, just to try and bring this forward for people, it is very interesting. We obviously as an institution have a lot of real estate. It is important to pick out of here a) the fact it is reasonably diverse the UK centric, Ireland, that Irish exposure is not all the country of Ireland. It is our Ulster banks and some of those exposures would be on mainland Britain as well. And as you will see from the bottom sector, we have a pretty broad spectrum and distribution of commercial real estate.

I think the two important things to pull out of here is a) that 80% of this portfolio actually is a financing investment and only 20% is development. So we are at a different end of the spectrum. And that whilst loan to values in some cases are under pressure, the range of interest coverage ratios go from about 1.2 to 2.9. So on average about 1.7 across the portfolio. So pretty, on a cashflow terms, this market pretty well funded and quite stable.

Flicking to page 11, in terms of the corporate exposure, again quite UK centric and obviously European centric or Eurozone centric. Again also quite diverse across the sectors that it is financing. So again no significant concentration per say. And here just to highlight on here in terms of exit strategies which we articulate further on. It varies wildly by asset class, between businesses, single assets, geographical cuts. So again a whole lot of options that arise out of that.

On page 12, I will hand to Christine.

Christine Palmer,
Chief Risk Officer, Non-Core Division

Good afternoon everybody. On slide 12, over 18% of non-core's asset mix is in the markets business and therefore we have had significant focus on reducing our trading risk exposure as part of our mandate. We have two main markets areas, firstly the structured credit portfolios area and secondly, the exotic credit book.

In terms of the structured credit portfolios, that is primarily exposure to monolines, where the Group has purchased protection mainly against asset backed securities. And our net monolines exposure which you can see from the slide here, has been reducing for the last five quarters and is now down at £1.8 billion at the end of Q1 from a position of £4.8 billion sterling at the end of the financial year '08.

Losses in the portfolio have moderated as a result of this. And we have reduced exposure either through trade, restructuring and where feasible commutations either on a mass or bi-lateral basis.

Moving onto the exotic credit book, the other significant trading portfolio that we have within non-core, that is largely exposure to CDPC's where we have purchased credit protection through tranched and single named credit derivatives. It is a large book, both in terms of gross notional size, but also in terms of the number of trades that we have in the portfolio. But during the last 18 months we have reduced all the risk measures quite significantly. You see there at the bottom left hand side of the slide, VaR reducing from the end of 2008 where it stood at £23 billion to £10.2 billion at the end of Q1 2010. And CrO1 reducing significantly across the piece at the same time.

The most striking thing however from this particular graph are the two charts on the right hand side. At the bottom there you see the daily changes in the ITRAXX between January '09 to May 2010. And obviously the volatility that we saw at the beginning of '09, February and March '09 was quite significant and comparable to the volatility that we have seen in recent months over April and May of this year. But if you look at the chart above, you will see the daily P&L move of that book. And whereas in February '09 and March '09 you saw significant volatility moves of plus or minus £50 million, the volatility move that we have seen in recent months has been much reduced in terms of the daily P&L, plus or minus £5-10 million equivalent. We have achieved that really through better controls, through tear-ups and through more dynamic hedging and understanding of the book as we have moved through the evolution of non-core.

Now I will hand you back to Rory.

Rory Cullinan

Moving through to slide 14. I think it is worth reminding ourselves what the objectives of this Division is. I mean every bank is doing these things slightly differently so they are not all the same. So I think it is important to say what we are trying to achieve here. And the first point about optimising the timing, the cost and the method of exit with the emphasis on the word 'optimising' rather than accelerating or being expedient. We are looking to accelerate some reductions of capital and funding, all at the extent that is judicious and logical. And obviously at the same time, trying to help the institution overall by taking down over £2.2 billion of cost out of the business over that period of time.

At the same time, the other wrap around here is also the big issue of the core business management have focus on the continuing business and I think results across the Group would probably demonstrate that by and large has been achieved, particularly last year, in a very chaotic year. Whilst also at the same time have been maintaining and been cognisant of relationships and reputational risk across certain markets and recognition risk. And also as Nathan and Christine said earlier on, we have been very cognisant of the overarching element of what this contributes to the risk reduction of the balance sheet of the Group overall and keeping that issue very much front of mind.

On the right hand side, this exit options tree. I think we did this last February, it has still stood the test of time. Viable whole businesses or portfolios just again to get it in context if people haven't quite surmised. Only 7% of our TPA's are actually in whole businesses. So the vast, the 93% of our portfolios are businesses are in portfolios. So our leverage finance is per say not a business, real estate exposures are not a business, it is a franchise, but is not something you can sell by selling a single share or by selling a just doing an SPA agreement. And back to the whole businesses of sell now. We have done 22 to date. So done a vast amount of those and there is another 3-4 near to close. And there are very few left in terms of whole businesses to sell over the remaining part of the cycle.

Which brings us down to the bottom part of the page and the close now. We looked at businesses which either we can't sell them or it makes no sense, we are running down 2-3 businesses across the globe. That is in train. Selling, again the other common myth that everything we have is for sale and has to be sold. Roughly only 30% of what we have got in the portfolio is what we think is something we should be selling ahead of its maturity. And the vast majority of what we have is what we say, something we should hold to maturity because the discount one requires to take to sell it now is disproportionate use of capital and uneconomic at this point in the cycle. So again that puts it on context.

And slide 15 shows you some of the faces and names around this and a couple of points to pull from here, a) this is a very experienced team in terms of just years and in terms of people who have been through recessions, people who have worked globally in different markets, in different times in different businesses. So there is a broad range of skills. I think the other thing to pull out from this is there are three very different types of portfolios and businesses inside here. We do, whilst you are probably used to looking at the Group on a donor division basis, if we look at it in terms of these three business constructs. So we have on the left, Euan Hamilton with the Portfolio in Banking. Again, predominantly the ex-GBM businesses, that is all the real estate and leverage infrastructure and large pieces. Again a lot of assets, quite a lot of RWA's, very few people, very specialist teams.   Phil McDuell in the middle, who has got quite a small number of assets and a small number of RWA's. But you can see nearly all the people in the business overall. And of that 13,000, 70% of those people are embedded in countries. So as countries go, those people will go. And a further 18% of those people are embedded within portfolios which is still from a managerial point of view, embedded within core. So they may or may not go to a certain and lesser degree. But you can see in that box, there is a lot of people risk, there is a lot of operation risk, a lot of regulatory risk.

And then in our markets business, very few people, they are all front office, but a lot of capital tied up in that business and a lot of complexity. So three very different businesses, very different challenges, very different optics. And it is very hard to look at the business in one simple optic and one simple view.

On page 17, this is the run-off profile of the plan that we have put out now for some time. Again the thing to pull out here again is two-thirds of this is run-off. And only c40% is asset disposals. As some of you who may have been following it for a while, remember last year we originally said we were going to securitise £30 billion of APS assets, towards the back end of this 5 year run-down. Due to the change in the structure of the APS, the first loss from £42 billion to £60 billion. And we now do not see in any base case where we would trigger the APS. Rather than securitising those assets we have decided that we will have to sell those assets ahead of time because there is nothing to securitise at the back end. So we have a slightly more, on an earlier profile, probably more steeper curve in terms of asset disposals and arriving broadly in the same destination. Again included in these numbers, you may not have seen before, is the numbers for Sempra when we used number 252 historically. It is now 258 as an opening position, of which Sempra is obviously 6. You can find another slide which says Sempra14 and that is not an error. That was just because there is a change in accounting terminology. So on our balance sheet it is 6, but when we sell it our TPAs will reduce by £14 billion which we will come to in a second. Again impairments the same numbers you will have seen before. And roll-overs and drawings with certain pressures we will come to again, pretty consistent with our past direction and advice to you.

Page 19, there is nothing, two things to take from here, a) the £64 billion of assets have been taken off the balance sheet and those are funded assets, so they are not synthetic, those are in straight risk reductions. And the positive news is these have been taken off across the board, across all businesses and by and large the majority of geographies. So there is this structured approach to taking this down across the board by geography, by business. A lot of people focused across the globe.

Going to page 20, in the £64 billion that we got rid of three significant categories. The country disposals which have dominated the headlines. So 90% of the total turnaround is 10% of the money. And we have basically the TPAs are a very small reduction so far in terms of revenue announced. And there is a further £4.4 billion of deals agreed and we did announce 4 deals last week and there are 2 or 3 very shortly in the pipeline. Again you will see those completing over a longer period of time as it takes time to close the asset and liability disposals mainly with Reg. transfers. We will have migration of systems, migration of people. So these deals will take some time to close. There have been other whole businesses sold which is £4.5 billion by the end of Q1, again most of those have been announced transactions. And quietly going on, the bit that most people don't see, we sold quite a lot of the loan assets so far, £10 billion in Q1. Last year we didn't actively sell a lot of our portfolio assets because we were still in the midst of negotiating the asset protection scheme. So we were unsure whether we should be selling them or not. So we did a) we thought the market was quite horrible anyway. And so as the assets were very heavily written down and we thought on the basis we were ensuring the assets, there was no point in particularly trying to sell them ahead of time in case that cover came to fruition. In the end, since the end structure changed, as lot of the shape and nature of the scheme, we moved back onto a very focused asset sales programme. Again the big hidden piece is the £44 billion run-off and amortisations last year. A lot of that was about people, pre-paying early, people went to. There were windows last year with the equity markets and bond markets with good credit. Went out and raised new money and refinanced a lot of their bank debt. And of course we actively sought to get our money back where we could. And also spent a lot of time with our teams, really getting under the skin of these portfolios to really understand what exactly has been going on inside them.

Moving to 21, again you see the curve there on the TPA run-off basically stayed, as I said on the previous page, and you can see from now, the end of the first quarter this year, at the end of this year, again quite a large bulk of disposals in the pipeline. Sempra has been well announced. There is still quite a lot of run-off to come, there is a good strong pipeline of asset sales, obviously rather choppy markets, which we can talk about later on. But as ever, as across the Division, we are there to create a wide spectrum of optionality and choice so that we cannot get hung up on one event in one place in one market.

On Asset Management Strategy on slide 23, just picking out some of the salient points here. Back to this issue of taking risk off the table, across the board, you have capital intensive pro-cyclical assets which to some degree have been less pro-cyclical than we originally thought. We have a lot of single name and sector concentrations as an institution as a whole. We have a disproportionate amount in the non-core sector. And we are also looking at that balance between further credit deterioration versus the expected upside, the balance of probability and likelihood of probability, migrating worse rather than better. We are opportunistic, we have to create a lot of optionality around the portfolio which is ongoing. Again we are talking about not rubbing up against the core strategies and conflicts there. And most importantly, and we will come to again in a second, making sure we don't just cherry pick the assets out and leave the excessive proper toxic bank at the end that as basically embedded with a lot of real dead either zombie assets or heavily impaired assets or unimpaired assets. We have constraints internally. We have capital management guidelines to try and tramline and work around. We have a lot of volatility still left in our trading lines, which we have to be cognisant of and impairments are still, you know obviously significant components and largely hopefully they are behind us in terms of the divisions impact. So the three very big things that will effect us and make these optionality move around is around the issues of our trading losses which are volatile, our impairments which we think are cognisant of and a potential to what extent do we lose money on disposal of assets. Those three big things have still potentially changed the shape and outcome of what happens here. And to make the last point, which is hopefully obvious. In our economic outlook for here is reasonably in line to getting better all the time. This plan does not view double dip recession which we think would change things. It obviously sees over time some sane or more logical levels of liquidity in the banking markets. And you have more wholesale funding in those markets. What it is not entirely cognisant yet and Nathan will expand on is, obviously there is a large element of regulation coming down which is invisible to most people. And the question whether it is just a small squall or likely to be a future hurricane or something in between or a sequence thereof. So that is still quite a large unknown for us.

Slide 24, back to emphasising the managing the portfolio run-off. You can see the rollovers by and large are concentrated into commercial real estate and we are cognisant of the fact that would be the most difficult asset class to potentially re-fi or to get our money back at maturity dates from what are otherwise sovereign borrowers during the course of this strategic plan cycle. The vast amount of our sales coming out of the corporate sector, between £50-60 billion, again looking to sell ahead of time our markets book. About 50% thereof. And again, just trying to attack it on all sides and all scales and all the geographies.

Going to page 25, back to what I talked about previously about the rump of what is left. That really falls into three categories. That which is money-good assets expected to mature during the period after 2014. So an example of that for instance our project finance book. A very long dated book, very low historic default rates, 20-25 basis points. To move that book today would be exceedingly expensive long term funding, low yields. The hit you would take from that from a capital point of view is illogical for us to sell it. There is also some very long dated good money, good assets like the housing associations which have zero historic impairments in the UK. But currently whose intrinsic value, you will creep back to par, but the funding, the yield on it now is so low the discount you would take to sell that would be again equally illogical. There are things that are definitely left that are higher risk, costly to exit. And we should at this stage, it has either been quite robust because it has survived the storm of the recession, it has either been restructured, it has either been impaired or it is still trundling through. And fundamentally we should be, you know this end book should be a real clarity around what it is. I think that sort of says that in the previous areas, we are looking to manage things that are capital and sell things that are capital intensive, things that are a disproportionate cost to funding, trying again to tackle things that are long dated in terms of the book. And anything that matures in a very short order by and large we should actually just let run-off. The discount is too large to sell. And what to do with this rump, is not a decision we feel we have to make today, make it when we get closer to where we are.

On page 27, there is a nice page of numbers. I will try and pick two or three salient points in here. Income from the trading activities, loss last year at £5.2 billion. 70% of that was essentially one off items, corrections to our CDPCs or capital relief traits. So that level of volatility we strongly believe will not occur going forward and our first quarter obviously is a very small number. But of course we still have quite a lot of exposure to the volatility of that sector. Losses on disposals, again none in the first quarter, quite a large number last year in the businesses we sold. Again it is, not also to confuse that losses and disposals means dilution to capital. Again we are trying to sell capital intensive businesses. So we may take losses through the P&L but we try and seek to where possible to be accretive to core Tier 1 as a guiding light. Expenses of £2.5 billion, 77% of those expenses are directly under the control of us as a Management Team, of which of that total 45% of those are people. We have a very visible plan to make the people go away over the next 2-3 years. Previous slide, slide 15, a lot of those are connected to the countries, they will start to flow out. And of the other balance of the 55% that is left, half of that is just depreciation which again will go and mostly related to our aviation capital business. So again that is a visible cost that will go away. So just on the whole shaping of this, we will come on to talk about impairments in a second. The three big numbers that are part of the cycle, are around the trading lines, the impairment lines and losses on disposals. The income is predictable and visible more for us than it is for you. Expenses for us again are clear and predictable and we can see a visible means to managing, running-off. And the other three items are what will change the scope of the answer.

On page 28, just to emphasise the point. I am not sure how helpful it maybe to you in trying to model this out, but just to make the point that TPAs, RWAs and therefore expenses do not go down at the same velocity at the same time. Our TPA reduction is visible, but we are looking to within, by the end of next year, I have taken half our cost base out because that is basically mostly people going away. And again looking at the rump of cost towards the end as this takes out over time. Again quite a visible, logical plan to taking down this cost base which will also be changed the cause cost of income ratios as we get to 2013.

I will hand over to Christine.

Christine Palmer

So on slide 29, in terms of credit risk and the portfolio quality, the credit risks we have within non core means that 34% of the credit exposures undergo a heightened level of portfolio monitoring and active credit stewardship. The graphs on this slide and the subsequent couple of slides are actually also on loans and advances basis rather than TPAs or RWAs. In quality terms, I think you will have seen this slide before. The majority of the book is either asset quality and Five, which will equate to a BB or lower. And overall quarter on quarter the active management of the book has led to a reduction in those names that receive heightened monitoring, but equally the number of defaulted assets has gone up by £2 billion between the end of ’09 and the end of the first quarter as a result of some of the lower quality portfolio assets being impaired.

In terms of the geographic spread of the portfolio, on slide 30, the credit risk is well spread geographically. The main concentrations are in western Europe, Ireland, Germany and Spain, and also the UK. And sector wise, the dominant sector is real estate.

Moving onto impairments, to date we have taken £16.2 billion worth of impairments from 2008 to the end of the first quarter. £10.9 billion of that was recognised between January ’09 and the end of March 2010. And the balance has actually come from earlier periods. We would expect the impairment levels to remain elevated going forward. We are not changing our guidance. We expect to take between £10 – 20 billion of insured impairments from here on. However the mix of those impairments is changing.

In terms of the cumulative charges that we have taken to date, we have seen significant charges from leverage finance and also some of our retail books. But latterly we are seeing retail and large corporate trends trending favourable. Going forward we would expect to see commercial real estate impairments to remain high, particularly in Ulster and we continue to revisit the forecasts that we have for impairments so that we understand the dynamics that actually move those portfolios both on a macro and micro economic basis.

I am going to hand back to Nathan now to conclude.

Nathan Bostock

Thanks very much Rory and thanks Christine. So to sort of come full circle, come back to the funding and the sort of macro picture. I think if you look on the left hand side of slide 32, you will see a picture here which really reflects how this macro nature of loans to deposits fits together. So the Group moving from 150 to around about 100 in loan to deposit ratio between '09 and 2013. If you look at the current position, the current position is around about 131. But 102 in core. So it shows you that clearly the big drive and the big reduction in the £252 billion of funded assets has a significant impact on the overall loan to deposit ratio and clearly this is why I say the two things act together. So continue to build deposit base in the underlying core franchises to move it only slightly, but ultimately moving to 100% overall.

On the right hand side you will see as well that the term funding, is a good profile versus actually the run-down of non-core. So non-core is running ahead of a term funding requirement going forward. So again the right type of profile from helping to create a better overall funding position.

If we actually look at slide 33, this shows you the breakdown of medium to short term funding for non-core. And so it won't surprise you to see that because we have got quite a lot of long term assets, we have also got quite a lot of long-term funding. I think the key point here is to link it back to slide 32 because in reality what you are doing is by bringing down the asset side of the balance sheet, you don't necessarily effectively have to exit the long term funding. What you actually do is again improve the mix across the Group as a whole. So the £258 billion clearly has a disproportionate impact on the short term funding scenario of the bank and at the same time you can use this to effectively help rebalance the overall mix.

Just coming to concluding comments, I guess very much similar to the opening comments in as much as non-core clearly a strategic part of the plan and a very central part of it. Clearly good progress to date so TPA is reduced by 25% so far. And I think risk significantly reduced. Now that is not to say that risk has gone away, it clearly hasn't. We have shown that in terms of the fact that we still have things like trading risk. We are still running things like VaR, but we believe that sort of holistically we have managed to reduce that overall volatility quite significantly, but there is still more work to do.

So that was what I was going to conclude with regard to the Presentation. I probably would just point you towards the Appendix. What we have done in there is we have put three examples of disposals. I think one of the key things probably for yourselves is the fact that, how believable are disposals? And I think Rory sort of articulated that in many instances we are trying to balance a lot of potential items to come up with the right profile. But we have been working very, very hard through 2009 to affectively create the greatest number of menu options that we can have and looked at the different sort of scenarios that might happen in terms of going forward and how might one be opportunistic as one goes to actually utilise those. So one of the best things to do I think is just actually put some examples in the appendix. That is what we have done, but again you know this is a journey and for us the idea is to create as many options as possible to actually manage that disposal programme.

So Richard I think over to Q&A.

Question and Answer Session

Q1 : Male

Can I ask you how you started off the funding for this division when you set it up? Over here you tell us that paying into group funding is mostly allocated for calculations only. Can you talk to us about the assumptions you used to determine the cost of funding for these assets and also perhaps if you could tell us what is the average cost of funding for the whole non-core bank?

Answer
First of all in setting up the division, the funding of assets, directly attribute asset by asset and on maturity and if they are long term assets, they had original funding provided by Group Treasury, so it is a direct, partial relationship from Group Treasury who provides the funding to the non-core division. Now those assumptions change over time, we have evolved it, but basically it is a direct one to one relationship which is what you see it.

Further question
Is the cost of funding of non-core significantly higher than the cost of funding of the on-going Group corporations?

Answer : Female
Only to the extent there is a teller difference otherwise it is very much dependent upon the tellers and the underlying assets. There is no specific additional risk being carried to funding for non-core assets.

Further question
But that would imply that costs are higher?

Answer : Female
That is right, but that funding will be dependent on the assets or one off costs.

Further question
Because you have no deposits the cost is?

Answer :
Correct, it has got to reach a proportion of the legacy term funding.

<u>Q2 : Male</u>
The plan seems to hinge on assets maturing and of course to get assets to mature maybe property companies or whatever have to refinance themselves from somewhere else. So I wondered if you could tell us about the refinancing risk for those assets which are dependent on finding new external finance so that they can repay RBS? If you could qualify that risk?

Answer : Rory
I think it would be best to go to say, pick a slide, slide 24, take the corporate side. I mean the corporate side has a lot more optionality. A lot of these are quite large corporates and when they access the bond markets, they get access to equity, quite a wide geographic spread. Retail likewise, there is quite a lot of competition there. So it comes down to the issue around commercial real estate. Again it is assets and geographies. I mean clearly across Europe very different pockets and very different markets. In the premium end in the UK, we haven't seen much challenge there at all. A lot of demand, there seems a lot of financing available for it. So come more towards the smaller deals, regional deals, secondary tertiary deals, again those will be more challenging. I think we are cognisant of the fact we will have to roll over more of those than we would like to do so. Again in Ireland quite a lot of that development land not much obviously, very little new liquidity in the Irish banking market. Again a large proportion of those will see to do. In Germany, a lot of German banks are active still in real estate, second largest exposure outside the UK in Europe. Spain, a lot of our commercial real estate exposure is actually corporate exposure rather than direct asset by asset exposure. So again there is more optionality available to them. France we see is quite buoyant, again not a huge exposure there, but the banking market is reasonably attractive. And it is back to the old issues, we can lend, banks can lend short loan to values at 280, simply by business points, it is probably not a bad time to be getting into the business to lend that marginal euro. So a lot of very selective challenges around the edges of this. And it is very hard to be very precise early on. It is obviously a constant. And the immediate macro view is that looks rather challenging. And then you start to chop it down piece by piece, you can see pockets of

where it is clearly much more challenging and others where it is not really challenging at all. And I think that is the position we have now got to. It will change I think.

Further answer : Nathan
I think also we have taken a balance here in the sense that of the £63 billion that you see there, we showed on an earlier slide that we are actually at around about £51 billion now because this is at the end of ’08. You can see that we have actually allocated, let’s call it the lion’s share of the roll-overs to the commercial real estate again. So we feel that we have given the right overall balance to the picture. And we have done that typically by looking at asset by asset and there is nothing like the hard work of going through each individual one to see where you stand.

<u>Q3 : Male</u>
Of that £51 billion, what percentages premium tertiary you referred to?

Answer :
It would be quite hard to be precise like that. Towards the higher quality end. Because the better quality corporates who refinanced. A lot of the big British, UK corporates, the Hamsons which are no longer in our division, but a lot of them tap the bond markets and equity markets. House builders was a big area and they all went to the equity markets in the middle of last year.

<u>Q.4 : Male</u>
Just to be clear, the forward process behind the numbers on that slide, is that contractual maturity or is that asset by asset, we think we guys can finance away? Do you think re-jigging at 5 out of 6 tens of billions to refinance in 5 years, given some of the pockets in there, is that just contractual maturity?

Answer: Rory
Well it is our general shape of the amortisation. To go through every single maturity, we would still be here doing it. A lot of assets in here. That is a general feel.

Further answer : Nathan
We have done that for the larger credits, yes. When you get down into something like an SME portfolio, then no.

Further answer : Rory
I can tell you there are 2-3 assets in the sale profile of real estate that we are trying to sell because we think they are a re-fi risk and we would take a discount there. We are still very cognisant of the fact there is re-fi risk among certain of these assets which we financed in 2007 with big numbers, big bridges. And we know they are not going to get refinanced so we are trying to sell a year or two ahead of those. We would sell them less than.

<u>Q, 5 : Male</u>
How often should we expect this plan to move? So in other words if you flex it if the world gets better faster or we deteriorate from here, is this something you will review every quarter or as analysts what should we expect in terms of revisions to this plan?

Answer : Nathan
Well to be fair, we constantly review it because we are very proactive around looking at the individual items that make up the constituent parts and what we can do about them. I think what we have tried to do with the overall picture of the profile, is sort of build in a sort of pluses and minuses so if the macro economy sort of moves in the general direction we are expecting, then we will have pluses and minuses, but the tract is the tract. If it was to suddenly, you know sovereign crisis blows up euro, etc, then that is not this plan.

Further Answer : Rory
I would also say our break is very sharp now, our accelerator is quite slow. So I think we can solve things very quickly but it takes a long lead time with a lot of these assets. I think if you saw a dramatic change in the markets, we would not rush to sell anything that was going to mature in a year's time. But the time you had got there it would have actually matured. Not really worth the effort. So I think you will see marginal changes around the maturity profile. So you will potentially see a bit more of the sales or a bit less sales, a bit more or a bit less in pebbles. There is not a huge, you are not going to see 50% swings in this profile.

Further question
And in terms of the assets?

Answer :
We report quarterly and so you will see what FX impacts there have been, what we have sold, what we haven't sold. So no doubt will get questions on a quarterly basis on it.

Further answer : Rory
It is hard to pick a straight trend off what we sell because we can sell a huge chunk of non-core and then nothing in the next. There are chunky deals and selling 5 million tickets or 100,000 tickets off the desk or to the instruction trades at £2 billion.

<u>Q 6 : Male</u>
It does strike me that the Division is quite clean. What is in non-core stays in non-core. Is there any chance if the world gets better you reclassify things back to being core?

Answer : Rory
There is never 3 years or 5 years these days. I think the issue around that is we are very rigorous on change controls around migrating things, leaking between the two walls. So we have very, very rigorous processes. And things have gone backwards and forwards are absolutely deminimus and are pure error rather than any construct or anything else around it. Another question, people say, are you just refinancing things out of core. Non-core assets being refinanced in core, is that not a way you do it? That is nearly deminimus. Remember the overall objective here is to reduce the TPA funding for the institution overall. You know all the things, for instance, things where you have had products which are really non-core for product geography for a client, so we have your core clients with non-core products. If they go to refinance and mature at the higher rates, you would put them on the core balance sheet. These things are not really happening in this market. And also where we had the rigour of the auditors all over that issue. And obvioiusly the regulators likewise

all over that issue. So the ability for things to seep backwards and forwards between the two is absolutely deminimus.

Further answer : Nathan
At the end of the day we are very cognisant of the fact that we have to solve this overall picture of RBS as a bank. It is not just non-core in isolation or core in isolation. We have to solve the entirety.

Further question
And is that go the other way as well. If you have something. One argument says if you want to sell something for 100, you go out and shop 120 and let the buyers pick out the 100 they want. Is there anything in core that if you are out talking to people about a non-core asset, they go not quite that bit, but I wouldn't mind that bit?

Answer : Nathan
We had one deal with one asset class. The core will be sacrificing itself for the greater good.

Further answer : Rory
Structured just long credit. We may take some stuff from core to sweeten returns on something else.

Q 7 : Male
What is the main risk to you not achieving your targeted run-off? I guess these assets unlike a lot of assets banks in Europe who are having trouble funding themselves can't be repo'd at the central bank. So the pressure is a bit greater. What is the risk that the run-off doesn't exceed the maturing funding to the extent you hope?

Answer : Nathan
We have tried here to build what we think is a realistic plan in a, I will call it a sensible scenario going forward. Does that mean it is a perfect smooth sort of recovery? No, I mean we expect some form of volatility and we are seeing it in the sovereign crisis. If indeed there was to be some form of big situation, I don't know, something like the euro or something like that, then undoubtedly if you know what I mean market liquidity as a whole would dry up. That market liquidity is the same liquidity that investors need or equity houses need etc. So that type of thing I think is a definite if you were writing down the big things that could happen, that is one of them. That is not what we have based it on. And that is not our view at this point in time. So we do assume that we continue to see a slow recovery. Again I think. The one thing I would say is that we have a very big portfolio, And actually in many respects that is as much a positive as one can argue it is a negative. So if you look around the world at some of the things that we have been doing, it is because the world isn't just a homogenous mass today. Look at the Canadian banks, they have got strengths, look at Australasia, they have got strength. It is not surprising some of those are making strategic decisions. So again you know it is all over the place in terms of pluses, minuses, more liquidity, less liquidity and in fact numbers of institutions that actually will use this point in the cycle as indeed their opportunity to advance. Now that might just be fund managers in certain investments. It might be you know banks making a strategic decision etc. But it is a variety, it really is a variety spread around the world. And the reality of this job is it is very different to your normal BAU. I mean ever day you have to get up thinking stewardship and divestment. That is what you

are doing, it is not the same as getting up each day thinking about the fact that I am turning over my balance sheet, how am I going to be giving this customer, what am I doing with the new business. This is about risk management, risk reduction. So that is stewardship and divestment.

Q 8 : Male

So what is proactive portfolio stewardship to get the 90 to the 100? That excludes disposals it says here. So what are you doing proactively to make these assets run-off any faster?

Answer : Rory

The reality is the run-off is not just to say, you will go away for a year and a £100 billion turns up in the bank which would be very nice if that was the case. At the end of the day, there are re-fi risks on some of these clients. There is a list of who they are, we are trying to help people find alternate sources of finance. We had a case in France recently, they said, we will repay you back at 90 cents and we said, no we would like 100. But that went backwards and forwards for a month. And then we said we would take some new equity, no wouldn't do that. So we helped them find another bank. They ended up taking a bit of dilution to help them find another bank and repaid us at 100 cents. So that is 4-5 months work. 120 million euro loan. So it was worth while. So you have to find people who will just say okay, we will try and cut a deal. So we try to get to them early to stop them cutting deals or cut a deal with somebody else and not with us.

Further answer : Nathan

But in terms of stewardship it means you know we take a view in terms of things like, if we have a single name concentration, do we want to do something about that? Either sell the principle hedge sum of it again. So the whole time we are looking at the overall risk profile we have got. Equally we have a knowledge of the assets. We may have a view, I think as Rory pointed out that in the future we can see actually that we think that is potentially a risk that we don't want. We may be prepared to actually exit that at a certain price. Now for others, we may have a completely different look to it. But for us portfolio management is effectively making those decisions on an ongoing basis across the portfolio, whilst you are still managing both the run-off and the other disposals.

Further answer : Rory

While leveraging on example where we managed on that book. Taken off a lot of single name concentrations and a lot of exposures. And I have just seen revolvers which is something you can't sell in the market, we have taken CDS against some of the names. A lot of that shaping of risk in that portfolio is dramatically different from what it was say 12-18 months ago.

Further answer : Nathan

And some of that again is just the case of the world moves. So if you went back to last autumn, people I think, not that many people would have said, guess what, there will be a big push up in leverage finance pricing in the first quarter of this year. Some people would have had a view, but it probably would not have been as strong as it was. Once that comes, guess what, you get some secondary liquidity. That means you can do some things about hedging some of your exposures. So again it is about being very much ready to do things as and when the opportunities present themselves. And so that is really something that Christine is looking at all the time.

Further answer : Christine

Yeah it is about understanding the dynamics and the portfolio, what drives them, what makes them move and what things change and how you take advantage of those change on both the sort of macro and micro environment.

<u>Q.9 : Male</u>

Can I ask something in a slightly different way? What is the level of interest in your assets currently? And can you give us a number of what proportion of bids you are turning away because of price?

Answer : Rory

We are catching up with people, they want to sell. We have a pipeline. We have over 100 things in the pipeline today. Single, discrete activities that can be ranging from £5-6 billion trades down to £10 million trades. All across the board. Last year the market, most people had money in equity last year wanting 20% plus returns. And there really were no buyers then. So a lot of the rush, particularly in leverage market was a lot of people saying, well you know what, I can either get nothing or I can get 15. So a lot of those markets, their return criteria changed quite dramatically when they came into the market. Again people looking for significantly high equity returns from us, we would not be a seller. Anybody above 15, broadly not having any discussions with anybody on any asset class because the base of our cost to capital versus their cost to capital, our shareholders take would be uneconomic and disproportionate to any economic reality. So we have had buyers, we have had a lot of buyers who were there, we had three deals in the week of the sovereign debt crisis, we had three deals fell over. It wasn't a question of the bid, it was a question of just no bid. Don't want to trade. That buyer has gone away, new buyers turned up with different pockets of money buying different things. It tends to be quite a lot of buying, there are not too many auctions, there are small mini auctions going on. There are a few, some with larger deals and more controls, discrete. 4-5 investors, big investors. There is just a whole raft of things going on across all the businesses.

Answer : Nathan

It is a little bit like a hopper as well if you see what I mean. You have got to put volume into the top such that you are preparing it, knowing that ultimately that will get thinner through time, either because markets will change or because investors will pull back or whatever. So constantly when we are looking at the pipeline, we are looking at a variety of things that we are building, not just for tomorrow, the next day. But these things have a gestation which is a reasonable period of time and then you don't know ultimately, necessarily which ones are going to be the ones that you are going to offload. So it is a constant you know. You can see the amount that you want to put in. You can start to structure things. I mean it takes lead times can be 6-9 months on certain things. And even a country sale. I mean if you look at it, you can go through a, let's call it a 3-6 month period to actually do the sale and then anything up to an 18 month period to actually complete.

Further answer : Rory

Well those four deals we closed last week, all started in the first quarter of last year. It is bizarre all four of them turned up in one week.

Nathan
And they were announced what July/August time,

<u>Q.10 : Male</u>
On page 10 on commercial real estate, the comments are not a surprise, LTVs under pressure. But I just wondered if you could talk about to what extent that is a constraint on speed of asset disposal or do you need to still see real estate values improving before you can?

Answer : Rory
Most investors here would be looking at the credit investors not capital investors so they would be looking at yield rather than capital values. So there is quite a different market in that sense. I mean we have very few real assets left. Obviously we see things when we were selling the Grosvenor, some of the hotel portfolios, but limited in terms of the number of equity positions or control positions that we own. So the pockets of money we are looking for are very different in terms of what you are thinking about in terms of the single asset borrowers.

<u>Q. 11 : Male</u>
Can I ask your impairments payment? Can I ask how you get to that £10-20bn figure?

Answer : Christine
Essentially it is a process of looking at each underlying portfolio, looking at the key assets in that portfolio, looking at what we have taken historically. Looking at what we might realistically expect to take over a cycle. Looking at the macro environment and the characteristics and changes to that that may drive different impairments and literally going through portfolio by portfolio by portfolio, to come up with a reasonable forecast under different sets of economic and other scenarios and options that we might have available to us.

Further answer: Nathan
But again just as with the maturity profile, I mean we have done this typically asset by asset certainly for material sized assets. And we have also done it cognisant of both experience to date and also the interest rate environment. And I think both of those are very relevant given that whilst typically people use history, there is shall we say, a slightly different scenario at the moment. So we have built all of those types of things into that.

Further question
The whole philosophy is more kind of underlined for value driven or is more demand driven, ie, how much money am I really likely to get from this? Because it might be, the fair value might be 90, but the realistic realisation might only be 70.

Answer : Nathan
This is impairments based on normal accounting standards that apply to those particular asset classes rather than fair valuing the overall balance sheet.

Further question

Okay, if I take just lets say mid point in that range, 15 and I add it to the 16 that you have booked so far. It is 31 which is just barely 10% total expected loss on the initial 258 of the portfolio which is a hit, but is not a worse case scenario. I mean 10% expected loss on a big portfolio full of trouble like this one is not.

Answer : Nathan
That is my point, if you go back to the very beginning. That is why I said it is very important to actually get the mind around the criteria of assets that went in. Because yes if you take a 258 and you assume that all of these are higher risk, and I think Rory illustrated some examples. If you were to look at for instance, well our social housing is £5-6 billion, £6 billion. Project finance again, decent size portfolio. If you look at the experience of these. I mean if anything they are at the other end. If you drew a normal curve, you would say, well hang on higher risk should put me this side. Guess what, these actually, well social housing would be a complete outlier off the left hand side. So when you take that overall picture and mix, then it becomes I think in my view very realistic.

Further answer : Richard O'Connor
Be careful, the impairments are based on loans and advances, starter loans and advances of 185 and not 258. Because you click all the markets in other portfolios. So therefore you are talking more like a different number to the number you are thinking about if you are basing it on the starting number.

Further answer : Nathan
And then you still have to switch as I say into what that portfolio really looks like.

<u>Q. 12 : Male</u>
Can I ask, how much is the Wilkie's mark to marketing now? And related to that I saw in first quarter, no write downs at all and I wonder if you could just talk about the potential for write backs in this book?

Answer : Nathan
Off the top of my head, I don't know how much of the book is mark to market. Some of it is AFS.

[All talking]

Of course the problem is I mean balance sheet isn't a great. For mark to market it is not a great representation of necessarily the risks that you are taking. No, it is all in John's. So if you look at.

Male comment
Page 15, certainly in the markets business and there is a split there and AFS and HFT.
[All talking]
65% is mark to market, about £20 billion.

Nathan Bostock
About £20 billion which will basically be that structured credit portfolio we are talking about. And if you go back to the Presentation, we were showing if you see what I mean that the exotic credit trading is now performing well in terms of overall volatility. That leaves you the structured credit

portfolio which again if you go to the financial numbers, you will see that in that first quarter we were round about 0.1. So to answer your question, I think you have to recognise the first quarter was a good quarter from a markets perspective. The second quarter has been a less good quarter. So if it was me, I wouldn't be sort of taking the first quarter and sort of extrapolating out. Equally, as Rory I think tried to provide guidance for you, neither would I take last year as being anything representative either of where we would expect, given the nature of the items that were within it.

Further question
Maybe you can expand on this. I know you are running this, I think your expression was stewardship and divestment are the sort of watchwords. Do you actually think of non-core as a profit centre in any way? Do you have a view about if and when you could see the division in profits. I mean clearly we have got lots of moving parts. But when we do our modelling we have to think about, how is income behaving with assets, costs? I mean I am just looking for a bit of help really.

Answer : Nathan
Yeah. No I don't think of it that way. Now does that mean that we don't take the opportunity to you know optimise income? Well if we can re-price an asset and it is due for re-pricing, then we will do it. But prima-facie if you look at the sort of the upside on those income lines, is nothing compared to the downside. It is asymmetric. So it is a bit like getting control of that exotic credit trading book and travelling through time with it, well controlled. It doesn't just stay static. Now I have no intention of driving that book to try and drive, making trading revenues, when it is an enormous book, where the downside if you see what I mean is by not managing the risk appropriately. So I think, yes we take any opportunity we can if you see what I mean to manage the income line. That net interest margin line though is pretty, I will call it pretty static, other than the major things such as asset reduction and those types of things. And the trading line. We are not trading the business in order to trade to make money. We are trading the book in order to risk manage and change the cone of uncertainty in the outcome.

Further answer : Rory
The best way of describing it, the people are very commercial people and trying to maximise profit. Commercial, very commercially aware. Good negotiators, good restructurers.

Further question
But just in overall terms, if we look at the profile of the run-off and let's just assume that that is achieved, I mean net interest income I would think would come down with the profile?

Answer :
Yes

Further question
Costs?

Answer : Rory

Probably.

Further question
And then it is the other elements, the impairments I would assume and the trading?

Answer : Nathan
You have got three lines

Further question
And that is the more difficult one. You are saying to us you are not quite sure, well you are just trying to narrow the glide path. But I mean the glide path is what to zero by the end of 2013 is it?

Answer : Nathan
Well it certainly would be to small numbers. Again these books are if you take the exotic credit trading book, the maturity profile of that goes out past 2013. So the key there if you see what I mean is to continue to take the risk down and to take it until lets call it a smaller and smaller cone of uncertainty, such that as you are travelling through time, that gives you more ability to manage the book. Clearly those are also the types of books though that have the most impact in terms of things like the regulatory changes. So your ability to do things with them other than tear up individual trades, hedge them etc is more limited, certainly until the changes to the regulatory regime change. In other words, whilst there is uncertainty, anybody you might talk to about any of these types of things that are impacted, clearly their mindset is going to be you know, enormous discount based on uncertainty. So again, fits anyway with the profile of what one would want to do. But I think there is some regulatory uncertainty that we all need to see land a bit more. And equally that will effect the rundown profile in terms of say the change in profile of TPAs versus RWAs. So if you think about it, the TPAs you can see are coming down, but you know in RWA terms, the key drivers are normally pro-cyclicality. Well actually you can probably part the pro-cyclicality reasonably and the bigger one is the potential tsunamis that sit there in the regulatory change world. And unfortunately I don't think any of us can say where they will land. What we can say is they are typically becoming less impactful. Still impactful, but less impactful and they are pushing out further. So if you look at things like CRD3, the impacts of that are potentially looking to be perhaps less than the market first interpreted because of the various discussions, QIS, all this type of thing. But also they are pushing out. So they were going to be 1st January next year, they are not likely to be 31st December next year. We take a very proactive approach to the concept of capital because it is one of the key things we are using as a metric in terms of looking at the overall book. So from our perspective again, we will want to try and do things where we can, where we see something happening in the future and we think we can take action before then. But it does leave us in an uncertain world as to what are the RWA impacts. But they are a headwind. So if TPAs are coming down, you still have to look at RWAs as with a significant headwind.

Further question
Has your thinking changed on that by the way, CRD3 effects? I think you had about £60 billion for market risk?

Answer : Nathan

No that was the bank, the Group as a whole. About half and half. No, I would say again, I don't see major changes at the moment in the way CRD3 is heading. I do see a lot of discussion around things like the liquidity regime and these types of things. And you do see a lot of discussion around quantity and quality being the sort of capital element rather than let's call it the trading risk RWAs. And I think there is a lot of discussion still to go on around those and potentially timing as well. But CRD3 I don't. I think that is moving faster.

Q 13 : Male
How much capital do you have currently allocated to non-core?

Answer : Nathan
Well 10% of the 171.

Further question :
And what is the main focus from say, Stephen Hester looking for you to ease the funding pressures that the Group is facing. Is that the primary goal or are we looking to maximise how much of that 10% capital is left at the end?

Answer : Rory
There is no single answer.

Further question
How you guys incentivised….If you succeed you are out of a job in 4 years time. So what is the?

Answer : Rory
I think the answer is the judicious use of capital, closing the funding gap, also being cognisant of our P&L and our capital and our ability to fund ourselves. All those three things go into the judgement. There is no single metric that trumps any other.

Further question
And if the Group was say struggling with its £25 billion or £30 billion of wholesale requirement, would the response be non-core shrinks even faster than planned? Or would we see some other action say from the core business slowing down?

Answer : Rory
Non-core as I said earlier takes 3-6 months for us to move things and breaks very sharp and accelerates very slow. So better tell us now, we want it in December. So it is challenging. And then you are giving prices around certain of our assets, would it be economic? I find it hard to think so.

Further answer : Nathan
Remember non-core is still only a proportion of the total balance sheet of the bank. About 22%. So it is very important from that overall funding perspective, but it is not the absolute.

Further question

Or the mismatch of the Group's funding concentrated right. So if you look at core it is 100% but not?

Answer : Nathan
It does, but it does not change your ability to carry out actions across the bank as a whole, be they from a funding perspective. So again, you know if you look at it. The slide shows you that effectively you know non-core rolls off and it is ahead of your term funding. It doesn't stop you going out and doing funding as a whole. It just says that actually your requirement to go out and do it changes dramatically. What you choose to do is very different picture. So you are managing a very big balance sheet overall with a lot of potential leavers and what we would do in non-core is we have a glide path if you see what I mean that is understood. We talk to Treasury all the time, but I think as Rory has said, in general our glide path is the glide path that today we would say is the right optimisation of all of the aspects, including funding.

Further question :
Is it possible that you would require more capital from the Group before you managed to liquidate the whole non-core?

Answer : Rory
Okay, in which case it would occur. It would occur if you didn't sell any assets and RWAs went up.

Further question:
The reason I am asking, if you have £17 million now and you say that you might lose between £10-20 million in terms of impairment and obviously it is anyone's guess what happens with the revenues, but normally they would be negative. So you will consume all that capital through losses before most of the non-core is sold. So I think it is not unrealistic at all to imagine that in three years time you will have to go back to the Group and say, can I have a few ?

Answer : Richard
If that is a pre-tax number, then you have got, then you trade losses on top.

Answer : Nathan
Then you have got run-off

Answer : Rory
And you have got focus on heavy RWAs usage. So again.

Further question:
It is difficult.

Answer: Nathan
And impairments itself takes down.

Further question :
What is your central lesson now, that you have just the capital that you need or do you expect to give some back or what is your kind of view, gut feeling in 4 years time?

Answer : Nathan
I think our capital forward view is driven by 4 things and unfortunately those 4 things are material and in which direction they end up, I think is uncertain. But basically they are the impairments number which we have tried to give a feel for. They are the trading line, and again what we have tried to do there is sort of give you a feel for how it has moved historically, where it is now and whether that is a real feel of where it is going. Disposals, which does remain again a variable, albeit if you were to look at the first quarter you would get the wrong feel, because overall we have said that we took disposal costs last year and we would expect that over time again it would cost money to make disposals. And then on top of that unfortunately we have got the RWA changes. So I think it is a range of possibilities.

Q 14 : Male
Insurance Division, how come that wasn't mentioned non-core if you are definitely going to sell it?

Answer :
The answer is it is not managed by non-core, it is managed by the insurance business and it is as you know, we will run it for the next 2-3 years.

Further Answer : Nathan
We should reverse it. It is only Sempra that is in non-core. So the other 3 aren't.

Further answer : Rory
They are so embedded, so big they will stand alone or they are so embedded inside the institution already. To be in non-core, we have to manage it. And for us to manage a disparate bunch of 18 branches, that would not make any sense or again the GTS business is pretty embedded.

Further question
I just thought from the point of view, when you are trying to model the 2013 bank, what it looks like, it would be easier to carve it into.

Answer : Richard
You have got insurance showing separately so it is not that difficult to model in terms of where you get to.

Further answer : Nathan
And if you look at something like Sempra, you know again coming back to our philosophy and my answer to Leigh's question is, the key is to grab hold of it and manage it quickly because it has potential volatility in outcome otherwise. The other ones again embedded, they are much more certain in that sense.

Q. 15 : Male
You said that 77% of the expenses were under management control. Can you talk about the other impacts on expense lines?

Answer : Rory
The other 23% allocated costs for the centre, premises, structures, systems.

Further answer:
There is a paper on these showing the allocations and how we allocate them. So that is in the Results Announcement.

Further question
And when you say you will be down to 15% of current expenses by 2013, which is roughly £400 million, do you anticipate that that gets as and when non-core gets disbanded, that would be a net wash to the Group? Or do you think there will be a residual negative impact to the Group from expenses?

Answer: Rory
When we say 15% reduction in costs these are …..

Answer: Richard
You could be talking about across the Group, allocate a few hundred million pounds which you would think about what you could do with. We have got 3-4 years to think more about that.

Further answer : Nathan
In our terms, direct costs will not be left with. And again I think many of these things it is about managing forward. I mean one of the key things that is actually one of the ways that you have to deal with people as well, but you have to think a long way in advance when you are dealing with non-cores, it is quite different in mindset. So you are constantly looking minimum of 12 months ahead because the organisation changes in step like amounts. And also you need to be thinking about what you are doing with people. So the way to motivate people. This is an area where you can really get great learning and really put a whole different skill set together for people. But at the same time you are managing people who are in a particular position with regard to their employment etc. so you have to be thinking constantly that much further ahead. So we will do exactly the same on costs. I mean again we will look ahead and we will look to see what we need to do in order to be able to manage those further.

Further answer : Rory
This is very clear with the business model we have chosen to run this, is we are not really pouring any concrete or putting in any systems. We don't have our own premises. We are heavily leaning on the institution as a whole. And in our office, we are only 60 people. We are essentially project managing out of the main bank all this connectivity. So when it goes away, to use the analogy of Glastonbury as it was on this weekend. You have a big tent, have a big party, take down the tent and it is just back to being a field. There is nothing permanent here. When we go, it goes.

Further answer : Nathan

Having said that, we have built all of the MI, all of the risk control, all of those types of things that we have needed to in order to be able to get control of this. And that is, I think we have done that very well and in a very short period of time.

<u>Q.16 : Male</u>
Is a lot of it outsourced?

Answer : Nathan
No

Further answer : Rory
Obviously there is shared within the core bank, some people still on the core payroll whose headcount numbers are in our numbers, but outsourcing very little.

Further answer : Nathan
If you think about it, if you are processing, I don't know a loan on a system, you don't want to extract those loans, put them onto a new system. I mean it would be a bad use of economies of scale.

<u>Q.17 : Male</u>
Just in terms of the MI you have had to construct to feed the bureaucracy, ie your APS reporting requirement, should I think of that as just being either deminimus or running-off in line or is there any drop off when you exit out the outsource?

Answer : Nathan
I think we have to look at, you have to again be careful not to think of non-core equals APS. So as we have said from an APS perspective, let's call it round about 45-46% roughly of APS is actually non-core, the rest is core. So the key to the APS cost base and what we have to do in relation to MI and in terms of compliance for that, those things will go on exit of APS as a whole, not linked to non-core. Clearly overall to be able to exit APS then you have to be able to pass your stress test, those types of things with your regulatory etc. But again that is not non-core per say, that is the bank as a whole.

Further answer : Rory
The likelihood that non-core assets go away quicker than the core assets in APS. There is 45% of the opening assets in non-core, 55% in core. Quite a crossover.

<u>Q.18 : Male</u>
Which regulatory changes could affect more deeply non-core? Is it the weighting of markets, RWAs or is it the gross up of securitisation? Which milestone?

Answer : Nathan
They are roughly, I would say they are roughly proportionate. I wouldn't say, there is not a big bias one way or the other.

Further question

And they are all fairly concentrated in GRN 2011/2012? Is that right? Most of the regulatory changes?

Answer : Nathan
Yes, the ones really the ones around exotic credit trading and securitisation, both of those come in at the latest from what we have heard, 31st 2012, at least that was last week. We all wait to hear.

Closing comments
Any other questions? Okay, well thank you all very much for coming. Appreciate it.

End