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PRESENTATION

Michael Helsby *- BofA Merrill Lynch - Analyst*

That is enough for me. I'm going to hand over to the Chief Executive of Royal Bank of Scotland, Ross McEwan. This is the second time you have been on the stage so welcome back. Thank you.

Ross McEwan *- Royal Bank of Scotland Group PLC - CEO*

Thanks very much, Mike. It is nice to be here. Interesting questions. I love that sitting on the fence as you have all done on the margin and also on the litigation piece.

In February 2014, I outlined our long-term ambition to be the number one customer service trust and advocacy bank here in the UK and we set out our initial steps of how we would achieve that. Since then I think we have made some very good progress against this plan, transforming RBS into a much stronger, simpler and fairer bank. The half-year results underlined our intention to go further and faster with that strategy and while we still have a lot of work to do I would be the first to admit that, I feel that we are making good progress against the strategy but also the targets that we set ourselves and I think you will see that in my presentation today.

You will have seen this slide before and I suspect you're going to see it a lot more because this is our blueprint for success. At RBS, we want to keep things very simple, simple in my view as complexity is distracting and also complexity is very costly. This outlines our ambition, our priorities and our 2015 goals which I will come to very shortly.

Importantly it also helps us communicate in a very simple way our plan to build long-term shareholder value through what is essentially a three-phase plan of transforming RBS and I want to spend the remainder of today just running you through that plan.

Phase 1 was substantially completed last year as focus was on de-risking the bank, starting to reduce costs, building capital and simplifying the organisation structure of the bank. We are currently clearly in Phase 2 and on schedule. We have already given welcome clarity to between our go forward and our exit businesses and we are working to accelerate the transformation of our go forward bank and the rundown of our exit bank.

I have been very clear about the conduct and restructuring issues that we face which we are dealing with as prudently and as we possibly can. These will continue to be a challenge for us in the near-term but as we get through them it should mean our materially -- we have a materially cleaner equity story for you. And this clarity is also allowing us all to focus more on the go forward businesses to be clearer and more transparent with you about where the future of this bank actually lies and to build toward the third phase of our strategy.

Phase 3 will focus on RBS becoming a market leader, serving customers better than any other bank in the UK and achieving attractive balance and sustainable returns.

I just want to emphasise how our strategy and the phases of it that you can see on the slide are designed with the aim of creating a business which supports long-term shareholder value.

We are focused on markets where we are the strongest, building on businesses that in many cases we are already healthly and closely controlling or reducing costs throughout each of these businesses.

So before I begin to speak about how we are progressing in Phase 2, let me spend a couple of minutes explaining what RBS in 2019 will actually look like.

RBS will be a UK-focused retail and commercial bank with a wholesale operation that meets the needs of our larger clients and particularly supporting the UK and Western European operations. The business mix measured by both income and RWA distribution demonstrates our focus on our home markets and our core retail and commercial businesses. You will continue to see us making increasingly an clear distinction between our go forward bank, substantially focused on retail and commercial franchises in the UK and in Ireland and our exit bank, the divestments, sales and runoffs that we will shed on the way with that capital that will be released from those businesses.

This allows us to establish clear sight of a future that will set us apart from other UK banks. Strong market positions will be held by all of our primary brands serving customers across all the markets we know we can win in.

The appointment of our new Chief Marketing Officer is a key first step in this and you will be hearing much more about this in 2016. Overall this is a model set up to deliver sustainable returns from a much, much lower risk profile.

It is important to emphasise how quickly we are dealing with our exit bank, moving at place with its rundown. At half-year results we reported that our risk-weighted assets were down to GBP148 billion from GBP172 billion at the start of the year. And as we continue with our divestment program notably with Citizens Financial Group, you will see the pull of RWAs and the exit bank reduced even more rapidly with a target of circa GBP30 billion to GBP40 billion by the end of 2016.

That is the outline of our strategy so let me update you in more detail on how we are progressing in Phase 2 of our plan.

You will see our 2015 goals outlined in this slide and importantly these build on the excellent progress we made during 2014. In each area, we are on track to deliver.

Our strength and sustainability are continuing to reduce risk and have now had six straight quarters of capital ratio increases. I have already mentioned a few of the points you see up on the screen but worth adding, we've also made good progress on RBS capital resolution with only GBP8.4 billion of funded assets remaining.

We continue to reduce our stake in Citizens Financial Group and we also completed a GBP2 billion AT1 issuance in this last quarter. By simplifying the bank, we are on track to meet our GBP800 million cost reduction target we set for this year. In fact we will now be GBP850 million given the increase in bank levy which just goes to show we are not going to step back from getting this bank back into shape on a cost base. And that is on top of the GBP1.1 billion we took out of the bank in 2014.

Customer experience, our Q2 net promoter scores across net worth personal, net worth business, RBS business, Ulster Bank, personal and Northern Ireland were all up year on year. We demonstrated to win back the trust of our customers, we are determined so I welcome these improvements that are starting to show through in each part of our business.

We are also supporting growth in personal business banking and commercial in the UK, our key customers segments. We reported a 43% uplift year-on-year on mortgage applications in July.

I now would like to spend a little bit of time talking about our priorities in much more detail, both our progress to date and our plans going forward.

As you have just heard me say, we are on track to meet our cost reduction target for the year. Tackling costs will be a constant goal for us and given our starting point, you can see that we are delivering.

Our aim of reducing our cost to income ratio to below 50% remains a key part of our plan. I would also like to highlight that we have got significant future cost opportunities in all parts of the bank, partly tackling the high cost in our franchises that we are repositioning but also through operational improvements in the UK personal and business banking and also in our commercial bank.

Across all of our priorities, we are investing heavily in our transformation program. This year we will see GBP1 billion plus invested in the go forward bank. This is already starting to pay off. Improving our go forward business means improving what we do for our customers and that is why between now and 2017 the investment figure will stand at nearly GBP3.5 billion as we transform the bank for our customers, for our employees and our shareholders alike.

A core part of making the bank stronger is our capital plan. We reported in the middle of the year that we have had six uninterrupted quarters of capital ratio increases. There is a clear marker of the focus we have on completing the job of having unquestionable capital resilience and a significantly reduce stress profile for the bank. You can see that we are making progress toward our target of 13% common equity Tier 1 ratio by the end of 2016.

Although we continue to consolidate Citizens Financial Group on our balance sheet for regulatory and capital purposes, our CET-1 ratio without Citizens would have been up some 300 basis points higher at 15.3%. However, the potential conduct and litigation settlements have to be factored into this progress.

As I said earlier, we are dealing with these as quickly and as prudently as possible but there will continue to be a drag on this business for the next six to 12 months.

You can also see that our leverage ratio has increased by 1.2 percentage points over the last 18 months and our nonperforming loans have decreased by a whopping 53% over the same period. It shows a bank with a stronger capital position and reduced stress profile.

And I will just ask the question, can any other bank in the world demonstrate this sort of progress?

As well as becoming a stronger bank, we also want to become a much simpler bank for our customers and for our colleagues. The changes we are making not only reflect our drive to reduce costs but also a function of the changes we are making in the overall shape of the bank. By the end of this year, we plan to have reduced our property portfolio by a further 16% on where it was a year ago. Similarly, we plan to reduce the number of costly programs that we are running to 150 by the end of this year compared to 182 at the end of last year and 550 about 24 months ago.

We are simplifying our front and back book product sets to the benefits of customers and employees and our Company structure is much simpler reducing the number of companies in the bank by 135 already this year and we have a long way to go.

All of these examples and there are many, many, many others of them demonstrate how we are taking cost out of the business and just making it much simpler. This is a bank that is becoming smarter in the way that it operates.

Let me just show you some of the measures that we are taking already to improve our customer experience. We are making the bank more resilient through our transformation program, investing in our IT, focusing on our home markets and transforming the way that we lead our teams. As well, we've also begun to challenge some of the things which customers find so frustrating about banking. That includes shorter account opening times, quicker lending decisions, simpler product ranges and getting our fees and charges on a single sheet of paper as opposed to the booklet of terms and conditions.

I know that this action can deliver a much simpler bank and a much better operational and customer experience for everybody as well. I want to emphasise that these changes are just the beginning.

Over time we will serve customers better and we will do it at a much lower cost ratio.

We are transforming how our customers can interact with us. In the space of a couple of years, we have gone from a static branch-based approach to a much more dynamic model based on what we call points of presence. As well as our burgeoning digital platforms, we will have added over 1500 self-service points by the end of 2015 and a huge expansion of access across the post office network, giving us much closer to customers and this is an example of the investment that is going into our core business to really utilise the market position that we do have. This will mean that in two years our access points for customers will have trebled.

From June 2014 to June 2015 alone, we saw a 22% increase in the number of active mobile banking customers. This is reflected in both the number and volume of mobile transactions all seeing 30% plus increase year on year and all three are market leading mobile app. All of this adds to a greater convenience and availability for our customers transforming how and where they can bank with us.

As you can see here, this investment is starting to pay off. Our Q2 net promoter scores across NatWest personal, NatWest business and RBS business, Ulster Bank Personal were all up year on year and there is still more to do but these are pleasing signs of progress and reflecting the work we are putting into improve our customer experience of this bank and for the customers that deal with us.

I would just like to take a moment to highlight the improvements that we have made particularly in our mortgage business which is a key area of growth for us. We have significantly increased our number of mortgages advisors and we are transforming our proposition to make it easier for our customers to do business with us. As a mortgage provider in the intermediary market, we serve the customer and we are punching well above our weight here where our market share is well above our stock share. This shows it isn't only an investment in capacity it is an investment in service delivery.

We are more focused on our strongest products with a much simplified product range. We are introducing new ways for our customers to talk to us, making it simpler to apply and looking at every step of the mortgage process. This will ensure our customers get the best experience possible.

Our customers are already responding to these changes with complaints being well down, net promoter scores up in both franchises and we are attracting more customers and growing in the market. These positive changes are being seen in our performance with mortgage balances up 3.5% year on year, applications up 43% in the same period and our market share is increasing. It is a positive trend in a growing but competitive market but we acknowledge that customers continue to switch from variable rate to lower fixed-rate offers and it does impact on margins.

Similarly in commercial banking, we are also seeing growth in our net lending of 2.1% year on year. This is well ahead of the market trend. I have been very clear about our ambition to be number one for customer service, trust and advocacy and it is based on a very, very simple logic, you look after customers better and they will actually do more business with you over time. And that simple logic is starting to deliver results for both our customers and for the bank.

At the same time as transforming our invest to grow parts to the bank that I've just been talking about, we are also reshaping three other parts of the business that are key to the future of RBS. It is our corporate and institutional bank, Ulster Bank and Private Banking currently have unacceptably high levels of costs in the businesses and require repositioning as leaner more efficient franchises. Both however are showing positive signs of change and have the opportunity to leverage off the experience, the customer and product base of the rest of the bank, something that they have never done in the past.

Our corporate and institutional bank business is undergoing a multiyear transformational program as well as reshaping the business in line with our go forward proposition. We will need to re-platform many parts of this business particularly its back-office processes to materially lower its cost base.

You see on this slide that as well as transforming the workings of the CIB business, we've also fundamentally altered its proposition to making sure it is in line with our strategy and serving clients well.

We are keeping our international hubs in the US, Singapore and Japan to serve the needs of our larger clients and also an extensive Western European network. This is a business that holds really leading market positions but it needs time to reposition itself and I will give it that time.

At its end state, it will complement, enhance the business mix which I outlined earlier, a bank that has the capability of serving its larger UK-based corporate and financial institution clients with market leading positions in its wholesale operations.

So you can see how we are going further, we are going faster on the delivery of a strong and simpler and clearer RBS. Our capital ratio is up, our costs are down, we are stripping out complexity and our returns at our go forward bank are improving. The RBS that is emerging will be capable of delivering strong returns from a lower risk profile. It will be the UK's preeminent SME bank, preeminent commercial bank and corporate bank with robust capital, leverage and liquidity positions. Overall we believe it will be a strong investment proposition.

Over the next year, we will continue to make significant progress against our plan and as you have seen today, our ability to execute is very clear.

With that, Mike, I'm happy to take any questions.

QUESTION AND ANSWER

Michael Helsby - ***BofA Merrill Lynch - Analyst***

I will get the ball rolling, Ross, and then we can open to the floor. We have already got a couple of questions in here as well.

Clearly the conduct peak as you have described it in the chart here is a very significant milestone in reaching points on capital. I think you have been hoping that maybe there would be some news flow on that by the end of the year. Is it fair to assume that has probably slipped now into 2016?

Ross McEwan - ***Royal Bank of Scotland Group PLC - CEO***

Much of the conduct and litigation unfortunately the timing isn't in our hands. It will come at us when court dates or when regulators choose to have the conversations and I think we are number 17 on the list of 17 in US court dates particularly around RMBS that have changed. But as each week goes past, it does come closer to having that knock on the door for us to have a conversation and that we will do.

So that is the major one for us is RMBS, and we've got some other issues that we would like to tidy up. It is very clear on more reputational piece around GRG and the Tomlinson Report is with the FCA through 166, but that has been two years now so that has still got a shorter period of time to go. So it is really the timing unfortunately not always in our hands but it is clear that we would like to get this tidied up.

Michael Helsby - ***BofA Merrill Lynch - Analyst***

Okay. One of the questions here is clearly -- that has come from the audience that you have been working very hard on improving the operating environment in Royal Bank of Scotland and making a lot of change. Can you give us an update on that, particularly reference some of the recent IT failures to give people confidence about we have passed the worst? Thank you.

Ross McEwan - ***Royal Bank of Scotland Group PLC - CEO***

Our biggest one that people go back to quite rightly was 2012 where we did have major difficulties and since then we have spent GBP750 million on our core platforms for our business.

The incident the other day where a file didn't go through which did disrupt a big number of customers was 5% of what actually went through the system and so you need to understand what it was it was 5% of what went through the system at night because we are one of the biggest producers will flow through for transaction banking.

Was that completely unrelated to what happened in 2012. The advantage of what happened in 2012 if there is anything, we knew how to fix it. We knew at all times where that file was and our teams that evening decided not to put it through because they had been working on it for some time and if there were difficulties actually the Company didn't have enough energy left to actually fix it again. So we made the decision to hold back for a day. So I think it was quite sensible the team in their thinking.

But we are building a much more resilient bank and our ability to get things back up again. Our biggest problem actually is around our complexity as an organisation not around do we have bad technology. We have very good technology but we have so much of it and that is part of our transformation program is to get down about 9400 systems and applications to a much, much smaller number which makes it a much easier bank to deal with.

Particularly in the payment space where we have something like 146 payment structures that needs to be more around the 10 to 20 than it does the 146 and you just get the complexity out of the structure and that is what we are working very hard on.

So certainly resilience was a big part for last year, a big play for us last year. We spent a lot of time and money on it. We are in much better shape but unfortunately because of what happened in 2012, we are the focus. If we go down for five minutes now, it is all over the websites and the likes but that is the price we pay for having let people down in 2012. We've got a much higher bar for us which we are quite happy with.

Michael Helsby *- BofA Merrill Lynch - Analyst*

Okay, fair enough. Would anyone like to ask a question verbally via your microphones? No. Okay. We've got one there.

Unidentified Audience Member

Obviously you have this target of a cost target of below 50%. Can you just give us a more clarity as to when that will happen? Is it the Fall of 2018 or at some point in 2018? And then secondly, do you need revenue growth to achieve that?

Ross McEwan *- Royal Bank of Scotland Group PLC - CEO*

I will start with the back end of that question. I think that revenue growth will be limited across the industry as you have seen across all banks and we have all relied for the last six years on interest rates going up and taking the advantage of interest rates going up. So my views and my team is to forget about that. There is a very limited chance that the limited amount we have put in for revenue growth because of interest rates going up so the issue is get the cost out because there has to be a cost plan for us.

We have said we are going to do that over a five-year period of time starting in 2014. We took 1.1 out, we will take 850 out this year and over the next three years through the end of 2018, we have got substantial amounts to get us down to the 50 or sub 50. So it is by end of 2018 going into 2019, we will be into a 50% cost to income ratio.

And to be honest at that point there is still more work to do because the bank of our structure and size at that time needs to be in the 40s not in the 50s. But our starting point was 73, end of last year was 68. We are making progress, we have got lots more to do. Our focus needs to go on taking cost out.

Unidentified Audience Member

Maybe I will ask another one. If we had gone back five years, maybe a little bit closer than that actually, everything that is going on in the world with commodity prices and oil and concerns around corporate names, Royal Bank of Scotland would have been front and center in people's worries. It doesn't feel like that is the case now but can you just talk about that a little bit and how should the audience be thinking about that risk that of commodities coming through, banks, balance sheets?

Ross McEwan *- Royal Bank of Scotland Group PLC - CEO*

One of my major drivers and that of the Board as well is to build a very, very strong capital base and get back into high markets where we are the strongest. And you have seen us coming out selling assets all around the world and that is interesting that today the big thing is around sort of mining exposures. Just a year ago, it about 4.36 billion. Today it is just over 3 billion exposure for us. So as we have brought the bank back to the UK, our exposures to some of these global phenomenon are much less, are much less for us and you heard Anthony talk about the UK and US. These are good markets to be in and we happen to be having an organisation that is coming back into this market where there is good growth.

So I think our strategy has worked. I think it was the right strategy for this bank to get back into the UK with some operations in Western Europe where we are very strong to hold a hub over in the US, to hold a hub down in Asia for our corporates and financial institutions. And every day goes by I am reassured that we are on the right strategy and we are going at it flat out and I think we have performed against this much quicker than anybody else thought we could have so we are getting back into a really good shape.

Michael Helsby *- BofA Merrill Lynch - Analyst*

And do you see any risk of the current environment slowing that pace down?

Ross McEwan *- Royal Bank of Scotland Group PLC - CEO*

To date, no. We have done substantial sales of assets all around the world from the old corporate institutional bank. Some of those -- a lot of those have already been announced so a significant portfolios. US, two-thirds of our commercial lending portfolio is gone. We've got places like Australia, Hong Kong many, many others, UAE. We are on our way up and having made sales so I think we are in shape. We have shown our results under RCR but that will be closed out after two years, not three years. So we have taken advantage of a very, very important market place to sell assets and get back here for the UK as much as we possibly can. I think it is proving to be the right strategy at the right time.

Michael Helsby - ***BofA Merrill Lynch - Analyst***

Anyone want to ask a question?

Unidentified Audience Member

Do you have any updated estimates of potential litigation and conduct fines?

Ross McEwan - ***Royal Bank of Scotland Group PLC - CEO***

No. We gave 17 pages worth I think in our six-month results. And as we were talking to the investment community and analysts, people all over the place thinking about particularly around R&D, FHFA, DoJ, the likes, so our view was just keep updating. So I think our latest update gave you the fullest that we were able to give and no update on that today. I keep saying, the sooner we can get through those the better because I think they are holding certainly people's feeling about the stock back. So those are the ones that we have set out in Phase 2 of our strategy of 2015 and 2016 of tidying up as much as we possibly can.

Also the other piece to that is the restructuring of the bank, do as much as we possibly can in as short a period of time so that you see the good bank emerging out of this which people are starting to see.

Michael Helsby - ***BofA Merrill Lynch - Analyst***

There's a couple of questions come in through the iPad here. It is linked into the previous presentation actually where there is a couple of remarks on margins and we asked the question can you give us your view on linking together the competitive pressures in the UK? Clearly banks are looking to grow again the market is not necessarily conducive to that massively at the moment but it is getting better. What would be your view on the outlook for net interest margin?

Ross McEwan - ***Royal Bank of Scotland Group PLC - CEO***

I think there will be a slight reduction in net interest margins so slightly different than the earlier speaker. I think there will be just given the level of competition going on in the marketplace. I don't however think it will be severe because I think everybody is under the same constraints of capital and all of the ratios. So I think there will be a reduction and most of that is customer driven. You need to understand the difference between what banks are doing and what customers are doing. They are moving from standard variable rate to fixed-rate because they are frightened of interest rates going up. So the conversation now with a mortgage client is around their need for security and most of them are going on to a two- or five-year fixed.

Our book is now down to 18% standard variable. About a year ago, it was just over 25% so you can see the move from standard variable to fixed-rate which is hitting the NIM. But that is a customer demand as opposed to us pushing up here and you have got to be there with customers if that is what they want. So we are seeing that. We have probably got the lowest standard variable percentage left in the book today. Just a quirk of where we started and where we are today and I think it is the right thing to do for customers and you get repaid by much better volumes and you get paid by much better loyalty of customers longer-term if you do the right thing.

This does hurt. In our first quarter, it was I think 7 basis points down on NIM on the mortgage book; the next quarter was down by 3%. I think at 18% is probably only 3% to 5% of that book left to go on to a fixed-rate because there are a lot of clients who actually like the flexibility of a standard variable rate.

I think there is going to be a bit of contraction it is not going to be dramatic and I think an organisation like us have to get our cost base down and we've got to find other ways of growing the business that is safe and secure. And we've got plenty of opportunities across the bank with the customer base that we have got, I think we've done a very, very poor job of cross-selling safely for the right reason into our customer base so we have got lots of opportunity and we are starting to find them as well.

Michael Helsby - ***BofA Merrill Lynch - Analyst***

You mentioned in one of your answers that the UK was a good market. As Royal Bank of Scotland, you have got the biggest franchise in corporate, large and SME in the UK. Is there anything you can see right now given the shift more internationally in trade or whatever that gives you a better cause for concern in terms of future volumes?

Ross McEwan - ***Royal Bank of Scotland Group PLC - CEO***

Part of what you are asking and I think Antonio was the same, you are seeing corporates deleveraging. You are seeing households with low income levels paying back principal quite quickly because their interest rates on a fixed-rate is down to 1.59. So the capacity to repay is very, very strong and they are taking that opportunity to do so.

So those are the sort of trends that you are seeing people borrowing but you are seeing the payments coming back very quickly as well. But I think you are seeing corporates in pretty good shape, you are seeing SMEs are starting to borrow again but they are not borrowing like they used to do. If you add up all of the credit growth in this marketplace even though GDP is up like 2.5%, it would be worth getting all the economists to have look at this. But actual credit growth isn't going anywhere, there is no growth in credit growth because the repayments -- people are repaying as quickly as their taking it out.

So the credit growth is there but the growth in the bank -- which is a good thing because it means productivity must be improving in a marketplace that needs it. So I think there are some very good signs there but it means that there is less borrowing to be done and that includes all the peer to peer lending at the same time. It is worth having a look at that. It is quite a phenomenon going on in this marketplace.

Michael Helsby ***- BofA Merrill Lynch - Analyst***

I think we have got maybe three minutes or so left before the next -- we need to go off. We've got one question here and then there is one more just came in on the screen.

Unidentified Audience Member

I have a question on IFRS-9. I understand it could be integrated in the UK stress test. Can we have more color around this please?

Ross McEwan ***- Royal Bank of Scotland Group PLC - CEO***

We will probably have to give you that color over the next six-odd months, we're just working through that at the moment. There will be some changes but we are probably not seeing as significant as people think. There will be some ups and downs but we are happy to give you some more color on that over the next six months on the likely impacts on the business. My view is it is not going to be as significant as people initially thought.

Michael Helsby ***- BofA Merrill Lynch - Analyst***

One question here just on the capital return hopes. Would you have any preference as you envisage it today in terms of would that be special dividends, would that be buybacks, what do you think?

Ross McEwan ***- Royal Bank of Scotland Group PLC - CEO***

First off, we have to get ourselves in a position where the PRA is very comfortable with us returning money through any of those forms back to our shareholders. And as we said very openly, we will want anything over 13% back to shareholders once we have gone through the conduct and litigation big ones. We will have to go through I think another stress test next year just to make sure that we are in good shape. We will be in much better shape this year than we were last year so I think we will have to go through another stress test. We have to conclude the sale of Citizens. We said we would do AT1 and we have done that and I think we just need to show our core businesses are performing well and that is why Ewen and I said look, it is more likely to be first quarter of 2017.

And then my own personal view on this -- and this isn't agreed with the Board, but my personal view I would rather participate as the government selling down, participate in the buybacks be a part of that exercise and at some stage we would like to put in a dividend policy in place. But I would like to actually participate. I think it is probably the best thing for all investors where excess capital goes back through buyback and you have seen very good examples of that in the marketplace through AIG I think did the same. The government sold out and that worked very successfully for all parties.

Michael Helsby ***- BofA Merrill Lynch - Analyst***

Unless there is any burning questions we can leave it there and we can move on to the next presentation. Thank you.

Ross McEwan ***- Royal Bank of Scotland Group PLC - CEO***

Thank you very much, Mike.