Q1 Results 2019
Host: Ross McEwan
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Operator: Good morning, ladies and gentlemen. Today's conference call will be hosted by Ross McEwan, Chief Executive Officer. Please go ahead, Ross.

Ross McEwan: Thanks from us, (Jeannie). And good morning, everyone. Thanks for joining Katie and I. I'm going to give you an overview of the bank's progress in the first quarter and then we are happy to take any question.

Before I get to the results for the first quarter, I'm sure you will have seen that, yesterday I let the board know that I will be stepping down as CEO. To reiterate what Howard and I said yesterday, I'll be around for a while to ensure an orderly transition, and there is no change on our commitments to delivering our 2019 and 2020 targets.

The first 3 months of 2019, we made a pretax operating profit of GBP 1 billion and a bottom line of attributable profit of GBP 707 million. These results reflect the challenging environment we are in.

Looking at our financial performance in more detail. Total income of GBP 3 billion was GBP 265 million lower than the same period last year. In Q1 '18, we had a number of positive one-offs, which would increase income in the Retail & Commercial businesses. We also continued to see competitive pressure affecting our margin.

Personal and Ulster and Commercial and Private Banking grew lending by (GBP 0.6 billion) in the quarter, which is 0.8 percent on an annualized basis.

Across the Retail & Commercial businesses, net interest margin of 2.07 percent was flat on Q4 2018. However, group NIM decreased by 6 basis points to 1.89 percent reflecting a reclassification of funding cost to NatWest Markets and an IFRS 9 accounting change for interest in suspense recoveries. And I reiterate that the in the Retail & Commercial businesses, where it matters, NIM was flat.

On other operating expenses, compared to Q1 2018, we have reduced cost by GBP 45 million. We don't see our cost reduction as linear, and we'd expect to see further reductions throughout the year.

In particular, we continue to see benefits of our property exit strategy coming through in the latter part of 2019. We remain committed to the GBP 300 million cost-reduction target for the year.

On strategic cost, we expect to be closer to the lower end of our GBP 1.2 billion to GBP 1.5 billion range by the end of 2019 with the remaining GBP 300 million coming through in 2020. Backing all these together, we generated a return on tangible equity of 8 percent for the first quarter.

Our capital position remains very strong with a capital -- our common equity Tier 1 capital ratio of 16.2 percent. That's up 20 basis points on our IFRS '16 pro forma position. This represents around 30 basis points of underlying growth before the dividend accrual of 2p.

Looking at Q2, we hope to see the completion of the Alawwal merger with Saudi British bank. You already know about the potential capital benefit from the reduction in risk-weighted assets.

But in addition, if the Alawwal share price continues to perform, we could see a P&L benefit. You should also note that there could be a significant positive recycling of FX reserves.

As we outlined in our full year results, we expect further capital returns in 2019 based off our target of circa 14 percent common equity tier 1 ratio by the end of 2021.

We are making good progress on our 2019 issuance plans with around GBP 3.8 billion and benchmark public transactions in the quarter, including NatWest Market's first onshore U.S. dollar issuance and our first SONIA linked issuance in the form of a covered bond from NatWest Bank.

Just a brief note on Brexit. The sustained uncertainty is causing customers to pause some investment decisions.

As we continue to support them, this week, we announced the doubling of the funding available through our Growth Fund to help businesses prepare taking the total fund to GBP 6 billion. Where there is customer appetite for new

lending and it's within our risk appetite and hurdles our return requirements, we stand ready to lend.

As we said that year-end, the continuing uncertainty posed a risk to income, add to this a flatter yield curve, and you'll have seen this impacted both our lending and income in the quarter.

In terms of our own preparations for Brexit, our NatWest Markets NV office in Amsterdam is now operational and have started to serve some European customers from March 2019.

We've also received approval for 2 license applications in Frankfurt, 1 inside the ring-fence and 1 for NatWest Markets plc, which will allow us to maintain access to the European payment structures.

Turning to financial performance in our franchises. In personal banking, the U.K. mortgage market continues to show unprecedented levels of competitive pressure.

Average rates across a range of loan to values remain at historic lows. And payment losses were GBP 44 million higher than in Q1 2018 reflecting lower provision releases and recoveries and the IFRS 9 model updates on Q1 2019.

With this in mind, we are pleased to report that in the first quarter, personal banking achieved an operating profit of GBP 498 million and return on equity of 25 percent. This was underpinned by gross new mortgage lending in the a quarter of GBP 7.6 billion and net new lending of GBP 1.7 billion.

At the same time, personal banking has grown personal loans by GBP 0.2 billion or 3 percent in the first quarter, and we're now seeing 40 percent of all sales being carried out digitally, which was 17 percent higher than Q1 2018.

Ulster Bank Republic of Ireland reported an operating profit of EUR 23 million. New mortgage lending was higher than in the quarter prior -- sorry, first quarter last year.

And the tracker mortgage book is more than GBP 1 billion -- EUR 1 billion lower than it was a year ago. As I've said before, the focus for 2019 is on resolving outstanding customer remediation issues and addressing more of the nonperforming loan portfolio. We're on track to do both of those.

In Commercial Bank, which now includes business banking, delivered an operating profit of GBP 437 million and return on equity of 12 percent for Q1 2019. This was helped by impairment being at historically low levels of just GBP 5 million for the quarter.

Commercial Banking orientated -- sorry, originated or refinanced GBP 4.6 billion of utilized term lending in the quarter, however, the net loans to customers were down GBP 0.6 billion to GBP 10.8 billion reflecting customer caution.

Private Banking delivered operating profits of GBP (80) million, return on equity of 17 percent through a 3 basis points increase in NIM compared to Q4 2018. Other expenses reduced by GBP 2 million compared to Q1 '18.

NatWest Markets income in the Core business was down 8.5 percent on Q1 2018 but in the pack with our peers. NatWest Markets franchise made a GBP 62 million loss in the quarter impacted by a change in funding cost allocations post ring-fencing and credit spreads tightening.

RBS International generated operating profits of GBP 93 million. It's up GBP 15 million on Q1 2018 on a return on equity of 29 percent. With income of GBP 151 million, it's up 10 percent on Q1 2018. The business delivered a 39 percent cost-to-income ratio.

We continue to innovate both inside and outside the Core bank investing GBP 1 billion this year to upgrade legacy infrastructure and improve our products and services. We're holding a technology and innovation seminar in June where we will provide you with further updates on how we're looking to improve for our customers.

So in summary, these results reflect the challenging environment we are operating in. We expect further capital returns in 2019 based on our target of 14 percent CET1 capital ratio by the end of 2021.

We're investing in digital innovation responding to customer shift to our digital channels and providing a lower cost to -- more efficient operating model. And with that, Katie and I are very happy to take any questions that you may have.

Operator: (Operator Instructions). And our first question comes from the line of Jonathan Pierce from Numis.

Jonathan Pierce: Can I ask 3 questions, actually all fairly short. The first one, Ross, maybe you can give us some sort of quantification of the Alawwal benefits? You just talked about FX reserves, P&L benefits, those sorts of things.

Secondly, can I push you a little bit on this flat margin comments in PB commercial because clearly, some of the more expensive debt from the first of Jan is loaded into NatWest Markets, and there wasn't a restatement going backwards.

So my assumption is actually margin outside of NatWest Markets is falling. Is that correct? And if so, can you give us an idea what it was down on the fourth quarter and the first quarter?

And then final question is on this return on tangible equity target for next year. I mean, clearly, with the revenue currently annualizing, it's is low 12s. Historically, you were talking about mid-'13 type revenue, a high 6 cost number, impairments of 30 bps to get to the 12 percent return targets.

That looks very difficult now, certainly the pre-provision profit level. Can you give us an idea of the shape of the P&L if you are to get to that return target next year which you clearly are still sticking to on that level?

Ross McEwan: That is great. Thank you for that. OK. We'll go to the Alawwal. On the current Alawwal pricing, if it remains at that level or around that level, there was a profit coming through there on sale, so it was likely to be about.

Katie Murray: Low to a few hundred in that kind of range.

Ross McEwan: We've also got FX recycling going through there. There could be absolutely -- could be significant on there as well. In the tunes is probably up to, I'd say, probably even GBP 1.5 billion across Q2 and Q3.

It'll probably come in 2 phases. So you're seeing this is why we're warning here that there is some numbers coming through. If the sale progresses on the time frame and both P&L uplift and also FX up, but remembering the FX changes will be capital neutral.

Katie Murray: Yes. And of course, Ross, you mustn't forget it actually releases GBP 5 billion of RWAs.

Ross McEwan: Correct.

Katie Murray: At that point which is an important addition to that number.

Jonathan Pierce: So sorry, on that, because it’s quite important, the FX reserve capital neutral but TNAV positive? Or is just a recycling?

Ross McEwan: Recycling.

Katie Murray: So currently, if you look at the balance sheet, you'll see we've got GBP 3 billion of FX reserves there. Those are obviously things that built up from our foreign holding, and this is one of our last significant kind of foreign holding that we've got.

So as you either dispose of those holdings or we designate the branch with different activity, it'll be -- it's normal practice that you recognize those FX gains or losses.

In our case, they're gains that you built up on the balance sheet over the time of the holding so that's get recycled in. So they're already in our TNAV. It's capital-neutral. What it will do -- it will change the shape of the sheet balance.

But when we do the Alawwal transaction, obviously, we'll do an RNS at that point, and we'll give you these numbers in some detail. But I think we want to make sure that people forgot -- because FX is recycling is more unusual item, it's not one that we talk about very often. We wanted to make sure it's kind of on your radar today.

Ross McEwan: Just on the NIM, Katie be worthwhile I think because we have made some adjustments here, worthwhile you just spending a couple of minutes taking people through the FX -- sorry, the NIM changes and their impact.

Katie Murray: Yes. You know…

Ross McEwan: Thanks for asking that question.

Katie Murray: Yes, happy to. I'll just spend a couple of minutes talking through the whole different pieces because there are number of things in there. So if you look at the group NIM, it's obviously (5, 6) bps to 189.

There's two main drivers for this. Firstly, it's a IFRS 9 accounting change for interest in suspense recovery; and secondly, a reclassification in NatWest Markets of funding cost.

I take the first point first. The IFRS 9 accounting change related to accounting treatment of interest in suspense per recent IFRIC guidance. When loans become impaired, interest income is held on the balance sheet.

And if the loan returns to the performing book, the interest is now released in the impairment line rather than as NII as was previously the case. The impact of this is around GBP 1 million or 1 bp of NIM in this quarter.

The second point relates to that NatWest funding market reclassification. As part of the standup of the entity, NatWest Markets now carries all of its own funding capital and liquidity cost, which means in reality, they are carrying more expensive debt in totality.

We reviewed treatment of these cost, and as a result, all NatWest Markets funding cost will now be included in the banking book as part of NII despite

being utilized and driven by the requirement of the trading business, which generates noninterest income. This has created the larger part of the group NIM reduction.

As a result of the inherent mismatch in NatWest Markets, we feel now the right time to introduce a Retail & Commercial NIM. All this does is take the group number and flip out the NatWest Market numbers. There are no other adjustments. It's an all-in number, including all of the funding, capital and liquidity cost as a group.

Across the Retail & Commercial business, NIM was 207 was stable versus Q4 2018. It was a 3 bps reduction within there from a reduction in central liquidity balances driven by the actions in Q4 with which you're all familiar.

However, this was offset by the impact of IFRS 9 accounting change, which I've already called out and also a couple of bits of competitive pressures largely reflecting the ongoing reduction in mortgage margin in UK PB.

As we look forward on Retail & Commercial business, we expect to face continuing competitive pressure, and we look to actively manage liquidity whilst, of course, noting the Brexit delay and continued uncertainty and, of course, be accompanied -- this is all accompanied by the current flatness of the yield curve. So hopefully, that covers most severe, most severe queries on NIM. Ross there was a last question as well on revenue?

Ross McEwan: Yes, as it related to -- and the impact on tangible equity, return on tangible base.

Katie Murray: Yes, exactly. Shall I kick that off?

Ross McEwan: Yes.

Katie Murray: So if you look at our Q1 number on the income side, (3037) if you just take a straight kind of times 4 of that, you're right, Jonathan, you'll get to the low 12.

However, I would -- we suggest (inaudible) if you take out some of the negatives in Q1, of which there aren't many, there was something you called

out in the notable items, a little bit of NatWest legacy which we know is negative this month and some other central one-offs.

What you get to is kind of normalized number. It's closer to 3.2. And then if you take that up and then annualize that number, it probably gives you a slightly better view of where we think income might be headed.

So if I take them and obviously there's many different shapes and pieces on the income statement that would drive the 12 percent return on impairment, I feel that you to get to 30 bps in 2020, feels quite a neglected assumption based that we're on 11 bps today.

And I think it's one of the things that we've always debated many times as at what point do we see us getting into the 30 to 40 through-the-cycle number. So that bit is probably a little bit – toppy of where we are. So I look at those different bits of pieces.

The fact that actually underlying return basis were north of 10. I accept impairments are very low, so that would impact this. It's not a huge step from that 10 to 12. And actually, the really important thing is capital out because that's going to be the differentiator in getting that 12 percent, that 12 percent. Thanks Jonathan.

Operator: Our next question is from the line of Joseph Dickerson of Jeffries.

Joseph Dickerson: I guess a quick conceptual. You've answered, Jonathan, some more questions I had on net interest margin. But I guess this is a conceptual one which is if I look at your NatWest Markets business, yes, you've got the legacy, some legacy funding a bit dragging down the business.

But you still have the negative PBT pretax losses, if you will, on that business, and therefore, negative 2 percent return on equity. I guess what's the strategic rationale for actually having this NatWest Markets business?

And if it's the commercial bank, why wouldn't it be integrated into the commercial bank if it's there to serve the commercial bank? It's more of a

conceptual question around that business. I know we've been through it before over the years.

But as you go through the results, there's still a very good story in these core businesses that seem kind of overshadowed by this business. So how important is it from a network perspective to the overall RBS?

Ross McEwan: Yes. That's a really good question, Joseph, to ask on there. And when we set the strategy for this business 4 years ago, it was just around repositioning it for 3 particular areas ahead of strategic advantage and just get rid of income out of everything else. And about 40 percent of that business links back into our commercial business and sort of the mid-market where we are incredibly strong.

Yes, some of those things, yes, we could bring back inside the ring-fence. But our view was we're better off having them out because of the size and shape that you get. There's still a lot of restructuring going on in that business this year to take cost out of it.

And Chris and the team have been delivering against that. But it does get overshadowed by a lot of legacy activity that's showing through. So here, you see it on income today as well down, but actually, the underlying income is about 8 percent.

So whether we've got NatWest Markets in its current shape, we would still be having to deal with these issues inside the core bank from funding, from bringing the cost of the systems and applications down with our inside ring-fence or not, and the marginal cost (inaudible) is not that great, probably a treasury operation and in small amounts of other things.

So our view at this point is they're doing exactly what we asked them to do. it's been a hard yard. Ring-fencing, Brexit probably haven't helped us out.

But at this stage, we're confident to what the team are doing. Still lots of work to be done. And the big parts of these restructuring stops at the end of this year and the investment which is being expensed drops quite dramatically as well.

Katie Murray: I mean the only thing I would add, Ross, of course, is that we couldn't combine it completely with CPB because of the ring-fencing rules as well, so it's obviously challenged. But I think you've covered it. Yes.

Operator: The next question is from the line of Ed Firth from KBW.

Edward Firth: Yes. I guess I've got 2 questions. One, just quick one. On Commercial Banking and your volumes, I'm just trying to square that a little bit with the Bank of England data, which seems to suggest that corporate lending is actually looking pretty healthy relative to where it's been in the past.

So I'm just trying to get a sense as to why is it do you think that you're finding that more difficult to take your share in that? So I guess that was the first question. And then the second question was bringing you back -- just go ahead with the second one?

Ross McEwan: Yes. Yes. Yes. Go on.

Edward Firth: Yes. I guess back to the 12 percent plus, I guess 2 things. One is I'll be honest I'm a little bit confused about your messages on capital because I think if I look at yesterday's AGM statement you were talking about towards 14 percent this year.

You're now going back to saying 14 percent by 2021, which I guess you can square those in the detail, but I guess the sort of broad message is very different one.

One is like a smooth, steady decline till 2021. The other suggest it's going to be something more radical this year. So I wonder if you could just try and help in terms of squaring those 2. What on the face with what appear to be slightly different sentiments. And I -- Sorry. Yes?

Ross McEwan: No, that's okay. I'll cover it.

Edward Firth: And then I guess the final point is just connected to what we're talking about revenue. Your 12 percent plus target was, I understand, reliant on the NatWest

Markets delivering a revenue of I think you said GBP 1.4 billion to GBP 1.6 billion.

Now I think we can accept that looks extremely unlikely. So if that is unlikely, is there something you can offset elsewhere? Or do we just accept that, that flows to the bottom line and we are going to be probably somewhere light against 12 percent?

Ross McEwan: OK. Why don't I just take them in the reverse order actually Katie feel free to chip in.

Edward Firth: No, that's fine.

Ross McEwan: NatWest Markets, if you take out the negatives, that their wearing from old structuring and activity coming off the books, I'm still predicting that'll be around GBP 1.4 billion of revenue this year.

And that's what (inaudible) whether they get there or not, but at this stage, they are (8 percent) off in the first quarter. But let's say, it's a number probably I should never move away from GBP 1.3 billion to GBP 1.4 billion which I started with about 4 years ago.

Edward Firth: So just coming back to that, Ross. If they're running at a run rate of minus 8 percent on last year, that's not going to get you to the GBP 1.4 billion, is it?

Ross McEwan: Yes, but it's going to be closer -- (inaudible) to a 4 -- what do they do in the first quarter 380 or something?

Katie Murray: 377 (inaudible)

Ross McEwan: 377 in the first quarter?

Katie Murray: Yes.

Ross McEwan: With all the disruption that went on. So I'd say if we stay around that GBP 1.3 billion to GBP 1.4 billion, I think it was -- remember, we had a poor Q2, 3 and 4 in 2018.

Katie Murray: I think, Ross, on the GBP 1.4 billion to GBP 1.6 billion, we're seeing here in Q2 2019. We're talking about numbers that are going to be a year from now plus in terms of the 2020 target.

So one could (inaudible) some new normal whether pre, post, in or out kind of Brexit story lands at some stage in those next 7 quarters. So certainly hope it does.

Edward Firth: But I guess my question is more about if this is a shortfall, do we just see that flow straight through to the bottom line? Or do you have a sort of arsenal of other levers that you can pull to offset that?

Ross McEwan: Well, you've got it. If it looks like it's a permanent pull down on the revenues of any part of the business, you got to go after the cost structure, the cost structure.

But we're still saying that the business pulled around their GBP 1.4 billion as where we're targeting that for 2020. And our problem was we did a lot higher 1 year. It's been around that numbers probably for the last 4 years other than 1.

On the -- I think we've been quite clear that we're sitting around 16, 16.2 at the moment. By the end of 2021, we want to be circa 14.

We said it won't be linear given that there maybe some larger chunks that are coming out of -- if the government does do a directed buyback with respect, but we are targeting circa (14 percent) By the end of 2021.

If you do take a linear line from that (16 to) the 14, in 2020, we'll be sitting with a number in the 4 -- mid-14s.

This is what we saw, mid- to high 14s. And it's quite crucial we get to that, get ourselves to a 12 or 12 plus. And that's probably in my mind the biggest swing factor of getting the capital out of the business because we don't need it.

And the only reason you'd need it if we did do a some form of acquisition, and let's be quite clear, there's nothing on the cards, but I'd say, if we were to grow

the business and there was something there that was valuable, you would have a look at it, but otherwise, it's a return to our shareholders.

And it is a line from 16 to down to circa 14 by the end of 2021. We haven't changed our view on that. Sorry if there's any confusion at the AGM yesterday, but that was our intention hasn't changed from an Executive Board perspective.

On the Commercial Banking, what we've been seeing is customers are paying down and just sitting in cash more. And I'm surprised that's not showing through the industry stats because that's what I thought was happening there.

It's certainly happening with some of our large corporates. It's even happening -- starting people pausing in places like our business in the Channel Islands. We're just waiting to see what the results are. They're not investing at this point in time.

So we have seen paydowns in some of our property areas, commercial property areas. I think people are just sitting on the sidelines. So I'm surprised industry stats say anything different to that.

Operator: Our next question is from the line of Andrew Coombs from Citi.

Andrew Coombs: If I could just ask a couple of clarifications. Firstly, on the NWM funding cost reallocation. I'm sorry if you said it, but can you just quantify how much that is moving from other operating income to NII in terms of the drag?

The second one on dividend. You talked about 2P accrual in the quarter. Can I just confirm that's for an ordinary dividend only and any special dividend accrual will be taken in the fourth quarter? And then my --

Katie Murray: If we do anything on specials we’ll announce it very loudly we won’t slip it through on capital.

Andrew Coombs: OK. So you're annualizing for an 8p ordinary dividend for this year?

Ross McEwan: (inaudible)

Katie Murray: (inaudible)

Andrew Coombs: And then the final question just trying to go down on into the UK PB top line. You talked about the interest margin being up 2 basis points Q-on-Q. Loans there are actually strong in contrast with commercial bank.

We've seen very large loan growth. And yet the NII is still a bit down Q-on-Q. So is that just the impact of the number of days in the quarter? Or what's driving that?

Ross McEwan: OK. I'll have to have a quick dig on that one. Just on the dividend one, we're going to update you in.

Katie Murray: H1.

Ross McEwan: At the end of H1. But we've only accrued for the ordinary dividend at a 40 percent ratio at this point in time. And as we go through, if we haven't been able to get the capital out there, we're going to have to speak to the board to do something at H1 because we can't keep accruing...

Katie Murray: Growing.

Ross McEwan: We keep growing our capital at the rate we are, we'll end up well over (70 percent) by the end of this year, which is not really where we want to be, and then we've got a major problem of getting anywhere near 12 percent or greater.

UK PB, you're absolutely right, we had a very strong quarter. And what happens while we stayed with our 2 percent to 3 percent growth in assets over the year of CPB and PB means that the renewal of loans and the roll-off actually drops off quite dramatically in the next 3 quarters.

The height of roll-off was in the fourth quarter of last year and a bit running into Q1. So we see strong growth of the book going through there. I haven't got the answer on the -- we're two fewer days in the quarter, so that's probably about, what, GBP 25 million?

Katie Murray: Yes. And the reality the margin is still is obviously in terms of what front-book, back-book margin is still lower. So you see that coming through as well. Yes, so I think it's flat by a different day count.

Ross McEwan: There's lots of pressure on that. Our view is keep writing the business at the volumes that we have because it's good profitable business and use the liquidity that we currently have.

Katie Murray: Yes. Why don't I take that first one. The easiest place to look Andrew, in the slide pack which you can kind of do afterwards. On Slide 16, you can see the NIM for the whole bank, including NatWest Markets and then also for the (inaudible) other than NatWest Markets.

And if you look at the difference in the other line, there's one bp that remains in the rest of the bank, which is the number I referred to in terms of the IFRIC interpretation we talked about earlier and then the one including the whole bank is 6bps.

The difference between two correlates basically to the interest charge, so they're now carrying, they're carrying that legacy debt. I think (inaudible)

Andrew Coombs: The rest of the other is all due to the funding cost reallocation?

Katie Murray: Basically. Yes, exactly, exactly. And we know that on terms of that legacy debt, I think Alexander shared some of the roll-off patterns with you all this morning as well. Debt that will -- 2/3 that will be matured by this time next year, and at the end of 2020, it will all be gone.

And it's currently at coupons kind of 5.5 percent. And as we renew and replace that debt, that will be half of that. So structurally, you'll see a natural improvement coming through as that debt does roll off.

Operator: Our next question comes from John Cronin from Goodbody.

John Cronin: Just a few. If I can come back to Ed's question on the arsenal of levers and when you referred to the cost potential, can I just probe down a little bit more

specifically. So I suppose what I'm looking at there is -- one is your strategic investment spend which you also said as lumpy.

You guided down to the lower end of this range this year but with the remaining coming through next year. I'm just trying to understand again, and I know this has been asked before, but what kind of fat might there be in that?

And then separately, on underlying operating cost, is there -- beyond what you've already committed to in terms of recalibration, is there more that can be done that we're not seeing? So just specifics around that would be helpful.

And the second question I have is just on that U.K. mortgages, particularly going back to your comment around on unprecedented levels of competitive pressure in the U.K. mortgage markets.

And anything more specific on that in terms of latest run rates? We're beginning to see that graduating, I guess, in the industry data and in these comments made by -- in Barclays' numbers yesterday. So if you could help me there, that would be great.

And then finally, just on the time frame around the CEO appointment. Obviously, you have to run an external and internal process, but kind of how long roughly would you imagine that will take?

Ross McEwan: Yes, that is fine. If I just start with the strategic cost, we have sort of guided down to the lower end of the range of the GBP 1.2 billion to GBP 1.5 billion.

The reasons for that is, look, I think there's only so much that an organization can absorb and change. Remembering, we're doing a base of GBP 1 billion of investment in the bank, and a GBP 1.2 billion to GBP 1.5 billion make up the full GBP 1.5 billion we see over a 2-year period.

As we're getting into the year, it's pretty clear that we'll be at the lower end. We got some quite significant properties coming out, 280 at Bishopsgate, big property in Manchester, 1 in Mumbai, 1 in Birmingham. I can think of right now. We've got 12 regional centers.

That will probably take up about GBP 500-odd million, slightly more of that GBP 1.2 billion. The rest of it will be around technology write-down as we take systems out but also obviously some staff cost as we go through this.

You can't flex that, but we're choosing not to because we do need to move quickly from bricks and mortar to a much more digital framework of the bank. But our view is that there'll be 300 of that 2.5 spill into 2020 and that's the way we've been thinking about it.

Yes, we could flex that. If we could find something to bring forward, we'd do so rather than push them into 2020. But we do have some things that will push back in to 2020 of things like data centers that'll take 3 or (4) years to get out.

We can't write them off until we get I think within 12 months from the date of close. So there's some of those things that will still -- that'll flow through in the 2020 and 2021, but they will be more minor.

Katie Murray: Yes. And I think what we've always said on strategic cost as we look to 2020 is kind of GBP 500 million number over strategic and conduct and kind of steady run rate basis isn’t an unrealistic number to be looking at. So it's not really a particular change in that guidance.

Ross McEwan: We should give you a better update later in the year on both of those numbers to make 500 up because, I mean, as we have stabilized at the bank, make it much better for customers, we are seeing a lot smallest flow into the sort of conduct areas.

So I think we'll give you a better indication later on this year particularly on the conduct cost as well. Underlying operating, a cost major pressure on the bank. We've done run a weekly meeting run by myself or Alison Rose and Katie always had them.

On we're monitoring staffing levels, commitments made by people, things like travel, entertainment, consulting fees, just about line-by-line with a spotlight each month. And we are determined to the take the 300 out this year and a bigger number next year. So it is getting the focus, and we're now starting to focus more on the 2020 than the 2019.

But the point I was making if the business is not performing and it will not -- if we don't see it performing long term, that is a strategic decision you have to make you've got to take the cost out of.

And the business that has been doing as we asked it to do is NatWest Markets. Ulster Bank, slightly different.

We've just given it 2 major tasks to do this year so that we can actually see the business next year, one of those around the remediation, and we've had around 16 remediation customer remediations going on, 2 of them incredibly large. Both of those big ones finished mid- to second half of this year. And but there’s hundreds of people involved in those, they're not in our expense rate.

But the problem with having those remediations going on, you can't see your own business. And so we're working very hard to get those finished and also the nonperforming book down, so we know the business. Interesting enough, the Irish lending business is going very well.

Katie Murray: Yes.

Ross McEwan: So Jane and the team are starting to see the growth coming through in the book, but you don't see it because we're taking EUR 1 billion of the old tracker mortgages off that make us no money whatsoever.

So cost have to come out. If we're not making money in the business, I'd have to close them out or restructure them to get them out. We're committed to doing it.

Katie Murray: I think John's last comment was on the question on U.K. mortgages and what we're seeing there. We are still seeing strong levels of competition. We're sitting nicely at kind of 13 percent flows, which we're pretty comfortable with.

And what we do see is our stock is keeping up with -- it kind of went up by 0.1. We see that continuing to do -- the reality is flow moves faster as it converts into stock, so we're kind of comfortable with that.

But it is competitive out there. You know -- you'll have seen a little bit of work on our pricing in April. And we feel that has been received positively, and we'll update you more on that at the end of this quarter.

Ross McEwan: And the most important thing we've got lower roll-off each quarter for the next 3 quarters. And remembering the 70 percent of the book that we've been writing in the last year or so is on a 5-year.

You see that staying on the book for a long, long while. So that's why we're staying with our 2 percent to 3 percent growth in the commercial and Private Banking -- sorry, commercial and…

Katie Murray: Retail first initiative.

Ross McEwan: And private has been doing well.

Katie Murray: No, we have indeed.

Ross McEwan: I know it's in purely the hands of the board, but the board have started the process. And as you can imagine, the board will be looking both internally and externally and taking both of those very seriously. I'm not involved in that process. That's quite right and I shouldn't be. It's a question for Howard.

But the board has started that. I've been very open with the board about sort of my thinking and timing over the last 6 to 12 months. And so it's no surprise to the board, and quite rightly, they've been working with the headhunters on should Ross go what does it look like.

So I think good, orderly process. And I have committed to staying on to make sure there's an orderly process. I've got a 12 months notice, so you might still be talking to me to at beginning of next year if things go badly in the process. I hope not and I don't think so either.

Operator: The next question is from the line of Christopher Cant from Autonomous.

Christopher Cant: I had a couple of quick ones, following up really from some of your responses to the earlier questions really. You mentioned though that you think GBP 3.2 billion type run rate for revenues quarterly is a more representative figure for

how you feel the business is performing and sort of steer us as to where you think revenues could go to point about 12 8 asset sort of annualized basis. And consensus for next year is 13.2. I think in the past, you have talked about wanting to do more than 13. So are you trying to steer us lower there on revenues?

Is that what you're trying to communicate by giving is that GBP 3.2 billion figure, please? And on cost, you just referenced, expecting to take out more than GBP 300 million of costing into 2020. It sounds like that process is underway.

Is there any more line of sight you can give us on how much cost you expect to come out in 2020, again looking at consensus? Consensus has about GBP 300 million coming out next year, so that would feel a bit light potentially given your comment.

One of the things that I've always struggled to get my arms around is this point around OpEx of investment spending in NatWest Markets. We don't get much visibility on how much is coming out there. Are you still expecting GBP 1 billion of cost in NatWest Markets?

And then finally, Ross, you've talked about the trajectory down in capital as a key determinant of whether you hit your 12 percent or not. It sounded from your commentary like if you don't get a directed buy-back in the next few months, you'd be looking at an interim special dividend. Is my interpretation correct there?

Ross McEwan: Just on the last one first. If we don't start to get capital levels down, we're having to find other ways of getting it down. And specials remember, are special, they shouldn't be seen as ordinary every year evidence. But we will have to start investigating doing another special if we can't get it away.

Because we don't have the use of the capital, we will make sure that we hold back well and truly enough if the government should go at any point in time and that (4.99 percent) in any year rolling 12 months. But we are building capital, and we have lots of excess capital we want to get back to you. So our commitment remains.

On the cost piece, yes, we said GBP 300 million this year. And our view is that we'll build for a number equal or greater than that next year. We have to get to the cost base in the right shape. And that's what the team are working at the moment.

We'll give you a clear indication later on in this year. But we can't sit just taking GBP 300 million out. We've got to take more out. And the flow-through from some of the activities this year falls pretty much in to 2020 anyway, but we have to do more than GBP 300 million.

Katie Murray: Now if you look at some of the spend on property you'll naturally get (inaudible)

Ross McEwan: (inaudible) really get some numbers that are helpful. But look, it's always difficult, particularly when you've got inflationary wage -- or wage inflation pressures coming through.

About 60 percent of our cost relate to people. Yes, one way -- the technology they use, the space they operate and the management of them, et cetera. So it's going to be a lot more useful. The income?

Katie Murray: So I guess what we're trying to do, Chris, is on the income is try to guide you to take the (3037) of this quarter as the run rate for the rest of the year would be, in our view, a little bit punitive.

So that's kind of, as you take the quarter, take out some of the negatives and get you closer to the 12.7. I'm not trying to give you a new income number for 2020. We've always been very open that we had expected yield curve to pick up for this year.

That hasn't come through yet. But at the same time, we also see some lending that's being held back. If that comes through, you'll naturally see this number begin to improve as well. So really, as I look at the income going forward, we talked about it's under pressure.

And those pressures are very much around what's happening on the yield curve and what's kind of happening in the economy as a whole. But what we're comfortable with is we see nice growth coming through in terms of the volume and within -- particularly within personal, the personal bank.

And they're all coming through making sure we continue the hurdle at the right level as well. So I think as you look at this year, don't just automatically times by 4 because I think you'll be a little bit on the low side.

Operator: Our next question is from Jenny Cook from Exane.

Jennifer Cook: Our Q4 results, you flagged that your 50 percent cost-income ratio for 2020 is looking challenging in the current environment and also that you expecting a rate hike in H2 '19.

Today, you're flagging once again that it's looking challenging. Is that characterization of challenging still including that benefit of a rate hike this year-on-year in your numbers? And then I guess...

Katie Murray: Jenny, (inaudible) again. I'm sorry.

Jennifer Cook: And then I guess following up on that, you've added strategic cost the coming lower this year, so say GBP 1.2 billion, but the residual following through in 2020, 2021. But shifts around maybe GBP 50 million in 2020 given consensus of about GBP 450 million across strategic and litigation (GBP 100 million) for 2021.

So that's kind of increases total consensus OpEx to, say, GBP 7.2 billion-ish in 2020. If I adjust the top line to reflect a slightly lower base this year, it gets me to around 55 percent cost income for next year. Is that a fair characterization?

Katie Murray: I think, Jenny, what I would say is 9 weeks since we spoke to you last time. In terms of it being challenging, we've not seen anything that's kind of changed since that time. You know that we work on consensus view of economics. So the consensus view just now would be the rate rises move out.

Into possibly very late 2019 or early 2020. I think that will continue to jump around, and we'll continue to react -- I would say the cost side of things, I would say your number it's a little bit toppy. But we'll see how I think this year evolves and as we go into next year.

Ross McEwan: The other thing we said, Jenny, going forward is restructuring of bank and conduct and litigation don't go away.

Now I think that the -- for us, the numbers drop dramatically after 2019 when we go from GBP 1.2 billion to GBP 300 million in strategic. And conduct and litigation, we've sort of put a place of around GBP 200 million per annum.

Whether you use it or not, it's going to be in our problem at the moment is we're still expecting quite high conduct litigation this year. The question is do they fall in this year, into this year, or do they drop into the year after or 2021 because it's not been a lot of action on the number of these things for quite some time.

So -- but it's really around just strategic cost of dropping dramatically from GBP 1.2 billion to the GBP 300 million, then your conduct cost being around that GBP 200 million per annum ongoing. These sort of numbers, I think you should think about not just for us but other banks as well.

Katie Murray: We're not looking to kind of change that view.

Ross McEwan: We're not changing that view.

Katie Murray: Jenny, as we give kind of you better guidance on this year's strategic cost.

Jennifer Cook: OK. Just to clarify, you do have a rate hike in your numbers in the (second half.)

Katie Murray: You're right, Jenny, so we work on consensus. But the consensus has moved out this year. So if it comes into next year, we'll be happy to take it. But I think at the moment, we don't have a lot of confidence as to what's actually happening on yields.

Operator: Our next question is from the line of Fahed Kunwar from Redburn.

Fahed Kunwar: I just have a few actually. So on the margins, sorry to come always back to it, you used GBP 8 billion liquidity in this quarter.

I mean you talked about the positive in that slide, I think it Slide 16, that you'll continue to kind of use liquidity. Now obviously you kept that liquidity because Brexit uncertainty.

What you're saying is it's still around. So how should we think about that liquidity benefit offsetting the competitive pressure you're seeing on margins over the course of this year? Can that come down? Or will you try to work that LCR down closer to the kind of (120 percent) mark still at 150-odd?

And the other question on margin I had, to supplement it with, how much of the decrease is from structural hedge roll-off? Obviously, the swap curve is very low. You reinvest automatically right now.

So when we think about I think it was 3 basis points margin pressure in the quarter from competitive pressures, how much if you were to split that out? How much was due to the roll-off of the structural hedge? That's question one-ish on margins. The other question, Ulster Bank. Shall I give all the questions now?

Ross McEwan: Yes. Go.

Fahed Kunwar: On Ulster Bank, it looked like a pretty bad performance. So you had 8 basis points in margin contraction. Your AIEAs was down 4 percent as well. Was that something specific that happened there? Or that's something we should think about going ahead? It seems quite aggressive Q-on-Q performance on both volumes and margins.

And the final question is on the commercial bank. I know you talked about the GBP 12.8 billion. But how much of an impact have you had from the incentivization scheme?

And how much kind of volumes and BCAs have you kind of -- have actually transferred away from you to those challenger banks? And how should we

think about the impact of that considering it's been going for a couple of months now on your income line going forward?

Ross McEwan: OK. I'll leave you…

Katie Murray: Shall I start and you join?

Ross McEwan: I'll do the Ulster Bank, and let's see who takes the next one.

Katie Murray: OK.

Ross McEwan: Just on Ulster Bank, look, the margin will have contracted because we have been competitive in the market there on the interest rates. But remembering this quirk from that market that a lot of people do a cash back that doesn't come through the NIM. It comes through the expense line.

We're choosing not to do that, so we're tracking it through the NIM line. But we are seeing good volume uplifts in the mortgage business of accounts forward, so a few better than 8 basis points will that continue.

I suspect it will. And there's also been I think some IFRIC impacts that we have at Ulster Bank as well in the last quarter. I don't know the exact amount, but there will be some impact there. Katie sort of, I think, already talked about that.

That's competitive marketplace, but still quite good margin there, and we are competing well in it. Not to be stupid, but we are competing well and not doing cash-backs, at the same time, we do take a lower NIM on it.

And Ulster Bank, I think it's starting to just become a more normal bank and getting back into the marketplace with home mortgages, business banking, and we'll get into the unsecured market there as well this year in a slightly more aggressive way.

Katie Murray: If I just start with off the margin and liquidity benefit. You remember we talked about it at the year-end that we had done quite a few liquidity actions in Q4 where they were kind of in the latter part of Q4. So what we really see

coming through in this quarter is the full quarter impact of those liquidity, those liquidity actions.

As we look at it we have said we'll continue to hold excess liquidity, until we kind of get through this kind of Brexit uncertainty. It's interesting to see how long it will go. You'll be aware that we've done quite a lot of debt raising, so we're not looking to further increase. I mean, our LCR was 153 percent for the quarter, so down a bit from Q4.

So we will -- our management is more going to look at things like TFS repayments, kind of tying of debt where we are and also where we -- what's kind of happening on the lending and deposit side of things as well. But I wouldn't expect that at this stage that you see us do any particular movement down to the 120 percent.

And of course, those of you I know who are -- will be shareholders were looking forward dividend next week as well, and that will be a nice a little bit of our liquidity at GBP 1.3 billion will come out next week.

So all those things go together. But certainly, at this stage, comfortable to stay at that kind of 150-ish sort of number, and we're not really looking to increase.

In terms of the structural hedge, we haven't shown you that split out entirely or within there but on the structural hedge, what we disclosed, we gave you the year-end. Our average is 1.02 percent.

At the moment we've got as a tailwind, as the long bit of the curve is supporting that, but it's a little bit better than that, but the one we're pretty much -- we're pretty close to the average of what you're actually seeing in the swap market as well.

Commercial banks, I nearly forgot. The incentivization, we've been running for a couple of months in terms of these results.

We've only really been be running for 4 weeks. So I would say there's little impact of any meaning of that in these results. Remember that we talked about

historically from the Williams & Glyn book total, the GBP 200 million benefit we get from income within that space.

There is some activity, and we're working hard to make sure that there is. It's too early to say. And what we'll do is at Q2 an agreement with the body that runs the whole incentivization scheme will agree with them what kind of numbers we can disclose. But at this point, the impact is pretty minimal; and if anything, really in Q1.

Fahed Kunwar: Perfect. And can I follow-up on that point. If there is little impact and you don't see kind of the current account market share you needed to over the next year, I mean, just corporate customers have always been very sticky, then what happens after that?

What was the next step? We had Williams & Glyn not obviously being divested. If this didn't work either? Do you see going -- try to remain different? Will there be a cost to this? And how does it work going forward?

Ross McEwan: Yes. Well, first off, we've got targets of numbers of customers who got to move across through the process in the first 12 months, and then I think it's either 18 months or 24 months.

On the current rate we're running at, we'll hit the 12 months target quite nicely because the volumes of customers won. We've got about 70,000 customers registered to take offers. We're now starting to see those coming through the process, and you're starting to see a fair shift of those customers going across.

We're of the view if this keep running at this rate, we will hit the first 12-month target quite nicely. But the question is if we don't get to a certain number by a certain time, the offer can be expanded into the NatWest customer grouping.

Now of course, we don't want to do that, so we're doing everything we possibly can to actually make sure we're complying and encouraging customers to go with other players, and at this stage, nothing quite favorable.

Operator: Our next question comes from the line of Chris Manners from Barclays.

Christopher Manners: So just 3 questions, if I may. The first one is on, sorry, on mortgage margins again. I guess just looking at system data it did look like that they had improved as the swap rates fell. You mentioned your writing more 5-year product than you have been historically.

And presumably, if you're writing a 5-year product today, you held down the balance sheet until 2024. So when you're pricing those, how do you think about the first stage of implementation of Basel III output floor, the PRA risk weight review where I think you've given guidance doubling of mortgage the risk weight?

And how has that impact your pricing? And do you still think that you're making competitors above your hurdle rate on front book mortgage pricing where it is? Obviously, we saw action took in April.

And the second question was just on the Term Funding Scheme. obviously, you did pay GBP 5 billion of that, that back. And arguably, 75 basis points is potentially extensive for you. And what are your sort of plans around that to normalize that? Could you pay off anymore?

And the third one was just on PPI. So if we look at the Q1 claims rate, GBP 136 million, that you sort of spend and compare that when we're only sort of 5 month since the end of March on PPI.

You've got 559 provisions still on the balance sheet. Is there potential for a write-back there? How's the claims volumes going do you expect a surge in complaints before we get to the deadline?

And then I saw you mentioned Deloitte being appointed to try and identify some PPI claimants or PPI policy holders who haven't claimed yet. Could you just maybe share a bit of color on what that means and how that process is working? Does that mean things could drag beyond the deadline in august for you?

Ross McEwan: I think we start at the back and work my way forward on the PPI. Look, it's pretty comfortable where we are at the moment because we wouldn't want to

be certainly adjusting anything between now and the end of this time. We do expect to see a surge. We've always thought there'll be a surge probably last 3 to 4 months, so we'll hold on for that.

And the Deloitte piece is really working with the official receiver on where there (inaudible) people had to go at the some sort of liquidation receivership and was there a plan to be made on NIM. We've been working with Deloitte and the team just to work through whether this is a big thing or not.

Some of the details haven't been that accurate. And some of them that thought were claimants weren't, so I think there's a lot of water to go under the bridge on that one.

But we'll be holding on to that provision until the last minute, I'd say. We will review again at the half year. If there's a surge whether we've got enough at this stage, we were pretty comfortable with it.

Katie Murray: And I think, Ross, in our forecasting, we obviously we planned for the fact that we expect some claims to kind of go up. And Chris, in terms of the extension of the deadline, there's been no suggestions (inaudible) extend the deadline at all. I think they're just looking to see some major pickup on there. So it may become something or not, but we'll wait and see what happens.

Ross McEwan: TFS?

Katie Murray: TFS, we did repayment its expensive debt, but you put your access liquidity on the deposit for the same price, so it doesn't actually, in the end, it doesn't really cost you anything, but it doesn't make you anything.

So we're seeing -- so we did a bit of repayment last year. We -- I said earlier we're not looking to grow our liquidity coverage. So we'll look at as we go through. We may not take some actions on that in some stage in this year as well.

And then in terms of the mortgage margin question, when we reprice these products, interesting pricing are very much what's happening in the market. So when we look at, we look at their overall return, we build in the change in the

capital rules in all of that and make sure that we're still very comfortable with their returns. We've given you the guidance.

That's the same the guidance we're using internally. But we are comfortable these longer-dated products that they do hurdle well, so not uncomfortable on that basis. And I think that was all, Chris.

Christopher Manners: Yes. So you hurdle well on the current spreads, but can you tolerate much more front book margin compression?

Katie Murray: At the moment, we're comfortable I think is what I would say.

Ross McEwan: And we do take account of the fact that those changes to risk weightings do happen at period of time and they have to be spread over the loan period. So we're still comfortable, Chris, at this point in time.

Katie Murray: Yes.

Christopher Manners: OK. So you look at the average ROE over the product life. So as time goes past and we get closer to those RWA inflation happening, then that would been factored into the calculation?

Ross McEwan: These mortgages get effectively get allocated to capital based on period of time beyond knowing that we're actually doubling the risk weightings on it as well. So each tranche, I would say tranche of mortgages must hurdle.

Operator: Our final question today is from the line of Martin Leitgeb from Goldman Sachs.

Martin Leitgeb: Yes. Just a follow-up on the mortgage space. And the question here, I was just wondering whether you could shed a little bit more light on the profitability of the new business in mortgages at the moment we're talking about.

Because, I mean, just looking at the return on tangible, you quote in the disclosure for UK PB was just around 25 percent. It would imply that even at that current rates, the front-book business in mortgages is still fairly high return on equity proposition.

And tied to that question, I was just wondering, just looking at the excess deposit base, RBS has within the ring-fenced bank, and I think it seems to be roughly GBP 40 billion.

Wouldn't there be scope for a bit more pronounced growth within UK PB within mortgages in order to try to offset some of the pressure coming through on the commercial side?

Or is there potential there to cannibalize existing revenues out of the mortgage book and that's why the current growth rate of around, I think the current rate implies around GBP 7 billion a year is where you feel more comfortable?

Ross McEwan: Yes, you're right. You've got to be careful you cannibalize yourself by driving the pricing down just to get some more business. I think it's a sort of a nil-sum game on it.

So we are -- Liz and the team are quite careful about our pricing strategy so that we -- one, is a great offer to customers, but at the same time, we've got to make some money. At the moment, we'd still think there's a greater than 15 percent return on the mortgage business we're writing, so we're comfortable writing it.

But it's highly competitive market. I don't think it's going away because I think we've got plenty of liquidity in the marketplace. And as I said before be very careful of the credit quality and how long your writing for.

So at this point, we are using some of the excess deposit base. Yes, you're right, it's massive. But be very careful that you don't cut your own revenues down dramatically when you're doing. Any other comments on there?

Katie Murray: No, I think what we -- seminar we had last year, we talked about on the new cap rule hurdle over 15 percent and at the moment we’re over 20 percent, so we're not looking to change that. Since that seminar, actually, relatively small changes in front- and back-book margin. We kind of -- we jumped around between that kind of 80 to 90 range. So no difference on that.

Martin Leitgeb: And the spread differential is still around 80, 90 basis points as before? Or has that slightly improved in the meantime?

Katie Murray: So it's still in and around. As the yield curve flattened, you get little upticks. We're taking bps at this point. So I mean, I think that 80 to 90 is a good, is a good number to use.

Operator: And there are no further questions. So Ross, I'll hand back to you for closing comments.

Ross McEwan: Yes. Look, thanks very much for joining the call. Look, in a very competitive marketplace with lots of uncertainty, I think this is a good set of accounts for our first quarter. We know there's still a lot of work to do to get cost out and to keep growing the business, and we are concentrating on that.

But let's see how the next quarter goes. And we have called out the Alawwal. If it does transact in this quarter, expect some noise in the numbers, some should be very positive. But thanks very much for joining the call, and we'll talk to you again.

Katie Murray: Thanks very much.

Operator: Ladies and gentlemen, that will conclude today's call. Thank you for your participation. You may now disconnect.

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