NatWest Group plc
Annual Results 2020 - Analyst Call

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Operator: Welcome everyone. Today's presentation will be hosted by Chairman Howard Davies, CEO Alison Rose and CFO Katie Murray. After the presentation, we will open it up for questions.

Howard Davies: Good morning, everyone, and thank you for joining Alison, Katie and me for our full-year 2020 results presentation.

It's fair to say that 2020 was a year like no other. Politicians, regulators and industry leaders had to come together to find urgent solutions to a series of rapidly evolving challenges caused by the pandemic. And the United Kingdom left the European Union after nearly 50 years of membership.

At the last minute, the trade agreement with the EU avoided a disorderly exit, but there's still a lot of work to do and significant uncertainty persists, particularly in financial services.

The direct impact of Brexit is not as significant for the NatWest Group as it is for banks with larger EU or markets operations. And we are as prepared as we can be through well-capitalized operational entities in the EU. Any wider economic impacts on the U.K. will, however, clearly have implications for the bank's performance in the medium term.

Against that extraordinary backdrop, we provided exceptional levels of much needed support to our customers and the communities in which we work throughout 2020.

Although the persistent low interest rate environment and ongoing COVID-19 restrictions will continue to challenge financial performance amongst all U.K. banks for the foreseeable future, our bank is well positioned to navigate the ongoing uncertainty and is making good progress against its purpose-led strategy.

By embedding our purpose at the core of our business, we have signaled our intention to deliver not only a sustainable financial performance for shareholders, but to make a positive contribution to society.

In December, the PRA made the welcome announcement that it was lifting restrictions on capital returns for U.K. banks, subject to certain sensible guardrails. Following that decision, we have announced a final dividend of three pence per share. And subject to permission from the regulators, we plan to distribute at least £800 million each year to 2023 through a combination of ordinary and special dividends, maintaining our 40 percent payout ratio for ordinary dividends.

The board are grateful to Alison and her senior team for the leadership and energy they've displayed in remarkably challenging circumstances. We firmly believe that we have a well-balanced leadership team in place with the necessary experience and expertise to deliver our objectives.

And with that, I will hand over to Alison and Katie, who will take you through our results and our strategic priorities in more detail. Alison?

Alison Rose: Thank you, Howard, and good morning. I'll start with an update on our strategic priorities before handing over to Katie to take you through the full-year results. We'll then open it up for questions.

So starting with the headlines. Against the backdrop of economic uncertainty, we have delivered a resilient performance while supporting customers throughout the pandemic and accelerating our digital transformation. Today, we're reporting an operating profit before impairment of £2.9 billion for the full year with impairments of £3.2 billion below our guided range. Our well-diversified loan book remains resilient and there has been little change in stage migration.

Taking impairments into account, this resulted in an operating loss before tax of £350 million and an attributable loss of £750 million. Despite the challenges of the pandemic, we have continued with disciplined execution of our strategic priorities, strengthened our executive team and delivered on our targets.

During the year, we grew retail and commercial lending by 7 percent versus our target of 3 percent. We reduced costs by £277 million above our target of £250 million, and we continue to reshape NatWest Markets,

reducing RWA to £27 billion, well below our £32 billion target. This resulted in an initial dividend of £500 million from NatWest Markets to the group this month.

As a capital generative business, we operate with one of the strongest capital ratios of our European peer group at 18.5 percent. And as I have said before, this gives us the flexibility to navigate continuing uncertainty, to consider options for creating shareholder value such as our recent acquisition for Metro Bank and to return capital to shareholders.

Following the Bank of England's announcement in December, I'm pleased to announce that we are reporting a proposed final dividend of three pence per share today, which is the maximum allowed within their guardrails.

Subject to regulatory permission, our intention remains to return capital to shareholders with a payout ratio of 40 percent for ordinary dividends and with distributions of at least £800 million per annum in '21, '22 and '23, giving us the capacity to participate in directed buy backs from the government.

You will have seen that we have also announced this morning the conclusion of our strategic review on Ulster Bank. Despite the progress that has been made in recent years, it is clear that Ulster Bank's business in the Republic of Ireland will not be able to generate sustainable long-term returns. So, we have decided to make a phased withdrawal over the coming years. And I'll cover this in more detail later.

So those are the headlines, and I'll move on now to talk about our strategic priorities on slide five.

This time a year ago, we set out a purpose-led strategy just before COVID-19. And it's an understatement to say it was not quite the year I had anticipated when I stood up in front of you last February.

Yet the experience of 2020 has shown that it has never been more important to put purpose at the heart of our business, helping people,

families and businesses to thrive. And throughout this year, we have done everything we can to put this into practice.

Our purpose is underpinned by four strategic priorities with a plan to drive sustainable returns by serving customers across their lifetime to generate value, powering the organization through innovation and partnerships, simplifying and digitizing our business to improve customer experience, increased efficiency and reduced costs, and by deploying our capital effectively to maximize returns.

Our purpose is also exemplified by three focus areas, removing barriers to enterprise, building financial capability and leading on climate change, which deliver benefits for all our stakeholders and deepen our ability to drive long-term sustainable returns. So let me give you a flavor of what putting purpose into practice has entailed in 2020 on slide six.

Over the last year, our people have done everything they can to support our customers in the face of exceptional challenges. And I'd like to thank my colleagues for their incredible dedication and commitment. At the start of the pandemic, we set up remote working for over 50,000 colleagues and kept 95 percent of our branch network open for customers who need us, whilst also accelerating our digital offering. We've provided mortgage holidays, capital repayment holidays, help for vulnerable customers, and approved over £14 billion of loans under government lending schemes.

Demand for this support has been tapering since the second quarter. And despite the ongoing pandemic and extension of government lending schemes, current trends show no increase in demand, no increase in impairments, and continued growth in mortgage lending.

Nevertheless, we recognize that there are tough times ahead for some of our customers as the pandemic continues and we continue to work closely with them to understand their needs.

During the year, we also responded to customer needs through our three focus areas which I'll cover on slide seven. We are committed to removing barriers to enterprise as a vital means of supporting economic growth and

job creation whilst also generating income for NatWest. We recognize the pandemic has presented particular challenges for entrepreneurs and we have pivoted to digital channels to continue to support them.

We migrated our 12 accelerator hubs around the country to digital delivery and welcomed over 1,200 new entrepreneurs to virtual accelerator programs. We helped more than 14,000 entrepreneurs through Business Builder, which offers advice and networking opportunities online, and we hosted over 1,000 virtual events for more than 45,000 business owners across the country.

We also supported female entrepreneurs in 2020 by creating a £1 billion fund to which we added a further billion this year. On learning, there has never been a greater need for financial capability. And the pandemic has left many people struggling with their finances and our banking app which offers customers dedicated support and advice has help them manage debt, understand personal credit scores and stay in control of their money.

We reached 2.9 million people in 2020 through activities such as free financial health checks, our financial education program MoneySense and training on forward awareness. We also helped over half a million people start saving with us for the first time.

Our commitments on climate change recognize that this is a risk of ever-increasing importance for investors and customers. We are helping the transition to a low carbon economy by aiming to halve the climate impact impacts of our financing activity by 2030.

During 2020, we reduced our exposure to the oil and gas sector by about 16 percent. And it's worth noting that oil and gas represents less than 1 percent of our loan book. We also help business customers raise £12 billion of new sustainable financing and funding, enabling us to bring forward our £20 billion target from 2022 to this year, which we now expect to exceed.

We launched our first green mortgage in the autumn, and having achieved net zero on our own operations in 2020, we remain focused on making them climate positive by 2025.

So looking at our activity across the year, our purpose has served us well. I'd like to talk now about progress on our strategic priorities on slide eight.

Our strategy remains focused on delivering sustainable returns over time. And our clear priorities are first to build sustainable growth with a continued strong risk discipline. We have lent above the market rate in 2020 and expect to continue to do so over the next three years.

Secondly, we are simplifying the business and delivering cost efficiencies. We expect to reduce costs by about 4 percent a year through to 2023 leveraging our investments in technology. And third, we are actively managing capital in order to maximize returns and aim to operate with a CET1 ratio of 13 to 14 percent by 2023.

So let me move on now to talk about generating income growth on slide nine. We benefit from having strong customer franchises across the business that provide multiple growth opportunities. And we are building on our strengths to serve customers across key moments in their lives.

In retail banking, we have a 16 percent share of current accounts, but a lower stock share in mortgage lending. We see mortgages as an attractive growth area and we continued to grow organically in 2020. Our stock share increased to 10.9 percent, up from 10.2 in 2019, with net new lending of £12.5 billion.

In addition, we acquired a 3 billion mortgage portfolio from Metro Bank, which supplements our organic growth plans and represents a positive contribution to income. We plan to build on this position and grow further, whilst maintaining strong pricing discipline.

In private banking, we brought our wealth businesses together last summer so that we can make better use of our asset management expertise to support saving and investment needs for customers across the

group. For example, our online platform, NatWest Invest, gives customers a simple way to invest in a range of funds managed by the investment team in private banking.

Over 1,600 new customers were onboarded by private banking in 2020 and assets under management or administration grew about 6 percent or 1.7 billion, almost half of which was net new inflows. By working across the group to help more customers meet their investment needs, we plan to grow assets under management significantly over the next few years.

Turning to commercial banking on slide 10. We are the largest supporter of businesses in the U.K., with a leading net promoter score and nearly 70 percent of our sales and our commercial bank with digital in 2020.

We are providing more services for our commercial customers by investing in technology-led innovation and products, such as our merchant acquiring platform Till which continues to gain traction and our new payment platform Payit. Payit was launched last June, using the U.K.'s open banking infrastructure to enable online payments direct from consumer bank accounts in close to real time.

We're also investing in digital capabilities that will enable us to deliver a relationship management experience to 16,000 more customers, but at a lower cost. We have enhanced our proposition for small business customers with our digital-only business bank Mettle, as well as online offerings such as Rapid Cash, which enables businesses to borrow against unpaid invoices and Path, a one-stop shop for HR and compliance that has been a lifeline for businesses during COVID.

Finally in NatWest Markets, the team are executing well and reshaping the business to serve corporate and institutional customers with leading products and capabilities in areas such as foreign exchange, interest rate risk management, and capital markets.

With a simplified and less capital intensive business that is better integrated into the bank, we are extending our expertise in foreign exchange across the group, deepening our coverage and product offering for commercial

customers, and leveraging our leading position on sustainable financing, where we brought forward our £20 billion target from next year to this year, as I mentioned earlier. And we expect to exceed it.

You can see on slide 11 how the pandemic has accelerated the rate of digital adoption over the past year, 58 percent of our retail customers now use digital-only to interact with us up from 46 percent a year ago, while transaction volumes through branches continue to decline as a result of changing customer behavior. We are investing in digital transformation to create a relationship bank for a digital world. In other words, a bank where customers can interact with us in person or online at any time of the day and from any place they choose.

Video banking is a good example of this, with meetings up from under 100 a week in January last year to around 15,000 a week in January of this year. The use of our artificial intelligence chatbot Cora grew 67 percent in 2020 to 9 million interactions, of which 40 percent were completed without any human intervention.

Our ongoing digital transformation together with the initiatives I've spoken about in each of the businesses will help us acquire new customers, drive additional revenue generation, and support our lending growth targets. It will also help us to increase efficiency and reduce costs, which I will cover on slide 12.

Customer journeys currently account for 30 percent of our cost base, so transforming them through greater automation will have a significant impact on our operating costs. We were able to extend over £8 billion of bounce back loans last year by creating an end-to-end digital application process within the space of a week. We also used automation to improve account opening in commercial banking last year, resulting in a net promoter score of 60, up from 16. And we are building on this experience to continue to transform other customer journeys.

For example, since last September, customers have been able to renew their mortgage online in a simple straight through process that takes as little as 10 minutes compared with anywhere up to 23 days when the

process was manual. Our mortgage retention levels improved to about 80 percent in 2020, compared to about 70 percent in 2019.

We're now planning to extend digital decision making across all our channels, creating greater speed and certainty for our customers. With further automation like this, we are targeting gross savings in the region of £300 million by 2023 as part of our cost reduction target of around 4 percent per annum.

Let me turn now to investment on slide 13. We intend to invest £3 billion over the next three years, of which more than half will support our income growth and cost reduction initiatives. Our aim is to build a technology- and data-driven business supported by greater automation, artificial intelligence and robotics in order to improve customer experience, increase efficiency, and reduce costs.

We're also expecting to reduce strategic costs to around £800 million in 2021 with a continued reduction through to 2023.

Turning to slide 14, I'd like to update you on our decision on Ulster Bank. After an extensive review, it has become clear that Ulster Bank business in the Republic of Ireland will not be able to generate an acceptable level of sustainable returns.

As a result, we have decided to make a phased withdrawal from the Republic of Ireland over the coming years in an orderly manner. We will do everything we can to ensure that customers and colleagues are well supported and that service is maintained. In the near term, there will be minimal change for customers and colleagues. And we have also made a commitment that there will be no job losses or branch closures in the Republic of Ireland this year.

As part of this phased withdrawal, the group has entered into a memorandum of understanding with AIB to sell Ulster Bank's performing commercial loan book and to transfer some Ulster Bank colleagues supporting this loan book. Naturally, any transaction is subject to the usual due diligence as well as regulatory approval.

We are also in early-stage discussions with other strategic partners about other retail and SME assets and liabilities. We expect the withdrawal from the Republic of Ireland to be capital accretive over the duration of the process. This decision has no impact on Ulster Bank in Northern Ireland.

We are continuing to actively manage capital across the group in other ways, as you can see on slide 15. In NatWest Markets, we're ahead of plan as we reduce risk weighted assets and expect to have largely completed our RWA restructuring by the end of this year. We're also managing portfolios and using synthetic trades across the business to reduce capital consumption, manage risk, and improve returns.

For example, we took actions to offset RWA growth in commercial banking last year, which reduced them by £800 million, and we will make further reductions this year. We expect combined exit and disposal losses from NatWest Markets and commercial banking of around £300 million in 2021.

In retail banking, we have sold about £3 billion of non-performing debt over the past four years. And we continually optimize our regulatory capital with liability management exercises. We are focused on maximizing our capital efficiency in order to improve returns to shareholders, which I will cover on slide 16.

As you know, NatWest is a capital generative business and our strong capital position has been an advantage over the past year, when it has given us both security and flexibility in an uncertain environment. Yet, with a CET1 ratio of 18.5 percent, we are operating well above our target ratio of 13 to 14 percent.

As I said earlier, we are reporting a final dividend of three pence today. And subject to permission from the regulators, we plan to distribute at least £800 million per annum in 2021, '22 and '23 through a combination of ordinary and special dividends, maintaining our 40 percent payout ratio for ordinary dividends.

This gives us the capacity to participate in directed buybacks from the government for up to 4.99 percent of issued share capital a year. Our intention remains to return capital to shareholders or pursue other options that create value. And we have now set out a clear glide path to reach our 2023 target CET1 ratio of 13 to 14 percent.

So let me conclude on slide 17. The economic outlook remains uncertain in an ongoing pandemic. And whilst we welcome the vaccination program, the duration of the current lockdown remains unclear. In this environment, we continue to do everything we can to support our customers, whilst advancing our strategy and accelerating our digital transformation.

Our focus is on driving improved shareholder returns by growing income, reducing costs and maximizing capital efficiency. With disciplined execution in each of these areas, we expect to deliver a return on tangible equity of 9 to 10 percent by the end of our three-year plan.

With that, I'll hand over to Katie, who will take you through the financial performance in more detail.

Katie Murray: Thank you, Alison, and good morning, everyone. I will start with the group income statement and I'm going to focus performance on the fourth quarter.

Total income of £2.5 billion was up 4.6 percent on the third quarter. Within this, net interest income grew 2 percent to £2 billion and non-interest income was up 13 percent to £564 million. This increase reflects strong lending volumes, increased margins on mortgages, and a non-recurring loss of £324 million on the liability management exercise in the third quarter.

Total income excluding all notable items was down 4 percent on the third quarter, as a result of lower levels of customer activity and tight risk management in NatWest Markets, partially offset by income growth of 2 percent across our other businesses.

Operating expenses grew 29 percent to £2.3 billion driven by the annual U.K. bank levy, higher strategic costs, which were up around £100 million and increased litigation and conduct costs. This means we're reporting an operating profit before impairments of £194 million, 68 percent lower than the third quarter.

The impairment charge for the fourth quarter decreased to £130 million. This represents 14 basis points of gross customer loans. And I will talk more about this later.

Taking all of this together, we reported an operating profit before tax of £64 million. The attributable loss to ordinary shareholders of £109 million reflects deferred tax movements in Ulster Bank and Royal Bank of Scotland, along with coupons on 81 bonds and preference shares.

I'll move on now to net interest income on slide 20. Group net interest income for the fourth quarter was £45 million higher than the third. If you look at the column for the third quarter on the left and the fourth quarter on the right, you can see that banking net interest income grew £26 million or 1.3 percent. This reflects strong mortgage growth, improved mortgage margin and lower issuance costs following the repurchase of legacy instruments in Q3.

The strong position in the center is in part the result of this repurchase. Turning to bank net interest margin, this increased 1 basis point in the fourth quarter to 166 basis points. This is the result of three factors. The lower yield curve accounted for a fall of 2 basis points due to the structural hedge. This was offset by a 1 basis point increase for liquidity and 2 basis point increase for mix and pricing. The change in mix and pricing reflects the full quarter benefits of higher overdraft fees, as well as the liability management exercise.

So moving on now to look at the drivers of net interest margin. On slide 21, we show customer loan and deposit rate for retail and commercial banking, which together account for over 80 percent of group net interest income. We also show the overall group gross yield and cost of interest earning banking assets, which covers the rest of the balance sheet,

notably the lower yielding liquidity portfolio and our higher cost wholesale funding.

On the asset or lending side, yields across the group continued to fall reflecting the past through of lower interest rates. But the pace of reduction slowed further in the fourth quarter. Gross yield for the group declined by nine basis points 285 basis points compared to 13 basis point decline in Q3.

This was driven by commercial banking where front book rates remain below the back book due to the rate cut earlier in the year.

On the liability or deposit side, costs reduced by a further 17 basis points to 50 basis points in the fourth quarter largely driven by the repurchase of legacy instruments in Q3. Overall, deposit costs have stabilized.

Looking at net interest margin in the first quarter of 2021, there are three main factors to consider. First, ongoing pressure from the structural hedge, we expect this to be greater in 2021 at a little over 3 basis points per quarter. This will not be completely linear and to be absolutely clear, over the year, it equates to a reduction in income of a little over £300 million from our hedge portfolio compared to 2020.

Second, a change in liquidity. In January, we repaid £5 billion of TFSME loans. However, our deposit base has continued to grow during our third lockdown and liquidity levels will depend on customer behavior in the coming months. The third factor is mix and pricing. Mortgage margins on the front book increased in the fourth quarter to 161 basis points, above an improved back book of 147 basis points. Application margins grew to 180 basis points. However, we expect them to reduce during the year as demand tapers.

Mix will also be affected by demand for higher margin unsecured and corporate lending, which will ultimately depend on lockdowns and the shape of economic recovery.

Moving on now to look at volumes on slide 22. Gross banking loans increased by £9 billion in the fourth quarter driven by mortgages, which grew £6 billion or 3 percent reflecting strong demand ahead of the stamp duty deadline. And of course the £3 billion portfolio acquired from Metro Bank.

Our retail banking flow share in the fourth quarter was 13 percent above our stock share of 10.9 percent. Mortgages now make up 51 percent of total customer loans across the bank. Unsecured balances declined slightly in the fourth quarter, both across personal advances and credit cards. Demand for government schemes also slowed further, but this still accounted for £1.6 billion of additional lending.

However, this was more than offset by £2.4 billion of RCF repayments in commercial banking with utilization in Q4 of 22 percent, lower than the usual pre-COVID levels of 27 percent. Average interest earning banking assets grew by £4 billion or one percent as Metro Bank completed late in the quarter.

Looking now at the charges year-on-year, gross banking loans increased by £36 billion or 11 percent driven by mortgage growth of £16.5 billion and government lending schemes of £12.9 billion. Average interest earning banking assets were £53 billion higher than the fourth quarter of 2019 reflecting increased liquidity. Customer deposits grew by £62 billion which reduced our loan to deposit ratio by five percentage points to 84 percent.

Moving on now to look at non-interest income on slide 23. Fourth quarter non-interest income excluding notable items was £645 million pounds, 34 percent lower than the same period last year and 19 percent down on the third quarter this year. Within this, income from trading activities decreased 59 percent from the third quarter to £122 million. This reflects a weaker performance on the fixed income business with lower levels of customer activity, tight risk management and a further reduction of RWAs.

Looking ahead, we expect NatWest Markets income excluding disposal losses to be in the range of £800 to £1 billion for 2021, as a result of more

normalized market conditions as well as the ongoing reduction in RWAs towards our medium-term target of around £20 billion.

Moving now to fees and commission for the retail and commercial bank, which increased six percent from the third quarter to £491 million. This was driven by lending and payment services in the commercial bank. Despite this recovery, fees and commissions remained below the fourth quarter of last year, in part, due to regulatory changes in retail banking. The impact on group income for 2020 was around £200 million and you will see the full annualized effect this year. The outlook for fees and commissions is uncertain given the current national lockdown, but we would expect them to grow as the economy recovers.

So to round off my comments at income, we are targeting lending growth above the market rate in 2021, which we expect to be more than offset by two main headwinds, the impact of a structural hedge and the income reduction in NatWest Markets which I just mentioned.

As a result, we expect income excluding notable items to be slightly lower in 2021 than 2020. I covered costs in my opening slide, so I'll move now on to look at ECL on slide 24. You remember from the half year that our modeling is based on four different economic scenarios, to which we attach a probability weighting. We used the two central scenarios to reflect expected outlook, each with the same probability weighting of 35 percent. Given the stabilization of economics, we have now increaser the probability weighting to 40 percent for our base case.

This scenario anticipates GDP growth of around 4.5 percent in 2021, while unemployment rate averages 6.3 percent with an improvement expected from Q4. A decline in house prices in low single digits is forecast for this year before steadily reversing from 2022 onwards. And interest rates are expected to remain low with an anticipated reduction in the central bank rate to zero in the second quarter this year. This 10 basis point decline feels a little conservative today, but as we're discussing negative rates only two weeks ago, this is clearly volatile. It would represent around £60 million of income for 2021.

We have included £878 million of post model adjustment for economic uncertainty in our ECL provisions until further credit performance data becomes available as government support protection unwinds. These assumptions are reflected in our expected credit loss provisions of £6.2 billion for the full year. You will see our updated sensitivities on this slide. If we were to weight a hundred percent to the extreme downside scenario, this would increase ECL by £2.2 billion and if we weighted a hundred percent to the upside, it would reduce our ECL by £840 million.

So let me now cover how this impacts the impairment charge on slide 25. We reported an impairment charge in the fourth quarter of £130 million or 14 basis points of gross customer loans. This was down from 28 basis points in Q3 largely driven by a reduced charge of £10 million in the commercial bank compared to £127 million in Q3. This reduction reflects a number of releases, the impact of refreshing our economic assumptions, and the post model adjustments I talked about earlier. Our active capital management in the commercial bank has contributed to this low impairment charge and we had no (tall tree) exposures in 2020 or indeed this year.

In retail banking, the £65 million charge is a slight reduction, mainly reflecting stage three default charges and updated economic scenarios. Any potential flow of new default is still being delayed by government support. Our impairment charge this full year of £3.2 billion is equivalent to 88 basis points of loans. We expect impairment for 2021 to be at or below our through the cycle guidance of 30 to 40 basis points.

I would now like to talk about our risk profile on slide 26. There had been little change during the quarter as government support measures our ongoing and customers have built up healthy cash balances over the year. Ninety-seven percent of our loan book is in stage one and stage two not past due, where customers remain up-to-date on payments. Stage two past due is 0.8 percent of the book, down from 0.9 percent at Q3. And stage three is 1.7 percent, down from 1.9 percent at Q3, reflecting write offs of legacy mortgages in Ulster. Our ECL coverage ratio is 1.7 percent with stage three coverage of 41 percent in line with Q3.

As we know, some of our wholesale loans are in sectors that we monitor closely. These amounted to £27 billion in Q4 which represents seven percent of gross loans. In these sectors, similar to the trend at group level, stage three gross loans were broadly stable at around £800 million and we remain comfortable with coverage at 52 percent.

Turning now to look at risk weighted assets and capital on slide 27. RWAs decreased £3.6 billion in Q4 driven by credit risk and counterparty credit risk. This reduction was mainly in NatWest Markets where we reduced RWAs by £3.1 billion to £27 billion ahead of our £32 billion target. We expect NatWest Markets' RWAs to increase slightly in the first quarter this year due to normal seasonality, but our year-end target remains appropriate.

This year we expect to achieve the majority of our targeted reductions down to around £20 billion. There was no impact overall from procyclicality for the full year, this reflects positive trends in retail banking which offset the negative trends in commercial banking. We ended the year with a common equity tier one ratio of 18.5 percent on a transitional basis under IFRS 9. This is 30 basis points higher than Q3 driven by lower RWAs and software intangible benefits. Partially, offset by the proposed dividend of three pence and the linked pension contribution of £266 million post tax. Together, these accounted for an impact of 36 basis points.

Moving on to the drivers of our CET1 ratio on slide 28. We have shaped the business to operate at a CET1 ratio of 13 percent to 14 percent and we plan to reach this level by 2023. As you can see, there are a number of factors to consider when modeling this evolution. First, we expect to generate capital as we move towards our nine percent to ten percent return target in 2023. Second, distributions to ordinary shareholders are a priority, and we intend to distribute a minimum of £800 million per annum through dividends while retaining capacity to participate in directed buybacks for which we have regulatory provision in place today.

These are also linked to pension payments where we have committed to pay up to a further £1.1 billion pre-tax into the pension fund over the

coming years. IFRS 9 transitional benefit which accounts for around 100 basis points of our ratio will taper down through to 2024 and will also be affected by stage migration which remains uncertain. On the denominator, we expect RWAs to increase relative to full year '20 driven by three factors. First, lending growth, we intend to grow above market rate in the U.K. and RBSI excluding government schemes and the mix of lending would impact RWAs.

Second, pro-cyclicality which to-date has been incredibly low and the timing of which remains uncertain. Third, regulation, we expect changes made by the PRA to increase our mortgage RWAs by around £12 billion. This reflects growth in the book and assumes risk weights of around 15 percent as we have previously guided. While this is effective from January the 1st, 2022, we would expect to see some of this inflation brought forward to 2021 as a result of pro-cyclicality. On Basel three we anticipate inflation of less than five percent in 2023 given the changes that will come into effect on January the 1st, 2022.

These impacts will be partially offset by the ongoing refocused of NatWest Markets. Taking all of these facts together, we expect RWAs in the range of £185 billion to £195 billion at the end of 2021 including all regulatory impacts on January the 1st, 2022.

Turning to our capital position on slide 29. Our CET1 ratio is now 450 to 550 basis points above our 13 percent to 14 percent target range and more than double our maximum distributable amount. Our U.K. leverage ratio of 6.4 percent is 315 basis points above the Bank of England minimum requirement. We have also maintained strong liquidity levels with a high quality liquid asset pool and a stable diverse funding base. Our liquidity coverage ratio increased in the quarter to 165 percent due to higher deposits and headroom above our minimum requirement is now £72 billion.

Turning to the outlook for returns on slide 30. As Alison said, we expect NatWest Group to generate a return of tangible equity of between nine percent and ten percent by 2023. The key drivers behind this are, first,

growth. While we expect income to be slightly down in 2021, we are targeting above market rate lending growth across our U.K. and RBS international retail and commercial businesses through to 2023. And we expect support from a normalization of customer activity as we exit lockdown and as the economy recovers.

Second, cost reduction, we plan to reduce other expenses by around four percent per annum, excluding the impact of the phased withdrawal from the Republic of Ireland along with continued reduction in strategic costs.

Third, capital. We intend to reduce our CET1 ratio to between 13 percent and 14 percent by 2023. And finally, we would expect ongoing impairment normalization.

So to conclude, we have delivered a resilient operating performance with growth in net interest income in the fourth quarter and continued progress on both cost and RWA reductions accompanied by a strong capital and liquidity build. And with that, I'd hand back to Alison.

Alison Rose: Thank you Katie. I'll wrap up with a brief conclusion before we open it up for questions.

We delivered a resilient performance in 2020 and despite the challenges of the pandemic, exceeded our targets on growing lending, cutting costs, and reducing RWAs. In an uncertain economic environment, we continue to do everything we can to support our customers whilst advancing our strategy and accelerating our digital transformation. Our focus is on driving improved shareholder returns with targets set to grow income, reduce costs, and maximize capital efficiency over the next three years. With disciplined execution in each of these areas, we expect to deliver a return on tangible equity of nine percent to ten percent by the end of 2023.

We are pleased to be able to recommence dividend payments and are reporting a final dividend of three pence for 2020. And subject to regulatory permission, our intention remains to return capital to shareholders with a payout ratio of 40 percent for ordinary dividends and with distributions of at least £800 million per annum in 2021, 2022, and

2023, giving us the capacity to also participate in directed buybacks from the government.

Thank you very much and we're now very happy to open up for questions.

Operator: Thank you very much. As a reminder, ladies and gentlemen, if you wish to ask a question, please press the star key followed by the digit one on your telephone keypad.

Our first question for today is from (James Irvine) from SD, please go ahead.

(James Irvine): Hi, good morning. Thanks for taking my question. Katie, can I just check something you said. You said that you have regulatory permission for a buyback from the government. So I think five percent of the market cap is just over a billion at the moment. So you have permission in place at the moment to do that if the government wants to sell next week.

Katie Murray: Yes. We actually have provision and you can find this on the FCA website to a maximum of £1.25 billion. We're limited by the five percent that we can do under the regulation, so that's all granted and has been approved. So if the government chose to act next week, we would be a willing buyer. Thank you.

(James Irvine): And if they don't choose to act and they don't want to sell, what happens to that permission? Do you use it in other ways?

Katie Murray: No. The way it works, the permissions are raised particular to directed buybacks, if you were to look on the FCA website you'd see that they're for six months and we will have naturally a rolling program of renewal. So it's sitting there waiting to be used for a directed buyback specifically.

(James Irvine): Lovely. Perfect. All right. And then my second question is on Ulster Bank. So clearly I think the – what we are aiming to do is sell the various parts of it.

If you can't agree a price with other parties, then would you put it into runoff? Is that a potential option or it's kind of sell it or maintain it?

Alison Rose: Thank you. So it's a phased withdrawal that we will be undertaking over the coming years. And clearly, my focus is making sure that's done in an orderly and considered manner.

You will have seen in the announcements today that we are in discussions with a number of parties as part of that phased withdrawal, so the non-binding agreement with AIB and a potential transaction, then also early discussion. So our preference is to continue to focus our discussions with counterparties who can provide customers with full banking services in the Irish market. So we'll do it in a very considered and orderly way and will give you an indication of some of the early preliminary conversations we're having.

(James Irvine): Thanks. Lovely. Thanks very much.

Operator: Thank you. Our next question is from (Rajiv Chandra Rajan) from Bank of America. Please go ahead.

(Rajiv Chandra Rajan): Thank you very much. Good morning. I have a couple please for Katie.

First one was on revenues; you cite a few areas including some of the margin drivers, loan growth, reduction in NatWest Markets revenues. The one that you might be able to flesh out a bit some further detail in terms of the guidance for revenue slightly down in 2021. And then the second was on risk weighted assets, so 2021 guidance is £185 billion to £195 billion, just after that there were a few moving parts be on that. So how should we think about that evolving through to 2023, please?

Katie Murray: Sure. Thanks (Rajiv), let me jump into them. So in terms of revenue, we expect 2021 income excluding notable items to be slightly down on 2020m driven by the three factors I mentioned in my speech.

So lending growth is targeted above market rate in 2021 excluding Ulster Bank. And then that gets more than offset by two headlines, the impact of the structural hedge which is this year slightly higher, a reduction of a little

over £300 million in that. And then on income reduction from NatWest Markets. So we expect NatWest Markets this year in terms of the income to go for the £1.2 billion that they did in 2020 to be between 0.8 and £1 billion. Obviously, on a – that's on an underlying basis, you then have things like disposal also separately. But I think that gives you enough to get there.

And then in terms of the RWA movements, there are certainly a few different things going on within that path. So I think we were pleased in Q4 to see the decrease of the £3.6 billion. As we move forward from here, what we expect for 2021, the RWAs will be in the range of £185 to £195 billion. And including on our pro forma basis, the impact of the Bank of England mortgage risk weight changes and other modeling changes introduced on the 1st of January, 2022.

So if I look at the mortgage change, that number at the stage we expect to be around £12 billion, it will be subject to the timing and quantum of pro-cyclicality whether a bit of it might come in a bit earlier in 2020, but either way on the 1st of January, 2022, we would expect it to be about £12 billion and that's in line with the 15 percent risk weighting that we've talked about over the last number of years.

I think the interesting challenge will be around what happens in terms of pro-cyclicality, how that comes on. And we also talked about 2023, I would expect that by 2023 that that pro-cyclicality has started to roll off again, so you will have a kind of a peak that comes through 2021, 2022, by 2023 you start to see that coming down.

So I would think as you look to 2023 I would think of that £185 billion to £195 billion number still being appropriate because you've got lending growth coming in, pro-cyclicality coming off and I think the one thing that I'd love to give you better guidance on today given the Ulster number but I think we'll wait and give you updated guidance later. The timing of that in terms of Ulster, so we do expect some movement on there, but that £185 billion to £195 billion includes Ulster number as we've currently got it printed.

(Rajiv Chandra Rajan): That's great. Thank you very much.

Operator: Our next question is from (Ralph Suna) from J.P. Morgan. Please go ahead.

(Ralph Suna): Hi, good morning. Thanks for taking my questions. I just had maybe three quick ones if I can. The first one is just on this mortgage income disclosure that you give.

I can see that your mortgage book is up 10 percent over the past year and you've got obviously some very strong mortgage margin trends. But if you look at your Q4 mortgage income, it's actually flat year-over-year and it's down quarter-on-quarter by about four percent and struggling to reconcile that against all of your commentary? I'm wondering if there's something specific that I might be missing there? That's the first one.

The second one, just on Ulster and this business that you sold to AIP, or you reached a memorandum of understanding on, if I look at the commercial revenue contribution, I think it's about £200 million, do we think of that as the size of the business that might get transferred over if the deal is complete?

And then third one, just very quickly to clarify on the directed buyback comments, if there wasn't a disposal for – by the government, would you consider sort of supplementing your 40 percent payout ratio next year? So if there is no possibility of a directed buyback over the next year or two because there's a lack of government sale, would you also look to supplement, that 40 percent payout ratio or would you just hold that capital in reserve for whenever that directed buyback comes through? Thank you.

Alison Rose: OK, thank you. Well let me pick up the directed buyback and after – and Katie can talk you through the mortgage question.

On directed buybacks as you know, it is a decision for the government when and if they sell and we are ready participate, if they don't see that, then my clear preference is clearly to return capital to shareholders or

explore other opportunities of value for shareholders, so we would review that at that time. But we have no intention of changing our 40 percent payout ratio and I think we've given you guidance from that.

On Ulster, just to be very clear, we're announcing today the phased withdrawal. As part of that, we are in preliminary discussions with a number of parties, including AIB, where we signed a memorandum of understanding. And so we will be working with them on that potential transaction as we go forward and it's subject to due diligence and negotiation but it gives you an indication of some of the intent that we have around this. So I think we will continue to update you on that as matters progress. But we expect withdrawal from the Republic of Ireland to be capital accretive over a multiyear period and we will provide you with further guidance as we go forward.

Katie, do you want to pick up the mortgage question?

Katie Murray: Yes. The mortgage point is actually in relation to the Metro Bank transaction, that slight softness in the Q4. So you can see in the notable items in the company announcement that we have a £58 million loss on day one on that and that bleeds back through into income over the next couple of years. So that's why you see the apparent disconnect and the strength of the rates that we're charging and compared with what you see coming through in income.

(Ralph Suna): Thank you.

Katie Murray: Thanks.

Operator: Thank you very much. Our next question is from Andrew Coombs from Citi. Please go ahead.

Andrew Coombs: One on capital return and one clarification as well please. On capital return, firstly, you've talked about ordinary and special dividends, you talked about directed buybacks. There's no discussion here of general buybacks in conjunction with the directed buybacks, so can we assume

that general buybacks are off the table as a capital return mechanism? That's the first question.

Second question more numeric, the £800 million minimum of dividend that you've guided to per annum, can you just provide some indication of how you triangulate to that figure? The reason I say that is even if you adjust for the five percent directed buybacks, the 13 percent to 14 percent quarter one, the £185 billion to £195 billion RWA consensus retained earnings, it looks a little low in order to hit that 13 percent to 14 percent core tier one ratio that you're guiding to. So perhaps you could just explain how you triangulated to that £800 million number?

And then my final question, just a very quick clarification, on the 2023 return target of nine percent to ten percent, what are you assuming for base rate out to 2023 for that? Thank you.

Katie Murray: Perfect. Let me – and I'll do you in reverse order if that's OK. So when we look at the – our functions in terms of the base rate is that there's a fall today of 10 basis points – sorry, in Q2 this year.

I would say that probably today that feels a little conservative but then there was no rising from that. So that's sort of in our budget plan that we're not really anticipating a rise and certainly from that. But the numbers that work for the 10 basis fall and we'll see what that comes to.

In terms of which you triangulate in terms of the CET1, let me try to help you look at it. So you've got RWA and target range of £185 billion to £195 billion. If you took the midpoint of that, that would use about 1.9 percent in terms of the capital that's available. You then have in 2021 the dividend of £800 million, as a minimum that would be another half a basis points, let's assume a directed buyback, that would be another 0.6 of CET1. Remember, that we'll also make our pension contribution which would take up 0.3 on that.

So you'd end this year with that math obviously taking your own views on pro-cyclicality. So just over 15 percent. And then as you start January, you have a little bit of movement going on with software capitalization and

also remember the IFRS 9 migrates down as well, sometimes that benefits. It's a hundred percent now, 75 percent, 50 percent, and so on that you'll see that piece come down.

So then NatWest Group will also be capital generative obviously you're adding on as well and then will continue to make some of those dividend payments, the directed buybacks second and third year depending on how those transactions are actually happening and where the government is on their disposal as well as some further pension contributions. So that should get you down to a range within 13 percent to 14 percent by the time we get to 2023.

Andrew Coombs: OK. So reading between the lines, that £800 is because that's where you feel comfortable doing this year, but the minimum phrase is because in 2022 and 2023 you could potentially go beyond that, is that fair?

Katie Murray: Right. I think if you look out to 2023 and you were at the nine percent to ten percent return, you would see that on a 40 percent payout ratio that your number will be a bit higher than that. So I think it really – it’s as a base and so the minimum word is not accidental.

Andrew Coombs: That's good. And on general buybacks?

Katie Murray: I'm sorry, I missed that (Andrew), forgive me.

Andrew Coombs: I'm sorry. I was saying that the wording directed buybacks and ordinary and special dividends but no general buybacks. Is that a fair read?

Katie Murray: No. Look, in terms of conversations that we've had with our wide investor base, I mean, the preference at the moment is there are definitely directed buybacks.

Andrew Coombs: OK. Thank you.

Katie Murray: Thanks, Andrew.

Operator: Our next question is from Jonathan Pierce from Numis. Please go ahead.

Jonathan Pierce: Good morning, both. I've got two questions, please. It's all on guidance, I'm afraid, all on the outlook. The first is income again in 2021. Just so we're entirely clear on this, slightly down on the income ex notable items. Consensus, I think, is about £200 million, £250 million down on 2020, excluding notable items. Is that within the bound result, a slight reduction?

In other words, are you happy with consensus ex notable items for 2021? And then can I ask about 2023? I mean the delta to a 9 percent ROTE versus consensus is ballpark £1 billion of pre-tax profit.

We know what you're thinking on costs. But maybe you can give us a feel as to where the other deltas are going to land in the P&L, particularly income impairments. If there's anything else going on there as well? Thanks a lot.

Katie Murray: Yes. Sure. Look, I probably won't to say anything more on the 2021 guidance. I think I've been quite clear in terms of the building block from where we are today to where you'll get to on 2021. So then, if I take and look at the ROTE, so we're targeting ROTE of 9 percent to 10 percent. That's not impacted by Ulster Bank. The key drivers of that is the lending growth that we talk about in terms of the above market lending growth.

We'd also expect to see a little bit of benefit from some of the investments that we're making in this year to come through into the income line as well. The cost reduction targeting around 40 percent – sorry…

Alison Rose: Four percent.

Katie Murray: Four percent, sorry. Quick clarification. Forgive me. It's 4 percent in 2021, excluding any of the change in that direct cost base within Ulster. You will see the strategic cost reduction.

We've gone from £1.4 billion to £1.1 billion, now down to £0.8 billion. We'd expect that reduction to continue within there. And I think one of the key things also would be the normalization of your impairment charge. Clearly, what we've talked about today is that we'll – we expect 2021 to be in the – at or around the 30 to 40 basis points.

As we look out to 2023, we probably expect that to tighten a little bit further, as you just see more things work their way through the system by then.

Jonathan Pierce: OK. So, if I were to be lucky enough to see your budget and put it next to consensus side, I would probably expect to see costs a bit lower, impairment maybe a bit lower, and income £200 million higher. What would that be sort of what I'd be observing?

Katie Murray: I think if you are lucky enough to see that, then you would probably be relatively pleased with some of those builds. So, I think we're – I think I appreciably on cost and have a rethink about impairments, and I think we've guided you a bit on growth as well.

Jonathan Pierce: Great. Thanks a lot.

Operator: The next question for today is from Alvaro Serrano from Morgan Stanley. Please go ahead.

Alvaro Serrano: Hi. Good morning. I had a question on mortgages and another one on the structural hedge. On mortgages, can you give us a sense of where pricing is at the moment? I think you said last quarter was around 160 basis points. And also, how you – how that's trending given we're probably now – all the offers now are in the post stamp duty world? And related to that, if we think about volume growth, I know you said you plan to grow above the market.

But would you say in mortgages, you expect to grow more or less this year than last year, obviously, excluding Metro? And the second question on the structural hedge, that – just above £300 million drag for this year. Are you – what curve are you assuming – you would assume the latest steepening or a bit of color on those assumptions? Thank you.

Katie Murray: Sure, Alvaro. So, if I look at mortgages and you recall it at our Q3 announcement that we talked about that we were really writing in Q4, the applications were around 180 basis points. That has continued into Q4

and even into the early part of Q1. So, what I would expect is that during kind of Q1 and into Q2, we kind of get the benefit of that sort of level, that we have said that we expect to see some tightening.

You'll have seen that in the last week, I think all the major banks have a little bit of tightening on different bands and in different places, but there has certainly been some tightening of that coming through. In terms of volume growth that we grew to 10.2 percent share – stock share to 10.9 percent, obviously, helped by Metro – sorry, we take that out. But we do feel that that still just gives us strong growth to keep moving forward. So, we'll continue to look at that and try to get to that.

When I look at the £300 million hedge guidance around the move-up in the yield curve, so what I would say is that the little over £300 million is our base case. It's worth just reminding you that in terms of the hedge, the purpose of it is to reduce our near-term sensitivity in rate changes. So, whilst this strengthening of the swap curve you see is helpful, we wouldn't expect to get a particular benefit of that in the first year.

You can see in the accounts on Page 234, that when you see a 25 basis point increase in interest rates, it adds £371 million in year 1, but only £37 million of that is in relation to the hedge, which then rises out to £200 million by year 3. And the reason for that is that these are – they're five-year hedges.

So, you only get the very small averaging impact coming in on that. So, it's our base case, but the recent move, it will help us in later years, even 2023.

Katie Murray: If it's sustainable and in terms of that move upwards, but it doesn't have a particular impact in 2021.

Alvaro Serrano: Thank you very much.

Katie Murray: Thanks, Alvaro.

Operator: Our next question for today is from Jon Peace. Please go ahead. From Credit Suisse.

Jon Peace: Thank you. So, my first question, I just wanted to ask Jonathan's question again in a slightly different way. To get to your 9 percent to 10 percent ROTE by 2023, if 2021 is going to be a down year for revenue, it looks like you might need a revenue CAGR of about 5 percent to 6 percent in 2022 and 2023 to hit the lower end. And I just wondered if you would agree with that back-of-envelope calculation and what the drivers of that rate of revenue growth might be?

And then my second question would just be on provisions for 2021. You mentioned you might be at or below the through-the-cycle cost of risk. Are you implying you could see some provision releases and how should we think about what might be the triggers for these? Thanks.

Katie Murray: Yes, sure. I'm probably not going to get into the math of your model and different kind of CAGRs. I kind of just repeat on the income piece. We're targeting above market lending growth across the U.K. and RBSI. And we'll see a bit of benefit coming through from some of the investments that we're making and that will get you the income.

I think you have all the building blocks you need to draw a picture out to the 9 percent to 10 percent and why we're comfortable in saying that. The 30 to 40 basis points and some of the release of provisions, it feels too early to be talking about release of provisions even at 30 to 40 basis points. That's still a charge that would be higher than what we would have seen in the years leading up to this crisis. So, still a meaningful number, though obviously quite reduced from where we are today at the 88 basis points.

When I think about what we'll – what you'll see happening to actually see any of those releases coming through, one is the improvement in economics. And you can see when you look at some of the Stage 2 analysis in commercial, that some things have moved in this quarter from stage two back into stage one and then that was really to do with the

strengthening of economics. But what we've done as a firm is that we've created in our post model adjustments.

So, what we're saying is that while the economics have definitely improved, the impact of the government support has been such that it's kind of protecting the quality of the underlying book. So, I think before you start to see any releases, you'll start to see that support coming off. And you will also then start to see business failures. But if really – although there have been a few, we haven't had any tall trees at all this year.

You need to start to actually see that real degradation coming through in them in the business failure. So, I – lovely to get talking about releases, but I don't think it's time to have that conversation just yet. That feels quite far away just now.

Jon Peace: Fair enough. Thank you.

Katie Murray: Thank you, Jon.

Operator: Our next question for today is from Guy Stebbings from Exane BNP Paribas. Please go ahead.

Guy Stebbings: Good morning. Thanks for taking questions. The first question was just on margin. Would you able to give any sense of sort of shape of margin for this year? And perhaps if we exclude an assumption around the base rate cut, but it sounds from your commentary like Q1, you're not expecting a lot of movement given the benefit from mortgage spread completions, quite elevated levels, hopefully offsetting other headwinds.

But as you look further into the year, you're sort of talking to mortgage spreads likely coming down slightly across the hedges and flowing through. So, would you expect a sort of gradual decline over the course of the year?

And just one quick clarification into it as well to check. Is your income going to 2021 a bit of a little down factoring any reduction in Ulster income for this year? And then my second question was just on the government-

guaranteed lending which is about £14 billion now in the balance sheet, which a good majority is the bounce back loan scheme.

Just wondering if you have a sense as to how much of that is sort of starting deposits rather than being utilized by corporates right now? And if the interest becomes due sort of one year post being drawn, would you expect to see a big decline in those balances? And associated with that, do you have any sense or any confidence as to whether there's much fraudulent businesses within your – the facility or should those be quite negative?

I'm just trying to think about whether that £14 billion of government-guaranteed lending could fall in balance terms quite quickly over the course of the next 12, 18 months or so? Thank you.

Alison Rose: Well, look, let me answer the bounce back loan scheme and then – and Katie, then will pick up the other question.

Katie Murray: Yes.

Alison Rose: So, we've advanced £14 billion under the bounce back loan scheme. And as I said at the outset, we were lending that to our existing customers, so customers who we know and who bank with us.

I think in terms of the behavior that we're seeing from our customers, and I think that's probably where our focus. Demand for those schemes has really tapered off and it's really the sort of second, third quarter last year. If you think at the peak, we were sort of getting in something like 70,000 applications a day, that's tapered down to around seven. And our deposits remain very high.

What we've seen when we talk to our customers is they – and it will depend on the sector because some sectors will be using their cash much more. It's that a lot of customers are sitting on the cash, they choose – they have equivalent amounts of cash on their balance sheet versus their loan that they could pay down their loan. However, while things are still

uncertain, they're not making that decision. So, we're in a sort of very benign period at this point.

You're not really going to see, I think, much of a change until those loans start falling due for repayment. So, towards the Q3, Q4 this year, in reality, I think, when customers have the choice to repay their loans, start repaying their loans, may take advantage of the pay-as-you-grow scheme where they could extend the tenor. And these are quite cheap loans. But I think the issue of how quickly that cash will burn as people start spending the money or paying down their loan will depend on the recovery of the economy. But I think really in terms of behavior, it's the back end of Q3 or Q4.

On the fraud point, just to touch on that. As you know, the bounce back scheme is predominantly a self-attested scheme, and we're required to undertake sort of minimal checks on eligibility and frauds. But we have abided fully by the terms of the scheme. We've implemented our usual fraud checks on the scheme.

So, we've put in the usual protection. I think where we've seen issues of potential areas of fraud where our customers are applying for multiple bounce back loans from different banks or where they haven't been trading, so not filling the eligibility criteria. But we've applied our usual fraud checks that we would do, and in fact, have put enhanced fraud checks during the period. So hopefully, that gives you a flavor both of behavioral and what's happening.

Katie, do you want to pick up the other question?

Katie Murray: So, in terms of income for Ulster, I would assume – I mean, I think you should take our guidance, assuming that we have Ulster in the numbers for 2021. So, I think I've given you quite a lot of our 2021 guidance on that already, so I won't repeat it.

If I look to NIM, so if I look sort of Q1 2021, I would remind you, there's three buckets that you need to think about the yield curve. So, we're now

expecting a three basis point decrease in Q1 from the lower hedge income driven by some high yield positions are due to roll off due – in 2021.

Liquidity. This is impacted by the TFSME repayment that we did in early January as well as the changes in loan and deposit volumes. And I think I'll leave you to decide what might happen on as of the micro or macro basis on them. And then mix and pricing. I've spoken a lot already around the mortgage applications in Q4 were a little stronger. Obviously, the commercial loan book is impacted by the lower front book yield. And we also expect in certainly in the early quarter, lower unsecured volumes just due to this lockdown that we're in at the moment.

Guy Stebbings: OK. Very helpful. Thank you.

Katie Murray: Thanks, Guy.

Operator: Our next question is from Chris Cant from Autonomous. Please go ahead.

Chris Cant: Good morning both. Thank you for taking my questions. Two follow-ups, really. The first, on the revenue guidance, just so we can get this straight.

I think what you're saying there, you've guided us to £300 million of disposal losses in 2021. So, that implies something like 10.9 of headline revenues post notable. And I think you've said with the base rate cut you've assumed, which hasn't yet happened, that might be worth about £60 million. So, I get that you're saying a bit less than the 10.9, but maybe with no base rate cut, we just get back to square 10.9.

Consensus is at 10.6 percent. I mean, there's a bit of upside there. Are you comfortable with that? Coming back to the early question on Ulster Bank. Maybe I missed the answer.

But if you do sell this portfolio of loans to AIB during 2021, which it doesn't seem like you're assuming, how much would that knock off that 10.9 of income guidance? And then secondly, on investment spending, your slide deck talks about £3 billion. How much of that is going to be OpEx, please? How much is going to be CapEx? And does that include the restructuring

charges you are guiding for in the P&L or are those entirely separate? Thank you.

Alison Rose: Chris, so look, let me touch on Ulster, and Katie can pick up the other. I think she sort of talked you through the revenue guidance, but we'll try and pick up those points. On Ulster, we're announcing a gradual withdrawal. As we said, the discussions we are having are at a very preliminary stage. The discussions with AIB relate to the performing commercial loan book, which is £4 billion. But I think we are at very early stages, so you shouldn't make any assumptions around completion this year.

Katie, do you want to touch on the other point?

Katie Murray: Yes, absolutely. So, just in terms of OpEx and CapEx, you can see from our accounts that we – the way that it flows through, and we shared this with you in the past that we have about a 60 percent OpEx and CapEx split, so 60 percent of the spend would come through. What I would say is that's not really time-relevant these days because obviously things have capitalized in the past. They're hitting our accounts today so it kind of moves itself out.

So, I wouldn't – I would probably encourage you not to hurl yourself down there too deeply. I have to admit, when we talk about the investment piece, that's – the investment numbers are embedded in our other operating costs. So, the impact of historical depreciation plus what we kind of have coming through today. Then when we talk to the restructuring or strategic costs that we've talked about, the £1.4 billion going to the £1.1 billion going to the £ 0.8 billion, those are very much in relation to things like redundancy and the property type charges.

So, that's separate from there. So, it really is around the big hits and you have to do things at some of your property. So, it's the £3 billion that goes into that base piece.

In terms of income, I was obviously talking to income, excluding notable items but I think you've got all the building blocks there, Chris, in terms of

the lending growth, the impact of the structural hedge, and the NatWest markets reduction. And then of course on a total basis, you have a £300 million of disposal losses that you've talked about. So, I think you've got all the building blocks. Thanks, Chris.

Robin Down: On the structural hedge, what reinvestment rate are you assuming for the £300 million? With the recent rise in five-year swap rates and assuming they're maintained, I would have expected that £300 million to be a little lower.

Katie Murray: Yes. So, at the moment, it's rolling off, I think, about 88 basis points. And our assumption would have been certainly below what you see today. If I look at the early parts of the year, it was much more around the kind of 20 basis points level.

I guess, I'd just repeat what I said earlier, and it's possible just around the timing of your question coming in on the web. It is really to do with the fact that these are five and 10-year hedges. So, you don't get an immediate uptick in the hedge income as a result of the strengthening of the curve. You can see the disclosure quite well on Page 234.

So, as the curve strengthens up by 25 basis points, you have a £37 million income benefit that would come into this year. Clearly, if there's a rate change, you then get much – you get a much bigger impact and much more quickly in terms of your managed margin which you, again, can see on that note. But in terms of the structural hedge, the advantage of, it takes time to roll out. But the disadvantage of course, is it takes a little bit of time to roll back on. And so, that's the £37 million this year. Thanks, Robin.

Operator: Our next question is from Edward Firth from KBW. Please go ahead.

Edward Firth: Yes. Good morning, everybody. Sorry to go back to this, but I'm just trying to be clear. In terms of – I'm sorry, I've got two questions.

One was in terms of your forecast out to 2023, they are based on your targets. They are based on assuming that you had kept Ulster, and you've

got like a sort of business as usual Ulster in there. Is that correct firstly? Just to be – to clarify that. And then…

Alison Rose: What I would say is – sorry, on you go.

Edward Firth: Yes. I'll give you my second question, sorry. And then the second question was just going back to Guy's questions on the bounce back loans. A number of your peers have suggested that obviously, during the course of this year, customers are going to have to start paying interest themselves on these loans, whereas at the moment, is paid by the government.

And a number of your peers have also said we might expect quite a big step down in those volumes once people have to pay the costs themselves. It doesn't sound like you're expecting that. Is that fair?

Katie Murray: Look, if I think of the bounce back loans and how they will unwind, I think it's obviously an incredibly interesting topic. They'll start making payments in May. What we've seen is a lot of extension of payment terms and how they can pay it. We know that people are sitting on a lot of cash deposits.

And I think we'll just – we'll wait to see how that unwinds but we're not necessarily assuming that we see a massive paydown come through. I mean, Alison what would you add to that?

Alison Rose: Yes. I mean, one thing I would add is bear in mind that on the bounce back loans, these loans are averaged £35,000 to £37,000 in terms of individual loans. They're at very cheap costs for the borrower. And if you look at the pay-as-you-grow scheme and the ability to extend the term, you could quite easily see a lot of customers taking advantage of that to extend the term and keep low borrowing.

I think we will start to see what will happen as those loans start coming due for repayment and customers start making the decision of what they want to do. At the moment, as I said, when I'm talking to customers, they're very much keeping their cash on deposit looking ahead at the uncertainty that they're facing. So, I think we'll have a clearer view on that going forward. I think for a lot of businesses, they will be facing the

choice of how is the economy going to recover? How are they going to position their business? Are they going to reopen their business? I think that is a consideration.

And how much uptake will there be of the pay as you grow, which gives them a lot more flexibility to manage both the recovery and the growth in the economy versus the extra debt they've taken onto the business? So, I guess that's a long-winded way of saying, it's too early to say but we can definitely see the attraction of people extending and keeping their loans for longer if they are going to continue trading.

Katie Murray: And if I could just add on the Ulster point in the 2023 target, try to be crystal clear. So, we expect to manage the withdrawal from Ulster in such a way that is gradual and supportive of our 9 percent to 10 percent group ROTE target in 2023. So, what you would see is income reduction will come with RWA reduction, and then we'll work on reducing the direct cost base as is appropriate. So, the Ulster plan is inherent in that guidance that we've given you today.

Edward Firth: OK. It's inherent within its – OK. OK. Sorry. Thanks very much.

Katie Murray: No problem. Thanks, Ed.

Operator: Our next question is from the line of Rob Noble from Deutsche Bank. Please go ahead.

Rob Noble: Good morning, all. Sorry, I have two questions. One on Ulster and one on capital return. How much of the book are you actually actively in negotiation on? I know sort of – I presume that there's a large proportion of the mortgage book but you don’t – actively talking about selling at the moment?

And then how confident are you that it will be capital accretive, given that I presume you're not – haven't completed negotiations yet? And then on capital return, I just wanted to clarify, is – you say payout ratio will be around about 40 percent. So, how much flex is there?

And I just didn't quite understand one of the answers, which was if the government doesn't do a buyback, a directed buyback, then are you happy to increase the 40 percent payout ratio or not? Thank you.

Alison Rose: I'll pick up – let me pick up Ulster. So to be clear, we are doing a phase withdrawal. The discussions that we are having with strategic partners and strategic counterparties are at preliminary stages at the moment. And as I mentioned, we've signed a nonbinding MoU in relation to a portion of the book, and we are also in early discussions with PTSB around certain retail SME assets and liabilities.

So, those discussions are preliminary and we will obviously work very hard to ensure that we have an orderly and supportive transition over a number of years. And once we have more detail on that, we'll update you. But we are – we expect our withdrawal from the Republic of Ireland to be capital accretive over a multiyear process.

Katie Murray: And let me try just, Rob, on the payout ratio to kind of help you. So we, like other companies, have our dividend practice that we adopt to. So, that's our 40 percent ordinary payout ratio in any one year. On top of that, you could expect us to do some special dividends, which – and if you look at the forward look, you would certainly – you would see that in the next couple of years.

So therefore, you would say, actually the minimum – what we said to you is the minimum today is around £800 million, and that will be a build of ordinary and special, keeping in line we've got 40 percent payout ratio as we go through because that's a longer-term ratio that we try to work with. We then also got capacity and retaining that capacity to do directed buyback transactions with the government. If we were not to do that, we've not made any confirmation, say, as what we would do with that but I would go back to our base philosophy, which is all our intention to return our capital back out to our shareholders. But our preference is the £800 million and directed buybacks and the £800 million being a minimum to start from.

Rob Noble: OK. Thanks very much.

Katie Murray: Lovely. Thanks, Rob.

Operator: Our next question is from the line of Benjamin Toms from RBC. Please go ahead.

Benjamin Toms: Good morning, both. Thank you for taking my questions. Firstly, on just conduct and litigation. In the quarter, you had a notable item of £200 million, which included the reversal of PPI provisions.

Is there anything particular driving the higher number here? Are you building up potentially a provision to deal with potential bounce back of loan litigation? So, this sounds like there's going to be no industry solution on the problem.

And then secondly, you said you plan to grow assets under management significantly over the next three years. Could you potentially do something inorganic here? Thank you.

Alison Rose: And so, let me pick up assets under management. As you can see, we've had strong growth in assets under management report, a real focus around that and making sure that we're using our asset management capabilities in all private banks to support our customers. So, we think there's very good growth organically within our existing business, and you can see that from the results that we've delivered. As always, we will consider inorganic opportunities if they offer shareholder value from that perspective.

Katie, do you want to take the other question?

Katie Murray: And if I look at conduct, so you can see in disclosures as – we've taken a small provision in relation to 166. It's in our litigation and conduct notes, so you can see that. But over the year, we had sort of our conduct charges of about £400 million made up of a number of smaller items. And that was obviously offset by and the PPI release.

And we were pleased that we've made our assessment with the official receiver as well so that's good to get that cleared up. And we're not – certainly not building up any loan provision in terms of bounce back lending. Despite that being old-fashioned accounting and in terms of being able to do that, it's not something that we feel that we have the need to do. So, that's that. But can't really find the detail on the litigation piece.

Alison Rose: Yes. And then on the bounce back loans, we're working very closely. One of the things I've talked about before is making sure that there are common protocols and standards so those customers who've been delivered this scheme in a very digital way have a very consistent way in how we run the collection process.

So, we've been working very closely with U.K. Finance and the Treasury team on recoveries protocols for those consistent customer treatments as we go forward. And that's our approach. Thank you.

Howard Davies: I think we're going to have to wind up fairly soon as we press on – I don't know if perhaps we could fit one more in.

Operator: Of course. Our next question is from Aman Rakkar from Barclays. Please go ahead.

Aman Rakkar: Good morning, Alison. Good morning, Katie. Good morning, Howard. Just one from me actually.

Just around – obviously the excess deposit formation that you're seeing in the system on the household side, so you are seeing pretty material growth in current accounts. Savings. It looks like it's probably going to balloon in the first half of this year given the lockdown. So, I was just wondering, I mean, how are you thinking about managing this? Are you ascribing much liquidity value to this?

Is there a chance for you to detune pockets of funding? Is there anything you can do on the hedge in terms of deploying additional balances? I mean, how are you thinking about this or are you having to look through it because of the uncertainty?

Katie Murray: So, look, it's a great question. I mean, and you might recall that when we spoke around Q2 and Q3, what we had sort of said there was that we were probably taking a bit of a cautious approach in terms of building that into the hedge just because we didn't really know then as to how that was. But I would say we're kind of managing it on a much more business as usual way now.

What we can see is there's huge saving build up. And I think the saving rate is 17 percent, whereas normally, you defer at 5 percent across the U.K. So, some big numbers there.

We think it will take quite some time to unwind and actually they are more than likely just kind of flow around the economy rather than necessarily leave it in any short order. There's some liquidity value ascribed to it certainly. So, I'm pleased to be getting and seeing the strength of the deposit growth within there. We have sought to manage rates down.

And you'll see a slight fall in the retail rate to 10 basis points of funding. That will come down a little bit more as we move into Q1 as well as some of the rate reductions to take effect. Thanks, Aman.

Alison Rose: Great. Well, thank you very much, everyone, for your questions. I appreciate your time today. Thank you very much.

Katie Murray: Take care. Thanks. Bye-bye

END