NatWest Group plc
H1 Results 2021 2020 - Analyst Call

This transcript includes certain statements regarding our assumptions, projections, expectations, intentions or beliefs about future events. These statements constitute "forward-looking statements" for purposes of the Private Securities Litigation Reform Act of 1995. We caution that these statements may and often do vary materially from actual results. Accordingly, we cannot assure you that actual results will not differ materially from those expressed or implied by the forward-looking statements. You should read the section entitled "Forward-Looking Statements" in our H1 announcement published on 30th July 2021.

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 up for questions.

Alison Rose: Good morning and thank you for joining us today. As usual, I'll start with an update on our strategic priorities before handing over to Katie to take us through the first half results. We'll then take your questions.

So, starting with the headlines, we're reporting operating profit of 2.5 billion, compared to a loss of £0.8 billion in the first half last year. This includes an impairment release of £707 million as a result of an improvement in underlying credit metrics.

Most of this release was made in the second quarter when we updated our economic assumptions in light of a more favorable economic outlook, and this results in an attributable profit of £1.8 billion.

We continue to make good progress against our targets. Net lending grew 2.8 percent on an annualised basis driven by growth in mortgage lending. We reduced costs by 5.9 percent year-on-year. So, naturally, our progress here will not be linear and we continue to target a reduction rate of about 4 percent per annum over the next three years. As you know, this is a capital-generative business, and we're reporting a CET1 ratio of 18.2 percent.

This capitals strength has enabled us to announce an interim dividend of three pence today, and to increase the minimum annual distribution over the next three years from £800 million to a £1 billion.

We're also announcing an initial on-market share buyback of up to 750 million in addition to the 1.1 billion directed buyback of almost 5 percent of our share capital from the government earlier this year.

This brings total distributions for 2021 to about £2.9 billion. And you will have also seen the announcement last week that the government intends to sell part of their shareholding over the 12 months from August onwards.

So, those are the headlines and I'll now move on to our strategic priorities on Slide 4. Against the background of an ongoing pandemic, placing purpose at the heart of our business with our commitment to helping people, families, and businesses to thrive remains of paramount importance.

We continue to execute on our strategic priorities, invest for growth, and accelerate our digital transformation in order to drive shareholder returns and deliver on our targets over the next three years.

So, let me tell you how we're putting purpose into practice. I'll start on Slide 5 with our three focus areas: removing barriers to enterprise, building financial capability, and leading on climate change.

During the first half, we published a report on what small and medium-sized businesses need to build back after the pandemic and contribute to economic recovery. This research found the largest drivers of future economic growth includes supporting more scale-ups, boosting female entrepreneurship, and achieving representative workforce participation.

We have re-launched our enterprise program to reflect these priorities and committed £6 billion pounds to support SMEs to scale up and grow with two thirds of this allocated outside of London. Our enterprise program has already supported 35,000 entrepreneurs this year, including more than 700 individuals on our current accelerator program, of which, 42 percent are female.

We also continue to help customers strengthen their economic resilience with measures such as free financial health checks, financial education programs, and help in starting to save for the first time.

In addition to supporting the recovery of SMEs and entrepreneurs, we're also helping young people whose lives have been badly disrupted by the pandemic. In June, we launched CareerSense, a service aimed at improving employability prospects for 13 to 24-year-olds.

And on climate change, the need to act is now well-recognised by investors. Our focus remains on financing and supporting our customers' transition to a low-carbon economy. During the year, we helped business customers raised

£9.5 billion of new sustainable funding and financing, which means we have now exceeded our £20 billion target.

We've also announced the collaboration with Microsoft aimed at helping U.K. businesses create plans to reduce their carbon emissions. And we're working with Octopus Energy on a scheme that helps our customers' transition to electric vehicles. And we have partnered with experts in carbon tracking so that customers can measure emissions associated with their spending via the NatWest banking app.

Turning now to Slide 6, I'd like to talk about how we're working with our customers as the economy starts to recover. Across our retail and commercial businesses, net lending grew by £4.1 billion during the first half, excluding government lending schemes.

With the gradual lifting of restrictions over the past three months, both debit and credit card spending has returned to pre-COVID-19 levels. And whilst credit card balances have declined slightly, that trend started to reverse in the second quarter.

Growth in mortgage lending in Retail Banking grew to £9.7 billion, with net lending growth of £3.2 billion. We are seeing some reduction in margins in a competitive marketplace, and Katie will cover this in more detail later.

In commercial banking, demand for new lending from businesses has been muted, given high levels of liquidity and significant government support. Revolving credit facility utilisation is now around 20 percent compared to a peak of 40 percent in April last year.

And looking at the government lending schemes, we approved lending of some £14 billion in 2020, of which, around 60 percent was Bounce Back Loans to small businesses, 30 percent with CBILS for medium-sized businesses, and the balance was to large corporates.

Since the first anniversary of the schemes when repayments started, 5 percent of all our Bounce Back Loans have been repaid in full, and of customers due to start repayments, 92 percent are now repaying on or ahead of schedule.

As you know, the government introduced Pay As You Grow in April, which enables businesses with these loans to request an extension or take a repayment holiday. Just 5 percent of our Bounce Back Loan customers have asked for a payment holiday through this scheme.

In addition to supporting our customers through the pandemic, we also focused on delivering growth by serving them at key stages throughout their lives whether it's borrowing to buy a house or saving for retirement.

You will see on Slide 7 that while our share of current accounts in retail banking remains stable at about 16 percent, we are gradually growing our stock share of mortgages. This is now 11 percent compared to 10.9 percent at the full year and 10.6 percent this time last year.

I told you in February how we are transforming customer journeys to drive growth, improve efficiency, and reduce costs. And a good example of this is the much improved online process for renewing mortgages that can take as little as 10 minutes compared to anywhere up to three weeks when it was done manually.

In Private Banking, we have brought together our wealth management businesses to make better use of our asset management expertise so that we can support the saving and investment needs of customers more effectively right across the group.

Assets under management and administration grew by over 8 percent or £2.6 billion during the first half to £34.7 billion. £1.4 billion of this increase was net new inflows, of which, about 30 percent were via our digital platforms.

These platforms give customers online access to a range of funds managed by the investment team in Private Banking. Digital inflows were more than double the level in the first half last year, which is testament to our ongoing digital transformation.

Turning to Commercial Banking and NatWest Markets on Slide 8. We continue to be the largest supporter of businesses in the U.K. with a leading

net promoter score. Lending and commercial banking has decreased since the year-end as customers continue to deleverage and revolving credit facilities are paid down.

As I said earlier, we have made a significant commitment to supporting small and medium-sized businesses as the economy recovers since they drive almost half of U.K. turnover and employ over 40 percent of the private sector workforce.

We're also providing more services for our commercial customers by investing in technology-led innovation and products. Our merchant acquiring platform Tyl and online payment service Payit are valuable additions for these customers. Tyl has processed over £1 billion worth of transactions since its launch. And we have carried out half a million transactions via Payit since customers started using it in August last year.

We're also extending online offerings such as Rapid Cash, which enables businesses to borrow against unpaid invoices, and Path, which is a one-stop-shop for HR and compliance. Both of these have offered a lifeline during the pandemic.

In NatWest Markets, the transformation into a simpler, less capital-intensive business is progressing well as we reshape it to focus on corporate and institutional customers in areas such as interest rate risk management, foreign exchange, and capital markets.

Our performance in NatWest Markets compared to the first half last year reflects lower levels of market volatility. Similar to others, we experienced lower fixed income activity whilst our currencies and capital markets businesses are performing broadly in line with expectations.

We remain comfortable with income growing to between £800 million and £1 billion over the medium term. And as our capital restructuring is almost complete, the business is now focused on growth.

We have recently established a dedicated climate in ESG capital markets team and continue to leverage our leading position in sustainable financing. As I

mentioned earlier, during the first half, we delivered £9.5 billion of climate funding and financing, bringing the total amount issued to £21.5 billion. So, we have both accelerated and exceeded our £20 billion target. We also increased our global share in managing green, social and sustainability bond underwriting to 3.8 percent, making us the fourth largest bookrunner in Europe.

I want to turn now to our ongoing digital transformation. You can see on Slide 9 how digital adoption has continued to accelerate whilst branch transactions have reduced by almost a third year-on-year.

Sixty percent of our retail customers now use only digital means to interact with us. This means people are able to access our services at any time of day from any place they want, making their lives easier and more convenient.

Use of our chatbot Cora is now well-established with 44 percent of these interactions completed without human intervention. And video banking accounted for an average of almost 12,000 interactions a week during the first half, enabling us to deliver personalised customer service efficiently without customers needing to travel.

I told you in February that we are investing £3 billion over the next three years to support both our income growth and cost reduction initiatives. Eighty percent of this investment is in digital and technology programs. And this includes the digitisation of key customer journeys.

I mentioned mortgage applications earlier. In addition, we are working on credit applications in our retail and commercial businesses in order to increase speed and ease of delivery whilst reducing costs.

I'll turn now to capital management on Slide 10. As you know, we have made strategic choices in relation to both Ulster Bank and NatWest Markets. We've made good progress on Ulster Bank and has now signed a binding agreement with Allied Irish Banks to transfer £4.2 billion of performing commercial loans along with colleagues supporting these loans.

We also announced last week a non-binding memorandum of understanding with Permanent TSB for the sale of £7.6 billion performing retail and SME loans as well as the transfer of associated employees and branches. If completed, these two transactions will account for about 60 percent of the Ulster Bank loan book.

Katie will talk more about the impact of this later, but we expect this to be capital-accretive over the multiyear withdrawal process. In NatWest Markets, RWAs now stand at £24.4 billion on a pro forma basis as we updated our model due to the end of LIBOR.

And we remain on track to achieve the majority of our targeted RWA reduction to about £20 billion by the end of the year. As you'd expect, we are also managing our portfolio to reduce capital consumption and manage risk.

And in Commercial Banking, this contributed to an £800 million reduction in RWAs during the first half. We're also actively managing our non-equity capital, and re-purchased or called £2.4 billion of tier 1 and tier 2 securities to optimise our capital stack and reduce interest payments.

Turning to Slide 11, our strong capital ratio, which is well above our target ratio of 13 to 14 percent, gives us scope to return excess capital to shareholders as well as to invest in the business for growth.

As you know, in February, we committed to a payout ratio of 40 percent for ordinary dividends and distributions of at least £800 million in 2021, 2022, and 2023. In March, we announced a 1.1 billion directed buyback of almost 5 percent of our share capital, the maximum amount possible in any given year.

Today, we are announcing an interim dividend of three pence and have revised our minimum annual distribution from £800 million to £1 billion. We're also announcing an initial on-market share buyback of up to 750 million.

And this brings total distributions for 2021 to a minimum of £2.9 billion. Katie will take you through a more detailed breakdown of how we plan to

reach our target CET1 ratio by 2023. And so, with that, I'll hand over to Katie to take you through our financial performance.

Katie Murray: Thank you, Alison, and good morning, everyone. I will start with the group income statement for the second quarter, taking the first quarter as a comparator. Total income was stable at £2.7 billion. Within this, net interest income was up 2.8 percent to £2 billion, and non-interest income was down 7 percent to £675 million.

Operating expenses fell 6 percent to £1.7 billion, driven by ongoing cost reduction and a legacy conduct release. This means we are reporting an operating profit before impairments of £954 million, up 13 percent on the first quarter.

The net impairment release of £605 million represents 66 basis points of gross customer loans, and compares the release of £102 million or 11 basis points in the first quarter. This reflects an update on our economic assumptions and improvements in underlying credit metrics.

Taking all of this together, we reported operating profit before tax of £1.6 billion for the second quarter. Attributable profit to ordinary shareholders was £1.2 billion, equivalent to a return on tangible equity of 15.6 percent.

I'll move on now to net interest income on Slide 14. Banking net interest income for the second quarter was £43 million higher than the first. This includes a one-off £32 million adjustment on certain releases relating to the change in corporation tax rates with an offset through the tax charge. Excluding this, banking net interest income is £11 million higher due to continued, strong mortgage growth, partly offset by lower commercial balances.

Turning to bank net interest margin, this reduced three basis points to 161 basis points. Higher liquidity levels resulted in a four basis point reduction. The lower yield curve accounted for one basis point decrease due to the structural hedge.

And there was a negative impact of one basis point from mix in pricing as stronger mortgage margins were offset by lower unsecured and commercial balances. These deductions were partially offset by the one-off tax adjustments, which added three basis points.

We also show our bank net interest margin adjusted for the liquid asset buffer, which accounted for £163 billion or 1/3 of banking average interest earning assets in Q2. This increased by one basis points in the quarter to 240 basis points, reflecting the one-off tax adjustments I just mentioned, partially offset by the lower yield curve and mix in pricing changes.

Turning to the drivers of net interest margin on Slide 15. On the asset or lending side, gross yield for the group fell by three basis points to 181, reflecting strong growth in lower yielding liquid assets.

Retail Banking loan yields saw ongoing pressure due to lower unsecured balances while Commercial Banking yields were broadly stable, excluding the one-off lease adjustments. On the liability or deposit side, group funding costs were broadly in line with Q1 at 30 basis points with a further small reduction in retail deposit costs to six basis points.

There are three main factors to consider in relation to net interest margin for the second half. First, a change in liquidity, which as you know, affects interest earning assets and therefore bank NIM.

Second, the yield curve, we continue to expect a reduction in hedge income of around £250 million compared to 2020, of which £157 million was in the first half. Taking into account the current yield curve and anticipated size of the hedge, we expect the impact from the hedge to be broadly neutral in Q3 and Q4 compared to Q2.

The third factor is mix in pricing. In the second quarter, mortgage margins on the front book decreased from 181 to 165 basis points. This is broadly in line with the back book, which improved four basis points to 163.

Average application margins in the second quarter were 152 basis points, below the back book, and they continued to reduce towards the end of the quarter to around 145 basis points, reflecting increased competition.

Mix is also affected by demand for higher margin, unsecured, and corporate lending, which will ultimately depend on the shape of the economic recovery. Finally, I'd like to remind you of the one-off, which will not repeat the next quarter.

Moving on now to look at volumes on Slide 16. Gross banking loans increased to £4.3 billion or 1.2 percent in the quarter to £361 billion. This includes £1 billion growth in our U.K. and our RBSI, Retail and Commercial businesses, excluding government schemes.

U.K. mortgage growth of £3.6 billion or 2 percent reflects continued strong demand in the U.K. ahead of changes in stamp duty at the end of June. Gross new lending was £9.7 billion, up from £9.6 billion in Q1. U.K. unsecured balances declined in the quarter. However, we were pleased to see growth in our credit card balances of £100 million or 3 percent in the quarter.

In Commercial Banking, gross customer loans fell by £3.4 billion as customers started to repay government schemes, which accounted for £400 million. We repaid £1.2 billion on revolving credit facilities and made further net repayments of GBP1.8 billion. Average interest earning banking assets grew by £14 billion or 3 percent to £494 billion, driven by the larger liquidity buffer funded by deposit inflows.

I'd like to turn now to non-interest income on Slide 17. Non-interest income, excluding notable items, was down 7 percent on the first quarter to £688 million. Within this, income from trading and other activities decreased 29 percent to £167 million. This reflects a weaker performance in fixed income in NatWest Markets, which was impacted by our reshaping of the business, alongside the significant decrease in market volatility experienced last year.

Fees and commissions in the Retail and Commercial businesses increased by £14 million to £484 million. This was driven by higher card and lending fees

as COVID restrictions eased. It also includes a number of non-recurring items in Retail banking, which, together, totaled £12 million.

We expect to see a short-term increase in fees payable from Q3 as we start to migrate the group's retail and business debit cards from our existing provider Visa to MasterCard. This impact will reduce during the second half and into early 2022.

Travel is an important driver of both retail unsecured balance growth and fees. And the outlook remains uncertain given the ongoing restrictions due to COVID-19 across Europe. So, to round off my comments on income, while we do not expect NatWest Markets' income to be in the range of £800 to £1 billion this year, we remain confident of this over the medium term.

We are targeting lending growth across our retail and commercial businesses. And together with fees and commissions, this is dependent on consumer and corporate activity. And finally, you do need to bear in mind the impact of the structural hedge.

I will move on now to look at costs on Slide 18. Other expenses, excluding operating lease depreciation and the direct cost base of Ulster were £1.4 billion for the second quarter. That's £113 million or 7 percent lower than the second quarter of last year.

This takes our year-to-date savings to 5.9 percent ahead of our guidance. However, as Alison said earlier, these cost reductions will not be linear. We expect higher investment spend in the second half as COVID impacts moderate, so you should not extrapolate this run rate.

We continue to expect to deliver savings of around 4 percent for the full year. Strategic costs in Q2 were £172 million and we continue to expect these to be around £800 million for the full year.

Turning now to impairments on Slide 19. We're reporting a second quarter net impairment release of £605 million or 66 basis points of gross customer loans, bringing the overall release to £707 million for the first half.

The Q2 release was driven by an update to our economic assumptions, improved underlying risk metrics in our performing book, and a continued lower level of default. Our updated assumptions reflect a more favorable economic outlook.

Our base case now assumes U.K. GDP growth of 7.3 percent in 2021, up from 4.5 percent previously, and for U.K. unemployment to peak at 5.5 percent, down from 7 percent. You will also see we have adjusted the probability weighting of our four scenarios and reduced our weighting for the two downside scenarios.

Nevertheless, the outlook remains uncertain, and we are mindful of the significant government support that our customers still receive. Given the net release of £707 million in the first half, we now expect a net release for the full year.

There are three key variables affecting the full year outcome. First, economic performance versus the weighted economic outlook we use in our scenarios. As you know, we update these each half so the consensus economic outlook as we get towards the end of the year will be critical.

Secondly, credit performance. While we see a low level of defaults and no tall trees at the moment, we will monitor credit conditions carefully as COVID support continues to roll off. And third, our post model adjustments, which I'll come on to.

Turning now to expected credit loss on Slide 20. Our ECL provision at the end of Q2 was £4.9 billion, down from £5.8 billion at Q1. This reduction was driven mainly by an improvement in both our economic scenarios and the risk metrics in our performing book, which together accounted for a release of £648 million.

Comparing the first quarter column on the left of the bridge with the second quarter column on the right, you can see we have reduced post model adjustments for economic uncertainty by £53 million to £834 million. The ECL release has reduced our ECL coverage from 1.56 percent at Q1 to 1.31 percent at Q2, and we are comfortable with this level of coverage.

I'm not going to walk through all the moving parts, but I would like to highlight that our PMA for economic uncertainty is now a larger proportion of our overall ECL coverage accounting for 22 basis points.

And the remaining coverage of 109 basis points is broadly in line with 2019 levels, which feels reasonable. We do not see any particular issues in the book at this time and are comfortable with how it is performing.

As we look to potentially unwind these post model adjustments, the major factor will be how the economy and our customers react to the ending of government support. But as long as economic and credit conditions continue to trend favorably, there could be some upside later this year and into 2022.

Turning now to look at the progress on Ulster Bank on Slide 21. As Alison said earlier, we now have a binding agreement with AIB for the sale of €4.2 billion of commercial loans and have announced a nonbinding memorandum of understanding with Permanent TSB for the sale of 7.6 billion of retail and SME loans.

We do not expect the AIB deal to complete this year and the transfer is expected to take place in phases through 2022. And for Permanent TSB, we hope to reach terms before the end of the year, however, completion is likely to be in 12 to 18 months later.

As you would expect, the reduction of the cost base will lag that of the balance sheet and we will provide some more guidance on the costs associated with exits at our full year results. As transactions complete, we will look to start dividend payments back to the group.

Turning now to look at capital and risk-weighted assets on Slide 22. We ended the quarter with a common equity Tier 1 ratio of 18.2 percent on a transitional basis under IFRS 9 in line with the first quarter.

This ratio fully reflects the updated dividend accrual, the £750 million buyback, and the linked pension contribution of £238 million pounds pre-tax, which together reduced the ratio by 75 basis points.

This reduction was offset by a 41 basis point increase from attributable profits net of changes to deferred tax and IFRS 9 transitional relief, 19 basis points benefit due to lower RWAs and a further 9 basis points from a lower prudential valuation adjustments following the reduction in expected disposal losses.

Our IFRS 9 transitional relief reduced by 27 basis points in the quarter to 73 basis points. This reflects the release of Stage 1 and Stage 2 expected credit loss, which would previously have been added back to our capital position.

As a result, the significant impairment release in the quarter had negligible impact on our CET1 ratio. RWAs decreased £1.7 billion in the quarter to £163 billion. Within this, a reduction for credit risk of £2.6 billion was driven by lower commercial and unsecured retail balances and a benefit of £400 million from procyclicality.

Market risk increased by £900 million, reflecting a temporary elevation of £2.5 billion following an announcement at the end of sterling LIBOR in March. A model update was received in July, which reverses this uplift to give pro forma RWA of £160 billion.

Moving on now to the drivers of CET1 on Slide 23. I want to set out the factors to consider as we transition to our 2023 targets of 13 percent to 14 percent. These impacts are all indicative based on our capital position at Q2.

Starting with regulation, based on what we know today, we expect this to consume around 350 basis points. This includes the unwind of COVID-related measures such as IFRS 9 transitional relief as well as RWA inflation, including Basel III.

We have said before that we expect PRA changes to increase our mortgage risk weights to around 15 percent on January 1st. Based on current book size and risk density, we expect our mortgage RWAs to increase by around £15 billion.

Taking into account these factors and the improved economic outlook, we now expect overall RWAs to be at or below the range of 185 to 195 at the end of 2021, including all regulatory impacts effective on January 1, 2022.

Of course, we expect to generate capital through to 2023 both through earnings and through our reshaping of NatWest Markets and withdrawal from the Republic of Ireland. We will also consume capital by our loan growth and through procyclicality, which to-date has been positive, and the timing and quantum of this remains uncertain.

And finally, distributions, these are a key priority and we intend to distribute a minimum of £1 billion per annum through dividends, which would consume around 155 basis points of capital through to 2023.

The buyback we announced today is fully included in our 18.2 percent ratio. Where we have the opportunity to do further direct buybacks in 2022 and 2023 in line with the one we completed in March, this would consume around 140 basis points of capital. And we would also have flexibility to do further on-market buybacks. You will find more details of these (inaudible) in our appendix.

Turning to my final slide, which shows the strength of our balance sheet. Our CET1 ratio is now between 420 and 520 basis points, above our 13 to 14 percent target range. This has more than doubled our maximum distributable amounts.

Our U.K. leverage ratio of 6.2 percent is 295 basis points above the Bank of England's minimum requirements. This follows the repurchase of £2.4 billion of Tier 1 and Tier 2 securities that Alison mentioned earlier.

We were also in a position this month to call one of our most expensive AT1 following successful sterling and dollar AT1 issuances during the first half. Given favorable FX, this will generate an eight basis point CET1 increase in Q3 and results in significantly lower coupon payments going forward.

We have also maintained strong liquidity levels with high-quality liquid asset pool and stable diverse funding base. Our liquidity coverage increased in the

quarter to 164 percent due to deposit inflows, and headroom above our minimum requirements is now £75 billion.

So, to conclude, we have continued to deliver a strong operating performance in the second quarter with good lending growth and ongoing progress on both cost reduction and capital optimisation. And with that, I'll hand back to Alison.

Alison Rose: Thank you, Katie. So, in summary, we have delivered an operating profit of £2.5 billion, which includes an impairment release of £707 million as we revise our assumptions in light of a more favourable economic outlook, though we do maintain a conservative approach as government support schemes wind down and the economy recovers.

We continue to support customers to execute our strategy and to invest in the acceleration of our digital transformation. We have made good headway on our phased withdrawal from the Republic of Ireland and expect to largely complete the refocusing of NatWest Markets this year. We're also making good progress on our three-year targets and continue to work towards the CET1 ratio of 13 to 14 percent, and return on tangible equity of 9 to 10 percent by 2023.

And finally, we're pleased to report that we're increasing our annual distributions to £1 billion a year in 2021, 2022, and 2023, and have announced today an interim dividend of three pence as well as an initial share buyback of up to £750 million. In total, this brings total distributions for 2021 to about £2.9 billion.

Thank you very much and we'll now open it up for questions.

Operator: Thank you. And, ladies and gentlemen, if you would like to ask a question, please press the star key followed by the digit 1 on your telephone keypad. We'll pause for a moment to give everyone an opportunity to signal for questions. And we'll take our first question from Andrew Coombs at Citi. Please go ahead. Your line is now open.

Andrew Coombs: Probably two, one just on the interim margin trajectory, in particular, the increase in liquid assets. Obviously, if you strip out the one-off item – one-off the benefits from the lease pricing change, it does look like you exit the quarter somewhat lower than consensus expected.

That's largely due to this impact on the liquid assets. So, perhaps you could just explain what the outlook is for the liquid asset buffer from here, what do you think the impact on the interest margin might be from that into the second half and beyond? That'd be the first question.

The second one is just trying to understand the dynamics around the capital return. You've announced an ordinary buyback. I'm sure they'll be welcomed. But in the past when you've talked about that your concern has been what that means for the government state given that they can't necessarily participate. So, should we assume that if you are doing an ordinary buyback, it comes alongside and other government placing in order to maintain their stake at the existing level or potentially even lower?

Alison Rose: OK, thank you. Katie, can I …

Katie Murray: Yes, sure, thanks. Good morning. Good morning, Andrew. And I missed the very beginning of your questions so if I don't catch all of it, don't hesitate to kind of jump back in. But if we look at the increase in the liquid assets, whenever we think of NIM going forward, there are always three things, the change in liquidity, what we would say is that affects the average interesting earning assets and therefore the bank NIM.

What we saw this year – this quarter was our growth in deposits of £14 billion. What we would know is that feels like it's slowing a little bit. It's down from the £22 billion in the previous quarter as things get back to normal. So, I think we'll leave you to think about how that might behave as we go into this next quarter.

You can see that we've also just shown you today what the NIM is ex – that – the impact of the liquid assets, which I think is quite helpful just on the bottom of that NIM slide, and you can see that it's more stable. It does benefit, as you

see, from the one-offs actually that it's in there, but it shows that it's a much more kind of stable number.

In terms of the dynamics around the capital return, so £750 million in-market buyback, you will have seen last week that the government also announced that they were doing an in-market sell down.

So, naturally, we'll end up scooping up a little bit of their stock as well as other stock that we – that we pick up in terms of that piece. So, it's not – it's not significant. And – but I think it's very difficult to say what the impact of that will be on the government stock in terms of you don't have (inaudible). What we will do is anything that we buy that we will cancel as a treasury share. So, it's therefore obviously beneficial to our share count and also our ROE in there. Thank you, Andrew.

Operator: Thank you. And your next question comes from the line of Omar Keenan from Credit Suisse. Please go ahead. Your line is now open.

Omar Keenan: Good morning. Thank you very much for taking my questions. I've got two, please, one on mortgages and one on NatWest Markets. So, firstly, on mortgages, mortgage margin was up four basis points in the quarter to 163. I was just wondering whether you could give a little bit more color as to where application margins are presently versus the last time that you disclosed them.

And just related to that, I was wondering whether you can – you think you can continue to take market share on increasing high retention – increasing retention without putting on the price lever further.

And my second question on NatWest Markets, so I've noted that you are keeping the medium-term revenue guidance of £800 million to £1 billion. But if I look at FIC revenues in the first half, it was about £60 million adjusted to the LME exercise. So, I'm just wondering whether the £120 million is just annualising (inaudible) the normalised run rate or whether when you say that the fact that FIC has been impacted by reshaping the business means that the other one-off losses in there, just hoping that you can help us think about what the normalised FIC number might be. Thank you.

Alison Rose: Thank you. Well, why don't I talk about NatWest Markets and Katie will come back to the mortgage business? So, on NatWest Markets, obviously, we are reshaping that business to make it simpler and more aligned.

And I think we're very comfortable with the progress that the team are making there, very significant progress in reshaping it. In relation to – largely, the capital reshaping will be done by the end of this year and the business is now positioned for growth.

Specifically, on the rates business, clearly, what you've seen is that business has been reshaping. We've taken around 14 billion of RWAs out of that business as we expected. But obviously, it's been a weaker quarter across the fixed income markets, particularly also given the exceptional levels of activity generated last year.

So, I think it's a combination of the reshaping and the lower volatility from last year. But overall, I think our guidance on the £0.8 billion to £1 billion remains comfortable. So, I think it's just that then I would – that I would point you to. Katie, mortgages?

Katie Murray: Yes, absolutely. So, in terms of mortgages, and, Omar, I'll just make sure we've got all the numbers, so we're all aligned. So, completion for the quarter came down to 165 basis points, broadly in line with the shape of the back book to kind of 163.

When I look at the second quarter, the average application was 152. I think what's important is we'll look at and see what was happening towards the end of the quarter, where it was at 145, reflecting the increased competition in the market.

And for the rest of the year, I think mortgage margins will depend on competition pressure and we note the recent step up in this pressure. I have to say, today, we don't really see anything that that's going to slow in the – in the near term.

So, I would remind you that our goal is to maintain above market growth each year and we aim to make sure that we balance growth with risk discipline as well as strong mortgage management.

We're very focused on retention. As you say, it's sitting at about 80 percent, so very pleased on that. We don't seek to lead on price particularly, and our goal is very much around creating a sustainable value as we move forward from (inaudible). Pleased to see stock share grow from 10.9 percent up to – up to 11 percent in this quarter. Thanks, Alison. Thank you, Omar.

Omar Keenan: Thank you.

Operator: Thank you. And your next question comes from the line of Chris Cant at Autonomous. Please go ahead. Your line is now open.

Chris Cant: Good morning, both. Thank you for taking my questions. I just want to talk a little more around mortgages, if that's OK, just a point of clarification. So, you've said the back book margin is 163 basis points. I think that's inclusive of your SVR book. So, could you just either give us the sort of ex-SVR book numbers so we can compare apples to apples with that application margin or give us sort of the spread on the SVR and the size of that book and we can back it out ourselves? That would just be helpful to understand the dynamic there.

And then on Ulster, what do you think you're going to be able to do with the rump of loans that you've got left there? It's a lot of tracker business, is my understanding. So, you're expecting to do some kind of securitisation with that, sell it to a credit fund? What do you expect to do with that book? Just wondering whether we need to think about that as being like a non-core item running off over a very protracted period of time. Thank you.

Alison Rose: Thanks, Chris. And, well, let me – let me talk about Ulster. So, with the two transactions that we've announced, the AIB and the PTSB, as you rightly say, that's around 60 percent of the book.

In terms of the other assets, our plan remains to be a phased withdrawal from the market. I think I did mention sort of earlier in the year that we had a

number of parties that were interested in a number of assets across our book, of which the tracker business is attractive.

So, we will continue to explore all options in relation to that book. Clearly, with the two transactions, the binding agreement with AIB and the memorandum of understanding with Permanent TSB, you can see we're looking to accelerate our withdrawal through transactions like that. So, we will consider all options. But I'm comfortable we will be able to do that.

And obviously, as I've confirmed before, we will expect this to be capital ratio-accretive over the period and we'll keep you updated as we continue to develop our plan, but I would assume a phased withdrawal over a number of years. We won't be running a huge rump for a long period. Katie, do you want to pick up the first question?

Katie Murray: Yes, yes, sure, thanks. Good morning, Chris. Good to hear from you. When we look at the SVR rate, it's kind of less than 10 percent of the book. It doesn't – it moves around a little bit in terms of the roll off and the timing of that.

The SVR rate today is 3.64 percent. So, we'll leave you to work out the math, if you don't mind, in terms of how you back that out of the blended group. But it doesn't – it doesn't move a lot, less than 10 percent of the total group. So, hopefully, that helps. Thanks, Chris.

Chris Cant: That helps, thank you.

Operator: Thank you. -And your next question comes from the line of Rohith Chandra-Rajan at Bank of America. -Please go ahead. -Your line is now open.

Rohith Chandra-Rajan: Hi, good morning. I just had a quick one, please, on the capital stack optimisation that you flagged. You've indicated the eight basis points CET1 benefit in Q3 from the AT1 redemption. I was wondering if you could help us think about the earnings impact of the actions you've taken, I guess both net interest income and also AT1 coupons going forward, please.

Alison Rose: Yes, sure. Katie?

Katie Murray: Thanks, Alison. Yes, absolutely. So, if I look at the AT1 number, it reads we have a savings of about £130 million in terms of that coupon. And then it's also just remembering to have a look at the AT1/ prefs which we show as the non-equity holding further down the page. It's going to be sitting at about £250 million in 2022. We've got a little bit of benefit of that coming through this time as well. Thank you.

Rohith Chandra-Rajan: OK.

Katie Murray: Thanks, Rohith.

Operator: And your next question comes from the line of Guy Stebbings at BNP Paribas. Please go ahead. Your line is now open.

Guy Stebbings: Hi, good morning, everyone. Thanks for taking my questions. The first one was on volumes and then second one back on NatWest Markets. So, on volumes, specifically on the commercial book, I'm just wondering how much you view the extent of the headwind from the reduction in Q2 from the government-guaranteed schemes is particularly elevated in the quarter just given the timing of when interest payments came due and whether that should moderate in future quarters, perhaps timing around that.

And then in the other direction, what you're seeing in terms of latest demand trends on the corporate side. And if we net that together, at what point you might expect to see the book grow at again or be flat again in the future.

And then on NatWest Markets, I appreciate the colour that you've given and the medium-term guidance sort of staying on the revenue side. But I just wondered, given the recent performance, whether it's impacted at all your view on what the right size and shape of NatWest Markets should be in terms of long-term risk-weighted assets or costs, any colour there will be very helpful. Thank you.

Alison Rose: Thank you. So, on NatWest Markets, no, it hasn't changed our view. We're executing the strategy. We're a year and a half into the reshaping and we're comfortable with where we are, so the plan remains the same, and we're

comfortable with the guidance that we've given you in terms of the revenue outlook.

On commercial lending and just to pick up on that point, I mean I think what you're seeing is it's really a demand – lack of demand rather than supply in the market at the moment, which, as you say, reflects that extraordinary amounts of liquidities and support that's been put in place from the government schemes. We certainly have capacity and willing to lend within there, but demand remains subdued.

When I think about as we move forward, what are the things that are going to influence that growth, first, it's going to be the degree and speed of the economic recovery and the resultant increasing working capital requirements as businesses come out of lockdown and scale up, and you've heard me talk about our view on a more positive economic recovery.

The second influence is going to be the customer behavior in relation to paying down the current government schemes, and I can certainly give you some more detail on that. And then thirdly, how customers use the Pay As You Grow features in relation to the new government schemes.

If I look at the sort of various different segments, as you know, we support – we're the largest lender to business and we support from micro right the way up to large corporates. If I try and sort of give you of sense of the segmentation, we're seeing sort of growth being more concentrated towards the mid and large end of the customer base with new business growth in our large corporate institutional business, at the moment, largely, being driven by infrastructure and ESG green lending. And our NatWest Markets businesses is sort of doing a lot of business in that space supporting our clients.

In the SME market, I think growth is going to be good for the wider economy and that recovery, and at the very small end, what we call the business banking end, that largely the take up of the Bounce Back Loan lending, that effectively has doubled the business banking books since March last year.

So, I think it would be limited growth in that small end as amortisation more than offsets new business. So, hopefully, that gives you a sort of bit of colour of what we're seeing from that perspective. Thank you.

Guy Stebbings: OK, thanks.

Operator: Thank you. And your next question comes from the line of Jonathan Pierce at Numis. Please go ahead. Your line is now open.

Jonathan Pierce: Good morning, both. I've got a couple of questions that are vaguely related. There's another £12 billion build in deposits in the quarter and £12 billion increase in cash at the central bank as well in the second quarter.

My two questions are, the hedge rescaling opportunity from here because the deposit base keeps getting bigger, given money creation at the Bank of England, one would expect deposits will probably grow again in the second half of the year at least at the aggregate level. So, what's your current thinking on potential for future hedge reshaping over and above what you've already done?

The second question is on your interest rate sensitivity. I mean I guess because the deposit base again is growing, you are now pointing to year one managed margin benefits of £414 million and then presumably, it builds as the actions to take effect on a full year basis into year two and year three.

I mean those numbers are clear to see. Can I just, for my own understanding, get some help on why the managed margin benefit is falling now in year two and year three? Is that because you're benchmarking it against your own expectations for increasing base rate?

And if it is, can you tell us what your expectations are two, three years out on base rate because that managed margin benefit looks huge now particularly in the context of what forward curves are telling us what happened to base rates over that period of time? Thanks very much.

Katie Murray: Yes, sure, thanks, Jonathan. And so, I'll just jump in, Alison, sorry, hurling myself there. So, if I look, first of all, at the deposits, say if deposits remain

flat today, we'd expect a further increase of £15 billion in hedging over the next 12 months, reflecting that higher deposit balances feeding through into 12 months rolling average balance.

I think, Jonathan, I will probably agree with your perspective that there will be a little bit of a further increase. We noted that the 22 from Q1 fell to 14, but you'll see some more come onto that, and that will come through.

If I look at the second piece around the interest rate sensitivity, so there are a couple of things going on there. What we have, obviously, there's – what's going on with the interplay between pass-through assumption as increases – as rate increases and the timing, which will do that. And I probably won't get too drawn on that just know as it's not decisions that we've made and we'd necessarily talk about.

Currently, we expect the base rate to go to [50 basis points in Year 3] compared with zero at [FY'20]. So, that increase over the three years will have an impact in that. The sensitivity is lower in year two and year three compared with year one as you start to see those – some of those rates – those rates coming through. And obviously, just given where we are, that sensitivity is quite heightened as you move forward with those rates coming through, particularly in that first year. So, hopefully, that helps.

Jonathan Pierce: So, sorry, just to clarify, but before you saw the impact of the managed margin from a 25 basis point rate rise increasing in year two versus year one, I assume simply because it took a few months to get the full benefit of that whereas now it's going down, and that is because this is relative to your base case, which has base rates going up already. Is that right?

Katie Murray: Yes, yes, so that would be fair.

Jonathan Pierce: So, really, what we're looking at clean is if there was a 25 basis point rate rise today, the year one impact will be £414 million, but presumably growing to circa £500 million once all of the actions have fully kicked in.

Katie Murray: Yes. So, you would see £414 million come through first – in the first year and then I don't think that the actions would particularly be additive. So, I would

go with what we've got in terms of those managed margin lines as what you'd see coming through in the – in the other year – in the other years.

Jonathan Pierce: OK, great. Thanks very much.

Katie Murray: Thanks, Jonathan.

Operator: Thank you. And your next question comes from the line of Rob Noble at Deutsche Bank. Please go ahead. Your line is now open.

Rob Noble: Good morning, all. Can I just ask again on Ulster? And I know it's early days with PTSB, but how theoretically would the stake in PTSB work? Would you hold it at Ulster level, group level, and how would it be treated from a capital perspective on that base as well? And then secondly, now that Tyl has got a bit more traction, what sort of revenue and profit are you seeing from it and where do you expect it to go to going forward? Thank you.

Alison Rose: Thank you. So, on Tyl, yes, we're really pleased with the progress, and you can see the number of transactions sort of going through. We think this is a product that all of our commercial customers will want and need.

I'm not going to give you revenue forecast specifically on it, but what it does do is increase the product offering and deepen the relationship with our commercial customers and as it continues to scale, we'll give you more updates on that as we go forward.

Katie Murray: Thanks. It's a good question, Rob. And here, we get ourselves a little bit into the technicalities of ring-fencing. So, it's basically an equity holding and so, therefore, you obviously hold it outside of the ring-fence.

We have our entity that sits on the edge – AA holdings where we hold a lot of those things. And so, we'll give you more guidance in terms of capital and things like that when it's there, but it does sit – it sits outside of the ring-fence, so it wouldn't be sitting in Ulster holdings or anything like that.

Rob Noble: Great, thanks very much.

Katie Murray: Thanks very much, Rob.

Operator: Thank you. And your next question comes from the line of John Cronin at Goodbody. Please go ahead. Your line is now open.

John Cronin: Hi, both, and thanks for taking my questions. And the first one is on mortgage margins and getting back to this ambition to grow your share. So, looking at where you mentioned application margins sat at the end of Q2 of 145 basis points and they still seemed to be on a downward trajectory with more rate moves this week by some of your peers.

And just looking to understand what the inflection point might be where you decided actually you're going to hold steady and stop competing for share. How far down – are we talking down to pre-pandemic levels and below or is there some kind of – any kind of quantitative guidance you could give me on that particular question just from a product perspective?

Then secondly, on credit cards, look, I know I've tried this before, but in terms of the breakdown of the spend on a per customer basis and your experience with respect to savings among your customer base, is that increasing nonpayers as it were in terms of increasing the proportion of those who are paying down their balances in full? And is that something that's likely to weigh on growth for some time owing to the savings both through the pandemic?

And then finally, just a short question on RWAs, thank you for the guidance on the hybrid margin models and the fresh guidance on that. Anything to say beyond at this point in terms of potential materiality of Basel III impacts from 2023 and beyond? Thank you.

Alison Rose: Great, thank you. And, Katie, I'm going to give all those to you know.

Katie Murray: No, that's fine. And, John, you've rattled through them quickly, so if I missed anything, jump in at the end and I'll come back to you. So, in terms of the mortgage margins and at what price you would – you would kind of stop, I'll guide to what we shared at the most recent spotlight that we did with Retail and what they talked about and what they shared was our mortgages are kind of earning at the moment over 20 percent.

Now, that's calculated on a book value that's very – that's very similar to where we're writing today. So, it's says about 145 to 150 basis points so, therefore, at that stage, and so importantly, including the mortgage floor add-on. So, we're comfortable at this level that you're earning above 20 percent.

Clearly, with the price competition, you'll see that ROE fall, but at 20 percent-over the 20 percent, you've got some good ground still to cover before you get anywhere close to saying actually, we're not going below that level. So, I wouldn't want to put a number – a number out there on that.

In terms of the credit card spending, what we've seen in this quarter is that we have had a small increase in their credit card levels. From the previous quarter, they've gone up by – just about 0.1, so not a big proportion.

And obviously, our overall balances are 3.6, so 3 percent on that. But what it's showing is that it's – we're starting to see the difference from people paying down completely to actually the balance growing a little bit, which obviously, from our numbers, a little bit of growth in balances is helpful in that from an income and also from a margin level.

If we then think to the RWAs, in terms of – specifically on the Basel side of things, the exact timing of that is relatively on – is relatively uncertain. I think on Slide 31 in our pack, we give you quite a lot of guidance and we sort of say it's less than 90 basis points in terms of what you'd see coming through on that. So, I think once you get a chance, John, if you poke around in that side, you'll see the builds from all of the different impacts of model changes.

John Cronin: OK, thanks. Can I just come back on the first one just in terms of 145 to 150? What kind of product [RoE] that is? It's above 20, but how far above? Is there anything more you can give us on that?

Katie Murray: So, I'd say, John, good try, I'll probably just stick with you with the disclosure we gave at the spotlight of it is just about above 20.

John Cronin: Yes, OK, thanks.

Katie Murray: Thanks, John. Have a good day.

Operator: Thank you. Your next question comes from the line of Alvaro Serrano at Morgan Stanley. Please go ahead. Your line is now open.

Alvaro Serrano: Good morning. Thanks for taking my questions. A very quick one on mortgages. Conscious we've beaten it to death almost. Am I right to think that that 145 basis points of – I think you said at the end of the quarter, that's still above the rates of which the business that's rolling over. I realised you've mentioned the back book but versus the fixed rate business rolling over, it's still above.

And when we think about the next few quarters, given the volumes and given its rolling over above, any reason why we shouldn't see sort of NII sort of growing obviously for the adjustment of the one-off but – put another way, is the commercial sort of banking drag something we should – we should take into account?

And then – and maybe one more medium-term one. I think you said to Jonathan's question that you have 75 basis points rate hike – rate hike expectations for the next three years. I'm trying to remember what you had in your 9 to 10 percent guidance at the beginning of the year for 2023.

And given the margin expectation, it just makes me think that there's upside to that 9 percent to 10 percent. Obviously, rate hikes had to happen and all that, but I just want to compare versus your earlier guidance in the strategy plan at the – at the beginning of the year. Thanks.

Alison Rose: Katie?

Katie Murray: Yes, sure, thanks. Thanks, Alvaro, morning. So, if we look in mortgages in 145, when I – I would kind of compare it more to the back book rather than going specifically in terms of what they're replacing because often, the manner in which they're replacing whether it's two-year or five-year, and actually, it's that total back book number, the 163, what we saw is margins going up that pulled it up. Clearly, as (inaudible) you'll see that kind of coming through.

I think in terms of the – in terms of the NII, it's really around what we are managing to do on volume to offset that. We've got a good track record of managing that so, we'll continue – we'll continue to see that kind of going through in terms of the income.

If I go back to when we talked to the 9 to 10 percent, you might remember, at that point, there was actually a small price decrease, I think, in terms of base cuts at that point. It was 10 basis points down.

So, if the rate rise comes through then it will be helpful, but we're very much market consensus for base rate, and at the moment, our first hike is not priced in in terms of that market consensus until the end of – into the second half of next – of next year. So, a little bit of positive news, that's helpful and then I think in line with just the general positivity we're seeing in the – in the market at the – at the moment.

Alvaro Serrano: So, can I just have a quick follow-up on the management adjustments? Sorry. I think they've gone up to £1.1 billion in the first half. Can I just confirm that's not included in your capital sort of return expectations? I think you still have the IFRS 9 unwind, which de facto means it's not included, but should we believe that some of that could be – could create upside to distribution? Thank you.

Katie Murray: Yes. So, that's – we haven't had any part of the PMA coming through in terms of our commitments today. Those commitments are things that we could all make, assuming that the PMA would be utilised in terms of – to pay for impairments.

And so, if it wasn't then you could see some positivity come through. I'd remind you, we do our dividend or policy based on the attributable income. So, if it's additive to that then that could see some upside.

But remember IFRS 9 unwind, you get a bit more complicated in terms of the capital piece. But I think good news, generally, works its way through to good news on distributions as well.

Alvaro Serrano: Thank you very much.

Katie Murray: Lovely. Thanks, Alvaro.

Operator: Thank you. And your next question comes from the line of Martin Leitgeb at Goldman Sachs. Please go ahead. Your line is now open.

Martin Leitgeb: Yes, good morning and thank you – thank you for taking my questions. Firstly, I would just like to ask on the outlook for volume growth within Retail Banking in the U.K.

And I mean looking at the – looking at the first half, mortgage volumes have been trending significantly higher compared to prior levels – prior year levels. Now is time to do holiday leveling off.

How should we think about the scope for volume growth in the second half? Do you see this as basically, a lot of it being a front loading or do you see some signs of structural strength in the mortgage market with essentially people looking for bigger houses, bigger mortgages, and so forth?

And to follow up on that, I mean a similar question on credit card. I think you launched your first 0 percent balance card recently. I was just wondering if you could shed a bit of light how the take-up has been. And I was just wondering how do you think about the scope for volume growth in credit cards over the near to medium-term?

And fourthly, just a quick follow-up on your earlier comments on Ulster dividend. I remember at the turn of the year, I think Ulster had a tier one ratio of around 28 percent. Have you in the meantime made an application for an upstream of a – of a dividend or is the first one really just to be expected once – I think when the first deal is complete? Thank you.

Alison Rose: Thank you. Katie, do you want to pick up for mortgages? And I'll just touch on the credit card and the new credit card that we launched. We're very happy with that. There's been very strong growth in terms of the launch of that. Our volumes are well above our plans and we're seeing significant growth there. So, that has really appealed to our customers, which we're very happy with. Katie, mortgage volume?

Katie Murray: Yes, sure, absolutely. So, if I – if we look at in terms of the mortgage volume, we are still expecting them to be pretty robust as we move forward from here. And obviously, there's been the spike in June as the final kind of –stamp duty came to an end, but we're comfortable in terms of moving forward.

And you can also see in our economic assumptions that we're also pretty confident about some ongoing house price inflation as well. So, though we've had this kind of peak, we'd expect it to moderate a little bit. They'll still grow in '22, but over the five years, it still is growth from there. So, we do see that still as a – as a positive market moving forward. Alison, I can pick up the Ulster dividend question?

Alison Rose: Yes.

Katie Murray: Yes, perfect. So, if we look at that, so, no, we haven't made any applications. We didn't think that was appropriate as we were doing the strategic review in terms of any capital withdrawal.

And we would – we would expect that as deals complete at that point, we'd start to make applications at that stage and see capital return. What we have done in the past when we've made applications, they've being granted. So, we're not expecting any particular issues on that. But it wasn't – it's something we chose not to do as we were doing the strategic review. Thanks, Martin.

Martin Leitgeb: Very clear. Thank you very much.

Operator: Thank you. And your next question comes from the line of Robin Down at HSBC. Please go ahead. Your line is now open.

Robin Down: Good morning. Can I come back to the commercial loan book? I guess we can all kind of have a guesstimate as to what happens with the non-government guaranteed lending in the second half.

But the government guaranteed lending, I guess, given the product basically closed now, it's obviously going to form potentially (inaudible) the next few

quarters. I just wondered if you could give us just for our modeling purposes some indication of kind of the margins. I'm guessing on Bounce Back Loans that the margin is probably just over 2 percent assuming you've kind of swapped that back into (inaudible) inflation rates. Is that – is that correct? And on the CBILS side, I wonder if you could kind of give us an indication of the margin of that so we can kind of do our models as that rolls off over the next few quarters. Thank you.

Alison Rose: Yes. So, I mean in terms of the Bounce Back Loans, the yield is 2.5 percent. And as you remember, the term is 6 to 10 years. The new Pay As You Grow option allows customers to extend their term. So, that's on Bounce Back.

One CBILS, it's more difficult to give you detail on that because that is specifically set by customer, but obviously, it benefits from the 80 percent guarantee rather than the 100 percent guarantee.

Robin Down: OK. But, so we can't – is it kind of close to the average margin for that division? Would that be a reasonable starting point?

Alison Rose: If you look – maybe if you look on sort of Slide 15 of the deck, that will give you a sort of a sense of the margins and where we're pricing it.

Robin Down: OK.

Operator: Thank you. And your next question …

Katie Murray: Thanks, Robin.

Operator: Apologies. Your next question comes from the line of Aman Rakkar at Barclays. Please go ahead. Your line is now open.

Katie Murray: Hi, Aman.

Aman Rakkar: Good morning, Alison. Good morning, Katie.

Alison Rose: Good morning. Good morning.

Aman Rakkar: My – I guess – I guess most of my questions have been asked. I had two, if I may. Just one on just your expectations for full year income if I might ask Katie given another quarter of performance and I guess another soft print from NatWest Markets. So, I think you talked previously about a touch under 11.1 billion ex-notable items that you printed in 2020. I'd be interested for kind of what your expectations are for that now.

And then secondly, just on RWAs, so, obviously, I note the NatWest Markets RWAs that are temporary that are coming off, so you're starting at £160 billion. I note that you're sticking with the kind of 185 to 195 albeit lower end. I'm just kind of interested in how you actually get there. I know you've got the £15 billion from mortgages. There's a bit more from other regulatory headwinds. So, if you could quantify that, that would be good.

But the – I guess the growth, it doesn't sound like there should be too much kind of organic RWA growth given the commercial books coming off in H2. So, I guess I'm trying to tease out whether there's maybe a bit of positive upside to that RWA guidance.

Alison Rose: Great. Katie, do you want – so we've got – well, we can walk you through the RWAs. Katie, if you want to go through that.

Katie Murray: Yes, sure, absolutely. So, let me take your first question in terms of the full year income guidance. So, we do we do expect income excluding the notable items to be lower in '21 and 2020. I looked back at the first half, it was then £5.3 billion, down from £5.9 billion in 2020.

Two things will be driving that reduction. One is the lower NatWest Markets' income due to the exceptionally strong first half and then secondly – so the strong first half in last year and obviously, the ongoing reshaping of the business.

The second is the impact of the structural hedge, which was £157 million lower and versus H2 '2020. It was offset by strong volume growth in our retail and commercial kind of businesses.

If I look to the second half of the year, for NatWest Markets, we have said we no longer expect the income to be a £800 to £1 billion range for 2021. I'll leave you to think about what the second half might look like – look like.

We are targeting lending growth, though together with fees and commissions, I would say none of that growth ex-retail is very dependent upon our consumer and our corporate activity. And you remember I mentioned there was a small nonrecurring fee in retail banking this quarter as well.

For the hedge, the majority of the year-on-year decline is in the first half, that 157. There's probably another 90 to come through in the second half of the year. If I think of the hedge from the Q3 and Q4 versus the Q2, I wouldn't expect the hedge to be a driver of NIM in the second half.

If I just move on to your RWAs now, so just to be clear, and what we've said is that we expect to be at or below the bottom end of the guided range on the 1st of January 2022. I think there's a number of – a couple of building blocks we should think about there. First, lending growth, we expect to grow above market rates excluding the government schemes. The mix of lending is obviously going to impact the RWAs.

Secondly is procyclicality, which to-date has been incredibly low and, in fact, positive. And I think the timing or even where – the extent to which it comes is still uncertain, but we probably expect a little bit still to come through this year.

And thirdly, of course, regulation, and you've clearly got a number of the numbers, but let me just go through. So, as we said before, we expect the PRA changes to increase our mortgage risk weights to around 15 percent on the 1st of January 2022.

If I look at the book growth to-date and the positive procyclicality to-date that we've seen, we would expect our mortgage RWAs to increase by around £15 billion, equivalent to around 160 basis points of CET1.

We're also expecting some other model changes, introduced on the first of January, including things like the standard approach for counterparty credit risk, that will absorb about 50 basis points.

And so, if I look – taking all of those together, including a remaining NatWest Markets RWA reduction, some of the improved economic outlook, that's where we get to this at or below in terms of the range of 185 to 195. Thanks, Aman.

Aman Rakkar: Thank you so much.

Operator: Thank you.

Katie Murray: Welcome.

Operator: And the last question comes from the line of Fahed Kunwar at Redburn. Please go ahead. Your line is now open.

Fahed Kunwar: Hi there. Thanks for taking the question. Just one question, it was just on Slide 31, excellent slide, thank you for providing that. Just in the Basel III amendments and the great less than 90 bps, can I get a little more sense on the timing of that? I think, obviously, Lloyd's talked about a neutral effect of – on Basel – from Basel III through to 2028. The number is probably a bit higher than I thought it would be.

Just a – just a sense of how you think about that 90 bps impact from '23. And does that mean before 2023, you would look to hold more capital than the 13 percent to 14 percent kind of target range to compensate or to kind of plan for the 90 bps hit that you have from Basel III from '23 onwards? Thank you.

Katie Murray: Thanks, Fahed. So, 13 to 14 percent, it's obviously designed looking forward to all of these things. So, we wouldn't look to hold anything back to cover it. It would be built in to make sure that we could make it.

Look, I do think the timing is uncertain as to the timing and the way that it comes through. We are working on a kind of '23 date at the moment, but I think we'll see how that continues to evolve in terms of that space.

But we're certainly not looking to hold that back and relatively small impact, less than 90 basis points, when it eventually does come in. Thanks, Fahed.

Fahed Kunwar: OK, thank you.

Operator: Thank you. There are no more questions at this time. I'd now like to hand the call back to Alison for any closing comments.

Alison Rose: Thank you very much. Well, thank you so much for joining the call and for your questions. Clearly, a strong and resilient performance for the half year, good progress on our strategy, which is executing well and on track for our targets and continuing investments to accelerate our digital transformation. Thank you very much and we look forward to catching up with you again.

END