2009 Annual Results

ANALYSTS PRESENTATION

held at the offices of the Company

280 Bishopsgate London EC2

on Thursday 25th February 2010.

Presenters

- **Sir Philip Hampton (Chairman)**
- **Stephen Hester (Group Chief Executive)**
- **Bruce Van Saun (Group Finance Director)**

Philip Hampton:

Good morning ladies and gentlemen and thank you for joining us at the RBS Annual Results for 2009.

We are now one year into a five year turnaround plan and I think we've come an awful long way in that short time. The Board is very pleased indeed with the progress that Stephen Hester and his new leadership team are making; and perhaps at this juncture I can actually show that they exist in human form and ask the new Executive Team to stand up and show themselves; so there they are – that's the new team.

In 12 months, both the Board and the Management Team have been completely restructured. We've secured the capital base of the Company and set out the strategy and performance targets that need to be met. Today's results represent real progress towards our goals.
In the coming year, we intend to increasingly show our core strengths as a business in which to invest. We completely understand that the public capital support we have makes us unusually accountable to the public and their political representatives; we respect that in all of our dealings. But it's in all of our shareholders' and customers' interests that RBS is run soundly and commercially.

Arguably no business issue has attracted greater public attention in the last year, than the subject of bankers' pay. We understand the anger and the reason for it. In recognition of this, I think RBS has led the way on reforming our remuneration structures. We secured virtually 100% - 99.96% - shareholder approval for our new bonus deferral scheme in our General Meeting in December; and we're also going to put a new long term incentive scheme to a shareholder vote at our AGM in April.

Uniquely for this year, as part of the accession arrangements to the Asset Protection Scheme, we also require the consent of UKFI - our controlling shareholder - to the 2009 bonus settlement; and I am pleased to confirm that as of yesterday, we received that consent.

The compensation ratio is probably the most meaningful disclosure we can give on staff costs. The settlement means that our compensation ratio at 27% for our GBM business is competitive against our peer group, whilst also recognising some of our particular circumstances.

I understand that there is some interest in whether this ratio is flattered by the impact of deferrals between '08 and '09 and I can confirm - it's in the release anyway - that the net impact of this on the ratio would be to take it to 28%, so it's pretty much *de minimis*.

The Board's decision here has taken into account all the relevant factors, the overall performance of the Group; the particular performance and strong recovery in the core of the GBM business; the market impact of policy support from many Governments and Central Banks, including of course the capital to support RBS and the overall risk position of the bank.

The cost of the bank payroll tax is expected to be £208 million in 2009, with a further £160 million deferred over subsequent years. The Board believes that this settlement represents the minimum necessary to retain and motivate the staff who are critical to RBS's recovery.

We're now going to focus all of our attention on the remaining four years of the turnaround plan. We are both determined and confident that it will succeed and I'll now ask Stephen Hester to take you through the presentation and show you how.

Stephen Hester:
Thank you Philip and good morning everyone. Conventionally I will go through a few of the things about our performance today and our strategy looking forward and then ask Bruce - who makes his debut physically in front of you as opposed to on the telephone - to take you through in some more detail the figures that we have published today. As a number of you have remarked, you have a nice weighty tome of additional disclosure, which we hope will be helpful and points the way to our determination to be transparent and investor friendly.

Starting with a recap of what we think we're saying today, where we think we are, we keep coming back to the three goals we have - serving customers well, restoring the bank to stand alone strength and rebuilding durable shareholder value. An important thing today, I'll talk about it more in a few minutes, is that we are reaffirming the Strategic Plan and the targets we published last Autumn. I know there was some debate about whether we would be able to do that post EU – I'll talk more about that in a few minutes, but we are reaffirming those targets.

We believe that during 2009, that we have either met, or in the vast majority of cases exceeded, every target that we set out for this stage of the plan. The management change decisively happened in the first half of the year and I believe is working well. The riskiest period is behind us, though with lots more to do. We see 2010 as the last foundation year. We are likely to be in overall loss as a Group in 2010, before moving into Group profit in 2011. There are likely to be precious few really splashy indicators of our success in 2010, as we lay the foundations, but they are being laid and I believe successfully so.

Our continuing businesses, the reason we're here, the reason we are worth supporting, the reason we believe that the shares will get past the Government's hurdle rate, we can get the Government off our share register and rebuild value, is in our continuing businesses. They all are market leaders in their markets; their markets are all customer driven, large, enduring; we believe that we can get 15%+ ROEs out of them, even with more equity held, and that they will gel as a group as well as individually.

The journey to that being the story of RBS, of course involves risk reduction, it involves peeling away the things that nearly brought us down; that journey is going well. We are something like 70% of the way through already the balance sheet reduction we have to make overall.
The funding profile has done very, very well – we'll talk more about this during the presentation. We obviously have tail risk protection in APS and we believe, and there are some areas you'll see that our tone is improving today, that impairments are likely to now have peaked.

Not dwelling really on all the stuff that we think we deserve pats on the back for last year, but I think in really summarising it, we were able from a starting point of a £24 billion loss, of a 10p share price, of chaos in our markets and with the bank, we were able to get our arms around the problems. We were able to make sure that the essential source of value, our customer franchises and the people who operate them, remained intact. We set out, I believe, a clear strategy and road map to recovery. We have the tools to do the job, some of them we've given ourselves, some of them have been given to us through a very substantial external support; and we are delivering so far ahead of plan.

You will see increasingly, the way we present our business is trying to help you unpeel the complexity that still will sit with RBS for a little while and allow you increasingly to focus on the investment case, which we believe will become successively clearer. The investment case of course is ultimately all about our core businesses and where we can take them, and I think that we can see that in 2009 we have some reasonably good things to say about the core businesses, but much work left to do. I agree that it's entirely illustrative at this point, but on an illustrative basis, our core businesses would have had a return on equity of 13%, operating earnings per share of 4.9p. What you will also see, is that we are beginning to see the upturn in our Retail and Commercial business; if you think about our business mix, in steady state one-third of our Group will be Investment Banking and two-thirds Retail and Commercial.

The story of 2009, of course, is about Investment Banking for us and everywhere else; but the story for the future years, as Investment Banking earnings come off, will be what momentum can we generate in our Retail and Commercial and at what point does that take over and drive the whole Group forward. In that sense, the beginning of the turn in Retail and Commercial that we saw in the fourth quarter are important indicators for the future. You can see that in net interest margin and you can begin to see that in impairments. The cost programme is also doing its job.

On the rest, away from our core businesses; as I mentioned on the previous slide, the impairment charges appear to have peaked - we think that they will come down slowly - but nevertheless they appear to have peaked absent another severe double-dip. We are making great progress on the loan-to-deposit ratio, both because loans are coming down, but also because deposits are coming up. In fact in our core business it is already at 104%. If you believe we can get rid of non-core, you can see how we get to 100%, actually not far distant from here in core.

I talked about the balance sheet progress; the Core Tier 1 ratio, post the APS and the B-share issuance, is 11%. That's important, because we want that to be able to absorb firstly, another year of loss; secondly, the extra regulatory charges that are coming down the pipe in the coming years, that plus future years retained earnings and leave us in the position where we are adequately capitalised for the future and we believe that to be the case.

A couple of slides on core and I think the essence of the year was for all our core businesses it was a foundation year in terms of our turnaround plan, but of course in performance terms it was a banner year for our investment bank, GBM.

But throughout our business, the customer franchises were sustained and intact. The key thing about GBM - and I'll mention it more on the next slide - is of course all investment banks captured buoyant markets; we were probably middle of the pack in terms of our capturing, but we had a hell of a lot more distractions as GBM was literally halved in its capital intensity and despite that, captured that, which I think gave the lie to many people who were not clear about the strength that we had in that area.

I mentioned our Retail and Commercial; very important for the future; it troughed last year, signs are beginning to be positive of the turn; and throughout the Group cost cutting programmes going to plan.

I won't dwell on this slide at all, you can read it afterwards; it simply provides evidence partly for the customer franchises being intact, in some instances for them growing, despite all the things that could have gone the other way last year. I think it also highlights for you the strength of our natural deposit franchises, an asset many banks don't have, which will be increasingly important to us in the new world of different bank capitalisation and funding.

GBM; perhaps an interesting slide for some people; in the top left here we've gone back to 2007 on the basis that was the last record year for the industry; shown you the GBM results as then reported and then showed you pro forma core GBM. In other words the business lines we are now operating stripped of the ones we have closed down and what that would have been in 2007; then where that went, to 2009. You can see that our profits are £5.7 billion in GBM, like-for-like compared with £1.5 billion in 2007 or with £3.2 billion if you include the businesses that we subsequently closed down. You can see the balance sheet has halved in that period, from £900 to £400 billion, the number of people has come down substantially as well. That's a really important restructuring and of course you can understand why we might be pleased with the results, not complacent, but pleased with the results.

The top right simply shows you where they have been accomplished and in the bottom left of this slide, the balance which of course is not in balance in profit terms - GBM drove our profit last year - but the essential balance of our Group which we believe is appropriate looking forward.

We have long said that last year was an unusual year for investment banking, the first quarter in particular. I think you can see in the last three quarters what we regard as a more normal run rate for our investment bank. Our expectations for 2010 would be more consistent with that, although it's fair to say that January has started above the more normal run rate trend line, but we always hope that Januarys do that.

To say no more in respect of our other businesses, our Retail and Commercial businesses, than last year was a foundation year; they were on their back mostly, as a result of the economy.
Of course, some important exceptions – GTS a terrific business that I think did very well to have a flat year relative to the prior year, our wealth businesses as well, but in general suffering from the economic downturn. Nevertheless, we are seeing the signs – the first signs of recovery - both helped by the economy and by our own efforts. You can see that in the fourth quarter revenue started to come up. You can see for now, two quarters in a row net interest margin had started to recover, driven by asset margins; there are still quite heavy headwinds on the liability side and we see in core impairments plateauing; in non-core they've peaked as we said earlier.
There's not going to be a dramatic renaissance in 2010, but we do think these businesses will improve in 2010 and then that slope of improvement can accelerate once economies and in particular interest rates normalise, and we can get some relief on the liability margin.

That's what I wanted to say about core, about driving the core forward. We think that increasingly we can see what those franchises can do. We can have some more confidence in the projections we've made for them. The management are operating their plan well. We have the unusual benefit, as many banks do, of the investment bank, a performance which we're very grateful for, but we're beginning to see some good things in the rest, which will drive us forward.

A couple of minutes now on the industry and then on the Strategic Plan. I won't take you through these words, you can read them; but obviously one of the crucial strategic issues facing our industry is change in regulation, a change in capital liquidity requirements and all the things that go with it. Generally, we are supportive of the initiatives that are ongoing, but clearly the devil lies in the detail, in particular the calibration exercise for this year and the timetable over which Basel changes will be brought in, which could make a very big difference to banks one way or another and clearly will cause inevitable uncertainty for all of us over the next year as these things ricochet around the international authorities. But we're preparing ourselves for them, we're not opposing them; we're just seeking that the implementation be appropriate with an appropriate period of adjustment.

Just to highlight the two important bites that this thing comes in: the first important bite is the trading book changes which come in at the beginning of 2011. There is still substantial detail to work through to be absolutely sure of the impact. At the moment, in very rough terms, we think it might cost us £60 billion of risk weighted assets; roughly half of that is continuing in core and half of it is in non-core, which obviously will go away subsequently.

Clearly the post 2012 changes, which mostly are about deductions from Core Tier 1 and changing the nature of capital, are far too early to give numbers on; they're speculative in terms of both the timing of implementation and what will actually be implemented. You will see in the 300 or so pages that you've got, disclosure of each of the items on this list; as to what those items are now, you can use your own skills to judge how those items will change over the coming years before they have to be introduced - some will go up, some will go down – and with what pace you think they will be introduced. We'll all be on a bit of a voyage of understanding as we go through this.

The vision for RBS - you've seen it before - I won't again go over it, but we are clear that our core businesses represent a coherent whole, something that can be a strong competitor in every one of its markets that makes sense and balance together both geography by funding a giver and taker, by type of business that the universal banking model is one that can work for us and we feel good about that as a competitive platform, albeit one which we have a lot of work to do upon.

I mentioned our targets; as you will recall we put out some comprehensive targets unusually last summer; we put them out for the Group as a whole and we put them out for each of our Divisions. We've kept all of those and in your papers is the divisional detail, which I don't replicate here. There was a setback; as you know, in the fourth quarter of this last year, with the forced divestitures from the EU, where lots of people worried about the earnings dilution that might hit us as a result of that; and with the Basel changes coming into greater view, the extra equity that banks would have to catch. Again, I know many of you worried about that as an impact on our returns; so I'm pleased to say to you today that we are reaffirming the targets unchanged. In other words, we believe that we can make up for those headwinds of divestitures and regulatory change and still produce the returns that we thought we could last summer.

In the Divisional detail, there's one minor change to the cost/income ratio in our GTS business as a result of the GMS disposal; but in essence our position is unchanged. Of course they are only targets; we might not hit them; there may be lots of things that go wrong, but for the time being we think this is the right thing to aim for and that we have a reasonable chance of getting there. You will also see the progress made on this chart in 2009 on many of the measures.

Let's just turn - having really concentrated on core business and strategy - to risk or the rest. What I'm going to seek to persuade you – not today – I'm going to give you the concept today, but I hope you'll start to believe it over time, is that increasingly we can see the wind down of non-core, the remainder of the risk profile as an NAV adjustor as opposed to a driver of value; something that is catered for in our existing capital structure, together with the retained earnings during the period. As and when you start believing that the risk, indeed, is down to that level, it makes the investment case much easier to deal with. I'm not saying we're there now, but I'm saying we're well along the path to getting there.

So again endless detail in your packs, but put very simply, as I said we're 70% of the way through the balance sheet reduction that we need to do. The liquidity improvement has been tremendous and the main effort now is to increase the Government bond component of our liquidity as opposed to the total liquidity; the funding profile has improved substantially, the counterparty credit risk exposures you've seen coming down. Importantly, in the bottom right here, the REILs, leading indicator of impairments, we believe flattening for the first time in quite a few quarters. If that trend continues that would be supportive of our impairments having peaked belief, but of course one quarter does not create certainty, as we all know.

Not a whole lot to say about the EU disposals; we're very pleased to make a fast start with the most volatile of them, which was the Sempra trading business, where you've seen a little over half of that business go at a reasonable premium to J.P. Morgan. We hope to get merchant acquiring and the UK SME done by the end of this year, and insurance as we always said: because we think we can improve the results substantially, because it doesn't use balance sheet or capital at present, it makes a whole lot of sense to save that disposal or IPO, because it's more likely to be into the outer years and that's our current plan. We have the other constraints upon us, which you are aware of.

Turning into the final strait of my remarks outlook; again, coming back to trying to make a start on helping you to unpeel the investment case - I'll do more on the next slide. We do see our core businesses as increasingly the things to focus on, as the uncertainties elsewhere recede. All our businesses should do better, regardless of economic climate, as we work on them and as our management actions over the next two or three years bite; and that's why we've so aggressively started in terms of management actions, costs efficiency, investment and so on.

In steady state, the two-thirds of our Group that would be Retail and Commercial, is very important in thinking of earnings drivers over the next four years. But nevertheless, even with more capital, even with less favourable markets, we are holding GBM to account, to produce 15%+ ROEs going forward.

In 2010, it's early days and there is uncertainty in the world economy, so we can't get too carried away; but our current view would be core profits will reduce because we think that GBM earnings will normalise faster than the recovery in Retail and Commercial will offset. That may turn out to be right or wrong, but that's how we see it today, but will nevertheless be healthy.

Non-core impairments and write-downs we believe will be lower than last year, but still high; so I expect 2010 to be the last year of Group loss and we'll see how that goes as the year runs through.

We do expect a gently falling Group impairment charge and a gently rising NIM if current trends can be sustained. Of course, we expect to make further progress in the rundown of non-core into the schedule that we've put out.

Of course, there are economic uncertainties which feed into the credit outlook. Of course there are regulatory and Governmental uncertainties and there is execution risk to our plan. All of these reduce over time and there will clearly be transparency as we go through that. I think as a postscript to Philip's point in his opening on bonuses, the bonuses that were paid in this Group for 2009, were the Board's recommendation; they were not an imposition and they were not reduced by the outside world. Of course, we reduced them in the sense that we wanted them to be restrained, we wanted them to be responsible, but they were consistent with the commercial running of RBS for its shareholders and we believe that that is the model that we must follow going forward.

Finally, again, starting to help you with the building blocks of the investment case; the business case for RBS I think is clear - market leading businesses in large enduring customer driven markets; the Retail and Commercial businesses to drive the earnings recovery from here, but GBM being very important to us. A group that is well capitalised with tail risks insured; a turnaround story, but with execution risk, and another year of pretty hard slog and low visibility before things get sunnier thereafter.

As we think about the investment case - and again, not in any way trying to rush our fences here - as we hit the planned targets in the coming quarters and years, as the external uncertainty, some of which are political and economic, particularly this year, and regulatory start reducing, we think that the RBS investment case will clarify. We think that there are really three building blocks that have to be concentrated on; the out year earnings per share driver, where we've given you our view of what we think we can accomplish in ROE, cost income and so on terms; a cross check to the risk - if we turn out to be right that the current capitalisation structure encompasses the losses from non-core wind down and if the book multiple from that is reasonable, then in a sense that's already in the book as opposed in the EPS. Of course, there will be for some period of time, valuation complexities around how to think of getting out of APS contingent capital and in particular the B-shares, which will take some time to resolve.

Nevertheless, I think that this onion will be peeling in front of your eyes and hopefully we won't be crying as that process goes through. With that, I would very much like to hand over to Bruce.

Bruce Van Saun:
Good morning; I'd like to walk through the consolidated financial highlights and then break that down into an analysis of our core and our non-core results. I'll then comment on our key funding and capital considerations along with a progress report on how we're managing risk.

Comparing full year '09 to '08 results, revenues increased by 43%, while expenses were up by only 7%. This drove an improvement in PBIL from £0.5 billion in '08 to £7.7 billion in '09. However, impairment losses were up by £6.5 billion in '09, reducing the operating loss improvement to £700 million. Our attributable loss in '09 was a smaller £3.6 billion, reflecting gains from liability management exercise and curtailment of benefits in our pension plans. Last year’s significant attributable loss of £24 billion reflects a £16 billion goodwill and intangible write-off.

For the fourth quarter, income was up 6% sequentially and we had a pre tax profit reflecting the pension curtailment; all-in-all signs of solid progress.

At the bottom of the schedule, take note of the progress in terms of funded asset and RWA reduction. Core Tier 1 ended the year at a robust 11%, reflecting the benefit of B-share issuance to HMT and the APS RWA relief. Our TNAV is now slightly over 51p; the decline in Q4 reflects the B-share issuance at 50p and an increase in the pension deficit.

A big driver of our improving performance over the second half has been rebounding NIM. During Q2 NIM reached a nadir of 1.7% but that’s increased in Q3 to 1.75% and in Q4 to 1.83%. This increase has been powered by improvement in asset margins in our Retail and Commercial businesses. We’ve been able to book new loans at higher margins in these businesses, which has more than offset pressure on deposit margins. Of course one other drag on the NIM has been our effort to strengthen our liquidity and our funding position. We now have a £170 billion liquidity portfolio, with £20 billion in FSA eligible Government securities and a percentage of wholesale funding that’s greater than a year in maturity now stands at 50%. That said, we should be able to continue to absorb that and post stable to improving NIM in 2010. As rates rise in 2011 and beyond that should boost NIM further, alleviating deposit spread compression.

Another driver of our improved operating performance in 2009 was the positive operating leverage I referred to on our first slide. Our cost-to-income ratio has improved to 59% as our cost reduction plan delivered £1.3 billion of benefits in 2009. The overall uptake in expenses reflects growth tied to higher revenues as well as foreign exchange. We do plan to bring expenses down on an absolute basis in 2010, as we continue to implement our cost reduction initiatives and we run down non-core.

Let’s focus now on our core performance. Core operating profit was up 89% to £8.3 billion as GBM drove higher revenues and positive operating leverage was 23%. While impairments were up by £2.2 billion, they have levelled off and stabilised. The illustrative ROE for our core activities was 13% for the year. Q4 results, adjusting for selected one-time items were broadly stable with Q3. Scanning through the core divisions on the next couple of slides let me offer the brief following observations. UK Retail PBIL was up 10% versus ‘08. We’ve made excellent progress in attracting new customers, improving our service model while lowering costs and gaining mortgage market share. Unfortunately we suffered a £600 million plus increase in impairments largely on the personal loan portfolio, reflecting weak economic conditions. The good news is that the PBIL momentum will continue into 2010 and impairments will level off driving better profitability.

UK Corporate showed stable PBIL versus ’08; loan volumes were off as customers de-levered and NIM dropped in the first half, but rebounded in the second as asset margins have expanded. Expenses were tightly managed, declining by 7% year-over-year. Again, similar to UK Retail, impairments were up over £600 million reflecting the weak economic environment. But as with Retail, we expect UK Corporate to perform better in 2010 with modest growth in PBIL combined with lower impairments.

Wealth Operating Profit was up 21% in 2009 given 5% income growth and tight expense management. That said, the low rate environment and competition for deposits has continued to challenge the business.

GBM was already covered by Stephen; suffice it say that had an outstanding year in refocusing the business model and taking advantage of market conditions. The first half of the year was clearly above trend line, but the business was able to generate £2 billion in income per quarter in the second half, which is back to trend levels. I’ll add that this year, so far, we are pleased with the performances of the businesses to date.

Continuing on with GTS, operating profit was essentially flat with ’08. Compression on deposit margins continues, but balances have resumed growth in Q4. Outlook is stable for this business.

Ulster has had a tough year; impairments were up by over £500 million reflecting the weak economy in Ireland. The business has taken steps to strengthen PBIL through pricing and expense reduction initiatives, but 2010 will be another tough year on the credit side.

The US businesses at Citizens suffered mightily from lower interest rates and higher credit costs, resulting in a small loss in 2009. We do expect actions taken to bolster the NIM as well as the improving economy, to return Citizens to profitability in 2010.

Lastly, insurance had a rough year as net claims were up by over £600 million, including a £448 million additional charge for personal injury claims, resulting in a steep drop in operating profit. Significant revamping of the business is occurring on the pricing, expense, underwriting and claims processing dimensions, which we believe will result in a bounce-back year in 2010.

Closing out the analysis of core, a snapshot of impairments shows that most Divisions have stabilised, save Ulster, at relatively high levels. We would expect to see some improvement over the course of the 2010.

Let me move on to non-core. Year-over-year, not a pretty picture. Non-core lost a little less money before impairments – about a billion less – but impairments jumped by over £4 billion resulting in a loss of £14.6 billion. One bright spot though, is that both impairment losses and operating loss have narrowed for the second consecutive quarter. Non-core's Q4 operating loss annualises to about £10 billion. While that's still significant, the trend is in the right direction. TPAs were down meaningfully in 2009 and RWAs dropped sharply in Q4. We continue to look for economical ways to accelerate the rundown of assets and trading exposures.

The next slide on impairments gives more detail on losses by sending division and by asset type. GBM and UKC drove the biggest losses which were centred around property and manufacturing assets. We expect impairments here to remain at a relatively high level in 2010 given the nature of these legacy exposures. Total assets declined from £343 billion to £221 billion over the course of 2009. Of the reduction, £53 billion was in derivatives and £65 billion in third party assets, of which disposals and runoff accounted for £47 billion. This is £15 billion ahead of non-core's 2009 TPA reduction target.

Let's move on to the Group balance sheet and we'll cover funding and capital. Our total balance sheet has decreased by almost £700 billion since the peak, about half of that is on the funded balance sheet and the other half is in derivatives. As you know, we bolstered our capital ratios through B-share and APS in Q4. As a result, our leverage, TCE, loan-to-deposit and Core Tier 1 ratios are certainly much improved versus a year ago. As we run down our non-core assets, we facilitate our ability to achieve better loan-to-deposit measures, which we expect to continue over the planning horizon. This gives us comfort with respect to rollover risk on wholesale funding in light of the winding down of Government support programmes. We simply won't need as much wholesale funding as our non-core assets runoff.

We still have work to do, however, to enhance the quality of our liquidity portfolio and to continue to lengthen the maturities of our wholesale funds. This will continue on a steady, but gradual basis, over the planning horizon and the cost is included in our NIM guidance given earlier. The new liquidity and funding guidelines by Basel and the FSA are directionally in line with our plans.

On the capital front, we gained 5.1% points of Core Tier 1 during 2009. The biggest positives were B-share issuance of 4.4%; net APS RWA relief 1.6%; and the liability management exercise in the first half, again 1.6%. These moves more than offset the attributable loss and other impacts.

Let me continue on to briefly cover the progress that we're making on managing risk, but first off I'd like to say we've developed a much more effective risk management paradigm. In the short time that I've been here, under the leadership of Nathan Bostock, working with our Line Managers and their risk teams. Having said that, we still have significant legacy issues to work our way through. The headlines here are that RWAs are down in Q4; credit metrics are improving and we're very focused on cutting some of our tall tree exposures.

First on RWAs, we suffered from pro-cyclicality over Q1 to Q3, but this was less of a factor in Q4. We focused on restructuring and hedging of exposures to monolines and CDPCs where feasible and this combined with tightening spreads on underlying assets, is showing benefits.
In addition, customer and our own deleveraging are also having an impact. Of course, APS will provide about £130 billion of relief based on the current composition of our balance sheet.

Going forward, we expect several negative impacts that will have to be absorbed. The first is the impact of migrating ABN assets to RBS Basel II, which, including the roll-off of historic capital relief trades, should increase RWAs at mid-year by about £15 billion. This estimate reflects mitigating actions we plan to take, plus the fact that we've already absorbed £8 billion higher RWAs in Q4.

Next is the new Basel proposals on market risk and securitisation treatment, to be implemented in 2011. We would expect the impact after mitigation to be a further £60 billion. Most of the additional capital required to support these higher RWAs in our core segment will be allocated to GBM who'll be tasked with maintaining targeted return on equity.

I've covered impairments already at some length, but I think it's worth noting however, that REILs were flat in Q4 relative to Q3 after previously showing significant increases. In addition, the case referrals into our workout group - GRG - have declined sharply over the past two quarters.
While the trend is definitely better, we still have a lot of inventory to pass though the pipe.
Rest assured, we've bolstered our resources in this area and we have highly skilled personnel all over these assets.

We’ve made good progress reducing our legacy credit risk concentration in areas such as country risk, sectors and single names. We’ve implemented new frameworks, policies and limits in each of these areas. It would be fair to say, however, that the process of de-risking will take time. This is a multi-year programme and there’s still much more to do.

Let me conclude by offering a few key takeaways. Certainly the strength of our core franchise was demonstrated in 2009 - operating profit up 89%; GBM had outsized performance in terms of the contribution in 2009, but we’re starting to see signs that the Retail and Commercial business is gaining momentum as we head into 2010. Our fourth quarter NIM strengthened after downward pressure earlier in the year and I’d say our outlook is clearly stable to positive. The Group impairments have shows signs of having peaked. Our capital position remains robust at 11% Core Tier 1 ratio. We’ve reduced a lot of balance sheet risk, but certainly there’s still plenty there but we’re hard at work on it, total assets having decreased by £696 billion in 2009. Lastly, as I said again, I think the rebounding performance in Retail and Commercial and the smaller losses in non-core bode well for 2010. With that I think we’re ready to take some questions.

Q & A

Ian Gordon – *Exane BNP Paribas:*

Three quick ones; firstly, can I ask you to add some colour on your comments around NIM in terms of the underlying 2011 rate rise assumptions you have by country, timing and approximate quantum. Secondly, on capital, I noticed that you reference all your remarks around your strong base to your core capital measures. Can you just update us, firstly, whether your views on the necessity of preserving your non-core capital have moved on since November; and, additionally, under what circumstances might you seek release from the contingent capital subscription, or more specifically, the cost thereof? Thirdly, just to help me with the rather more modest 2010 dilution arithmetic, can you advise, firstly, whether any share-based compensation will be issued with new shares, or whether you'll be buying shares from the market to satisfy it? Secondly, apologies if I've missed it, but do we yet know what proportion of holders of the US$1 billion and 200 million Sterling convertible preference shares have exercised their conversion rights?

Philip Hampton:

We may as well start as we intend to continue.

Bruce Van Saun:

I think your first question was on the NIM. I think you want the 2010 outlook, you said 2011, but 2010. I think, if you look at the fourth quarter, we posted a 183. There are a few unusual items in that, I'd say in non-core such as some restructuring income. It's probably closer to 180, but if you looked at 170 up to 175 up to 180, we're seeing about a 5 basis point improvement over the last two quarters. That is being led by a dynamic in the market where we're able to re-price roll-over facilities and new loans attractively. How long that continues is a question, but I think currently it seems like we have momentum in that space. On the liability side it's still intensely competitive for deposits and we have some of the swaps rolling off, but it's still showing some compression on the liability side. I think, broadly speaking, we would expect to see, as Stephen described it, a gentle continued improvement in NIM. Potentially the things that could take us off that are changes in the competitive situation, a change of our ability to get the margins we're getting on the asset side would be one thing. Then, potentially changes in the shape of the yield curve or the level of interest rates could also have an impact to that.

Second question was on, I think, the amount of capital and how we're thinking about capital. I think in general - and Stephen you may want to weigh in on this as well - but we have, I think, a very robust capital ratio, recognising that we're still in a loss-making situation for the next few quarters in any event and then we also have the regulatory uncertainty around some of these Basel capital proposals. I think having more capital, a war-chest if you will, is a very good thing to deal with some of these things going forward. As Stephen indicated, as non-core runs down, I think we'll see what kind of capital management flexibility we have; but that probably won't be evident until some of the Basel proposals clarify later in the year.

You want to add anything to that, Stephen?

Stephen Hester:
The only point on APS and contingent capital, really what we've said that it is not economic for us to get rid of those things until we're in the end of 2012, but somewhere in the 2012/2013. It's our ambition by the end of 2013 to be out of both.

Bruce Van Saun:
The last one on dilution. Clearly we're very sensitive to the increase in share count, that's taken place to now; and so, as we think about how we're funding the employee bonuses and these conversions of these preferred securities, we're going to be very mindful of that. I'd say we're not going to give explicit guidance today as to what the amount is, but I think in general it won't be very material.

Philip Hampton:
Who's next, why don't you just sling it along.

Peter Toeman – *HSBC:*
In slide 41 you've kindly given us a net stable funding ratio, which I'm assuming is how it will be calculated under Basel 3. Commensurate with that there's a wholesale funding proportion, 50% more than one year, 50% presumably less than one year. I wondered if, because you're reasonably close to the 100% net funding ratio, are you actually telling us that the mix of wholesale funding is now going to be, as you show it here, as 50% short-term/50% long-term and that you're happy with that particular mix.

Bruce Van Saun:

I think we would expect to see that improve, that wholesale funding and part of it relates to what we said on these slides about the rundown of non-core. If you looked at wholesale funding being 50/50, a lot of that wholesale funding is oriented against a non-core asset portfolio. As non-core runs down, let's say in 2010, the funding that will run off is going to be the wholesale funding that's less than a year. Just by dint of that, as overall wholesale funding goes down; it is running off from the less than 1-year pocket. The percentage that's greater than a year is going to go up. We don't have a real hard target on that; when we see opportunities in the market to lengthen i.e. when market conditions are favourable, we'll continue to do that and chip away at that. I don't expect significant headwinds on the lengthening on the wholesale funding side. Where we still have some water to carry is on improving the asset quality in the liquidity portfolio, taking our FSA eligible Government bond portfolio from £20 to £50 [billion] over the next 4 years, and so there's a cost associated with that and the give up of the interest we're making on the collateral that we will be replacing with those Government bonds.

We've already got that baked in. We did a lot of that in 2009 so I don't think that's an incremental impact to the NIM.

Manus Costello – *Autonomous:*

I have a couple of questions on UK Retail please; firstly, there's been recent data showing a slight tightening in competition in the UK mortgage market. I wonder if that's something you felt over the last few months and if you could give us some colour that?

Secondly, in the fourth quarter you saw a drop down in non-interest income in UK Retail as a result of the lower overdraft fees. Do we have a full impact of that in the fourth quarter and should we roll that forward as a quarterly run rate for next year?

Brian Hartzer *(Chief Executive, RBS UK Retail, Wealth & Ulster Bank):*

On mortgages, yes it is becoming a little more competitive, but we've done very well and continue to grow market share and I think we can continue to do that. There are a couple of reasons for that. One is that mortgage competition at the moment is highly dependent on the availability of deposits to fund those mortgages. We've been doing very well on deposits and that gives us a fair amount of leeway to continue to grow our mortgage book. The second thing, from a structural point of view that I think is very exciting about RBS is that our share of mortgages historically is very low relative to our share of current accounts. Simply by regaining what I would consider to be our natural share which is a function of simply fixing our sales processes in the branches, ramping up marketing and so forth, we can take advantage of the strong brands and strong relationships we have to grow that business. We've more than met our Government targets and I think we'll continue to do that and at very healthy margins I might add. Mortgages are looking like a great growth opportunity for us.

On the fee side we didn't see the full impact of the fee reductions that we made in the fourth quarter, although that certainly did flow through, so there will be a continued run-rate effect of the overdraft fees and non-interest income in 2010. We clearly have taken a divot on fee income from the reduction in PPI insurance revenues as well as the overdraft related fees. Some of that we're beginning to address through pricing on personal loans and some of that we still have a gap that we need to fill on the overdraft side and we are thinking that through and it will be interesting to see how that plays out in the industry.

Stephen Hester:
Full-year fee impact is what? About £200 million…?

Brian Hartzer *(Chief Executive, RBS UK Retail, Wealth & Ulster Bank):*
The fee changes that we made in September were about £270 million on a full-year basis, so some of that still needs to flow through.

Tom Rayner – *Barclays Capital:*
Could I just maybe clarify what I think you're saying on the Group margin guidance, obviously a gentle increase this year. Is this really saying that the positive asset re-pricing trends you're seeing all-in is going to outweigh the stiff competition that you're still seeing on deposits, plus all of the issues of term structure on wholesale and new liquidity rules? When you whop it all together, is that the answer, that it's a gentle upward trend?

Bruce Van Saun:
That's what you've seen in the last two quarters and we would see that continuing.

Tom Rayner – *Barclays Capital:*
Within that, the UK we just heard on the mortgage side - could you give us a feel for how the mix of the product pricing is changing. SVR, I think it said in the release, is becoming more; people are now having to go onto SVR which is obviously much more attractive from the bank's point of view. Can you give us any figures on where the percentage is today and where you think that might go in terms of the mix of the mortgage book? Also the deposit, I think savings margins were stabilised in Q4; could you comment on that as well please whether that's sustainable?

Brian Hartzer *(Chief Executive, RBS UK Retail, Wealth & Ulster Bank):*
On the first one we've certainly have seen a shift to SVR which is helping our margin and will help our revenue growth in the year ahead as well, because the margins are healthier on SVR and I think as long as rates stay low where they are, that's probably likely to continue. It could turn around if rates start to spike up obviously, but for the time being that's going to be a good contributor. I would say - I forget off the top of my head the exact proportion in variable rate - but I would say in aggregate it's probably around the 30-40% range and heading up, and we'll see that continue to flow through. That will underpin good revenue growth for us this year on mortgages side.

The second question; we've continued to see huge competition on the deposit side. Some of the pricing that was going on in the savings side in 2009 I think reflected probably borderline panic of some of the banks about being seen to sustain their deposit-to-loan ratios at reasonable levels. That seems to be settling a little bit, although it still remains very tough. I think what the industry has done is increasingly manage the overall NIM and the relationship between deposit pricing and mortgage pricing reasonably effectively; so I think the indications that Bruce gave are a pretty good summary of how we think we'll continue to manage that.

Tom Rayner – *Barclays Capital:*
Just on slide 14, Stephen, your comments on the thrust of regulatory change and calibration being a key issue. It sounds as if they don't make some changes on some of the proposals you think economic growth could suffer. Is your view that there's going to be a pragmatic solution in the end which means that some of the more severe proposals actually get watered down in order to help the industry as a whole get back on it's feet. I'm trying to get a sense of what you really mean by that slide.

Stephen Hester:

I think in order to be responsible we're prepared for a worse outcome and obviously we're trying to do our sums as if these things come in reasonably quickly after 2012 with only modest lags. However, I do think that there'll be quite a lot of sentiment volatility this year in particular, as different hawks and doves pronounce during this argument process around Basel. What seems to me the case is that by and large, regulators and Central Banks feel quite hawkish about tightening up on the banking system and the politicians think that's a great idea until they understand the consequence of the cost and the availability of credit and then they think it's a lousy idea, and so there's going to be a push and pull as you go through there.

My view is that the most likely is simply have a fairly generous implementation period - I don't know, 5 years, even longer - as things are brought in and that will be incredibly helpful for us who want to defer taxed assets is the most obvious example, where if we have five years to bring that in it is a complete non-issue for us; if it comes in straight away it will be an issue for a year or two. I think deferral or staged implementation is the most likely compromise. But if you think about it, RBS used to run - stupidly, but nevertheless - used to run Core Tier 1 of 4%; we're targeting above 8% and when you include the capital changes that is probably another 4 or 5 basis points from start to finish; so RBS would have tripled the amount of capital it holds behind its business. If you multiply that by the world's banking system, you have a safer banking system and more expensive credit. You won't notice that when interest rates are low, but you sure as hell will notice it when they come up; and I think that will be a really big policy issue that people have to grapple with. As I say, at the moment it feels to me they will grapple with it by pushing the problem out, rather than by backing off the actual proposals; but we'll see.

Philip Hampton:

4% of course was the height of wisdom at the time.

Simon Samuels – *Barclays Capital:*

On page 20 of your earnings release, looking at your strategic update and your divisional targets. I am trying to understand what you're trying to tell us about the 2011 targets for the UK Retail and UK Corporate. Everything obviously suggests that the margins in both those businesses are getting better and provisions are obviously getting better as well, yet they seem very modest, just greater than 1% ROE in Retail and greater than 5% in Corporate.

Stephen Hester:

You've got to give us a chance to brag about it and doing better than our targets sometimes, don't you? What I said I would do and what we have done, is we haven't done a full revamp of our Strategic Plan and updated all the targets. All we did was we said since August there are a series of threats from the regulators that are becoming clearer and there is a series of earnings dilution from disposals that we haven't factored in. So we have only updated the plan for those two things; and those two things are obviously negative. We believe we can offset them by positive operational income, but we have not attempted to in a sense reflect in each of the divisional targets where they could be upgraded. I plan to do that more on an annual, rather than a semi-annual rhythm. I think you're right to point out that there are some of the 2011 targets that are ripe for upgrade, which we will more formally do on a once a year rhythm.

Arturo de Frias – *Evolution:*

I have three questions also please. First of all on UK Corporate impairments, you were mentioning that you think that impairments might have peaked, but in UK Corporate how already has started to fall quite noticeably; I would like your comment on that. Obviously H1 impairments were high, but the macro hasn't strengthened much in the second half, so I wonder why impairments are falling in H2 in UK Corporate.

The second question is on the branches that you expect to sell by the end of this year. You have mentioned that you have, I think, £146 million operating loss in those branches. That compares with overall Retail ROE of 4% and overall Corporate ROE of 10%. I wonder why the branches you want to sell are performing so weakly versus the Group in general, and if that could make it difficult. Maybe you don't want to discuss on price or anything like that, but it might be difficult to sell at book value with these numbers.

Finally, a bit more of a philosophical question on the targets for Retail. The 100% loan to deposits, obviously 150% was bad, 170% was bad, but why go into 100%? Banking is a leverage business; I think it is reasonably healthy to do a bit more lending than deposit gathering. Why do you want to go to 100%? Is that not a bit tough for the Retail network?

Stephen Hester:

Shall I take two of those questions and ask Chris to take one specifically on deposits?

On the branch and SME disposal, if you broke down our UK Corporate business between SME and all Corporate, the SME bit will also be losing money last year, because that is where the impairments worsened and where the margin improvements have been slower. What I believe is over time, the profitability of the thing we're disposing should not be that much different than the profitability of the host businesses. We do believe that that business is capable of greater than 15% ROE once it gets past the impairment peak and once the costs are taken out that we're taking out of the business generally. But it is not to say we will get a good or a bad price for it, but just in order to help you. It has not been an adversely selected business from our point of view.

On the loan to deposit target, and I can understand coming from Spain why you might take the view that also Ireland and the UK took, which is it is fine to use lots of wholesale funding to finance Retail businesses. I am not sure it has helped the three economies to take that view. We're not tied religiously to these targets. We're going to always operate with a pragmatic view, and of course if the marketplace meant that it was sensible to take a different view, we would. However as we pointed out, already the loan to deposit ratio of our core businesses is 104%. So we're already in the zone and that is because we enjoy very powerful deposit franchises which are a great asset of this Group and will be a greater asset when interest rates normalise and we can actually make some money out of it as well.

I believe that over the long term the gold standard for banks has been, zip code – as Bruce would say – zip code, 100% loan to deposit which leaves all of your non-loan things to be financed with wholesale funding. Obviously we have a significant investment bank that will be largely be funding through wholesale funding, although even some of that in terms of structured equity linked deposits has a Retail character. I continue to believe that if we are to establish ourselves in the undoubted capital strength category in the gold standard of banks, that that is the zip code we must be in.

Chris Sullivan *(Chief Executive, Corporate Banking):*
Just on the impairments side, first half we took some extra latent provisions which we don't obviously have to take in the second half. We actually found some loans and we identified them earlier so we took them as latent provisions, and it is about £350 million, something like that in the first half. The other thing you have seen is as the year has gone on, you have seen a decreasing level of businesses that are becoming impaired. The identification of those amounts are becoming smaller month-by-month and that has continued into 2010.

Jonathan Pierce – *Credit Suisse:*

I have got a couple of questions. The first is on the liquidity portfolio; from what you said in the presentation this morning, it sounds like there is about £40 billion of Government bonds in there which are not FSA eligible, and the other disclosure on the debt securities portfolio suggests most of that is sub Triple A Government bonds. Can you confirm where those bonds are held? Is this the portfolio you're going to start selling to move into FSA eligible bonds and will that create a loss?

Bruce Van Saun:

The actual math is about £35 billion on top of the FSA eligible £20 [billion]. A good chunk of that is the investment we received for the B-shares which we put into T-Bills because we received that money right around Christmas time. We have short term UK gilts for £25 billion-ish in the number and then there is another £10 billion which is basically Government held, either in Citizens or in ABN Amro, which is very high quality paper, but since it is not in the Plc we can't count that in terms of our liquidity buffer that the FSA is requiring.

Jonathan Pierce – *Credit Suisse:*

I'm with you; and the general increase in the cash balances in that portfolio, is that just a simple function of loans on the balance sheet falling particularly to financial institutions and you're just then parking it with the Central Bank?

Bruce Van Saun:

I think in general we're much more liquid. GBM's balance sheet is more liquid; the Group balance sheet is more liquid. As loans have paid off we have had additional liquidity and I think that is a good thing.

Jonathan Pierce – *Credit Suisse:*

The second question is, on slide 40 which shows some of the maturing of the wholesale funding portfolio, can I just confirm that doesn't include SLS funding? Whether you're willing to give us an update of - I know you can't disclose this to the exact amount - but the amount of SLS funding give or take that you have relative to maybe CGS. On the more detailed net stable funding ratio table, which I think is on page 144 of the release, whereabouts in there does the SLS funding sit? I am not entirely clear whether it falls entirely into wholesale lending, greater than one year or not.

Bruce Van Saun:

The SLS funding overall is down appreciably from where it was a year ago. Go ahead do you want to take it?

Stephen Hester:

I am not allowed to give the number; it is not a big number; SLS is not a big number. It is a very small number of tens.

Steve Hayne – *Morgan Stanley:*

I just had a question around the Investment Bank. It seemed like a lot of the fourth quarter reports from the US had significant reductions in their Investment Bank. Both yourselves and other major banks who recently reported seem to indicate that the fourth quarter wasn't so bad from a European angle, or at least the print that you have delivered. I was wondering if you could give a bit more flavour on what went actually quite well in the fourth quarter in the Investment Bank.

A second and related question is, what sort of cost income we should expect in that for 2010, given what you have just delivered, as you say 27/28%.

John Hourican *(Chief Executive, RBS GBM):*

The fourth quarter had some positives and negatives in it from the point of view of the Investment Bank. Client flows, particularly in the flow of businesses were weak across the market and were weak for us in general; but our Equities business did well particularly in the structured deposits area where we made some good revenues there. It was really from a customer flow perspective quarter weak in line with the market; but in terms of the revenue delivery we had a strong Equity quarter and we had a strong DCM delivery quarter as well from our client franchises. The pure trading and flow businesses were in line with the market and we were experiencing relatively weak demand from the institutional flow side.

Looking forward, clearly when you have got one huge quarter in the First quarter of 2009, that is not going to repeat. You're more likely to see the cost income ratio of the ensuing three quarters to be repeating through to 2010 and beyond. That is probably all I want to say.

Stephen Hester:

I think your subset of that was comp-to-revenues and I am not making a prediction for 2010, but I think the more natural place for comp-to-revenues for us is mid-30s.

Leigh Goodwin – *Citi:*

I have got a couple of questions on the impairment trends of what we saw in the fourth quarter and how we might think about run rates for 2010. Just going back to the question you had on the corporate side, I noticed you have a negative charge against house building and construction. I wonder whether what we're seeing now is perhaps some writing back of any of the losses that might have been taken in previous quarters, and to what extent therefore the trends that we saw in the fourth quarter reflected movements in the commercial real estate prices.

Secondly, on Ulster Bank there was quite a big jump in the fourth quarter. To what extent was there an element of kitchen-sinking in there, or whether we're really are on a much deteriorating trend which we might expect to continue through 2010.

Bruce Van Saun:
I think in general it is a bit early to spot one number there where you see a net recovery and to start to bake in. We're going to see a lot of that. I would just be cautionary, I don't know Chris if you want to add some….

Chris Sullivan *(Chief Executive, Corporate Banking):*
The movement from core to non-core…

Bruce Van Saun:
A small re-class; and then I guess on Ulster, there was a big top up to the latent provision in Ulster, given what has happened to the Ireland economy. We certainly wanted to get ahead of things a bit and so we did a deep dive in the fourth quarter and that is why that popped up so much in Q4.

George Grissom – *Execution:*
I just had two questions; the first being if I look at your 11 billion of preference shares, I was wondering if there is anything you might do to convert that into tangible common to improve the capital structure further, because you have done a brilliant job so far of improving the capital structure and if that may not help you to get out of the APS earlier than your guidance.

Question number two; in the UK we're seeing record levels of corporate debt issuance and we're seeing banks lending balances in commercial contract. I am wondering if the disintermediation trend will finally take off in Europe and if this would help you produce more robust revenues in GBM this year, because this has been very much a lagging trend in Europe relative to the US.

Bruce Van Saun:
On the first one, clearly we have a window here to study a liability management exercise.
We certainly are considering our alternatives there. I would say it is not an easy equation with all the changing regulation around capital quantity and capital quality. We're certainly looking through that and considering what course of action we should take. I would anticipate that some time, maybe mid-March, we would have formed a view and we'll certainly let you know what we're going to do at that point in time.

Stephen Hester:

On your second question on deleveraging. Of course the capital markets had probably their record ever year from a bond standpoint last year. I think probably that gets worse this year, not better. As you know, the actual new issuance isn't the highest margin activity out there; it is then the subsequent trading that is facilitated. I don't think we would point to any great secular trend there, but it is the case, of course, that as a universal bank we are able to service our customers when they go to the capital markets if they're not taking loans from us. That is a benefit of the business structure.

Mike Trippitt – *Oriel:*

Two quick questions; one on the non-core. You talked a lot about impairments, but I just want to ask you about the income line which was a game of two halves, positive income in both the third and fourth quarters. Are there any blips in there, or should we now think of that as being a sort of positive income, albeit obviously on a declining asset base going forward.

Secondly on GBM, you've given clues on 2010 and the size of the business in the future, but I just wondered in terms of either by assets or risk assets, are you there or thereabouts in terms of balance sheet size that you would like the business to be going forward?

Stephen Hester:

The second one first; on GBM I would say for now the GBM balance sheet is in the rough territory that we think it should be. The risk weighted assets will inflate substantially with the Basel changes, albeit we don't expect to take more risk in GBM than we're currently taking; but that won't be apparent when you work through the regulatory changes. That is how we feel about GBM. Of course it will be important to see how regulatory changes impact all of our industry, but that bit in particular, and there are individual business lines that could be particularly impacted such as the Mortgage business from the Basel changes. I think at the moment all one can do in a sense is have a holding view, pending the working through of some of those things.

On non-core I don't know whether you want Nathan or you want to take it.

Bruce Van Saun:
In non-core we have had some volatility around the trading activity line. We have the special asset unit there and we're working down those exposures. The fact is those positions as the markets have improved, the losses there have reduced and we have also been taking active steps to restructure and hedge that exposure. I think you're starting to see the fruits of that in the second half of the year. We also, I think, have a much cleaner allocation of interest income, and so the interest income levels that you're now seeing in the fourth quarter we would expect to sustain in 2010. Is there anything you would want to add to that?

Mike Trippitt – *Oriel:*
Can I just sneak in a little follow up? Net interest income was pretty well double the run rate Q4 over the previous quarter. You're saying that is a sort of…

Bruce Van Saun:
There is an updraft from our allocation models internally as part of that, but then as I mentioned earlier when I said 183 was probably closer to 180. There was also some restructuring interest that we received that boosted that number to some degree.

Michael Helsby – *Bank of America Merrill Lynch:*
I have just got one question and just two small points of clarification. Firstly, clearly the US business has been very challenging over the last couple of years. It feels like with NPLs plateauing, the margin has clearly gone up and you're signalling a sharp increase, it looks like, for 2010. I was just wondering if you could give us more colour on the US business.

Just on points of clarification; I am trying to read between the lines on your margin guidance. It feels like you're telling us that the 5 basis points increase we have seen in the last couple of quarters is what we should think of as a reasonable trajectory going into 2010. I would just appreciate it if you could comment on that. Also, very appreciative of the comments around the Group still being in loss in 2010. I was just wondering if you could clarify, is that at the operating level or at the statutory level?

Bruce Van Saun:
I guess I will start with … do we want to have Ellen offer anything on the US business to start? I would say one thing, I said that the US business would return to profitability, I didn't say sharp. While I think the conditions drove a small loss in 2009, the things that you're pointing out in terms of improving pipeline on NPLs and impairments, that is going to be positive and the NIM, some of the actions we have taken on the NIM also will be positive. I think they will return to profitability. I wouldn't say it is a huge rebound at this point but certainly it is better to be profitable than unprofitable. Ellen, do you want to add more?

The next thing on the margin guidance, I don't think we like to be in the explicit guidance business of telling you exactly the number of basis points; I think we said gentle. You have seen 5 basis points normalised for the last two quarters, and until we see some competitive dynamic change or something in the yield environment, or interest rate environment change, that kind of feels okay, something 0-5. There are a lot of things that move through the NIM and that can be volatile from quarter-to-quarter. Anyway that is what I would say on that.

On the losses…

Philip Hampton:
I think we should invite our audience here to identify who has been really accurate at forecasting bank profitability or losses in recent years. It is not a fantastic track record. Robert, you had a question.

Robert Law *–Nomura:*
I have two questions on the balance sheet please. Firstly on the capital position, you have emphasised the strength of the capital position, but I think you regard it in your statement as appropriate or adequate, which isn't particularly strong phraseology. I think from the presentation, I got the impression that you view the capital as supporting the run off in the non-core assets. Could I invite you to just comment a bit more on this? What would it take for you to feel that you actually now have more than an appropriate level of capital position? Do we from this, take the view that you expect the run off of the non-core assets to absorb the capital that is now backing them?

Stephen Hester:

I think the best way, Robert, to answer that is that as we said our target where non-core is no longer is an issue and when the new regulatory rules are in place, is 8%+; that is what we have reaffirmed for 2013. Now of course you can put square brackets around that if you want because it does depend on what the new regulatory rules are and so forth. For now I think we're thinking that the 11% that we currently have can go down to a steady state 8%+ after absorbing non-core losses and increased regulatory requirements. But you could easily imagine for example if the regulatory requirements came in very abruptly and in a severe way you could imagine us dipping below that level, particularly in something like the DTAs. Or, if the new regulatory requirements came in at a much slower and milder way, you could imagine us having a very substantial capital cushion above that, which we will then need to decide what to do with. I do think we and all banks are in a particularly difficult position to comment on these two things, but at the moment that is probably the best that we can say in terms of our thoughts about capital.

Robert Law *–Nomura:*

I appreciate it is difficult given the uncertainties around, but you'd only regard your capital position as adequate; that was the phrase you used.

Bruce Van Saun:

I didn't say adequate; I did say I thought we had a strong capital position. I think I might have even used the word war chest; but I think it is appropriate to have that in light of the regulatory changes and the forecast for the non-core run down.

Robert Law *–Nomura:*

I was referring to the CEO's comments initially, but anyway … if I move onto the second question which was on the funding structure. In slide 40 you're helpfully referring to the run off the non-core assets and the maturing wholesale funding that you have got. Could I ask you to just comment on what your funding requirements you think will be despite that situation in the wholesale markets? Do you think the market is responsive enough to allow this kind of run off to proceed at this point? If I may ask, what is the total amount of Government backed funding that you have at the moment?

Bruce Van Saun:

Just as a data point, we issued £20 billion of unguaranteed wholesale funding last year. I think that type of number is a number that we feel comfortable we can get done this year, without commenting specifically on what those plans are and again some of that will relate to the path of the non-core rundown.

In terms of the Government guaranteed funding, I am not sure we have disclosed that; is that disclosable? It is about £50 billion.

Philip Hampton:

Has anybody else got a brilliant and burning question? Stephen, do you want to make the final remarks?

Stephen Hester:

Thank you for sitting through all of that. I just – in sort of bringing it together – wanted to be clear where we are. We are very pleased with the progress that RBS has made last year. We think that we have hit and beaten the targets for that stage of the journey, and we think that that makes the rest of the journey more credible. That positive sentiment is echoed in some of the minor body language around NIM and impairments for next year and the other targets that we have reaffirmed for the outer years. We do have to be very, very clear that while the worst year maybe behind us, there is plenty of heavy lifting to go and there are plenty of uncertainties in the world economy. We do expect 2010 to be a tough slog. We are not particularly trying to change consensus for 2010 with this meeting, although hopefully it will narrow. We are still cautiously positive, turning to more positive in the outer years, this is a big ship to turn around. We think we're doing it. The people are doing a fantastic job at that, but it still is a big turnaround.

Philip Hampton:

Well I hope you enjoy your 280 pages of reading. It certainly sorted out most of your weekends I hope. Thank you all for coming and see you next time.

END