

RBS

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JP Crutchley:

Okay, I've got a few still coming in, but I need to start. I'll kick off the introduction. The next section is RBS -- Royal Bank of Scotland. It's my great pleasure to introduce Bruce Van Saun, the CFO of RBS. I mean most people know the RBS story is one of mostly cleaning up the legacy of the past and moving the rest of the group forward. Bruce joined the group in 2009 and has been very much instrumental in moving the group forward and dealing with those legacy issues.

And sometimes I think the scale of what's been done at RBS sometimes gets belittled and I think just in the last quarter having seen the 11 billion reduction in Non-Core, a £27 billion reduction in its funded balance sheet and a £23 billion reduction in the short-term wholesale funding requirement, is very much testament to what's being done at RBS. So for an update, I'll hand it over to Bruce. Thank you.

Bruce Van Saun:

Thank you, JP, with me is also Richard O'Connor, Head of Investor Relations, and Alexander Holcroft, also on the team. Good morning, it's a pleasure to be here with everyone today. Let me start off first flashing our cautionary language, which you should look at, at your convenience. So today I'd like to start out by giving you a progress report on the first three years of our recovery plan, including the significant improvement to our risk profile. I'll set out the value proposition offered by our Core franchises, and then I'll provide some details on our Q1 business highlights. I'll wrap up with a few thoughts on regaining standalone strength.

Back in 2009, we initiated our recovery plan. The plan rests on three foundation objectives. Namely, to serve our customers well, to restore an appropriate risk profile, and to rebuild shareholder value. These priorities are interconnected and mutually supportive. The better we do on each, the stronger the group. Our strategy is based on strong customer driven franchises delivering attractive and sustainable returns in the context of today's external challenges.

Each one of our Core businesses must be attractive in their own right, as well as having valuable cross-business linkages such as shared infrastructure, expertise, and customers. Underpinning all of this, we're transforming our risk profile paced by the run-off of the Non-Core division. Bottom line, three years in our plan is working well.

So taking a closer look at our progress, we've reduced the group's balance sheet by around £650 billion. Non-Core assets have declined by more than two-thirds and now represent less than 10 percent of the group funded balance sheet. Our short-term funding profile has reduced by nearly three-quarters and we've increased the liquidity portfolio, which now represents 1.9 times our short-term funding need compared to only 0.3 times back in 2009.

Our Core Tier 1 capital ratio has increased significantly to 10.8 percent placing us towards the top end of our peer group. The improved capital position combined with our asset reduction has seen our leverage ratio almost half over the last three years to 16.4 times, which is comfortably below our medium term goal of 18 times. The loan to deposit ratio for the group has fallen to 106 percent and Core to 93 percent, well ahead of plan. We're tracking well on the group level to our medium term target of 100 percent.

This focus on our safety and soundness agenda has come at some cost to the P&L, but we viewed quick progress as essential for promoting the rest of our agenda. We've significantly improved the group's risk profile. For example, we've reduced our CRE exposure by over a quarter in the last three years. Credit risk concentrations have also declined as illustrated here by the almost 75 percent fall in single name concentrations in our corporate loan book.

The volatility of the Non-Core exotic trading book has seen a steep decline in VAR and P&L moves. Group impairments have decreased consistently year-over-year, down by almost half from the peak in 2009.

One area that received significant investor attention in our recovery plan is Non-Core. So let's take a closer look. Non-Core has been the primary driver of our risk reduction. At the end of 2008, 258 billion of non-strategic, overly concentrated or distressed assets were placed into a separately managed run-down division.

This is a big bank in its own right and has represented a meaningful execution challenge. The plan was to run the assets down over five years, balancing risk reduction with value maximization. Cash proceeds of the run-down were earmarked to pay down wholesale funding. In effect, success in this endeavor would improve both the left and the right side of our balance sheet.

Key challenges we have faced include managing asset complexity and accessing demand at appropriate prices. But we've built a good organization, we've made excellent progress and we are confident about our future targets. So how did we go about it? The main drivers have been run-off and disposals with some impact from impairments. Run-off is the biggest single driver, 42 percent of the asset reduction to date. It is clearly capital efficient and cheap to execute.

However, to do this requires a systematic approach that means we must not only stay close to clients, but we need to maintain a robust stance on haircuts on repayments and on roll-overs. Impairments have been lower than forecast despite the headwinds from Ireland and lower than expected economic growth. We foresee impairments coming in at the lower end of our original 2013 cumulative target of 20 to 30 billion.

Asset disposals also represent about 42 percent of the reduction through the end of 2011. To date, the average disposal loss has been around three percent of our carrying value. However, as we work through stickier assets, we expect this friction cost to increase over 2012 and 2013. That said, with impairments trending lower, we would expect to see the

overall Non-Core loss continue to decrease over 2012 and 2013. In fact, at Non-Core's bottom line we expect roughly a comparable percentage decline in 2012 to what we saw in 2011.

The run-down of Non-Core's funded assets continues to progress ahead of targets. We finished the last quarter at 83 billion. During the quarter, funded assets declined by 11 billion; about half of that was run-off and half of that was asset disposals. Looking out over 2012 and 2013, we project 10 to 12 billion of disposals per annum. With five billion of deals not completed and another five billion of likely deals in our pipeline, we are well placed to reach our 2012, 65 to 70 billion target and we feel confident in our 2013, 40 billion target.

Our plan estimates the 2013 rump to be about 40 billion. The majority of this will comprise corporate and other assets with low yields, but generally good credit quality. About a third will be CRE, of which 60 to 65 percent will be longer term workouts with good provision coverage. We expect that natural run-off will reduce the 40 billion rump by about half over 2014 to 2016. Our view continues to be that rundown going forward will be capital accretive assuming reasonable economic scenarios.

A major emphasis in redefining the group's risk appetite has focused around our investment banking business GBM. In 2008, we restructured GBM to focus on our customer driven flow business while reducing balance sheet use and capital intensity. This effort saw GBM's funded balance sheet decrease from almost 700 billion at the end of 2008 to 360 billion at the end of 2011. A key first step was moving 169 billion of assets off to Non-Core which at present have been run-down by about two-thirds.

We also tightened up usage in the remaining Core by another 137 billion with much of that in liquid fixed income positions and loans. We've also taken trading risk down by 56 percent over the three year period. This focus on customer driven activities and greater efficiency has really paid off. Over the three year period, GBM produced cumulative profit of 10.7 billion, which is about one and a half billion higher than our plan, and an average ROE of around 18 percent versus 11 percent back in 2007.

So if the first phase of this restructuring was so successful, why are we now in Phase 2? Well, the investment banking industry has been dealing with three headwinds in recent quarters, which I'm sure you're all familiar with. First off, the slower economic recovery and flatter yield curve have presented headwinds tempering customer activity levels. Market related issues such as customer risk aversion and dislocation of the funding markets have led to higher funding costs and more conservative usage of wholesale funding. And the changing regulatory environment, probably the most important, has led to higher capital funding and liquidity requirements for investment banking businesses. All these factors acting together have put unprecedented pressure on investment banking returns. Our response to this environment has been to focus on the competitive position and the capital intensity of each of our businesses and to make some hard decisions.

This slide shows that we've chosen to exit businesses where our market position was weak. Where it is strong and it's relatively capital light, we will invest and we'll grow. And where we have a strong competitive position, but capital intensity is increasing, we will work smarter around the balance sheet. We believe that we can be a strong, focused, competitor who maintains our FICC market share, serves our clients well, and delivers solid returns.

Stepping back to analyze our market business briefly, it's client focused and it offers important financial products. The business will use its strong market positions to serve the group's institutional and corporate clients for their treasury and risk management needs, as well as acting as an intermediary between issuers and investors. Markets product offering will be centered around its strong Core franchises of rates, currencies, and asset backed products.

The market's business is important because it provides strong linkages with all parts of the group. These linkages total 1.9 billion in revenues. While connectivity between Markets and International Banking is the strongest at 1.1 billion, linkages to Retail & Commercial businesses provide significant revenues for the group. For example, our position as a leading U.K. corporate bank rests on having a full set of products and global reach for our customers. Markets does this well. We are well-coordinated and we're very customer centric.

Looking at International Banking, this new division will combine GBM's banking business with GTS International and will be a leading player in the market. The rationale for the new structure is to provide a full banking suite to internationally focused companies. Products will center on lending and deposits, payments and cash management, trade finance and access to all of the market division's products. By bringing these businesses together, it will allow us to extract meaningful cost synergies while also simplifying our client coverage model.

We believe that our medium term targets for markets and International Banking are achievable. We will reduce asset and capital usage to improve our funding profile and our returns. And while the small balance sheet will adversely impact revenues to some degree, we anticipate that there will be some normalization of revenues from the subdued second half of 2011, and in fact, we saw that some in the first quarter.

Aside from the balance sheet and RWA reduction, cost efficiencies will be the principal focus of the MIB for enhancing their ROE and we will continue to drive revenue synergies through connectivity with our other divisions. So while we're confident in these plans, it's worth saying that we're committed to further restructuring as necessary over time to get ROEs to target in this business.

Next, I'd like to turn to the value proposition of our Core business. To start off our Core businesses are built on strong customer franchises. Our Retail & Commercial market positions are either market leading or are top tier and our customer metrics are stable to improving. International Banking's customer franchises are market-leading in the U.K. and they're top tier in Europe. Markets is placed in the top five globally across our Core product areas.

Our Core franchise is well-balanced and diversified. It has generated stable profits through a challenging external environment, and each year we've had ROE overall in excess of 10 percent in Core. The businesses have a good blend of ROEs, as you can see here on this slide. Retail & Commercial businesses excluding Ulster Bank produced a 13 percent ROE in Q1, despite the lackluster economy. We see opportunities to further improve our strong performers as the global economy strengthens while also continuing to improve the laggards such as Ulster and the U.S. Retail & Commercial business.

Looking at the loan to deposit ratios, our Retail & Commercial and Core divisions are appropriately geared and in the round, we're already below our medium term target. Note that International Banking and Ulster are both outliers. In each of these cases, we have

strategies to improve each of these over time. Our plans to restructure GBM will further enhance the attractiveness and sustainability of our revenues as they shift even more towards Retail & Commercial.

In fact, on a pro forma basis for the GBM changes, almost 80 percent of our revenues and RWAs would have been Retail & Commercial in 2011. The group also has a strong geographical diversification. We're anchored in the U.K. with 65 percent of our revenues, 20 percent comes from the U.S., and 15 percent from the EU and the remainder of the world. On business mix, the group has an attractive business compared to peers including a strong domestic base, good international presence, and appropriate scope of our Market's revenues.

Looking at the Core P&L, it is clear that a sustainable and profitable business is emerging. The NIM has been relatively stable of late and we expect continued resilience in 2012 in spite of the low rate environment. We remain focused on expenses. We've reduced Core's expenses in real terms and in absolute terms over the last year. And we've identified further initiatives to continue to take our cost base lower. Core's impairments are normalizing; they now represent 80 basis points of loans and advances. We expect this positive trend will continue.

However, it is worth noting that we expect Ulster losses to remain elevated for some time. We've made excellent progress in restricting Cores balance sheet. You can see here the loan to deposit ratio is down nine percentage points, since Q1 of 2010. I'll turn now to our Q1 performance highlights.

To start off, Q1 saw a strong rebound in operating profit for the group. The Core division ROE was good and that was aided, of course, by rebounding revenue across our Market's business. We've maintained the pace of our risk reduction with the group balance sheet decreasing by another 27 billion to 950 billion, which was paced by reductions in both Non-Core and in Markets.

We're off to a good start in the investment bank restructuring plan. We're tracking well to all our targets. This will lead to lower earnings volatility over time and a lower, more sustainable funding requirement. The impairment trends remained favorable; down nearly a quarter on Q4. Our capital position remains strong with the Core Tier 1 ratio increasing 20 basis points to 10.8 percent. Our loan to deposit improved again by two percentage points.

We've continued to take strides towards standalone strength. All U.K. legacy government funding will be repaid by the end of this week and we continue to adjust our capital structure to our third successful liability management exercise. You may also have seen that we announced the resumption of our preference share dividend last week, which is another important step.

This slide summarizes the key financial highlights for Core and for the group in Q1. I'll pick out a few key points.

For Core, the operating profit was up 46 percent, Q-on-Q to 1.7 billion driven by the strong performance from markets, and the ROE was 11 percent. RNC's NIM has stayed resilient, increasing on the quarter. Impairments that continue to follow a favorable trend and the loan to deposit ratio is now well-below our medium term target. On the lower half for group, our operating profit reached 1.2 billion in Q1. That was driven again, by

the rebound in markets and Core, as well as a reduction in our Non-Core losses to 500 million.

The Q1 overall bottom line pre-tax loss of 1.4 billion reflects a two and a half billion own credit adjustment as our spreads improved dramatically over the quarter. This performance stacks up well against our medium term targets. We're ahead on the funding, liquidity, capital, leverage ratios and we've made good progress on the group loan to deposit target. We've more work to do in improving our returns, while further efficiency programs and a little revenue tailwind down the road will help us to deliver the cost to income target.

Today, RBS already compares well to U.K. and EU peers across these key balance sheet metrics, but we're not done. We target significant further improvements across all metrics and aim for top quartile funding and liquidity position by 2014. In short, we aim to be one of the safest and soundest universal banks. 2012 shapes up to be a big year for us in terms of milestones on the journey to standalone strength. You can see here the things that we needed to accomplish in the first half of the year, we've accomplished already.

So as I mentioned, we just announced we'll resume the dividend payments on the preferred securities and that we'll pay our final CGS debt this week. In the second half another big agenda; we'd like to float Direct Line Group. It's probably sometime September, October. We want to exit the APS. We hit the minimum fee in October. That's subject to FSA approval, of course, and we'd also like to close the Santander transaction, although that one is quite complex and it may spill into the first quarter of 2013.

These are all necessary events in setting our future course and eventually allowing the government to exit its holding. So to sum up, we believe we've made good progress on fundamentally restructuring the group. This report card shows what we've achieved and where we need to make further progress. Our Core bank is a viable, attractive set of businesses with appropriate capital usage.

However, there's more work to do on improving returns. Good progress has been made on improving our risk profile and setting an appropriate risk appetite, and our historic under investment in key franchises has been addressed. Turning to the investment case, we provided a clear path towards delivering a sustainable business model. However, we've not yet achieved sufficient profitability to both meet higher capital requirements and restore the dividend which will take a bit more time.

You can look over the points on this next slide. I guess in summary, I think we've demonstrated that we've made very good progress so far, but there's still obviously a lot more to do. Thank you. With that, I'm happy to use our remaining time to take some questions.

JP Crutchley:

We'll open up the questions. As the mic's coming out, maybe I can kick off with the first one. Bruce, you did allude to eventually getting back to a dividend payment for the ordinary shares. Clearly, you've taken the first step by turning the preference shares on. I just wonder if you can just walk us through how you see the progress eventually getting back to that point. What still needs to be done in terms of getting to the point where you can actually consider a dividend policy for ordinary shareholders.

Bruce Van Saun: Sure, JP. I guess the first things to contend with, we want to exit the APS. Today, we get about 85 basis points of benefit in the Core Tier 1 ratio from being in that program. By the time we look to exit, it should be down to about 60 basis points, so that's an impact to contend with. And then the implementation of CRD4 later in January, if it stays on schedule of 2013, would probably impact us by another 60 basis points or so. So we have to continue to build capital either through improved earnings profile or continued deleveraging in order to offset those things and keep the Core Tier 1 ratio I think above 10 percent.

When we feel we have sufficient capital, clearly we have to make sure the FSA and other stakeholders think that we're in a position to put the dividend on. But then the next thing to contend with is this complicated government shareholding for -- many of you are familiar with it, but there's an A share and a B share holding, and then there's a what's so-called dividend access share which the B shares hold which entitles them to a superior dividend, which I think makes it hard to envision putting in a common dividend.

So we probably need to sit down with the government and renegotiate how to retire that dividend access share. So really, it's up to us to continue to deliver on our progress, absorb coming out of APS and the CRD4, and then have a conversation with the government around how to retire that DAS.

JP Crutchley: Questions from the floor?

Alistair Ryan: There's continued discussion I guess in the U.K. on whether the return to recession is likely to lead to a challenge on the bad debt side, and I think recent evidence and your numbers suggest that's not been the case so far. But if you could just discuss a little of sensitivity to the bank now to a weaker U.K. cycle versus where you were perhaps three or four years ago. Thanks.

Bruce Van Saun: Sure. I guess the U.K. environment has been sluggish, but it hasn't really been bad for our recovery plan. So we're in a period of extremely low interest rates which certainly has helped borrowers delever and improve their fiscal position, whether they're corporates or whether they're individuals. And so we've seen a nice steady improvement. I'd call it a gentle fall in impairments over the time period. We've also tightened up some of our risk appetite.

And so in the U.K. retail space, we used to have much more exposure to personal unsecured credit and a lower market share in mortgages, and over the last three years, we've changed that mix and had an increased appetite for mortgages, again, at LTVs of on average, 60 percent. They're pretty safe instruments. So we've taken down exposure to the personal unsecured. So I think, again, some of the stats say that the U.K.'s in a slight double dip. I think when the final revisions come out, that may or may not be the case. So it's either a slight positive tick or a slight negative tick. I think as long as we stay in this pattern of gradual recovery, that'll be okay.

The other thing that low interest rates have also increased investor appetite, plus the LTRO, for taking on risk assets. And so as we continue to work down the Non-Core exposures, this environment has also I think been helpful in staying ahead of the curve and achieving our targets on the Non-Core side.

Unidentified Participant: You talk about the need to build up capital in light of some of these hits that are coming, and you've done some liability management and exercises before. What are some of your thoughts going forward in terms of doing some liability management exercises?

Bruce Van Saun: Well, I think we've picked over the inventory quite a bit, having gone to that well three times already. But I think again, the Basel rules are clarifying and the FSA is working in conjunction with where Basel is going in terms of the right capital structure and instruments for the future. There's certainly, I think, a desire to see more loss absorbency, explicit loss absorbency, in some of these instruments. And so, we're watching that market with interest, the whole CoCo arena where the Swiss banks have started to issue and make that part of their capital structure.

At this point we have a contingent capital facility with the government which runs through 2014, so I don't think we need to be in a big hurry there, but we'll certainly look at that. So I guess I don't see anything imminently right now, but I do think it's likely that over time we will look to do some things to reshape the capital structure more in line with where regulation is going.

Unidentified Participant: Just as a follow-up, in terms of some of the securities where you've turned the dividends back on and other coupons that have come out of your restriction, are there restrictions in terms of doing liability management and exercises on those?

Bruce Van Saun: It's complicated, I guess is the short answer. There's some opportunities, but then there's also dividend stoppers and we have to work through the forward schedule on that. So I think you can talk to our IR folks who could fill you in on some of the specifics on that. Any other questions? Okay.

JP Crutchley: We'll draw it to a close. There is a breakout session if you wish to continue the discussion in a more intimate environment. Meanwhile, if I could just thank Bruce and the IR team for their time today. Thank you.

Bruce Van Saun: Thank you.