



Capturing Value in a Challenging Environment

Fred Goodwin
Group Chief Executive

Capturing Value in a Challenging Environment

What Challenges, What Impact?

- Uncertain economic outlook → income/provisions?
- Lower equity markets → income?
- Increased competition → income/margins?

Capturing Value in a Challenging Environment

What is our Goal?

- Generating superior sustainable value for our shareholders
- To achieve this we need to add value for:
 - Our customers
 - Our people

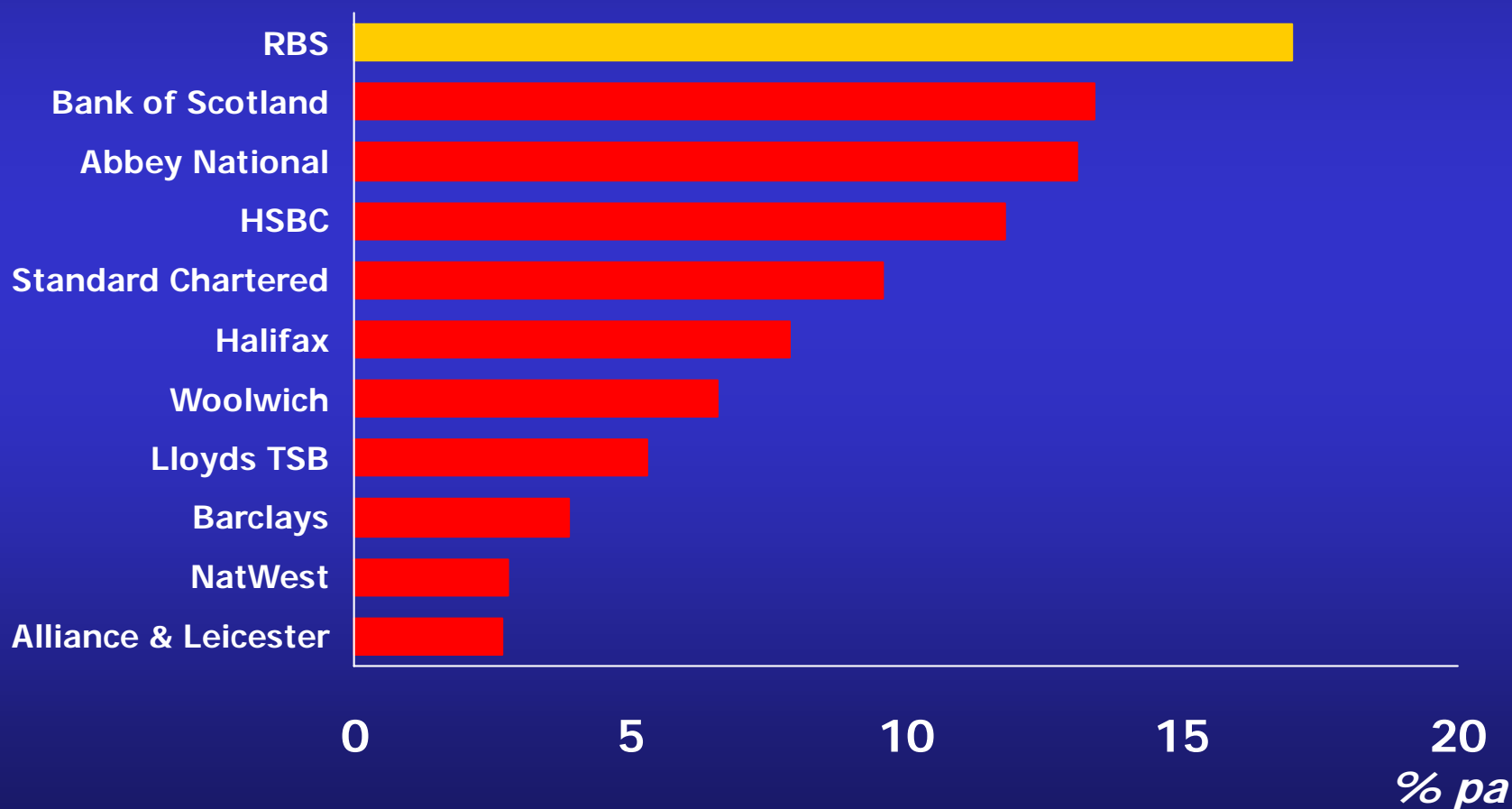
Capturing Value in a Challenging Environment

How?

- **Income growth**
- Improving efficiency
- Good credit quality

Income Growth

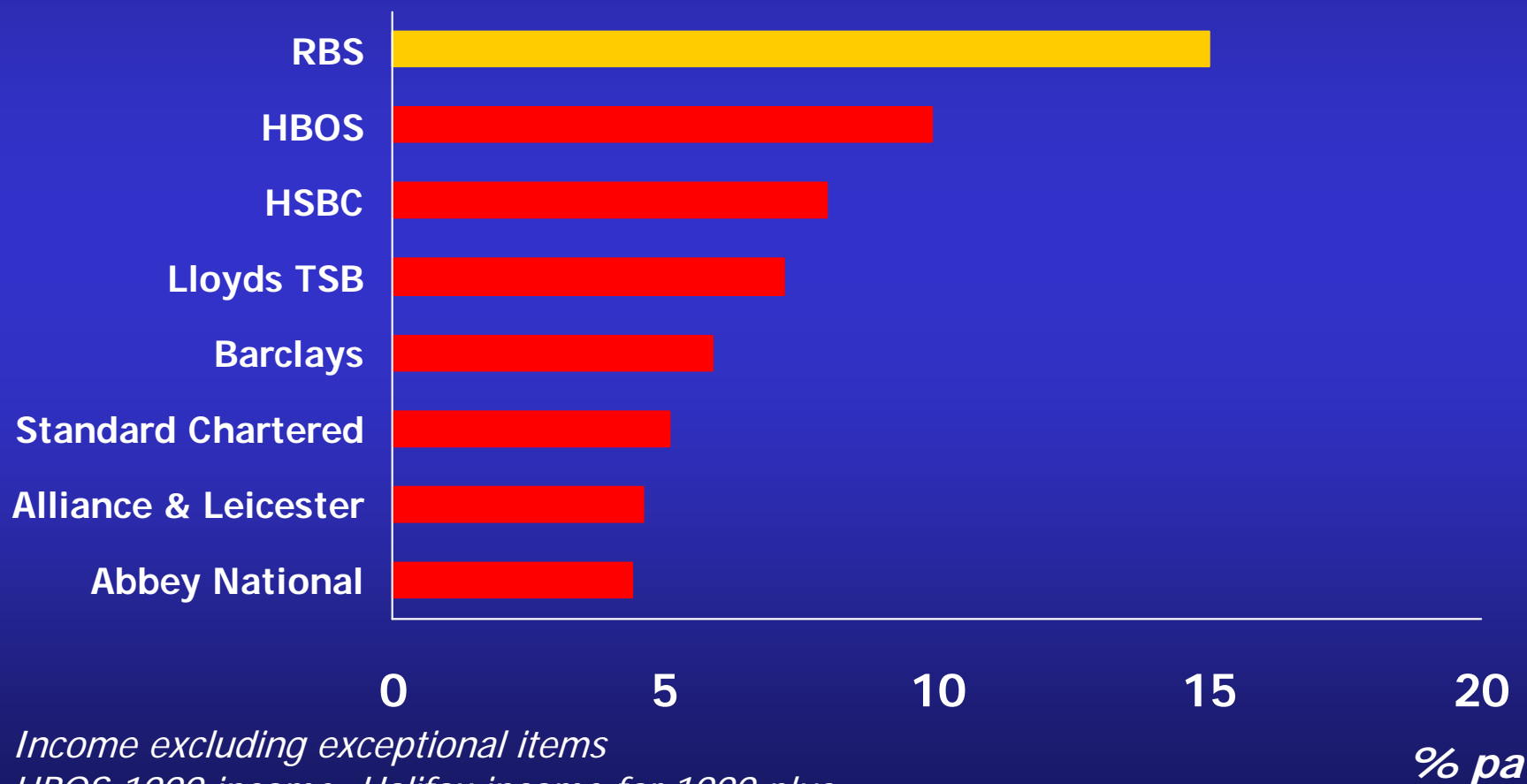
Average Growth in Income 1992 - 1999



Income excluding exceptional items

Income Growth

Average Growth in Income 1999 - 2002



Income excluding exceptional items

HBOS 1999 income: Halifax income for 1999 plus

Bank of Scotland income for year to 28 February 2000

% pa

Income Growth

<i>Income</i>	<i>Pro forma</i>		
	<i>1999</i>	<i>2002</i>	<i>Change</i>
	<i>£m</i>	<i>£m</i>	
Corporate Banking and Financial Markets	4,459	6,052	+36%
Retail Banking	3,305	4,193	+27%
Retail Direct	971	1,590	+64%
Manufacturing	–	–	–
Wealth Management	782	907	+16%
Direct Line Group	896	2,139	+139%
Ulster Bank	379	520	+37%
Citizens	576	1,716	+198%
Central items	(303)	(302)	0%
Total income	11,065	16,815	+52%

Income Growth

	<i>Pro forma</i>		<i>Change</i>	<i>Change</i>
	<i>1999</i>	<i>2002</i>	<i>Change</i>	
	<i>£m</i>	<i>£m</i>	<i>£m</i>	
Total income	11,065	16,815	+5,750	+52%

<i>Components of Income Growth</i>	<i>£m</i>	<i>% Total</i>
NatWest transaction benefits	+712	12%
Acquisitions since NatWest	+1,036	18%
Organic growth	+4,002	70%
Total	+5,750	100%

Income Growth

But what about the Challenging Environment?

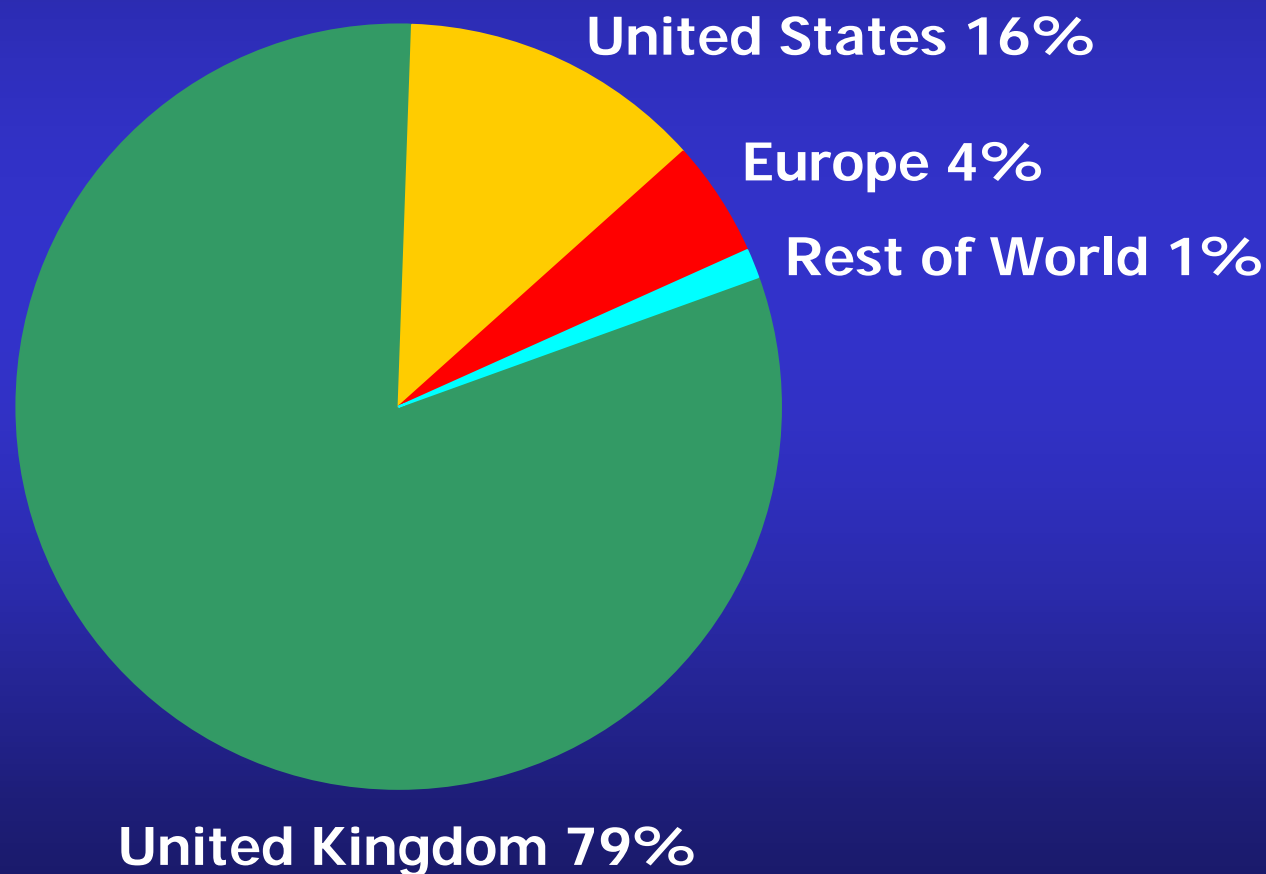
- Uncertain economic outlook
- Lower equity markets
- Increased competition

Uncertain Economic Outlook

<i>% Growth Real GDP</i>	<i>2000 Actual</i>	<i>2001 Actual</i>	<i>2002 Actual</i>	<i>2003 F'cast</i>	<i>2004 F'cast</i>
US	3.8	0.3	2.4	2.3	3.6
UK	3.1	2.1	1.8	1.9	2.4
Germany	2.9	0.6	0.2	0.5	1.7
Japan	2.8	0.4	0.3	0.8	0.8

Uncertain Economic Outlook

2002 Income £16,815m



Lower Equity Markets

	<i>% Change from Peak to 25 Apr 03</i>	<i>Peak Date</i>
US	-41%	Mar 2000
UK	-44%	Dec 1999
Germany	-65%	Mar 2000
Japan	-80%	Dec 1989

Source: Datastream, US S+P 500, UK FTSE 100, German Dax 30, Japan Nikkei 225

Lower Equity Markets

Activity

RBS Involvement

Wealth management

Some

Mergers and acquisitions

None

Equity trading and sales

None

Fund management



Negligible

Life insurance

Limited (joint ventures)

Increased Competition

Level of Competition

- UK personal banking 
- UK small business banking 
- UK corporate banking 
- UK general insurance 
- UK private banking 
- UK offshore banking 
- US retail banking 

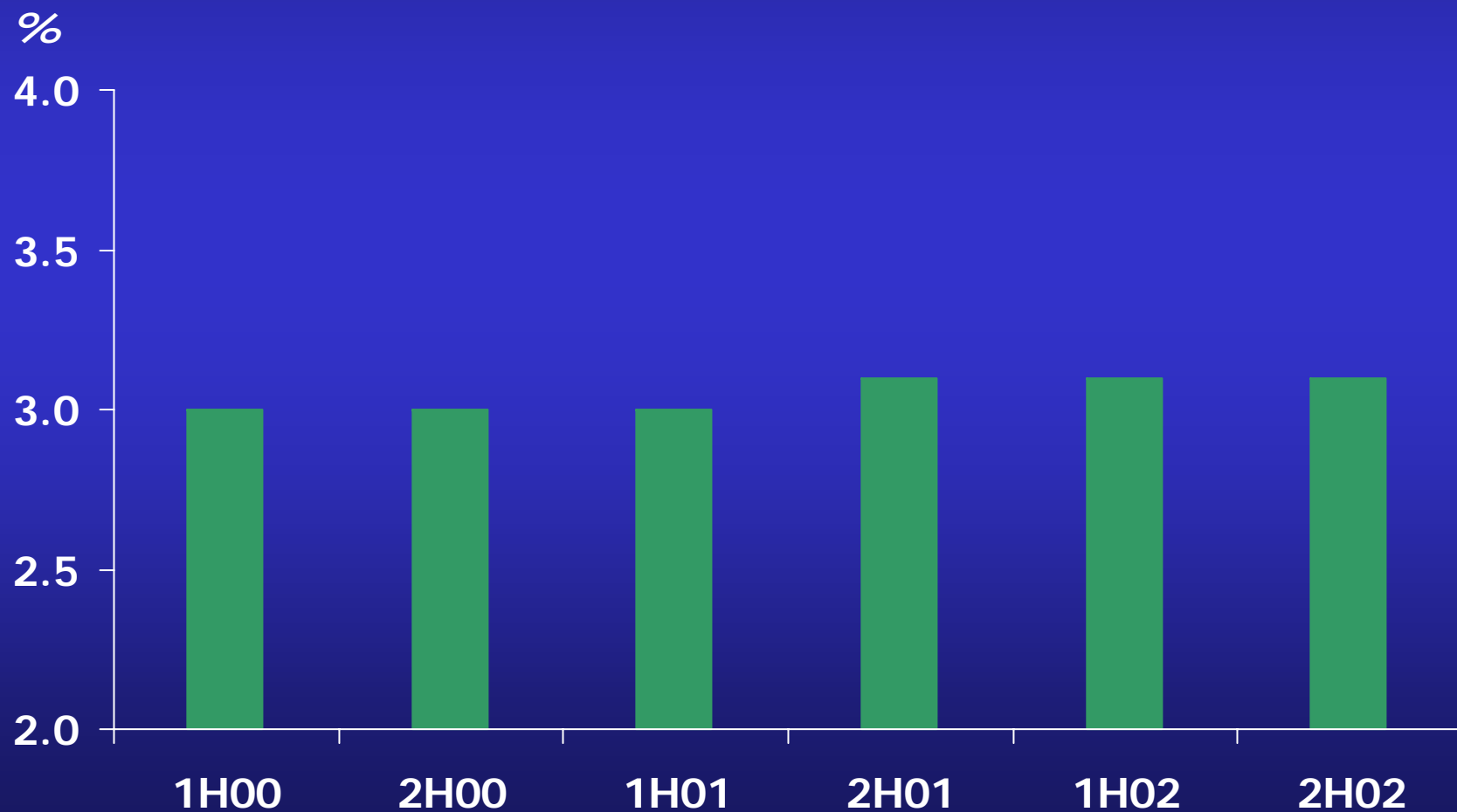
Increased Competition

Examples of UK Personal Banking New Entrants

- Scottish Widows Bank 1995
- Goldfish 1996
- Sainsbury's Bank 1997
- Tesco Personal Finance (RBS JV) 1997
- Egg 1998
- Standard Life Bank 1998
- Marbles 1999
- Smile 1999
- Cahoot 2000
- Intelligent Finance 2000
- Zurich Bank 2001-03

Increased Competition

RBS Net Interest Margin



"Headroom" for Growth

<i>UK Market Shares</i>	<i>RBS + NatWest</i>	<i>Other RBS</i>	<i>Total RBS</i>
Current accounts	21%	–	21%
Savings accounts	6%	2%	8%
Personal loans	6%	4%	10%
Mortgages	4%	1%	5%
Credit cards	–	17%	17%
Life insurance	2%	–	2%
Motor insurance	–	16%	16%
Home insurance	1%	6%	7%
Small business relationships	30%	–	30%
Corporate lead relationships	33%	–	33%

Source: NOP 2002, NFO 2002, RBS estimates

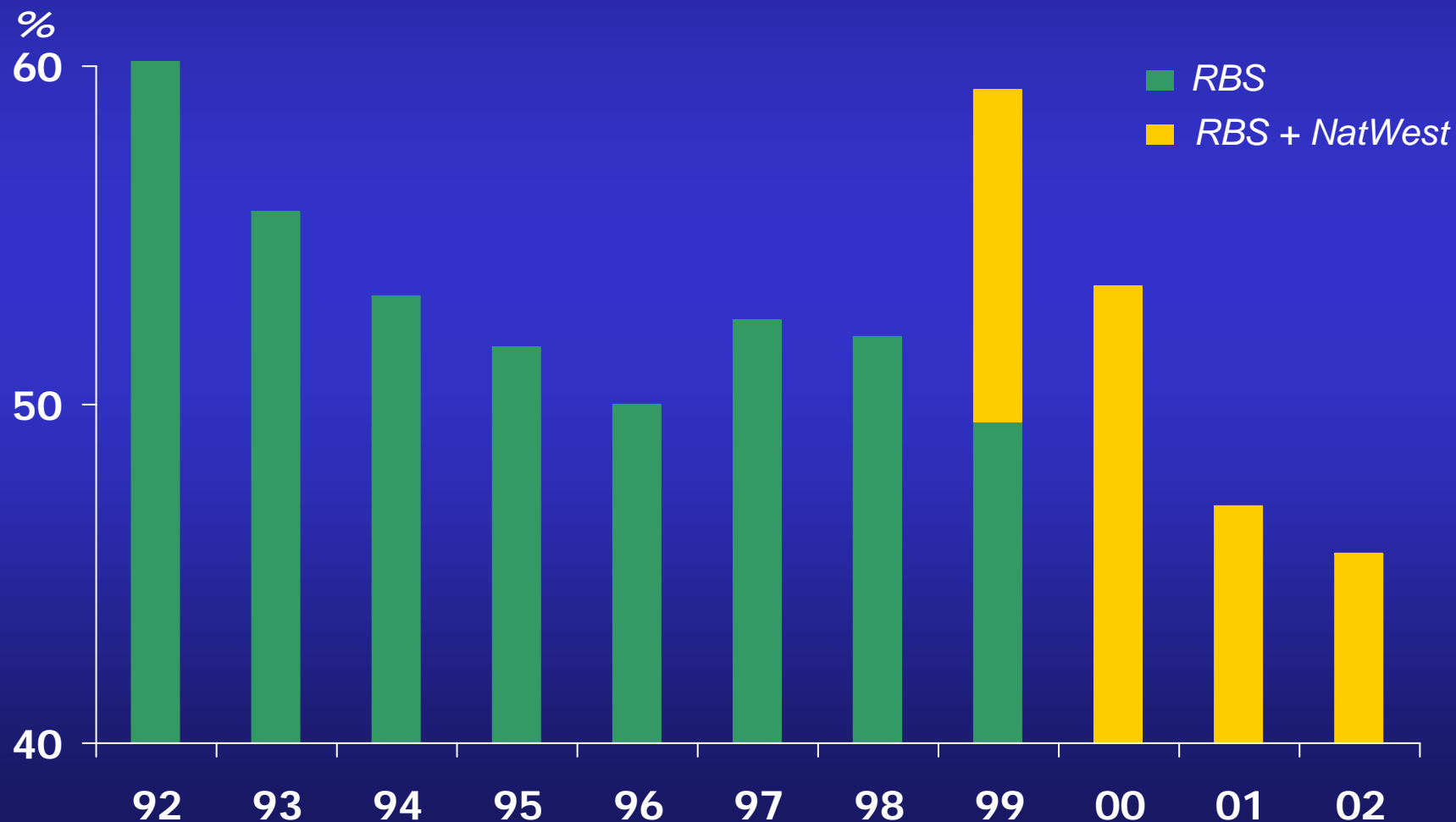
Capturing Value in a Challenging Environment

How?

- Income growth
- **Improving efficiency**
- Good credit quality

Improving Efficiency

Cost:Income Ratio 1992 - 2002



Improving Efficiency

<i>UK Banks</i>	<i>2002</i>
<i>Cost:Income Ratios</i>	<i>%</i>
RBS	45.6
HBOS	46.5
Lloyds TSB	50.0
Standard Chartered	52.9
Abbey National	53.5
Barclays	53.7
HSBC	55.0
Alliance & Leicester	56.1

Excluding exceptional items, goodwill amortisation and integration costs

Improving Efficiency

RBS Cost:Income Ratio

	<i>Income £m</i>	<i>Costs £m</i>	<i>Ratio %</i>
2002 results	16,815	7,669	45.6%
Transaction benefits achieved	712	1,154*	
Sub-total	16,103	8,823	
Full transaction benefits	890	1,310*	
Illustrative total	16,993	7,513	44.2%

* Cost savings less costs of income benefits

Improving Efficiency

- Further progress possible
- Continue to centralise Manufacturing, where appropriate
- Eliminate duplication, simplify processes
- Specific objectives with income/cost benefits
- Self-financing programme
- Largely insulated from the environmental challenges

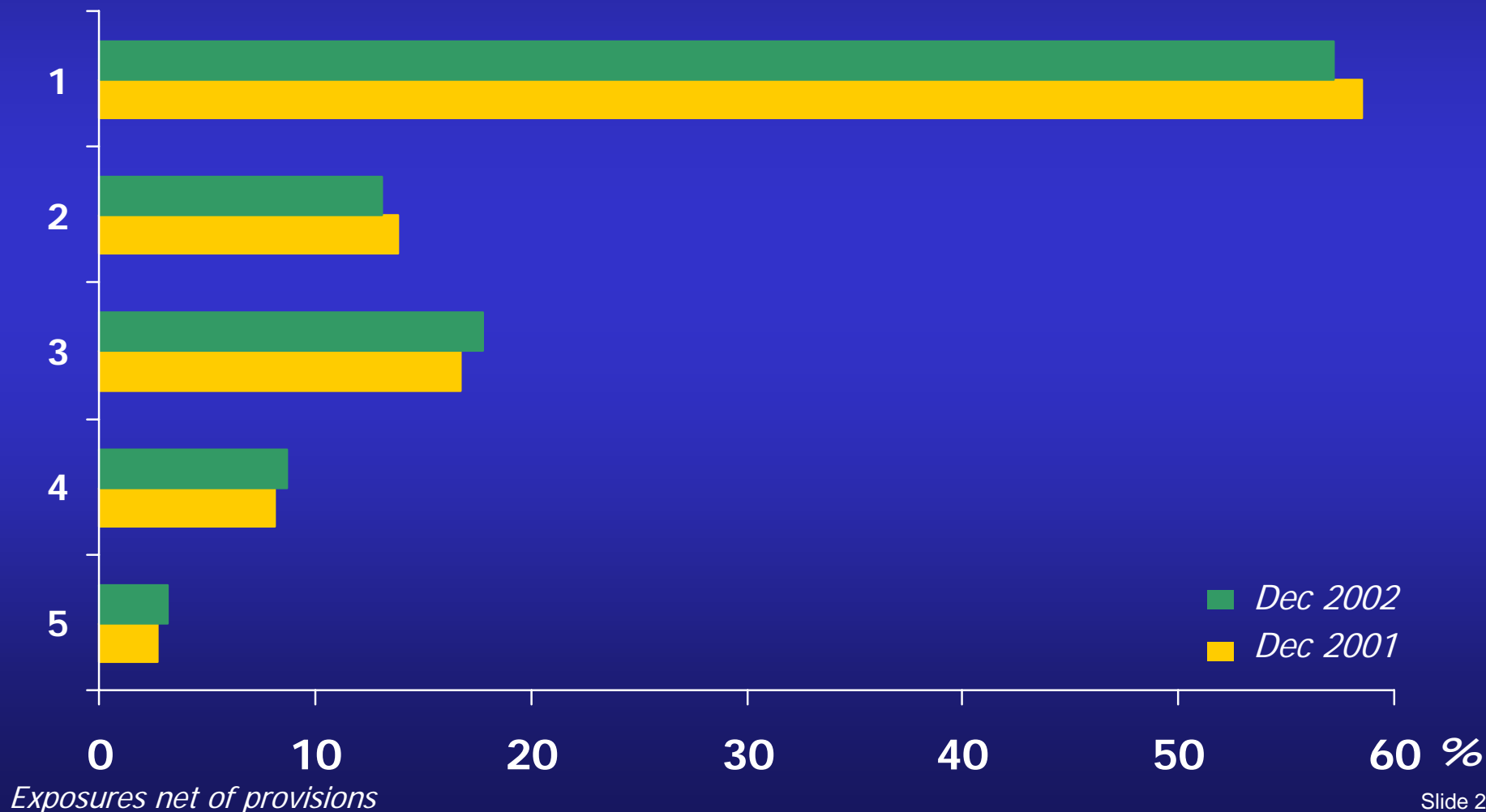
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How?

- Income growth
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- **Good credit quality**

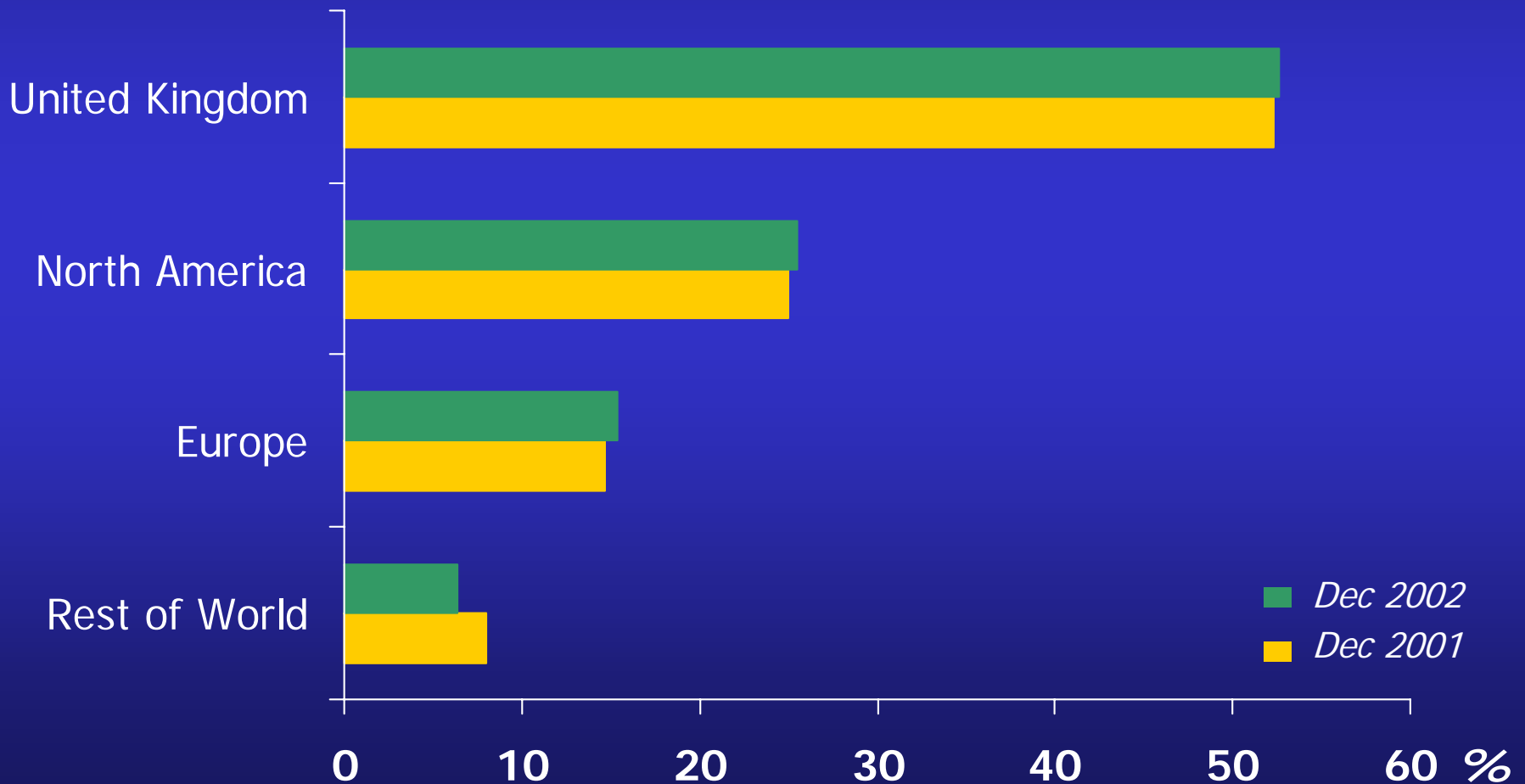
Credit Quality

Group Risk Assets by Credit Grade



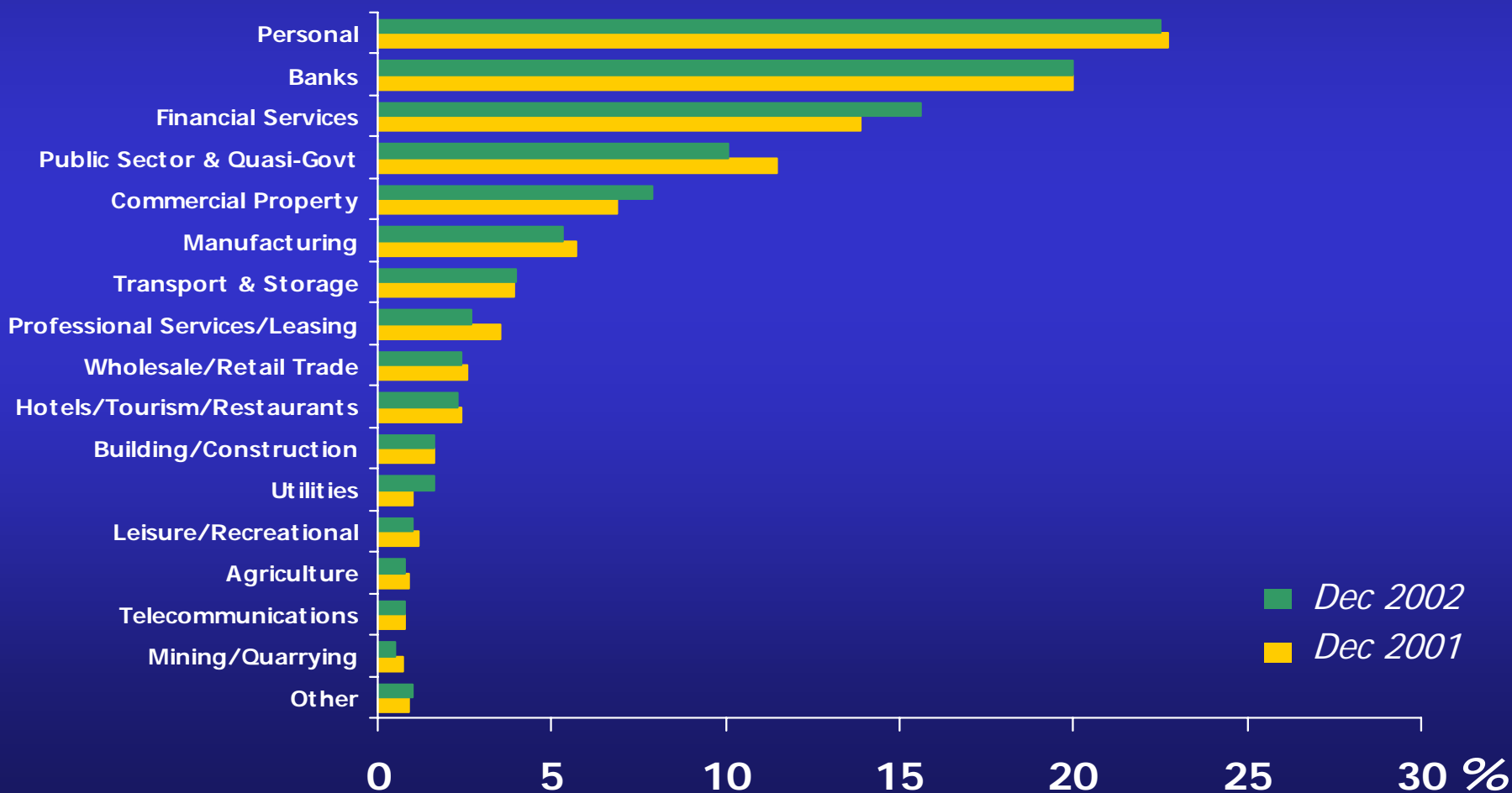
Credit Quality

Group Risk Assets by Geographic Area



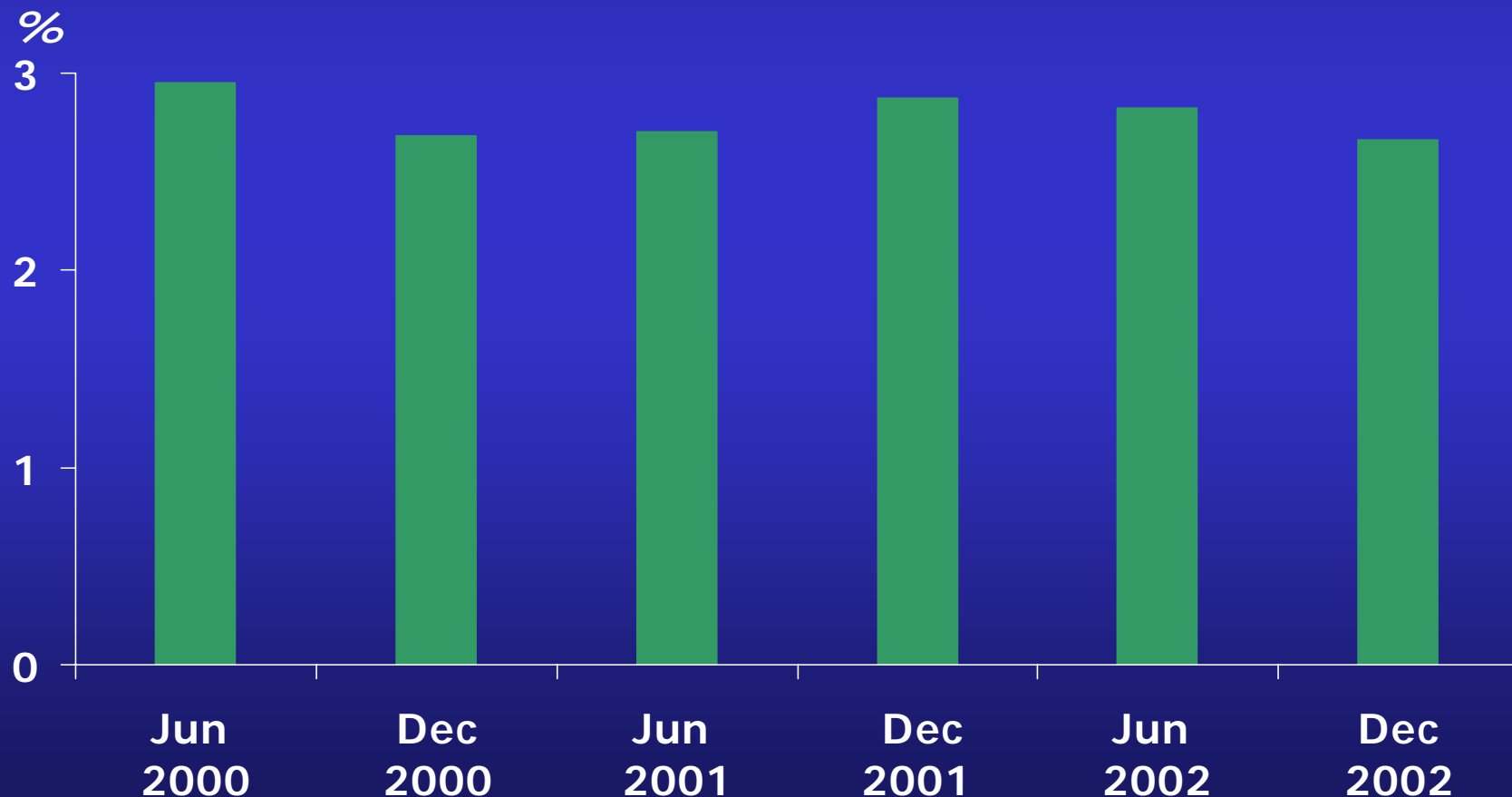
Credit Quality

Group Risk Assets by Industry Sector



Uncertain Economic Outlook

Risk Elements in Lending and Potential Problem Loans as Percentage of Loans and Advances to Customers



Acquisitions

<i>£bn</i>	<i>2001</i>	<i>2002</i>	<i>2003</i>	<i>2004</i>
Gross capital generated	3.5	4.2		
Less non-recurring items:				
Integration costs	0.6	0.7	0.1	—
AVS dividends	0.4	0.8	1.5	—
Total non-recurring items	1.0	1.5	1.6	—
Net capital generated*	2.5	2.7		

* Profit attributable to ordinary shareholders before goodwill amortisation

Acquisitions

- Not essential
- Could be in US, Continental Europe or UK
- Could be small, medium or large
- Maintain bias towards lower volatility
- Meet Group hurdle rate
- If suitable acquisitions not available, consider share buy back

Capturing Value in a Challenging Environment

RBS Outlook

- Continuing superior income growth ✓
- Continuing efficiency improvement ✓
- Maintaining stable credit risk ✓
- Maintaining bias towards lower volatility ✓
- Maintaining options for future growth ✓

Capturing Value in a Challenging Environment

Conclusion

We remain well positioned to continue
to capture value in a challenging environment



The Royal Bank of Scotland Group

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Fred Goodwin
Group Chief Executive