Royal Bank of Scotland
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FORWARD-LOOKING STATEMENTS

Operator: Good morning, ladies and gentlemen. Today's conference call will be hosted by Ross McEwan, RBS Chief Executive. Please go ahead, Ross.

Ross McEwan: Thanks very much, Cath, and thanks for joining the call. You've seen our RBS Q1 results today. Two months ago I set out a plan for RBS, focused on building the number one bank for trust and service in the UK. The results we are posting today show the steady progress that we're making, making this a much simpler, smaller and fairer bank.

As you all know, we still have lots of work to do and plenty of issues from the past to reckon with. You will see that we've also started to cut costs out of the business so that we can invest in what matters to our customers. Again, a good start to a process that we are determined to maintain.

Following the announcement of our new strategy in February, we have moved from seven divisions to three customer businesses, personal, commercial, and corporate, and put the executive teams for these new businesses in place.

From the half year, we will change reporting structures so that you can see how these businesses are performing, both against customer metrics and against shareholder returns.

And we've started to deliver on the commitments to customers we made on February 27 as well. I said we'd call time on teaser rates and zero balance credit card transfers. These things erode the trust of our customers, and that is exactly what we've done.

We have to ensure that the pricing across the Bank is consistent for personal customers and we're committed to ensuring this is the same for small business customers by the end of this year.

We are also making good on our promise to be a much simpler bank for our customers. We have already reduced by a quarter the number of personal and small business products and, by the end of the year, we'll have cut this by half. These steps have set out our direction for the future as a smaller, simpler and smarter bank that is easier and reliable to do business with. And I look forward to highlighting further progress towards the goals, as we move forward.

Before I hand over to Nathan, I've just got one important issue I know you will be interested to hear about, is the decision taken by our major shareholder regarding the remuneration and the one for one bonus cap.

CRD IV clearly gives shareholders the right to direct policy in this area and we understand the difficult position that has put our major shareholder in. We're not going to pretend that this is ideal, as our statement made clear last week. Not having this flexibility involves an element of risk, but this is a risk that we will manage.

I'd like to pass over to Nathan, but also to acknowledge that this is Nathan's last results session with me. Nathan, I think, has done an excellent job and played a key role as part of our strategic review and I'd personally like to just thank him for his efforts in making this a better Bank for customers and shareholders.

As you know, Ewen Stevenson starts with us May 19 and there'll be a good handover between the two of them. But Nathan, over to you for your last set of quarterly results.

Nathan Bostock: Thanks very much, Ross; appreciate it. Joining me today are Richard O'Connor, our Head of Investor Relations; and Rajan Kapoor, our Financial Controller.

I will offer some brief comments on our first quarter results before leaving plenty of time for us to answer your questions.

The key features of the quarter were; we reported a first quarter attributable profit of GBP1.2 billion, up over GBP800 million on a year ago.

Ulster Bank returned to a small profit, the first time for five years.

RCR reduced RWA equivalents by GBP14 billion.

We've reached agreement with the government for the future retirement of the dividend access share. Independent shareholders will get to vote on this at the upcoming annual shareholders' meeting on June 25.

The first quarter has seen an improved performance across the businesses. We've benefited in the quarter from several favorable one-off items, including AFS gains and the absence of negative, above or below the line, charges.

While we see encouraging early signs of momentum, we know we still have a long way to go and expect to face further headwinds in the coming quarters. As a consequence, we caution on a full-year read-through from the first quarter's results.

Turning to our Q1 financial performance and the key lines of the P&L. Q1 total income of GBP5.1 billion was down 2%, compared to Q1 2013, but up 28% on the fourth quarter.

Versus a year ago, higher income in UK Retail, UK Corporate and AFS gains was outweighed by revenue declines in Markets and International Banking as we right-sized these businesses.

Net interest margin improved 18 basis points year on year, and 4 basis points quarter on quarter, to 2.12%. The year-on-year move is driven by re-pricing initiatives across a number of divisions.

Costs improved 6% year over year and 2% on the prior quarter. The year-over-year cost reduction reflects good cost control in retail and commercial, as well as progress on the right-sizing of Markets.

Staff expenses were down 10%, driven by headcount reduction and a decline in variable compensation.

Our Q1 cost performance is flattered somewhat by the absence of a number of the one-off costs seen in Q4.

We are working hard to implement the new cost reduction plan and expect the benefits to begin to accrue in the second half. We reiterate our plan to reduce total costs by GBP1 billion this year. Restructuring costs relating to these changes will be reflected over the coming quarters.

The cost/income ratio for Q1 improved, year on year, by 2 percentage points to 66%, as costs reduced faster than income.

Impairments improved further in Q1 2014, down 65% on a year ago.

Ulster Bank saw a strong improvement in impairments, reflecting improving mortgage arrears and rising house prices.

UK Corporate impairments benefited from the absence of large individual cases, while RCR saw partially offsetting recoveries of circa GBP100 million.

Group coverage of non-performing loans remained strong at 65%, up 13 percentage points year over year.

Q1 operating profit of GBP1.5 billion is more than double the Q1 profit a year ago. As mentioned, we recorded a Q1 attributable profit of GBP1.2 billion, reflecting improved cost and impairment performances.

Tangible net asset value per share was 376p, up 13p from the year-end. The medium-term outlook for TNAV remains sensitive to timing of restructuring costs, RCR disposal costs, and the extent of further legacy conduct and litigation costs.

Looking at the highlights from our businesses; retail and commercial's Q1 operating profit of GBP1.4 billion was up 36% on a year ago. This increase was seen across all the retail and commercial businesses, with the exception of Citizens, which was also impacted by the strengthening of sterling versus the dollar.

UK Retail and UK Corporate Q1 performance improved year on year, driven by stronger revenues and improved impairments. Both these businesses saw balance sheet growth in the quarter.

Net mortgages grew by GBP1.2 billion, while SMEs drew down GBP2.4 billion of new loans in Q1, up 23% on Q1 2013.

Markets' operating profit of GBP318 million increased 14% year on year. Q1 revenues were down 8% on Q1 2013, and include some gains on deleveraging and de-risking the business in the quarter.

Costs were down 15% over the same period, as the reshaping of the business continues.

Markets' RWAs were GBP87 billion at the end of the quarter.

RCR got off to a strong start in its first quarter. Operating losses were held to only GBP114 million, while funded assets declined by GBP4.6 billion, or 16%, to GBP24 billion, including GBP2.4 billion from run-off, and about GBP1.9 billion from disposals.

RWA equivalents were reduced by GBP14 billion in the quarter, to GBP51 billion, reflecting good disposals performance.

Turning to capital, we finished the quarter with a fully loaded Basel III Core Tier 1 equity ratio of 9.4%, up 80 basis points on the last quarter. The improvement includes 30 basis points increase from retained earnings, and 30 basis points gain from RCR reduction.

RWAs were down GBP15 billion quarter on quarter, to GBP414 billion, with RCR acting as the main driver. We reaffirm our 2016 target of a fully loaded Basel III Core Tier 1 ratio of greater than 12%.

Our leverage ratio was 3.7%, an improvement of 20 basis points in the quarter. And we continue to target a medium-term leverage ratio of greater than 4%.

Before I hand back to Ross, I want to add that we're making good progress in transitioning to our new, three-segment business structure, and we will be reporting on this basis from the next quarter. We will publish, though, the restatements ahead of the Q2 results.

Operator, can we have questions, please?

Operator: And your first question comes from the line of Chirantan Barua from Sanford Bernstein.

Chirantan Barua: I just had actually one quick question on Ulster. There's been lots of speculation on corporate finance activities out there, about private equity floating that business. So why are you pressed to do anything with that business, and why wouldn't you just let it run organically, now that it has turned positive? Some clarity would be appreciated. Thank you.

Ross McEwan: Thanks very much for the question. We did examine the running of it just on its own. When you've taken out RCR, when you examine the size of the tracker loan book, which gives a very, very small, if any, return out of it, and you take the Northern Ireland piece off this, the business itself is only about GBP10 billion to GBP15 billion of RWAs -- sorry, of assets.

That, with the cost base that's on top of it, will not give shareholders a long-term return that is what we'd expect from that sort of business. So we're looking at the optionality around it. And that's what we signaled on February

27. It's our plan, I think, by end of summer, we'll be able to come back and say what the plans for that business are.

But we are looking at all options. It's just too small for the shape of that business today. Our estimation was a very low return on equity over the medium term to longer term for that business if we don't reshape it.

Chirantan Barua: So are you planning to -- so what are the options on the table, Ross?

Ross McEwan: I'll come back to you after summer and let you know those. We either do it with somebody else, or we do it ourselves. But we are looking at options to make that a third bank in the Republic that is a good challenger bank. My view today is, it's just too small to be that. And we do want to stay there and give the services to customers.

Chirantan Barua: Got it. Thank you.

Operator: Chintan Joshi, Nomura.

Chintan Joshi: I've got three questions, if I can take them one by one, please? First one is on RCR. If I look at the run-off this quarter, it's about 8.6%. I just wanted to check if we can expect the run-off rate to be that high over the next coming quarters?

But also, if I look at the disposals, that's about 6.6%, so overall a 16% reduction in total assets. Again, should I expect a fast pace of reduction that you've shown in Q1? Or Q1 is typically a little bit better, in terms of disposals? That's the first one. I'll ...

Nathan Bostock: Let me just pick up on that one. I think it's true that we've had a strong performance in the first quarter. It's been a good period for us, and the markets have been favorable. I think, like all these things, I would caution against reading too much into just one quarter, particularly given the nature of the type of assets that one has to deal with, the relative size of different assets and, therefore, the speed with which taking a large number off versus taking lots of smaller exposures off.

So I would say that we maintain our guidance as it was for over the full period. We certainly are, at the moment, going faster than we had originally put on the glide path. But this type of thing has all the potential to oscillate and to have volatility in the speed. So I wouldn't draw too many conclusions. And again, we reiterate our guidance as well for this year, not only just for the overall period.

Richard O'Connor: Chintan, it's Richard. There were a couple of lumpy deals, one in disposals, one in one-off, in the mid to high hundreds of millions of pounds, and there's not that many of those left. So I wouldn't do the extrapolation on that basis.

Ross McEwan: And you always get the easier assets to get off the books. A great job, this is a very, very experienced team that we've got in RCR, running assets off. We're running about 280 data rooms at any one point in time. It's running well and truly now, but I'd just be a wee bit cautionary; easier assets always come off first.

Nathan Bostock: Yes, the other thing to remember, and again, it's probably relevant for the likes of impairment guidance, is that whilst there has been improving trend in impairments overall, RCR did have some offsets in the first quarter. So if you're looking at our overall impairments number, I would be saying think more of GBP100 million, GBP150 million, probably higher than that as a total, if you're looking to have a more even number of quarters, and that would give you a better feel.

Chintan Joshi: Thanks, that's helpful. Second question is on capital. You've had improvements in both expected losses and DTAs, but if I think about this quarter, positive underlying profit, sorry, positive statutory profit, and that's helped ELs and DTAs to have a positive swing as well, so a bit of double leverage.

But if your guidance is correct, then we should expect this to swing the other way whenever you have these losses come through. Would that be the right way to think about it?

Nathan Bostock: So again, I think you've picked a number of the right components and, obviously, the connectivity of them. Yes, is the short general answer. Think of it that you're moving through the year with the elements of headwinds that we talked about, but countering that, ultimately, will be the pro forma of the first tranche of Citizens. So I think you're in the right type of territory, but a couple of moving parts probably through the year, neither of them that dramatic.

Chintan Joshi: Okay. And finally, UK R&C, if I look at the top line, it's weak, sequentially. If I look at NIMs, they are flat, but the beta's really, or the improvement has really come on the cost and impairment line. When can we expect top line to see some growth in UK R&C? I would have thought this quarter you would already have seen something.

Nathan Bostock: Well, I think on that basis -- I'll let Ross comment on the broader business. Again, I think clearly right on the dynamics. The reality is, we are doing the things we need to do around the cost side. We are getting improvement in the impairments. We have been managing NIM, and so NIM has been improving as the assets haven't been moving up in the past quarters.

But we are starting to see, I'll call it some of those green shoots of asset growth, and particularly, again, our focus on mortgages is already starting to show good progress. So I think general comment, correct; everything is about the timing.

Richard O'Connor: Chintan, you've got to be careful. Q1 v Q4, Q1, there's fewer number of days ...

Nathan Bostock: Exactly.

Richard O'Connor: …net interest income. So really you've got to look at it on a longer-term basis than that.

Ross McEwan: If you look at it on quarter to quarter, from Q1 2013, Q1 2014, we're starting to see the growth in the book, which is nice to see. You're starting to see growth in income for the first time in, I think, about four years. So the green shoots are there.

We are going to be cautious in our growth; we're not going to explode this business. This is a business that we've spent a lot of time on, particularly in the mortgage market, getting our business very secure. But we have seen it start; it's gone through the GBP100 billion of assets now in mortgage. It was up GBP1.2 billion for the quarter. Remembering, too, last year we spent a lot of time training and developing our people. So starting to see the shoots.

Nathan Bostock: So again, if you look at year on year, which I think is a very relevant point, given the number of days' differences between the quarters, then we're up roughly about 4% in income on the retail side, around about 2% on UK Corporate.

Chintan Joshi: Thank you.

Operator: Peter Toeman, HSBC.

Peter Toeman: I was just wondering about whether any of your guidance in the strategy presentation on restructuring costs had changed, because I had a feeling you were looking for about GBP5 billion of restructuring costs over a three-year period. I wondered if you could confirm the quantum and timing of when those will materialize.

Ross McEwan: Peter, first off, we're not changing our guidance on that. The first quarter was a much slower quarter for us in restructuring in the sense that we're building the programme. You'll see the heavier restructuring starting to come through and emerging in Q2 through into the second half of this year, just with the nature of the changes around people, property, reviewing our systems, processes and the like. So I'd stay with that guidance at this point in time. We don't see a change.

So Nathan, timing-wise as well, would you see --?

Nathan Bostock: No, I think keep with the guidance and the timing at the moment, as Ross says. We are in the early parts of this as well. We will, of course, have a real intensity of focus, of looking to get the right return from our restructuring cost. So again, this is something, I think, that you need to wait for a few quarters to get further guidance.

Peter Toeman: Could I also then ask about the RCR and whether the charges that you intimated in previous presentations, whether they might now be somewhat lower, given performance in Q1? Or should one -- is it too early to change?

Nathan Bostock: Yes, so too early. Again, we've given a circa GBP1.5 billion for the year. Again, I would say take that as remaining good guidance. In fact, the general comment would be take the year-end guidance; it has been well interpreted by people and I think it remains very relevant. We've said the markets are better so, again, we will continue to do everything we can in those situations. But the guidance remains.

Peter Toeman: Thank you.

Operator: Michael Helsby, Bank of America.

Michael Helsby: I've got a couple of questions, actually. Firstly, on the Markets performance, I think clearly that's probably surprised everyone. But in the text, you mention there's some gains in rates from derisking, which looked particularly strong versus last year. So I was wondering if you can give us some more colour on that.

Then in UK Retail, the bad debt remains extremely low in your unsecured book. It's just a check whether you're happy that that level is sustainable.

And just on the Group tax charge actually, I think it's 22% in Q1. It's the first time, for a long time, that I can remember it being even close, remotely close, to the UK tax rate. Have we moved over with the RCR? Is that a consequence of that, that we should now think of your tax rate as being closer to that normal 21.5%? Thank you.

Nathan Bostock: Okay, thank you very much. Well, I'll take one and three and Ross will take the retail one. On the Markets side, yes, I think some interpretation of that number is clearly important for you.

So firstly, I think one needs to think, in terms of quarter on quarter, from 2014 to 2013, our Q1 last year was a low number. Remember, we had a lot of the what is happening to the business, etc. type headwinds at that point in time. So in terms of relative to that, you're seeing it coming from a low base.

You're seeing around about GBP100 million of one-off numbers vis-a-vis from the deleveraging side. If you put that into the mixer, it means that the overall FIC element is pretty much in line with the circa 20% down that you're seeing in the European-type banks.

Personally, I think that is a very good performance, given all of the other things that are going on, but I would be, again, very cautionary. Our guidance for the year remains in the GBP2.3 billion to GBP2.5 billion territory for income. So you can see classical first quarter, good in terms of execution, given everything else that is going on. But really do need to think more about the forward trajectory.

Ross McEwan: On the retail bad debts, particularly on the unsecured, good, clean tidy book. It's not growing substantially, nor is that market, but the bad debt side I think are being kept under very good control. That has been a concentration for the team, so good quality book. And I'd expect the bad debt levels to stay about where they are. I don't think you would see any -- there's nothing that we're doing in that business that should see it lift or decline much further than this.

Nathan Bostock: And your third question vis-a-vis tax, again, the short answer would be no. We remain in the situation where there's an awful lot of nuances around tax, given where profits are made, where our losses occur, given the types of expenses which are or are not deductible, and all the rest of it.

So again, I think, typically, we have guided more to the circa GBP1 billion or so in terms of the full year. Again, I would say guidance remains relevant.

Michael Helsby: Thank you.

Operator: Andrew Coombs, Citigroup.

Andrew Coombs: Just one question, please, on your impairment losses; clearly, a substantial improvement there, and you're actually running below your guidance for 2014 to 2016 in terms of the annualized rate. But when I look particularly at UK

Corporate and then at Ulster Bank, you have had some write-backs both in shipping and UK Corporate, and commercial real estate development in Ulster. So just trying to get a feel for what's driving those write-backs. And secondly, how sustainable is this quarter's loan loss provisions?

Nathan Bostock: So again, I'll pick up that; Richard might add comment to it. I think what I tried to do in my comment previously is say that I agree, and I recognize a number of those things. You are getting, as you get further and further through these cycles, of course you do get to the stage where occasionally in that you do have some write-backs; that's a natural part of the length of the cycle. I think, in overall number terms, our overall impairments are round about GBP362 million for the quarter.

I would be saying, think GBP100 million, GBP150 million, more than that, and if you took that as the average for the quarters, then I think you would be in the territory that we would be considering. Impairments have improved. We do think that there are some elements to that, not least, of course, we have set up the RCR, so there is a period whereby, since you moved the higher probability of default assets into RCR, we took one-off forward provisioning against a number of those assets.

So for a period of time there is some, shall we say, slightly more difficulty in getting that clarity, but we maintain as well our guidance of the 40 to 60 basis point territory for the organization. The reason we gave that was to try and help you, if you see what I mean, given that again we've got some noise in the short term. So if you take the 40 to 60 basis points, you take the add-back type number I was talking about, you'll get the right feel.

Richard O’Connor: The only thing I'd add, Andrew, is to say we have GBP100 million for our recoveries in RCR in the total just mentioned. We also didn't have any notable single names; typically you get two or three of those a quarter, we had none of those this quarter. But obviously, over two or three years, you would expect some quarter where you get them and some quarter where you don't get them.

Andrew Coombs: Thank you.

Operator: Chris Wheeler, Mediobanca.

Chris Wheeler: Just a couple of questions on two areas. The first one is just looking at the UK deposits. I think corporate deposits fell about 3% and the loan to deposit ratio crept up a couple of percentage points. And then in the UK they were flat, I think, with the savings down and current accounts up.

I'm just wondering, having seen your competitors perhaps do a little bit better in that area, what would you attribute that. Is that, do you think, part of the noise around the bank early in the year, or is it perhaps more to do with the way that you're managing the changes in those two businesses? That's the first question.

And the second question just is to look at the RWAs in the Markets division. As Nathan said, you went down from just short of GBP100 million by about GBP12.5 billion. I just wondered where the main reduction was by business line?

And related to that, we've seen one or two other banks who are in the securitization business, the asset bank business as you are, seeing an uplift in their securitization RWA on the back of some CVA adjustments. I just wondered if you could tell us whether you'd suffered that, or whether that's something you're concerned about, or whether it's already dealt with? Thank you.

Nathan Bostock: Well, let me go to the last ones first and come back to the deposit one. Firstly, I guess the quick short answer on the CVA side is that we've already taken account of that so we dealt with that historically. So that's good news.

In terms of the GBP99/100 billion to the GBP87 billion that you're seeing, you're absolutely spot on; that is the headline. But what we've done in the IMS is, we've also given a transfer schedule, I think it's appendix 3 Rajan? In appendix 3, you'll see some of the transfers in and out which are, again, that noise around the likes of RCR.

So the Markets numbers are closer to a GBP92 billion to an GBP87 billion, if you exclude the RCR movements. I don't have the specifics in terms of the individual numbers that are below that in terms of the reduction. But it is true that, generally, we will have a lower asset-backed RWA because, again, we have been managing that book. So it's generally across the board in the Markets area, but it's GBP5 billion as the real reduction rather than the headline number.

I guess the other thing just to be aware of is that GBP87 billion is more a clean number if you're thinking of the old legacy concept, etc. So if you think of that more now as a clean number of the RWAs being employed in that business. Again, we expect it to come down further, but that gives you a better idea of what they're employing.

In terms of the deposits, again I think this is one of those things where we have been proactive in managing our re-pricing. It's been one of the things that we have looked to do. But it's also connected to the management of the liquidity portfolio that we talked about previously.

So again, to try and be as helpful as possible on that, as you know we said we had excess liquidity portfolio. We said we were going to look at optimizing that and managing it better, so we have been re-pricing away, particularly the more expensive institutional type deposits in the corporate arena. So that's flowing through; you're seeing that; that's been going on for a period of time.

I guess, on a forward basis, we're about at GBP131 billion now liquidity portfolio. Again, question how much of that really is likely to be reduced further in order to do these types of things. I would say probably think of something in the order of GBP5 billion or GBP6 billion or something like that. Not a very large number.

The reason being, although it looks like we've got the headline size for that, the reality is that we do need to start thinking ahead and our liquidity coverage ratio we think ought to be circa 100% for that. And so we are going to manage across these various criteria. So that's why we tend to be looking at managing another GBP5 billion or GBP6 billion. And again, we will look to manage that relative to our deposits.

Chris Wheeler: But on the retail side, would you expect that to start to pick up again in the second quarter? Because obviously, I get the corporate answer entirely.

Ross McEwan: No, it's fully funded, so I think Les will be just balancing off the liability side of his book now. So I wouldn't see too much change there.

Richard O'Connor: Seen very good growth in current accounts across the board. We'd expect that to continue, but we'll obviously price the savings book to see how we fund the mortgage growth.

Chris Wheeler: Got you, makes sense. Thanks guys.

Operator: Rohith Chandra-Rajan, Barclays.

Rohith Chandra-Rajan: A couple from me as well, please, if that would be okay? First actually, just returning to the margin in UK Retail and Corporate, and following up on Chris' question just on the deposits. Given that you're re-pricing away, or you're re-pricing your deposit book because you don't really need them, I wondered if you could comment on the margin outlook a little bit for UK for those two businesses, given that it's been relatively stable in both in the quarter? Do those moves on deposits lead you to expect some margin improvement from here?

Nathan Bostock: Generally, I would say, think of our overall margin is 2.12%. I think best way of thinking of it is that we'll probably have around about 1 basis point a quarter; might get a quarter with a couple of basis points of improvement. It's that sort of magnitude. We would, generally, think that we've done a lot of good margin management around our retail and corporate book, so those are going to be in that thought process and moving sideways during the year.

I think the only thing I would say is, we are expecting the Ulster NIM to drop reasonably significantly; it could be 25, 30 basis points in the next quarter as we have to deposit circa GBP3 billion or so with the Central Bank. That will be a negative, so I'm giving you the overall numbers net of that. So there will be some elements of small growth, but think of it as small.

Rohith Chandra-Rajan: Sorry, Nathan …

Richard O'Connor: Retail has obviously grown mortgages and less so unsecured. Obviously, that has a negative mix impact on margin, but overall keep it really flat. But risk-adjusted improving.

Nathan Bostock: We think we can manage well that balance.

Rohith Chandra-Rajan: Okay. All right, thank you. And I'm not sure to what degree you'll be able to give an answer to the question, but just in terms of the Markets revenues, agree that the underlying 20% down is a good outcome, and you've talked about some of the one-offs as well, do you have a view in terms of what the revenue performance of the ongoing Markets business is? I appreciate that's not a straightforward question, but interested if you have any insight there.

Richard O'Connor: It's headline GBP950 million, ongoing about GBP900 million. It's in the (multiple speakers).

Rohith Chandra-Rajan: Sorry, so everything else is in R&C?

Richard O'Connor: Yes.

Nathan Bostock: That's right.

Rohith Chandra-Rajan: Thank you.

Operator: Tom Rayner, Exane BNP Paribas.

Tom Rayner: Market reaction very positive today. One thing I sense it liked was the better than expected TNAV progression. I think it's hard to ask this without effectively asking you for some sort of profit forecast, but the progression through the rest of this year and into next year, when you look at, obviously, your underlying earnings but then the RCR run-off, the restructuring charges building up, I guess, as we go through the year; you are still talking about some future litigation risk which may or may not yet have come through.

Can you give me any sort of steer on maybe where you would expect TNAV by year-end versus Q1? There's enough variables there for you not to have to give me an earnings forecast, I think.

And I have a second question just on the stress test, please.

Nathan Bostock: Sure. Again, not going to change our original guidance where we said we expected for the TNAV to move sideways for a period of time with a number of moving parts. I think we used the term headwinds in our script of the results, and so again, it's worth reminding people that there is, indeed, a snapshot of the strength of the core underlying franchises. But it was a clean quarter, so I've already said that the impairments number was probably lower than generally, on a forward basis.

We haven't got the restructuring costs that you would see potentially in future quarters. You haven't got the RCR number running at the same run rate as I indicated, and there, of course, remains some uncertainty around conduct and litigation. So I think you put that into the mixer and I think our previous guidance remains the right sort of guidance for the, I'll call it, for the nearer term.

Tom Rayner: Sorry, Nathan, just to be clear, is that based on the year-end 2013 when you're saying sideways, because obviously you've jumped up quite a bit in Q1 already?

Nathan Bostock: Yes. I'm saying that you should take the guidance we gave at the year-end as remaining as good guidance.

Tom Rayner: Thanks for that clarity. And I guess just on the stress test, you're still comfortable with your go-to targets; obviously, the stress test has injected some more uncertainty into the process. Can you give us any color on what you're thinking, post the methodology announcement from the PRA? Has that changed any of your thoughts re your capital targets and your capital build?

Nathan Bostock: So the short answer, it hasn't changed the thought process. Tried to do an awful lot of forwarding thinking when we originally went through this; that included us looking at a number of different scenarios back in the October and November period in terms of the types of things that might impact.

We carry out these types of stress tests in any case. These types of asset movements, unemployment movements, these types of things are not out of court against the types of stress and macro conditions that you would expect. And, again, the PRA are fully aware of those types of stress numbers and that we run internally, and again, were fully on the table when we agreed our capital plan and our trajectory.

So I say it's a short answer which is, no, I don't think it changes at all what we've put out there.

Tom Rayner: Lovely. Thanks very much.

Operator: Jason Napier, Deutsche Bank.

Jason Napier: Three quick ones, please, if I might? Firstly, the trust and fairness agenda is obviously central to the new strategic plan and I think that's right. Could you talk, perhaps, a little bit about the state of product structure and pricing on the front book? Is it, in Q1, at a place where you expect it to be broadly stable, or is there still further work to be done there?

And then, as you look at the total revenue tally, is there any component that you'd like to call out that relates to a legacy product that is no longer being offered and that you'd expect to taper, that won't be replaced by new revenue? So that's the first one.

Secondly, perhaps some color on where you see product spreads on the asset side, in particular in the UK? One of your large competitors yesterday shared the view that mortgage rates in the UK would continue to fall for the better part of 2014, whether you had a perspective on that.

And then lastly, Ross, you spoke quite a lot at results about your readiness for MMR and the time taken last year around training. Could I just confirm, please, that your underwriting standards, for a long while, have already been in line with MMR; that it wouldn't be your expectation that there'd be any kind of tightening now versus in Q1 or Q4 of last year, at least as far as RBS is concerned? Thank you.

Ross McEwan: Fine. Let's just start with the first one which is about front book pricing. I think we're where we want to be on our front book pricing. I think the big issue for the industry is around back book; that needs to be managed.

Our objective, particularly across the savings-type area, is to have the back book equaling the front book over the next two years, so no major changes on that because you've got the rating all over the place from, as you can imagine, a big portfolio of our business.

So we'd look to bring back book to front book as quickly as we possibly could without destroying value, but it is around fairness for customers. I'd see, on the back end of that, the revenue would stay flat because the pricing is both up and down, so I'd see it reasonably flat from that move. So I wouldn't expect any deterioration in product profitability in the retail bank where most of this will happen.

On the product spreads, I'd see them, particularly on mortgages, slight down. But, look, I'm more optimistic around the flatness of that, and if you have a look at our pricing, some of our pricing around, particularly our SVR, it's not the lowest in the market, but it's pretty well below many of our major competitors on that part of the book.

And our other pricing pretty well matches up, so I think there may be others that probably need to come down. We're probably sitting where we think is a fair pricing for customers.

And, on the MMR, I don't see any changes now to the underwriting standards that we've had in place for quite some time. I think, with any bank, you just need to stay within the risk parameters and your risk appetite statements. I think that's where banks get into strife, that they start moving out and trying to justify themselves moving out of those risk parameters. So I'm pretty comfortable.

Our MMR; we really instigated that first half of last year, and that's why our mortgage book was down, our growth was down fairly significantly. I don't see that we're going to have any difficulties with the implementation of MMR. There will always be some teething on the edges as you move from parts of your business, which is your telephone centers doing non-advice and moving them to advice, but all of our people are now trained.

There's always some movement of having to pull them on and off the phones to keep their training levels and the standards up. But I don't see we'd need to tighten our underwriting any further than we did over the last two years.

So pretty stable, I think, if you're looking there. The big issue for us in our retail bank is getting the growth in the volumes. We've seen the improvement in the margin; now we need to see growth in our volumes coming through, and I've been pleased with what's going on in the mortgages.

Nathan Bostock: One thing I'd just add. I think on the underwriting one, I don't think there's any change in the approach people take to the underwriting standard. I think what MMR does is basically it tries to gain, for both the underwriter and the applicant, a clearer understanding of their cash flow ability, and stressing those cash flows has always been a part of the underwriting standard. It always has to remain the same. So I think it's more to do with that than it is about anything to do with changing your underwriting standard.

Jason Napier: Just perhaps a tiny follow-up. On the front book pricing, getting away from interest rates and so on, just looking at the income by product, it's not obvious where current account fee income sits and relative to perhaps some of the peers that the numbers don't look so big. Is there any pricing changes on late payments and so on that you might be looking to make? And then, which category would those things sit with, within your disclosures, please?

Ross McEwan: Those changes have already been made; they were made last year, particularly around overdrafts. There might be some tweaking that we want to do this year, but most of those changes were done last year so I don't think you'll see major changes in there.

Richard O'Connor: Jason, the current account income is in the personal deposit line ...

Jason Napier: Perfect. Thank you.

Richard O'Connor: -- in the statement. Just on mortgages, Ross, we are expecting increase in our capacity to underwrite new mortgages, so that's in fact an important point as well.

Ross McEwan: The numbers of writers is up well and truly on last year. We started the year last year 325 face-to-face, end of the year at 425, now got 440. I'd say by the end of this year face-to-face we'll probably have another 50 on the road or in our branch network, and growing the numbers on a telephone basis as well. They're fully trained, operating. It takes a lot longer to get the people up; that's one of the issues with MMR, which is fine. You get a better quality you will hold on to the business longer as well, I suspect, over the long term.

Jason Napier: Thank you. That's clear.

Operator: Thomas Rahman, Brown Shipley.

Thomas Rahman: Just a few questions. The first question is on the PPI; I notice that both yourself and Lloyds yesterday have not made any further provisions on the PPI. I was just wondering if you could provide further comments as to whether or not you believe that it had now sort of peaked, and how much more future provisions you would account for. That's the first question.

Nathan Bostock: Shall we take them one -- it's probably best to take them one at a time, if you don't mind?

I think on that one what I would say is, we obviously look at this very closely. We look at the methodologies that we've used and the modeling forward, and I think that there is seasonality in these numbers, which you do expect. There is still a little bit of noise from the past business review where I think it's true that probably numbers remain slightly higher than people would have thought. But I would say, in the general broader PPI, they're perhaps a little lower. So for us, certainly at the moment, the numbers very much stay in line with the type of modeling that we did, and that modeling does clearly, over a period of time, come down.

Thomas Rahman: Okay. Thanks. My second question was in relation to the stress test. I was just wondering if you could provide more color on that. You would expect some banks within the UK to actually feel the stress test. If all the banks passed the stress test then it wouldn't really be a stress test. What is your view on RBS; would you believe that you could pass the stress test? And it ties into another question that I had.

If the Bank of England raises interest rates next year, how would you believe that would affect RBS, given that yes, your net interest margin may increase, but then again, your impairments may increase as well, given that number of borrowers may struggle to pay interest, given that there may be a higher interest rate? So any further color on those would be appreciated.

Nathan Bostock: Okay, let me just do the stress test. On that I'm not going to give any broader comment. I think that the stress test, you're right to think that it, clearly, has to be an effective one from the regulator's point of view. So it needs to move more into -- I'll call it the extreme rather than just a one in 7, one in 10 year, even one in 15 year type scenario for it to do its job. I think these are the types of things that banks have been considering now for periods of time, and it's all been part and parcel of the capital re-strengthening that you've been seeing. So I think it's a good -- banks are generally in the UK ahead of the curve in terms of balancing those things up.

From a real absolute, it's a low bar that they'll be looking to actually effect. I think it's about 4.5% is the stress bar. From that perspective, you have to burn up one year's earnings plus capital to get there. I think they will have to, say, tread a fine line to be able to make the thing as effective, because it has to be an extreme, but it also has to have the realism that goes with it.

Your second question, in terms of the interest rates. Again, we do model this type of thing, as you would expect; generally rising rates is a positive for retail and commercial type banks. I would say, think of it more in the circa GBP500 million, GBP700 million type territory, probably, for ourselves. You may get a bit of movement in impairments but, typically, the impairments one tends to be relatively short-lived as typically smaller companies, and that can overstretch themselves. But as you go through that, you still retain the earnings that come with the uplift from rates in general, and those impairments then normalize.

Richard O'Connor: And the majority of our new mortgage business is on fixed rates. So the earnings benefit you get from the deposit side and you're protected somewhat on the asset side.

Operator: Joseph Dickerson, Jefferies.

Joseph Dickerson: Just a couple of quick questions, please. Firstly, on loan growth, if I look at slide 11 in your slide deck, you've talked about the growable book within corporate which seems to be up, relative to the run rate. And then in mortgages, you're showing the 21% increase quarter on quarter in applications. It looks like loan growth in mortgages was plus 1% year over year in terms of your balances. I'm just wondering what's the trajectory in each, particularly, I suppose, in the mortgage piece, what's the trajectory going into the end of the year?

Ross McEwan: If the market stays in the condition it's in, I'd like to see the growth stay at about those levels. We've got more people on the road, talking to customers, so we're building capacity inside the business and we have been doing that over the last 12 months. So I'd think you'd see that growth continue, quarter on quarter, as the year progresses.

On the corporate side, we are starting to see more growth in the small end of the market which you're starting to see on the growable book. I have warned people that we've still got some of the non-growable book that's going to come off, particularly commercial real estate, as we realign that portfolio. So there's still a bit of commercial real estate coming off.

It's good to see some slight growth in that book, and I would see that continuing but I wouldn't get ahead of myself, knowing that we've got the commercial real estate coming off and other banks will be picking that up in their growth figures.

Joseph Dickerson: Thanks.

Ross McEwan: Thanks very much for your time today. I think that's all we have time for questions. I know Richard and his team are very happy to take questions that you have. We've got a good quarter from us, but we're being realistic about the fact that we've got a big restructuring program on.

We had a good quarter out of RCR but, as we've said, Nathan's reiterated, some of the easier bigger assets start to go out first and you get into a lot of more gnarly assets as time goes on, but we were delighted with that performance. So we're looking for -- it won't be probably as easy in the next three quarters, given the work we've got on the restructuring of this business, but a good start to the year. Thank you for your time.

Nathan Bostock: Yes, thank you all very much.

Ross McEwan: And Nathan, again, well done. Nice to go out on a good result. Cheers, thank you.

Operator: Thank you, ladies and gentlemen, that will conclude today's call. Thank you for your participation, you may now disconnect.

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