



Conference Call 26th January 2017
Moderator: Ross McEwan

FORWARD-LOOKING STATEMENTS

This transcript includes certain statements regarding our assumptions, projections, expectations, intentions or beliefs about future events. These statements constitute “forward-looking statements” for purposes of the Private Securities Litigation Reform Act of 1995. We caution that these statements may and often do vary materially from actual results. Accordingly, we cannot assure you that actual results will not differ materially from those expressed or implied by the forward-looking statements. You should read the section entitled “Forward-Looking Statements” in our announcement published on 26th January 2017.

Operator: This is conference # 60246489.

Good morning, ladies and gentlemen. Today's conference call will be hosted by Ross McEwan, CEO of RBS. Please go ahead, Ross.

Ross McEwan: Good morning everyone and thanks for joining Ewen and I this morning, especially at such short notice. We'll take questions shortly, although we will be constrained in what more details we can actually share with you.

First, I'd like to talk you through this morning's announcement. I thought it was important that you heard from Ewen and I so that you can provide some clarity on what has been announced.

Today we are announcing a further GBP3.1 billion, or \$3.8 billion provision in relation to RBS's various US residential mortgage-backed securities investigation and litigation matters. We have considered it appropriate to take this provision in the context of our ongoing cooperation with the civil and criminal investigations of the Department of Justice, as well as other RMBS litigation matters. However, it is important to stress that we have not yet reached an agreement with the Department of Justice.

The provision will be reflected in our full year results, announced on February 24 and takes our aggregate provisions for such matters to GBP6.7 billion. This, of course, is a very large number, however, it does reflect the legacy of a time when RBS lost its way as it embarked on a quest to build a global bank. And as part of this misplaced global ambition, RBS, through its RBS Greenwich Capital business, was very active in the US RMBS market, where it acted as an issuer, sponsor and an underwriter.

It's clear to me that RBS became detached from the customer-focused values that have to underpin and be at the heart of any bank. This bank and, of course, the British taxpayer paid a very high price for this decision -- these decisions that were made before the crisis. Today's announcement is yet another painful example of the cost of that legacy.

It's important that today's announcement is also viewed against the backdrop of a very real progress that RBS is making in the implementation of our

strategy. And one of the first decisions I made as CEO was to exit out US-based RMBS origination and trading activities. This exit was completed in 2015.

I'll now hand over to Ewen for some comments.

Ewen Stevenson: Thanks, Ross. We talked for some time about our various US RMBS exposures. Two parts, just as a reminder, a number of outstanding litigation claims, the largest piece of which is FHFA. And several ongoing investigations both by the US Department of Justice and various state attorney generals.

Today is an important step in making further progress in addressing the financial costs of our remaining legacy issues. Q4 2016 results will now include an additional \$3.8 billion, or GBP3.1 billion US RMBS provision and to put that provision in context, on a pro forma basis, had we taken the provision into our Q3 2016 results, TNAV per share would have been reduced by 27p to GBP3.11 and our core tier 1 ratio by 135 basis points to 13.6 percent. To declare this provision does not directly impact the distributable reserves of RBS Group plc.

In total, this takes our US RMBS provisions as at the end of Q4 2016 to \$8.3 billion, or GBP6.7 billion and this relates to both the outstanding litigation and the ongoing investigations.

You'll also see in the release significant health warnings. To be very clear, this announcement is not due to us resolving any further of our US RMBS exposures and as a result, there could be material additional provisions in due course. And as set out in the RMBS and our existing market disclosures, I would emphasize that the timing and eventual outcomes continue to remain uncertain.

As a reminder, we'll be back to you in four weeks' time on February 24, with our full year 2016 results.

And with that, I'll pass back to Ross to host some Q&A, but please do note we'll be constrained on what more we can say at this point.

Ross McEwan: Thanks very much, Ewen. Laurence, let's open the line up for some questions please.

Operator: Thank you, Ross (Operator Instructions). Your first question today comes from the line of Raul Sinha of JPMorgan. Please go ahead and ask your question.

Ross McEwan: Hi, Raul.

Raul Sinha: Morning Ross, Morning Ewen, just three quick ones from me please. The statement actually doesn't say how much of the \$3.8 billion is specifically for DOJ. So I was wondering if you could comment on that and maybe give us any detail, if possible at all, on the assumptions you might have used to get to the \$3.8 billion.

Then I've got a couple more, I don't know if you want them straight up, but I'd like to know how you would plan to treat any customer relief going forward, if there was going to be any, from an accounting perspective.

And then thirdly, would this charge actually help you in the stress test later this year, if there wasn't a settlement by the time of the stress test? Thanks.

Ewen Stevenson: Yes, so look, we haven't broken out, either in our existing provisions or the new provision that we've taken today, the split between the Department of Justice and other regulatory investigations and litigation. I think we told you in the past that the majority of the existing provision relates to litigation, particularly FHFA, so -- but I think we've been very clear in the release that not all of today's provision relates just to the Department of Justice.

Raul Sinha: OK.

Ewen Stevenson: I think it's very speculative at the moment to comment on -- we continue to cooperate with the DOJ, we're in discussions, not in any form of adverse negotiations. So it's sort of speculative, I think, for us in terms of what that

final settlement and form of settlement may be and how we would ultimately treat it for accounting purposes.

Ross McEwan: The same would be, Ewen, on the issue of consumer relief. It would just be sheer speculation on the form of any discussion, so we wouldn't make any comment on it.

Ewen Stevenson: And then in relation to the stress test, I think Raul, there's a right way to think about this. Obviously within our capital planning assumptions for many years there's been assumptions on settlement costs and US RMBS provisioning, which would have also been reflected as part of last year's stress test. Today's announcement doesn't involve us closing down any of that exposure, so it would continue to be in our capital planning assumptions and continue to be within the stress test analysis for this year. So I don't think this alone would change anything in that respect.

Raul Sinha: OK, perfect. Thanks very much.

Ross McEwan: Cheers, Raul.

Operator: Thank you and your next question comes from the line of Joseph Dickerson of Jefferies. Please go ahead.

Ross McEwan: Good morning, Joe.

Joseph Dickerson: Hi. Good morning, how are you? Just a quick one, this is basically similar to Raul's. I was just wondering how you arrived at the \$3.8 billion number. It's fairly precise, so I guess, what drove the calculations? Was it looking at what others have done with, for example, DOJ? Because presumably whilst you haven't carved that out for us, it's presumably a material piece of the settlement. So I'm just wondering how you arrived at this kind of precise number? Thank you.

Ross McEwan: Yes, thanks, Joe. Look, for obvious reasons, I won't go into any of the detail really around that. As a Board, we just believed that was the appropriate

provision to take at the time in relation to the investigations and other RMBS-related litigation matters.

We, of course, did note the recent settlements announced by other European banks in respect to it and you do take some guidance out of that as you look at making your own provisions. But I'm really unable to give you any more additional details at this time.

Joseph Dickerson: Thanks.

Operator: Thank you. Your next question today comes from the line of Chirantan Barua of Bernstein. Please go ahead and ask your question.

Ross McEwan: Hi, Chira.

Chirantan Barua: Morning, Ross. Just a quick one, Ross and Ewen, on how should we think about your core tier 1 ratio requirement once this is all done and settled? Obviously you're much closer to this right now. In the past, Ewen, you've told us a 13 percent core tier 1 ratio, that obviously includes the regulator would put certain assumptions around your litigation provisions and things like that. So once this is done, so 2018 let's say, what is to your best understanding the core tier 1 ratio that you'd want to run the Bank at?

Ross McEwan: Yes, I don't think anything -- that's always been, Chira, a medium-term target for us, the 13 percent core tier 1 target. So -- but I think it always factored in that we -- it was effectively a post-legacy cost core tier 1 target for us.

And in addition, I think we continue to have significant regulatory uncertainty around RWA rules at this point. So we'll have to see how all that plays through in the next couple of years. But for the time being, under the existing RWA construct that we operate under, we're comfortable that 13 percent is the right target for us medium term and as and when we're able to do so, we will seek to optimize our core tier 1 ratio to that level.

Chirantan Barua: Just a quick follow-on on that, so Ross, how should we think around the dividend assumption? In the past you've said US RMBS litigation and

Williams & Glyn, these are the two big factors before you start. 13.6 percent against 13 percent doesn't look that healthy.

Ross McEwan: Well, as we've given you the health warning on, this isn't the final number here. So let's get to the resolution of it before we get to that point. And the other thing to remember, the other factor we've always put into our disclosures and conversations with you is about the stress test and making sure we do pass well a stress test before we get into any discussions with our regulator about resumption.

Ewen Stevenson: But Chira, as you know, I think when you -- we're continuing to run down capital resolution, which is a capital accretive exercise for us, given the RWA, less the disposal costs we expect to take. And the core underlying business over the last seven quarters has made about GBP7.5 billion pre-tax.

So again, the core business is very capital accretive too. So we do expect that the business model is going to -- the natural business model that we're creating is going to continue to be capital accretive over the coming years.

Ross McEwan: Which was the plan we set up back at the beginning of 2014. I'd get through these issues first and through a stress test and we'll be updating you on the look forward for the next three years on February 24 as well, Chira, when we do our results.

Chirantan Barua: Perfect, thank you.

Ross McEwan: Cheers.

Operator: Thank you. Your next question comes from the line of Ivan Jevremovic of UBS. Please go ahead and ask your question.

Ross McEwan: Hi, Ivan.

Ivan Jevremovic: Hi, good morning. I just have a question more specifically coming back to is there any potential consumer relief, just to help us to understand because I'm sure you've been spending a lot of time thinking about the potential

ramifications of the settlement and we have seen elsewhere that consumer relief can make up to around half of the headline figure.

So if consumer relief might mean loan modification and you find yourselves in need of having to buy loans that need modification, presumably they come at below face value and therefore, that might lessen the net financial impact for you. Could you clarify how something like that might work please? Thank you.

Ewen Stevenson: Yes, Ivan, I think we're trying to over think things at the moment. As we said earlier, we're in ongoing discussions, we're cooperating with the DOJ, we're not in any form of active negotiations. So I think it's just highly speculative to assume what the nature of any settlement could be with the Department of Justice, what the form of that settlement is and what the accounting consequences would be. So we're not at a point where we could even speculate on that issue.

Ross McEwan: No and nor should we.

Ivan Jevremovic: Understood, thank you very much.

Ross McEwan: Cheers.

Operator: Thank you. Your next question comes from the line of Tom Rayner of Exane. Please ask your question.

Ross McEwan: Hi, Tom.

Tom Rayner: Good morning, chaps. Just something confusing me a little bit. For quite a long time you carried no provisions against the DOJ because of the uncertainty, but you say it still remains pretty uncertain, no settlement's actually been reached. I'm just trying to get a feel for what has changed which has allowed you to make this provision.

And thinking about what maybe one of your peers has done, if the final settlement is too extreme, is there still an option that you might turn it down and go to court? I'm just trying to get a better understanding of that.

And also, where you mention the adverse consequences, you mention your market disclosures but I wonder if you could just add a bit of color to what you think in the final outcome those other adverse consequences might be.

Ross McEwan: First off, just going back to what we are announcing, just as a provision today and the Board just thought it was appropriate to make this provision of this number at this time. We gave the health warning about I think some way to go yet to tidy up all of the RMBS issues and as I say, we are cooperating with the DOJ. But we're not in any form of anything other than that.

I think it's just too early at this stage to be speculating, but the Board did as one of its factors consider what the other settlements had been made, ones closer to home, particularly around the European banks. And we felt it was in a position to be able to do this today.

Tom Rayner: OK and just on -- I mean, I guess you probably can't answer this. I mean, I guess there is a level at which you would refuse to settle and perhaps go down other legal options.

Ross McEwan: Yes, look, at this stage today I won't comment on that. So we are cooperating and let's see what the outcome is.

Tom Rayner: OK. And the adverse consequences, I'm just trying to get a feel, is that impact on RWA and things?

Ross McEwan: They're pretty well covered under the risk factors in the annual report, no real change -- I don't think there's any change to those at this stage today, other than the announcement of a provision.

Tom Rayner: OK, right, lovely. Thanks a lot.

Ross McEwan: Thanks.

Operator: Thank you. Your next question comes from the line of Paul Fenner from Societe Generale. Please ask your question.

Ross McEwan: Hi, Paul.

Paul Fenner: Hi, morning, gents. I just wanted to understand a little bit the accounting around the available distributable items. The language is a little bit ambiguous in the sense that there's no direct relationship.

Does that mean there's no relationship? How do you avoid it and is it because it gets paid out of the US subsidiary? And does it mean that there's no impact at all? I just want to get an understanding of that, thanks.

Ewen Stevenson: Yes, obviously in coming up with the adjustments we made to distributable reserves in Q3, we did value and used calculations for various subsidiaries. Within that there were capital planning assumptions on US RMBS settlement costs, so it says -- what it says is there's no direct impact when those settlements are finally made, depending on what the total quantum is at that point.

But within today's announcement, there's nothing there, I think, that would change our views on the reasonableness of our current distributable reserves. But until those final settlement costs align and working through the value-in-use calculations, we can't say that there's no indirect consequence.

Paul Fenner: OK.

Ross McEwan: Just to complete that, we continue to work on the basis that we will be putting to shareholders at our AGM this year a capital reorganization to create additional distributable reserves.

Paul Fenner: Very good, thank you.

Ross McEwan: Cheers.

Operator: Thank you. Your next question comes from the line of Tamara Burnell from Legal & General. Please go ahead.

Ross McEwan: Hi, Tamara.

Tamara Burnell: Hi, actually both of my questions have just been asked by the previous two people. So it sounds like you've got nothing further to add, thanks.

Ross McEwan: Thanks very much.

Operator: Thank you. Your next question is from the line of Andrew Coombs from Citigroup. Please go ahead.

Ross McEwan: Hi, Andrew.

Andrew Coombs: Good morning, a couple of questions. One I apologize for repeating, but can you just confirm that the \$3.8 billion provision, is that just cash, or have you factored in a borrower relief component within that as well?

And the second question is could you just confirm what's the tax treatment on the provision? Thank you.

Ewen Stevenson: Yes, on the second one, I think you should assume that it's pre and post-tax, i.e. that post-tax impact will be the \$3.8 billion. On the first question of the cash it's, yes, again, just to repeat and confirm, we're not in any form of active negotiations with the Department of Justice. So I guess in your terminology think of it as a cash cost.

Ross McEwan: Yes, I was going to say think of it as straight out cash, as opposed to anything -- any construct.

Andrew Coombs: Just the cash component, OK.

Ross McEwan: Yes, it's a straight-out provision.

Andrew Coombs: Thank you.

Ross McEwan: OK.

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

Ross McEwan: Thanks very much. And look, thanks very much for joining us and thank you for your questions and taking the time this morning. In closing, I'd just like to remind you that we've been actively building capital, as you know, so that we had capital here for the number of legacy issues we had to still deal with. And the largest one, that we've been very clear about, has been in relation to RMBS.

Once these issues are behind us, we can focus 100 percent on our efforts on improving this bank and getting the core of this bank in even better shape than it is today and serving our customers better. We do look forward to catching up with you on February 24, which is our full year results, so looking forward to that and talk to you in about a month.

Ewen Stevenson: Yes, Ross.

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

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