



THE ROYAL BANK OF SCOTLAND
Moderator: Ewen Stevenson
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FORWARD-LOOKING STATEMENTS

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OPERATOR: This is Conference #54462050

Operator: Good afternoon, ladies and gentlemen. Today's conference will be hosted by Ewen Stevenson, Chief Financial Officer of RBS. Please go ahead, Ewen.

Ewen Stevenson: Thanks, hi. It's Ewen here and thanks a lot joining the call particularly at short notice. I was planning to talk through some of the detail in relation to the announcement that we put out in the last hour, and then open up for your Q&A.

You'll appreciate for legal reasons though above and beyond what's in that announcement. There's a limited amount I can say and I've got no update at this point in relation to the Department of Justice.

As you've seen, we've just reached agreement with the Federal Housing Finance Agency or FHFA. This concludes several months of close negotiations that we flagged as part of our Q1 results.

The headline settlement with FHFA is for £4.2 billion or \$5.5 billion. It relates to approximately \$32 billion of U.S. RMBS securities issued over the period from 2005 to 2007.

As we have indemnity agreements with third parties, for \$754 million, the net cost to us of the settlement is just under 4.75 billion. So, we'll take an additional provision of \$196 million or £151 million as part of our Q2 results.

At Q1, we had total U.S. RMBS provisions of \$8.3 billion. Post the FHFA settlement, this will reduce to some \$3.7 billion of residual provisions, of which, the great majority relate to Department of Justice.

The magnitude of this settlement, is clearly difficult and humbling to have to announce, but does represent resolution of one of our last large legacy issues. We were one of 17 financial institutions to have now settled RMBS claims filed by FHFA.

We've known; and we've been very public and saying the settlement was coming. And despite the size of this settlement, as you can see from today's announcement, this was very much in the region of what we've been anticipating.

So, we'd already substantially provided for it. Coming off the back of the 2008 rights issue shareholder litigation, today's settlement shows our continuing determination to put our last few remaining legacy issues firmly behind us.

However, before we can draw a line under our U.S. RMBS exposure, we've still to resolve some small remaining litigation and several on-going regulatory investigations, including with the DOJ.

But at this point, I've got no further update on where we stand with the DOJ. And I'd also caution against any read across from today's settlement to any potential Department of Justice settlement in due course.

With that, I'll open up to your questions. Again, just to caution, I'm limited from a legal perspective from what I can say beyond what I've just covered. (Alex), if we could now open up please for Q&A?

Operator: Thank you Ewen. Ladies and gentlemen, if you would like to ask a question, please press the "star" key followed by the digit "1" on your telephone keypad. We will pause for a moment to give everyone an opportunity to signal for questions. OK, and we have a question from the line of Joseph Dickerson from Jefferies.

Joseph Dickerson: Hi, Ewen. Thanks for taking my call. Could you just discuss, if you can, withdraw of the calculation of the \$5.5 billion settlement. And I know you mentioned that was in line with the provision that you had on the balance sheet.

However, if you look as a proportion of the OPB that was sold to the GSEs, it's quite a bit higher than some of the other major banks. I was wondering what drove the calculation of that number, if you could give us any color on that, that would be useful. Thank you.

Ewen Stevenson: Yes, so on a gross basis, Joseph, as you said on OPB, it was just over 17 percent and on net basis just under 15 percent. It is at the high end of all the settlements, that we acknowledge but these things very much a matter negotiation.

They're very much dependent on the individual facts of each case and very much dependent on actually case law that exists at the time and the strength of the respective positions of both counterparties. So we acknowledge, its at the high end, equally, we're very happy to have it resolved.

Joseph Dickerson: Certainly, certainly, but good to have it out of the way. Thanks.

Operator: Thank you. The next question comes from the line of James Invine from SG. Your line is open.

Ewen Stevenson: Hi, James

James Invine: Hi there, good afternoon. Can you just tell us please, how this will with your stress test results that will be announced in Q4 today?

So obviously the stress test is done on the 2016 balance sheet and this was a risk of the time, but isn't anymore. So, is it still going to be in there? And then, just wondering about the total size of the kind of litigation and conduct charge in the stress test because clearly, just before Christmas, we saw some pretty large numbers demanded by the DOJ from Barclays.

So, that's probably increased the scope of possible settlements that you may have with them. So, I'm just wondering how all those things will kind of come out in the wash when we get the results in November or December?

Ewen Stevenson: Yes, look at – I mean every incremental legacy issue that we get resolved, certainly helps in terms of stress testing.

I would say, given the range of precedent that existed around FHFA, this was certainly comfortably within the sort of planning assumptions that we had and had been discussing with the PRA so I don't think there is going to be any surprise around today with the PRA.

But the biggest delta that we had in from our stress testing perspective would be around the Department of Justice settlement rather than the FHFA settlement. So, this won't have any material impact, I think, in relation to the stress test results.

In relation to Barclay's settlement, I think, remember also at the time though, there was also the Deutsche settlement and the Credit Suisse settlement. So, that is more precedent now around the Department of Justice, but that continues to be a significant stress -- part of our stress delta that we have.

James Invine: OK, thank you.

Operator: Thank you. The next question comes from the line of Christopher Cant from Autonomous. Your line is open.

Christopher Cant: Hi, thanks for the call. I just want to follow up the first question on the very high settlement relative to UPB. You mentioned that you don't think there should be read across to DOJ.

But I'm just trying to understand, are you saying the higher settlement really just a function of having been at the back of the queue, other people having maybe more pressure, or just different negotiating positions, or was that something potentially different in terms of the quality of the underwriting?
Thank you.

Ewen Stevenson: Certainly, nothing on the latter. There has been no discussions with the DOJ, any substance so far, though there's nothing that you can read across from this to the DOJ, we think.

It's not just the individual facts of us or how others are settled over time. Some of those settlements, as you know, have been part of umbrella settlements with the Department of Justice.

So -- and it's also that was sort of missing was this clearly a whole set of case law that's continuing to progress through the U.S. court system. Some of those court cases are favorable to us, some of them would be favorable to the FHFA.

So, it's a mix of things, and ultimately, down to a simple negotiation. We also saw value in resolving this because we think the continuing overhang of this Department of Justice was impacting our ability to move forward with the bank.

Christopher Cant: OK thank you, and if I could just follow the stress testing question as well. Looking forward, in terms of potential for future capital return, I think in the past, you used to talk about several hurdles.

So it feels like you made good progress on W&G, DAS, major part of RMBS out of the way, still left with DOJ and the passing or comfortably passing future stress test.

In the event, that you didn't pass or get the DOJ sorted out this year, looking into next year and next year's stress test, let's say, you have to settle the DOJ half way through the year, how do you think that would impact your 2018 stress test performance.

I'm just conscious -- if everything is viewed as of the first January 2018, it may be than necessary to wait until the 2019 stress test to have the DOJ fully dropout of the picture. Thank you.

Ewen Stevenson: Yes, so I think, some of these issues, which are known issues, particularly, some of these larger issues, we have a very interactive conversation ahead of the stress test results getting published.

So if I would -- under that set of assumptions you just made, I would assume that if we hadn't settled DOJ by the end of this year and we would settle them sometime during the year next year, that we would be had a very sensible conversation with the PRA to have that backed out of the -- stress sensitivity of that, backed out of our stress test results for next year. So, I wouldn't assume that this -- if we settle at mid-year, that means that we can't pass the stress test in that year.

Christopher Cant: OK, very good. Thank you.

Operator: The next question comes from the line of Andrew Coombs from Citigroup.

Andrew Coombs: I had two questions from me. I want to read across given already asked that question. But specifically, with the DOJ investigation, can you just update us on how discussions there are progressing, particularly, given the current vacancy there, something you expect you can resolve this year or could it drag into next year?

And then, my second question would be on the third-party indemnities. Is there anything similar in place with respect to that DOJ investigation?

Ewen Stevenson: Well, we said – (Ross) and I said full year results that aspiration was Department of Justice settled, that was obviously a statement that we made at the end of February.

We are now sitting here in early July. We really haven't started any discussions of substance over recent months. So, that aspiration continues to be our aspiration. But obviously, as the year progresses, gets increasingly challenging.

But we would still like to get it resolved if we could during this calendar year. And there are no -- there is no read across. I mean, this was a litigation claim where we had indemnity agreements in place for part of the settlement. Yes with the Department of Justice is a regulatory investigation against just us, there is no indemnity against them.

Andrew Coombs: Understood. So you're that the majority of rest of the provisions the 3.8 billion relates to the DOJ case? There's nothing – very little for civil?

Ewen Stevenson: So if you back out the on the 3.7 billion that I talked about earlier, we separately disclosed at some point that \$383 million provision that we have in relation to an FHFA claim against Nomura.

We believe we're indemnified from Nomura, we would expect to get that \$383 million back at some point. If you back that out of the 3.7 billion, there's about 3.3 billion of other provisions that we haven't broken down but you should assume the (inaudible) great majority of that relates to the Department of Justice.

Andrew Coombs: Very clear, thank you.

Operator: Thank you. Ladies and gentlemen, as a gentle reminder, if you wish to ask a question, please press "star 1" on your telephone keypad. The next question comes from the line of Martin Leitgeb from Goldman and Sachs.

Martin Leitgeb: Yes, good afternoon. First of all, congratulations from my end for removing one of the main uncertainties, obviously affecting the company. I had one question; the question relates to the milestones.

And I think at the time you laid out the milestones, there was passing some what we could see externally, fairly limited amount of provision in place for the DOJ, and that obviously has changed significantly since the beginning of the year.

And I was just wondering could there be any situation, where for some -- for whatever reason, the DOJ or the potential settlement with the DOJ just drags out further and further and where RBS could reassess those milestones and actually say, given provisions in place and so forth, that dividend assumption could occur irrespective of a settlement with the DOJ? Or do you think the DOJ settlement is crucial before any form of capital return could be considered?

Ewen Stevenson: Yes, so just to repeat, we've -- in terms of what we've got left to do, obviously, resolve the Department of Justice, pass the stress test and make a profit -- we've never sought to engage in that discussion with the regulator around the what if scenario the Department of Justice doesn't get settled for a long time.

Sitting here today, I find it hard to imagine that it would be straightforward to resume capital distributions, given the range of potential outcomes on the Department of Justice, which obviously, we saw last year in relation to one potential institution. So, it's sort of theoretical question, Martin.

Martin Leitgeb: OK, we'll have to wait then I guess. Thank you, thank you very much.

Ewen Stevenson: Going back to the last (aspirational) comment, that we'd like to get it settled this year if we could.

Martin Leitgeb: Yes, thank you.

Operator: Thank you. As a final reminder, if you wish to ask a question you can press "star" and "1." The next question comes from the line of Raul Sinha from JP Morgan.

Raul Sinha: Afternoon, you can hear me yes?

Ewen Stevenson: Yes.

Raul Sinha: Just a quick follow up on the indemnities, the \$750m odd. Who exactly are the counterparties that are providing you these indemnities?

And do you think they're substantially covered in terms of their own provisioning for it? What is the sort of expectation in terms of timing, if they're already through the door in terms of payment or is that something that you can rely over the next sort of quarter or two?

Ewen Stevenson: Look, obviously, we're subject to confidentiality undertakings. So we're not able to disclose the line parties involved. So -- but you should have seen in our press release, we've got a high degree of comfort around those indemnities.

Raul Sinha: OK, thank you.

Operator: Thank you. We don't have any further question, over to you.

Ewen Stevenson: OK, well look, thanks a lot for joining the call, particularly, given it was short notice, and thanks for the questions. In closing, it's always difficult to have to make these types of announcements.

But for (Ross) and it is one of our last remaining legacy issues. We're very focused in closing out the last few issues, so that we can spend our time where we think that should be spent, talking about the core bank.

On that, we'll be back to update you on progress, obviously, in a few weeks time with our half one announcement on the 4th of August. So, thanks a lot for you time today.

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

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