Barclays PLC Full Year 2015 Results

Fixed Income Analyst and Investor Conference

Paul Fenner, Societe Generale

Thanks for taking the questions and for the presentation. I've got three very quick questions. First of all, on MREL. Thank you very much for the disclosure around the spot MREL as opposed to the transitional. You're obviously currently being measured on a Group basis. Is there a stage at which the PRA starts to ask you to be measured on a spot basis, i.e. the requirement flips from Group to HoldCo? Or is that not the way it works?

The second question is, I hear what you say about the 7.8% MDA minimum, if you like, a buffer over which you can make as many distributions as you like. You're obviously aware of the debate there's been on the continent around whether it's SREP or whether it's the total capital requirement. And it's become clear that it's the SREP. My question to you is, do you think that there's a stage at which above the 7.8% that the PRA would probably start putting some pressure to limit distributions? And if so, where might that be?

And then the third question – there was no mention of it today on the earlier call – Brexit. How is it that you're thinking about it and what sort of planning can you put in place to get a sense of contingencies?

Steven Penketh

So, MREL fundamentally is a single point of entry home regulator target, so you're looking at it from a holding company. And the end number, the spot number that will be given further on in 2016 by the regulator will flow from the holding company down to the underlying subsidiaries. There have not yet been targets set for what will become independent subsidiaries ie. ring-fenced banks and non-ring-fenced banks, for good reason, because they don't actually exist as yet. Everything today will go straight to BB PLC. There will, of course, if you look at material overseas subsidiaries, be effective MREL targets set, although it's really divided up as TLAC at the moment, for the TLAC term sheet, from overseas regulators.

So, for example, from a US IHC perspective, you see that it's 14% by 2019, plus the 2.5% buffer; 16% by 2022 with a 2.5% buffer. But fundamentally, we would expect the MREL figure that we've given at the top of the house to be the overall consolidated requirement and then we distribute it appropriately across the Group.

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Dan Hodge

Thanks, Paul. Just taking the comments around MDAs and SREP, so what I would say around that, is I don't expect, after the minimum distribution restrictions, to move towards an SREP type world. I think it's pretty clear to us, as we've laid out here on slide 7, that we're going to need to meet the solvency minimum plus Pillar 2A, plus the phased-in buffers. We're showing the point in which we have the distribution restrictions, and therefore, as we've articulated, it's very important that we have a material buffer above that, and that's about 3.6% to Jan 2016. That's really the key around that one.

Do we think we're going to come under pressure before we hit those kind of levels? Yes, I think it's fair, if you do start getting towards that point, we'd like to put a lot of pressure on ourselves, I think, in advance of the regulator putting pressure on us. It's really, really important that we don't go near the levels at which distribution gets restricted. And in fact, we size our buffers in a way to make that a remote possibility. We do a lot of work in terms of calibrating the 100 to 150 basis points. We look at BAU volatility and noise we see through risk-weighted assets and capital. We run large one-off events. Also we size our buffer in a way to make sure we pass our stress tests. So I think we've been putting ourselves under a lot of pressure long before the regulator taps us on the shoulder.

To the other point around Brexit. As you'd expect of a global institution, we are assessing this through multiple perspectives, including what it will mean for risks and operations. This does involve estimates on secondary impacts on macro variables such as FX and interest rates. But it's very hard to say exactly, of course, what the outcome is going to be and the impact largely depends on how arrangements with Europe will be structured in terms of the single market access. So there are many potential outcomes to the vote. What we are focused on doing is scenario planning for those different potential outcomes.

Lee Street, Citigroup

Good afternoon and thank you very much for taking my questions. A question on RWAs. You guide for £360bn of RWAs, which is about where you're presently at. But you obviously don't have the rundown of the Non-Core for about £35bn. My question is, where is the growth going to come from in RWAs that will take you back up to the £360bn level?

Secondly, you mention that Barclays is working very hard to manage all of its legacy issues. Just any commentary you've got, for your remaining conduct and litigation issues, which ones worry you the most and any comments on the proximity to settlement of any of them?

And finally, will you actually be allowed to disclose your specific MREL requirement? Is that clear yet?

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Tushar Mozaria

So, on RWA levels, as you rightly point out, Dan suggested that we should use £360bn or we can use £360bn as a reasonable planning assumption. Of course, you're right to point out that we would want to wind down Non-Core and we intend to wind down Non-Nore, so you'd expect, if that gets down to £20bn, which is our expectation, another £35bn or so comes out of there post the perimeter change. And then at some point as we wind down our holding in Africa, that would have a further reduction as well.

In terms of growth, I wouldn't use the £360bn as a target. Dan was quite clear that don't think of it as a target, but just as a near-term planning assumption. But in terms of growth in RWAs, I think, the areas that we would like to grow steady is probably more on our consumer and corporate side, but we don't expect them to grow in these kinds of scales. So to put that into context, our ring-fenced bank which obviously houses our UK consumer and business banking franchise, is about £70bn of RWAs. So just looking proportionally, you wouldn't expect that to be growing in £10bn size or anything like that. It would be much more modest growth than that.

The other place where we would like to grow in the international entity would be our US card business and our corporate banking business but, again, they probably exhibit similar characteristics to our UK business in the sense you wouldn't expect them to grow in significant scale. So I think it's probably reasonable to assume £360bn as a near-term planning assumption. But I would think that, over time, that continues to drift down as we wind down Non-Core and deconsolidate the Africa business.

What we won't be doing is expanding the utilisation for our Investment Bank, and we'd like to think the things like fundamental review of the trading book, and other Basel type revisions to RWA won't either: we'll be able to absorb them just through management actions and various other opportunities that are available to us; or Pillar 2A may substitute that into Pillar 1 and Pillar 2A reduces.

The second question on the legacy issues. A lot of people would like to know exactly where we are on some of these items, and it's very hard for us to talk very openly about them because they are fluid and ongoing in nature. I'd say that the one that's perhaps the most significant, that we would like to resolve and get behind us as expeditiously as we can, also being economical about this, is the DoJ investigation on RMBS underwriting. I can't give you a timeframe on that but you'll have noticed some of the American banks have worked through that issue with the DoJ and other banks have commented on their status with them. That's the one that we've focused on trying to expedite.

Then the only other one I'd probably call out is that we did take a large additional provision for PPI. That's on the assumption that the FCA's window to react is consistent with their consultation that they've put out, and it's an estimate of the claims experience that we would expect over there. So again, that may have some variability in there as well.

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Steven Penketh

The MREL numbers, obviously, are subject to a consultation process at the moment. The one thing that we do know, which is why we've illustrated it this way, is that G-SIB banks will have to be at the minimum from a TLAC perspective by 2019 and 2022. The MREL number itself actually comes in and crystallises in 2020. At the moment, it is set at the minimum capital which is for Barclays 13%. I think that the timeline from here on is a discussion between us and the Bank of England as to what that actual MREL number will be for Barclays. And then, once we've actually got visibility on that number, I would expect that there'll be a communication policy agreed as well around that, not just for us but also for the UK industry. So watch this space.

Greg Case, Morgan Stanley

Firstly, I note that your HoldCo down-streaming slide from the previous quarters has disappeared. I was wondering if there was anything to read into that in terms of your policy on down-streaming?

Also, just in terms of excess liquidity, I note the comments that you made around your LCR and your access to funding. With the maturity profile that you put out there, the Non-Core run-down and the HoldCo issuances that you're planning for this year, are there any other levers other than LME that you could be pulling to reduce those excess liabilities? I assume you don't want to be running those cash balances that you're running today, and I'm assuming they will be growing from here.

And then also just on the ratings of the whole of the non-ring fenced bank. I was just wondering if you had any comments around the IG rating and whether or not that's achieved through a level of ALAC or loss-given failure-based instruments lifting up the senior ratings? Essentially, the question is, really, would you see a material difference between the sub ratings and the senior ratings for the non-ring fenced bank?

Steven Penketh

Nothing to read into the fact that the down-streaming slide on a like-for-like basis has been taken away, apart from the facetious observation that it obviously hasn't done us an awful lot of good in the context of spread performance, generically in the market. But yes, fundamentally we still are raising capital and funding at the holding company and down-streaming it to BB plc on a like-for-like basis.

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Dan Hodge

Thanks for the questions. In terms of the surplus liquidity, you're right that we have taken some steps already on that. If you look at Non-Core rundown and the need to issue more wholesale debt, you might form the view that we're going to be generating a large surplus here. But that obviously ignores the fact that, as Tushar was just saying, we're intending to grow some of the Core business as well. So I wouldn't anticipate seeing material increase in the LCR from where it is today.

Clearly, we also look at liability management exercises when it's the right thing to do so from an economic, capital and regulatory perspective. And I would expect to see the LCR running close to levels that we have been running it at, and I don't view that as a large drain on the returns of the organisation. And the reason for that is that the really expensive liabilities are the ones we go after anyway through our liability management exercises. That's where the cost of running surplus liquidity comes in. And that's actually quite a small portion of the total liabilities we have. Most of the liabilities which one might regard as surpluses, if you like, are actually fairly inexpensive, and you can attribute it to cheaper deposits or shorter term wholesale money market funding. And so we're very comfortable running at these sorts of levels.

In terms of the ratings of the non-ring-fenced back, let me talk a little bit about that one. Now, we obviously can't predict precisely what the rating is going to be in the future. That's for the agencies to determine. We are, however, very confident that both the ring-fenced bank and non-ring-fence bank, by which we mean BB PLC won't be materially different from the present ratings that we see for BB Plc so that's by way of reminder A2 for Moody's, A- for S&P and A for Fitch. And that's very much because of all the work we've done on designing the distribution of businesses, designing the allocation of capital and funding and to hit all those metrics for those entities.

So we looked very, very hard at capital strength, credit quality, asset quality, funding, liquidity and returns. So we hope to achieve solid investment grade ratings and you can actually see some of the data we've already started to share about the strong performances and the strong balance sheets of these two parts of the Group at the end of 2015. So we think these are fundamentally well diversified entities and we are very confident about BB PLC now and in the future.

Greg Case

Okay and just on the sub debt as well would you expect the ratings to remain broadly similar or are they more at risk?

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Tushar Mozaria

The sub debt in the end will actually come from the holding company as you would expect so to the extent that you end up with additional support as tranches thicken at the holding company you would expect that benefit to fundamentally go to the senior debt rather than subordinated debt. I would expect the overall subordinated debt to remain pretty much stable and the expectation is that we would not be issuing sub debt from the operating companies.

Robert Smalley, UBS

First, following up on Greg's point what interests us is down streaming on a not like for like basis because when that happens essentially you'll be demoting the entire senior HoldCo asset class so continued disclosure on that would be important. But a couple of questions, one, just in terms of the Non-Core assets you had a one-time increase in that, can we assume that there won't be any traffic between the Core assets and Non-Core assets that essentially those are the Non-Core assets and they'll be worked down and there won't be any interchange between the two?

Second question, disclosure of distributable reserves is one step but you're going to be a more frequent issuer in the AT1 market. Besides the market settling down what else do you think as an issuer you can do to restore confidence in that market?

And then, three, in terms of page 12 and 13 in funding and capital between the three entities, B PLC, the ring-fenced bank and the non-ring fenced bank I'm hard pressed to see how, from a funding perspective, even though we can look at the consolidated entity, how funding wouldn't be more expensive even if you raise as much as you can from the holding company and downstream it to the non-ring fenced bank. There will still be some funding that the non-ring fenced bank does so how do you mitigate higher cost from funding?

And then, while I know we have to look at capital on a consolidated basis we will have to apportion it between the three entities, how do we get the regulators to make sure that they don't look at capital allocation between the three units, and instead of one and one making two, they want one and one to make three and impose higher individual minima on each one of the units?

Tushar Mozaria

Thanks Robert, I take your point on the down-streaming and the transparency on that so take that feedback on board.

In terms of Non-Core it is a one-time perimeter switch in the sense that we have transferred, in this case, not so much heavy balance sheet orientated businesses, but they're the more expensive businesses from a cost standpoint. So it's relatively modest in pounds sterling for RWAs but it also resulted in the transfer of over £600 million of expenses or costs.

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In terms of the two-way traffic between the two we haven't transferred anything one way or another; they both have got a brick wall around them. It's the first time we're putting more into Non-Core and that's when Jes came into the company and did his own review of businesses he considered strategic and non-strategic. I think at the end of this our confidence has been pretty high and when we get to the end of 2017 and RWAs are around £20bn I think at that stage we'd consider folding Non-Core back into the core division. So I don't think you'll ever be in a situation where Non-Core literally whittles away to zero.

It'll just be de-synergistic for us to have. At the moment we have walled management teams. At some point that becomes de-synergistic. My sense is that at around 5% or a bit below 5% of Group resources and risk-weighted is probably a reasonable measure as is perhaps costs. And therefore the dilution effect of Non-Core folding back into Core is minimal in terms of returns or from a P&L perspective.

Steven Penketh

On AT1 confidence, what we have here is a fundamental sell-off at the beginning of the year that, to be honest, surprised us and I think surprised many because I think there's been a dislocation that is actually divorced from idiosyncratic credit risk if you're thinking about the deferral risk of these underlying securities, certainly from our perspective. With respect to deferral risk I think Dan's already touched on these points very persuasively around the importance to us of maintaining a management buffer that is significantly above distribution restriction zones to ensure that we can actually keep paying AT1 coupons as they fall due.

We've also made a statement in the past about the fact of how we view the capital hierarchy, although we cannot actually give verbatim comforts for CRR reasons around different capital hierarchies, we have always said in the past that we intend to respect capital hierarchies when it comes to distribution payments on our securities. And I think the other action to point out is that irrespective of your management buffer you also have recovery actions that you would take well in advance of actually hitting a distribution restriction zone as far as AT1 is concerned.

So we would hope, as you see the common equity tier one story unfold, you see the capital build and as you see the market generally settle down over what has been frankly a very fractious period since the middle of January, that the AT1 yields will actually come in as well and then priced appropriately in the context of the capital stack versus equity.

Dan Hodge

I'll take the final question. We talk about this potential risk, the sum of the parts risk and I think you've captured it well there with the arithmetic. We are quite confident on this point and here's why. The capital requirements are still evolving so we don't have absolutely end state certainty yet in terms of what the ratio is going to be for the ring-fenced bank or for BB PLC. Some of the reasons for those I articulated earlier for the Group as the various buffers are moving around still.

From what we can see at the moment, we don't expect the requirements to be significantly different in terms of the minimum capital ratio requirements for the ring-fenced bank and BB PLC so not that different from each other and not that different from the Group either. In addition, I would say that we are very, very deliberate in terms of how we allocate our resources and for these different entities to specifically avoid getting into a situation where we're trapping capital or funding within these subsidiaries.

I think the best example I can give, I talked about the average risk-weights being quite similar earlier, that's really important because if you have one entity with a very low average risk-weight and one with a very high average risk-weight the one with the low risk-weight will become leverage constrained and you'll need to downstream extra subordinated debt capital there. And so this is also about the design and we're happy we've got that design right.

So the desired end state here is for the opposite to be true, and rather than have dis-synergies from our various subsidiaries from a capital perspective, we have synergies and we think that a holding company model can help us achieve that. We are raising our debt and equity at the holding company; we can concentrate diversification at that level and ultimately see the benefits of that diversification to our subsidiaries.

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