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Barclays PLC FY 2023 Results

Fixed Income Conference Call Q&A Transcript

(Amended in places to improve accuracy and readability)

Lee Street, Citi

I have three, please. Just firstly, on the Investment Bank, and I know it was discussed a lot this morning, but I'm just trying to get my hand on why the Investment Bank capital allocation is the right number. And just to delve a little bit more into why allocating half your capital to what still looks like will be one of your lowest return businesses, if that makes sense.

Secondly, on the rating, thank you for your comments there. I know you said you're targeting a composite A rating at the HoldCo. You are targeting A ratings at both S&P and Moody's, and have you held any discussions with them to see if the new 12% RoTE target and associated targets might be sufficient in the medium term?

And then finally, just a point of clarification. Do you think the MDA threshold has peaked at 12% now?

Anna Cross

I'll take the first question, and then I'll hand over to Dan for the other 2. So in terms of the broadly 50% to the Investment Bank, clearly, within that, there is a real reduction because we are asking the Investment Bank to absorb the changes associated with Basel 3.1. And whilst it's returning a fairly low RoTE right now and below the overall group average, that is not our ambition for this business, and we set out some clear targets today for it to be broadly in line with the group by 2026.

On the other side of the percentage, the £30 billion [increase in RWA allocation to Barclays UK, UK Corporate Bank and Private Bank and Wealth Management], we think is the right level of scale of growth for those businesses to absorb over the period for that 3-year journey. And I would say that the 50% [of RWAs in the Investment Bank] is a point in time. It's purely where we believe we'll be in 2026. It's not supposed to be any indication of a sort of perfect balance between the Investment Bank and the rest of the bank. So hopefully, that's a bit clearer.

Daniel Fairclough

So getting to a single A composite, it would require a ratings upgrade with either Moody's or S&P. Clearly, we have ongoing dialogues with the agencies. And clearly, as you would expect, we've discussed the investor update with them. We think that what we've got here is really positive from a credit perspective. Clearly, the returns target is helpful. We think it provides further diversification and we think it fits within the existing risk appetite. And clearly, we've been very firm on our commitment to the capital ratio target.

So we think there is lots to like in here from a credit perspective and from a rating agency perspective, and working with them will be a key management focus for us.

And then I think your last question was just on the MDA level and where it might go from here. So obviously, we go through an annual review with the PRA. I think our expectation is there are good reasons to think that the MDA may go down with the implementation of Basel 3.1.

I think the PRA has been reasonably clear that they wouldn't expect to double up in capital items. So we'll have to see how that goes. I think there'll be a consultation paper out on it, but I think there's good reason to think that that may reduce. And obviously, that would reduce our minimum requirements at that point.

Daniel David, Autonomous

Congratulations on the results. I just want to fix on capital generation. Looking at the MDA buffer and CET1 target, this remains a bit low compared to peers. And I guess with £10 billion of payouts coming, this could scare investors that you're prioritizing equity over credit. So just to drill down on that a bit more. If you're running at the lower end of your CET1 guidance range for a prolonged period, would you consider reducing the equity payout to boost the MDA headroom? And following on from that, do you think the low CET1 target and headroom impacts your spreads and hence cost of funding?

And then finally, just on the AT1 stack. I know your comments on being a net negative issuer, if I look back over the last few years, I think you've always maintained 3.5% to 4.0% AT1 on an RWA basis. Is this the range we should think of longer term? Or is there a chance that that could fall away and reduce that over time?

Daniel Fairclough

So in terms of the capital ratio position, I think I covered some of it in my speech. I think firstly, the capital generation is really important here. So 10% RoTE is 150bps of CET1 generation. And we think that really gives us a lot of flexibility.

The second point I'd probably make is that we have a lot of flexibility in the velocity of our RWAs. That allows us to manage our capital base in a very nimble way and in a more nimble way than if we were purely a banking book balance sheet. So for both of those reasons, we think that the capital ratio target is appropriate. As I said to my earlier answer, there may be reasons why the MDA will reduce over time, but we'll have to keep that under review.

And then your question about relative priority. I think it's really, really important and Anna said it in her comments, the number one priority for us is to maintain a prudent regulatory capital position in the target range. And we've been quite clear that that is our number one priority. So hopefully, that helps with that question.

Second question was about the AT1 stack. So you're right, we've said we will be a net negative issuer in 2024. So we think we can do with slightly less AT1. I won't give you a guide on exactly where we're going to be. But we're comfortable issuing less in 2024. And there'll be an element here on RWA density [given] the switch to [an] IRB model [in US Cards] and Basel 3.1. So all other things being equal, that will create a bit more leverage capacity.

Paul Fenner, Societe Generale

The first, I guess, is a 2-parter and really comes back to this Investment Bank versus UK refocus. I guess you've been reticent to do that for a number of years, right? I mean it's been in all of the papers, there's been a constant sort of discussion on these kind of calls. I guess my question is, what's changed from this point last year to this year in terms of your outlook for Investment Banking, just so we understand and put that into context. And likewise, what's changed about your outlook in the UK? What is it that's either fundamentally changed in terms of the outlook or what is it that you have misunderstood in terms of risk return?

And in particular, within the UK, you're obviously now going to be taking market share in some of the riskier parts of that spectrum, including high LTV mortgages and consumer credit, which kind of feels a little bit opposite direction to traffic. So a bit of commentary around that would be super helpful.

Second question, commercial real estate, I don't think it's been mentioned in any of these calls. Could you just give us your two cents on where your book is and what you think about the noise out there around that asset class?

Third, on supply, thank you very much for the very clear comments around 2024. Given your refocus towards the UK and consumer, in particular, does this mean that we should expect looking out 2025, 2026, that you will be a smaller issuer?

Daniel Fairclough

We spent a lot of time with investors as we work through the investor update. So probably the first point is here that we've listened to what investors have told us and their views and preferences on shape. In terms of the Investment Bank specifically, we view that we are at scale, and we need to be at this scale to really ensure that we're relevant for all of our clients. So it's not that we've radically changed approach here, but we think it's important to put a cap on the total size.

In relation to the other areas of the bank that we're going to be growing, which obviously do have a UK focus, I think a lot of this is also consistent with some of the things that we've discussed before. We certainly took a prudent risk view post-Brexit, and we were particularly prudent on the UK consumer.

I think the UK consumer has been very resilient since that point. And I think the UK macro environment has actually been pretty resilient as well. And we have reduced our presence in a number of those key markets. So we've reduced market share in both the UK cards and in unsecured quite materially over that period.

So we look at situation now and with the relative stabilisation we've got, we feel there is an opportunity to step back into those spaces. Clearly, we've started some of this with the Kensington acquisition. And I think we flagged already that we were rebuilding our UK cards presence. Tesco is a continuation of that journey. So we don't really view it as a material increase in credit risk appetite, but reaffirming some of the appetite that we had historically.

Anna Cross

I think the only thing to add would be we are starting from a very different place here. So if you look at our UK cards, it's 35% lower than it was. The arrears performance is consistently below 1% and has been for multiple quarters now and much, much lower than we would regard as a normal amount.

Similarly on UK mortgages, the arrears rates are extremely low. And actually, our starting position for the book as a whole is just a touch above 50% for the LTV of the book, we're acquiring typically at around 63% and only 1.6% of our book that's over 90% LTV. So these are extremely low-risk portfolios as we have them now. And we're talking about well-controlled, well-defined steps using capabilities that we've acquired or have in-house.

I think the Kensington piece is very interesting. Clearly, when we bought that business, we said at that point in time that we were buying it for its risk capability. And actually, the other thing that we've done since then is we've demonstrated that we can do high loan-to-value risk transfer in the UK in order to dynamically manage the risk on the balance sheet. So we think it's the right time and we have the right opportunities to take advantage of it.

Daniel Fairclough

We've long had a very conservative approach to commercial real estate. So our exposure is £15.8 billion. So it's relatively modest. We're really not at the front line of the evolving situation in this market. The LTVs are low. So [overall,]49% LTV with no subset greater than 57% and about 11% of it is in offices. So again, relatively modest. The other point I'd probably make is we do have SRT protection on a portion of this book as well, which further helps the prudence on it.

Anna Cross

The only other thing I'd highlight is [29%] of the book is in the US and [71%] outside. And obviously, the US and offices are the points of greater investor focus at the moment. But we feel both as an LTV matter, but also in terms of being just very diversified across counterparties and sectors that we're in a good risk position. And as I highlighted this morning, as we grow more in UK corporates, we will not be undoing this positioning on commercial real estate.

And I think you have one more on supply.

Paul Fenner, Societe Generale

Yes, just on longer-term supply.

Daniel Fairclough

I mean most of the public market issuance that we do is for capital and MREL purposes. And so we would expect that to be actually broadly similar going forward. Although the Investment Bank will be shrinking as a proportion, it will be relatively stable overall. So I don't think that should materially impact the funding position. Clearly, we would expect to see a bit of funding consumption in UK. But clearly, they start with a very strong liquidity position and a very high level of deposits.

Rob Smalley, UBS

Before I start with questions, two things. First, thank you very much for the structural hedge talk a little while ago. It was very informative.

Secondly, my line went a little bit terrible when you talked about Tier 2 issuance, if you could repeat those comments, that would be great.

In terms of questions, and I guess, I'm following up on Paul with my first, if we're going to see a prolonged period of stagflation in the UK, where do you think it manifests itself in the economy? And how is that reflected in your portfolio and your loan loss provisioning and migration from stage 1 to stage 2, 2 to 3 as we go?

Secondly, on Slide 17, you talked about the LCR, 78% cash. Is there an opportunity to increase profitability by investing at higher rates or is there a reason why you want to keep this in cash for longer?

And then third, with respect to the US card portfolio this morning or last night, Capital One announced it was acquiring Discover, making a very big competitor to your business. Can you talk about how you see that competitively? Does it make it harder? Or are there pieces you think are going to come off of the combined company that you could pick up where you see some opportunity?

Anna Cross

Why don't I start the first question, and then I'll hand to Dan for any further comments and pick up the LCR and then I'll pick up the Capital One point and perhaps, Dan, you could reiterate your points on Tier 2 along the way, since Robert's line cut out.

So just to give you some headlines in the macro assumptions that we have for the UK. We are expecting the base rates will fall to around 4.0% by the end of this year and about 3.25% by the end of next. And we're expecting that unemployment will peak at around 4.8% in early 2025.

I think that probably doesn't coincide with what we would describe as a stagflation environment, probably more stable than we've seen actually across the UK. And given where we start from in our asset book, as I said before, both in terms of their risk positioning and the quantum of lending that we have. It gives us confidence that we can stay within the low loss ratios that we've called out for the UK on a longer-term basis, which is around 35bps.

Daniel Fairclough

This cash position is quite consistent with where we've been in the past, Robert. We've run a deliberately conservative and prudent position here. And we look at the portfolio, particularly through a stress test lens. And clearly, if we're running asset risk or outright rate risk in the liquidity pool that will have an impact on our capital consumption through a stress test. So I think it's prudent to maintain a high cash balance in the liquidity pool.

Your question on Tier 2. I think really, the message we were trying to give there was that we will be active in Tier 2, but relatively modest, but we're not guiding to a specific number.

Anna Cross

And just your final question. Yes, we noted that. I mean the way we see it is, it really highlights to us the commercial attractiveness not just of the cards business in the US, but also the ability to control payments and control payment rails. We've got more to hear about this deal, but that's how we interpret it from the outside. And we feel the same.

We think we've got an attractive opportunity, both in the UK and in the US. As related to a particular point on relative competitiveness in the US, we're very focused on improving the returns of the business that we already have. It performs extremely well. It's very focused. It's only a partner asset business. And so for those partners, it's not just about pricing, it's about the relationship and the service that you can provide to what is ultimately their customers, you carry their brand, and that's very important.

So we think we're quite uniquely placed within the US market in that we don't compete with our partners in the customer's wallet, and we think that's important to them. So we'll remain interested in what will come out over the next few days, but confident in the decisions that we've made around the US and indeed the UK business.

Daniel Crowe, Goldman Sachs

Just coming back on the Tier 2 issuance. Obviously, you haven't filled your bucket that you could fill and you have excess AT1 which helps on leverage. I'm just wondering, I know you don't want to give an exact figure, but would you assume that you will head back towards filling the Tier 2 bucket completely as you reduce your AT1 requirement?

Just on the UK review on motor financing. I know it's not a major part, but could you just give me what was roughly your market share before you stopped lending into that pre-2019?

Daniel Fairclough

So Daniel, no radical change in our approach to AT1 or Tier 2 mix. I mean, we still view that there's a lot of value in filling up that total capital bucket with AT1. We think it's cost-effective, given the leverage benefit that we get, given the returns that we can earn on liquid deployment of leveraged balance sheet. So no material change. We're certainly not going to look to fill up that Tier 2 bucket.

But the point on being a negative issuer was, we think we can run slightly lower than we have done recently. We've been sort of 3.9% of AT1 as a proportion of RWA, so really at the upper end of where we operated. So we'll run a little bit less than that, but no fundamental change to the strategy.

Anna Cross

And just on your final question, Daniel, I mean it varies by year, but I would characterise it as consistently low single digits across the years in which we were active in the market. And of course, we fully exited in around the middle of 2019. So that's the message you missed this morning.

It looks like there are no further questions in the queue. Thank you so much for joining us today. Thank you for your continued interest in Barclays. We really look forward to seeing many of you on the road over the next few weeks. And until then, take care.

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