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Barclays PLC

2014 Interim Results

Fixed Income Q&A Transcript (amended in places to improve readability only)

Tushar Morzaria, Group Finance Director

Thank you, and with that, I'd like those on the call to question, and I would reminder, we are joined here by Dan Hodge, our Group Treasurer, and Steven Penketh, our Head of Execution of Capital and Term Funding. So, with that, operator, do we have any questions?

Carlo Mareels, RBC

Yes, good afternoon everyone. I had a quick question on the Pillar 2a equity component. I was wondering whether that's actually part of the combined buffer, or if that needs to be seen outside of the combined buffer?

That's the first one, and secondly, if you have any view that you can share on potential future buffers that may come in, such as the counter cyclical or sectoral buffers that may increase further capital requirements from the current levels?

Tushar Morzaria

Thanks Carlo, I'm going to hand that to Dan. Dan, do you want to answer that?

Dan Hodge, Group Treasurer

Yes, sure. Let me cover both of those. The first question was around Pillar 2a and whether that forms part of the combined buffer. It's not the expectation that it forms part of the combined buffer. What it is likely to do is to increase the minimum regulatory target levels, but the significance of this not being part of the combined buffer actually relates to the second part of your question, which is around the PRA buffers.

So, the PRA will basically make a determination of the potential capital hit to the bank in a stressed environment, and in a situation where they judge that the amount of that stress on capital is higher than the combined buffer, which to remind you for Barclays is 4.5%, through the use of conservation buffers, they may seek to apply that buffer on top of the 4.5%.

In terms of the second question around our expectations of future buffers, let me start by answering around the counter cyclical buffer. Obviously, this is something that the regulatory authorities are going to determine, rather than ourselves. Specific articles in CRD IV detail how it should be calculated by regulatory authorities, deciding the rate based on levels of credit advancement in the economy. We've currently kept it at zero. The calculation is focused on credit and GDP growth, but also other indicators, such as bank leverage and financial markets activity; so although credit levels in the UK are high, credit to consumers has actually been consistently weak since the crisis, and hence the counter cyclical buffer remains at zero %. What I would say is, if it were announced, basically you have 12 months advance notice, so we would expect to be just short of 11% before it took effect.

I'd also say about a counter cyclical buffer, it's right-way risk, if you like, because we should be accumulating earnings in an environment where we're seeing a pickup in credit through a rise in GDP.

The other one about sectoral buffers, that's another tool, which the PRA have to focus on specific sectors, so an obvious one might be the housing market, for instance. Again, we don't have any anticipation that that will be used at this current stage.

I think the key point really to take from this is that we will manage an internal buffer above the sum of all the regulatory targets, so when we talk about our end-state level at 11.5 to 12%, what that really constitutes is the sum of all of the various minimum buffers, plus an internal buffer for prudential purposes.

Carlo Mareels

Okay, thank you very much.

Tushar Morzaria

Thanks Carlo, shall we go to the next question?

Robert Smalley, UBS

Hi, good afternoon, thanks for doing this call, and thanks for doing it during New York hours as well, greatly appreciated. Also, first on slide seven, and I do appreciate the disclosure on Pillar 2a and requirements there, particularly as it pertains to the contingent capital market, so thanks.

You have an AT1 number currently at 4.3 (billion), you had said with minority interest, that goes up to 4.6 (billion), and the target end state capital at 2%, does that translate into another 3.8 to 4 billion equivalent AT1 over the period, bringing your total to about 8 billion outstanding? Am I in the right order of magnitude there?

Tushar Morzaria

Yes, Robert, and you're welcome about trying to arrange a call so that it's suitable for folks on the US side as well.

Yes, you're right, as a longer term matter, we'd like to run the company at about £400 billion of risk weighted assets, so you get to roughly £8 billion of total AT1 target, so you're in the right ball park, somewhere around £4 billion still to go.

Robert Smalley

Okay, and translating that into interest expense, that would be roughly £325 million a year of extra interest expense?

Tushar Morzaria

Yes, somewhat driven by the coupon levels on future issuance, which perhaps Steven might give us some more colour on?

Steven Penketh , Head of Capital Market Execution

Yes, so obviously as you say, it depends entirely on what the coupons are on the bonds and where you swap as well at the time, where swap levels are. The other thing I would also mention is, we have no particular hurry in the context of raising additional tier one capital, so as far as the net interest cost is concerned, that's going to be spread effectively on the assets you're creating as well at the same time, throughout that process. So you can't look at it on the spot basis today, and load that cost on top of where the bank is. And, obviously the other thing to mention is at AT1 is tax deductible as well, in the UK.

Robert Smalley

Right, great. You had mentioned the exchange, and the take-up was very good for some tranches and a little less for others. What are your plans on essentially the rest outstanding there, and if you were to go and do another tender, how would the regulators work out the terms? And, by that I mean, would they look at a repeat of the same terms as something that is possible, or would they say, look, the investors have gotten a bite of that apple already, you should tighten the terms next round? How do they go about looking at that kind of thing?

Steven Penketh

I think the response I would give to that is that the target securities were obviously legacy tier one capital securities, which we know will never qualify as Tier 1 under CRD IV because they don't have the requisite contractual write-down provisions in them.

The terms that we offered, we thought were fair, that strike a balance between what trading levels are, about what you think is a fair market premium at that point in time, and then it's just open to the investors as to whether they would accept the uptake.

Because, effectively it's a one for one exchange between your legacy to new AT1s, it's not something which ultimately is driven by a big regulatory concern, it's just a matter for us of house cleaning of legacy capital securities and wanting to get the CRD IV benefits for the exchange securities that we're actually going to issue.

If there is a subsequent exit price going forward, there's no certainty around take-up, like there isn't in any LM exercise, it's just going to be a market dialogue between us as issuers, and the premium prescribed, and whether investors find it attractive or not.

Robert Smalley

Okay, thank you. If I could just ask one or two quick questions on funding? I'm on page 36 of the release today, and in the table, on the senior unsecured privately placed line, I've got £13.4 billion less than one year maturing, and just seeing the amount that you're planning on raising, are you finding that what was raised privately before is not being placed privately now, given lower rates and tighter spreads? Is that how the funding is evolving, more from what you did privately to publicly?

Tushar Morzaria

Dan, you want to take that?

Dan Hodge

Yes, I think a lower rate environment is definitely a factor here, in terms of influencing the scale, the demand for structured notes and medium term notes. I would also say that historically, we have been very dependent on that particular class, and I think going forward, we wouldn't want to be as dependent.

Also, it's not yet clear that these structure notes will qualify as GLAC, so this is partly supply driven as well as demand driven. That said, we still feel it is a very valuable funding source, so we will be regular issuers.

Robert Smalley

Okay, and last one, as mentioned, GLAC, any concerns or questions about that getting done by Brisbane? It seems that everything is pointing to that, is that all on track?

Dan Hodge

From our perspective, we just follow the developments as and when statements come out from the relevant regulatory community. Brisbane I think is going to deliver something on GLAC, but whether it's the final word on GLAC is yet to be determined. We will follow the debate and take any actions that we need to take on the back of that greater clarity, and also of course feed into any consultation papers that come out as well, in due course.

Robert Smalley

That's great, very helpful, thank you.

Tushar Morzaria

Thanks Robert, can we take the next question, please?

Corinne Cunningham, Autonomous

Hi there, a couple of quick ones, I think. First one is the timing of the UK stress test. I guess it's going to be after the EBA and ECB stress tests, but do you have any ideas when that might be concluded, and if and when we get to hear what the results are, or if it's just a more generic statement from the Bank of England?

Tushar Morzaria

We've submitted our input into the stress test, in terms of running the scenarios and submitting our results into the PRA, and we've also done the same for the EBA. I'll hand over to Dan, but our expectation is that the PRA will report back on the stress test findings sometime late in the fourth quarter. Dan, do you want to give anymore colour than that?

Dan Hodge

It's the same, I've heard November was the latest. The publication should come up after the EBA.

Corinne Cunningham

By bank results, do you know?

Dan Hodge

They haven't come and said they'll be giving that level of detail. Certainly, the EBA will be doing so, on a bank by bank basis. Historically, the Bank of England haven't done that, and it's not sure at this stage whether or not they will depart from that. We don't have any information to suggest they will depart from that.

If you recall what happened last year, when they were looking at capital shortfalls to the FPC's 7%, that was very much done in the aggregate across the UK banking sector, so they may do something like that again.

Corinne Cunningham

Okay, I had another small question. This one was on the deductions for own capital and own AT1s, so there's a big deduction at the year end, and much smaller deduction as of H1, but how much of your own securities do you own, and how does that come about? Where are they held? Is it in client's funds, or is it on the trading book, thank you?

Dan Hodge

You've obviously seen that that number came right down, so there's a very small residual amount that continues to be held, and the reason numbers came down was actually that the number at the end of the year, was a little bit too conservative. We've since had a lot more improved visibility and time to go through the numbers.

Previously, we had looked at the whole lot of fund investments and had taken a conservative assumption in terms of a portion of those funds being Barclays own stock. That proved to be overly conservative. We've also unwound some of our own internal hedging arrangements around share awards.

We do have some residual amounts, and it's really through the indexed trading activity, to answer the question, but that is really subject to some very tight internal limits, because obviously it does cause a one for one deduction.

Corinne Cunningham

Thanks so much.

Tushar Morzaria

Thanks Corinne. Operator, do we have any more questions?

Gildas Surry, BNP Paribas

Hi, good afternoon, thank you very much for the call. I would just like to hear your thinking on the leverage ratio computation and the impact it could have on AT1, whether for the conversion or write-down, and also the indications on the MDA, thank you.

Tushar Morzaria

Dan, you want to cover that?

Dan Hodge

Yes, sure. Talking about the CP, it's important we don't get too far ahead of ourselves. This is just a consultation paper and there is no calibration in there. This was mostly in regards to the methodology, bringing leverage in line with capital by having regulatory minimum plus buffers.

That said, in terms of impact on the AT1 market, I suppose, thoughts around that, size could impact the total amount in issue, especially if it's an AT1 for any reason didn't count, although that actually isn't recommended in the paper. I would say that there's a possibility of this having quite a lot of complexity.

If you have distribution restrictions on falling into a leverage buffer, again that wasn't made explicit in the CP but you could see that that may be a potential outcome. Then, it's not really clear how the CRD IV MDA regime, which was designed to capital ratios, could be legally applied to leverage ratios. The CRD IV is the maximum harmonisation directive after all.

It is possible of course for the PRA to introduce some form of restriction if you went into those buffers, using general prudential powers, and if so, then the market would need to adapt to this, by getting comfortable with that, and that's clearly a reason why the banks should seek to hold buffers above those regulatory buffers.

And, the points around, could leverage triggers potentially be added for AT1? Again, I repeat that wasn't recommended, if that did happen, I think the idea of dual triggers would be very complex. I make the same point around the maximum harmonisation directive; I don't know how that actually would get implemented in practice. We'll monitor the outcome of the CP and react accordingly.

Steven Penketh

The only thing I'd add to that, is that as a principle, we'll try and be as anticipatory as we can, with any future regulatory developments, and to the extent that we can anticipate them, we will manage ourselves such that we're well ahead of that as you can see from our leverage ratio objectives, we will ensure that we're ahead of any developments in either, so hopefully that answers your question.

Gildas Surry

That's very useful, thank you very much. If I may have a follow up, just to be clear, the current terms and conditions of the existing AT1 will not allow moving or introducing another trigger that would not be based on solvency?

Steven Penketh

That's right, to reiterate what Dan said, it's quite clear what the terms are for the AT1 that's currently outstanding; it's also very clear in the CRD IV what the terms need to be, to qualify for AT1 capital, and that has not changed. I think that the only read-across that you could take from the consultation paper is that there is a general discretion anyway with most regulators, if not all regulators, to think about distribution, looking at their other supervisory powers. It is not something specific to AT1s and certainly has no impact on the AT1s that are currently issued.

Gildas Surry

That's clear, thank you very much.

Tushar Morzaria

Thank you, and I think that's it. Thank you very much for joining us this afternoon, and we hope you found this useful. We will continue to do this at the full year next time, and with that, good afternoon.

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