Barclays PLC Q1 2019 Results

29 April 2019

Sellside Breakfast Q&A transcript (amended in places to improve readability)

Tushar Morzaria, Group Finance Director

I'll just make some very short opening comments. We can characterise Q1 as another clean quarter, clean in the sense there was no unusual items below the line, and we had minimum conduct and litigation this quarter, so we are pleased with that. We've had a few quarters like that, so I think we're beginning to see, well and truly, the below the line items becoming less and less frequent and, hopefully, more of a thing of the past.

Excluding the relatively small litigation and conduct, we booked a 9.6% return on tangible equity in the quarter. We are pleased with that given the choppy conditions that we had in Q1, particularly in the CIB. We're also pleased that we posted positive jaws in Q1, showing some of the cost flex that is available in the Group. I'll just give you a reminder on some of the guidance, or key points, that we called out.

On BUK, we have talked about it in the past and reaffirmed that we would expect negative jaws in the first half of the year, but positive jaws in the full year. We would expect income to be higher year on year, and sitting here now, at the end of April, that still feels like pretty decent guidance.

On CIB, we did have a very low IB fees quarter. It definitely feels different sitting here in Q2. I would expect fees to be higher – a little like Q3 last year, where we had a calendar effect in the way our deals were closing. Looking at Dealogic tables, it looked like we picked up a bit of market share as well in Q1, so we feel pretty good with that.

CCP continues to grow at around mid-single digits, at 6%. We've talked about this in the past, this is somewhat consistent with the risk stance that we're taking: slightly more lower-margin, higher FICO business, but growing at a reasonable pace, so we still feel pretty good with that.

In Head Office, just to remind you, we did have the Absa dividend come into Q1 this year, as opposed to Q2, and we've called the RCIs, which you will have heard about.

And then on costs, which is probably the more significant guidance. Even though we will leave our cost guidance unchanged for the moment, between £13.6-13.9bn, if the income environment isn't where we would like it to be, then we are prepared to go below £13.6bn in order to find a balance between current profitability and medium and longer-term investments.

Finally, on impairments, all the indicators you would expect us to be looking at suggest that the impairment environment continues to be very benign. I think there will be a seasonal shape to impairments, mostly reflecting the US Cards business, where you would expect Q1 to have the lowest impairment and Q4 to have the highest impairment. This just reflects the spending behaviour that takes place in that US Cards business.

I don't think there's much more I would call out other than that.

Joe Dickerson, Jefferies

I find it interesting that yourself and other investment banks called out the choppy conditions for trading in Q1, and yet you delivered a 9% return on your Investment Bank with a cost lever. I'm just wondering when things turn around, what would the shape of RoTE look like? Do shareholders get the benefit from the pick-up, and does it go out to people as variable compensation? How should we think about the RoTE in a good environment if, in a choppy environment, it was 9%?

Tushar Morzaria, Group Finance Director

The CIB still isn't earning its cost of capital, it's really important for us that we continue to drive profitability up in most market conditions, so that we show continuous improvement. I think if the environment were to improve, you would expect to see returns going up as well. We've been reshaping and resizing the Investment Bank, as you're aware, for some time. It's really important that every year we continue to drive profitability up, until it's at least earning its cost of capital.

Jenny Cook, Exane

One feature of the recent US bank results is that we saw the transitional impact of CECL (the US version of IFRS 9) being revised higher at a number of banks, driven mostly by credit cards. Presumably this is something that will be applicable to you in the US GAAP accounts of your US IHC? Given that book yields predominantly US credit cards, I'm assuming that you'll be phasing in quite a big hit to equity over the next four years in the US GAAP accounts. I'm just wondering how you'll be looking to balance the growth aspirations of that book as you're facing this hit to equity in the US accounts and looking to pass CCAR going forward?

Tushar Morzaria, Group Finance Director

CECL, as you say, only affects our US GAAP reported accounts. We're obviously an IFRS reporter, so we're already on IFRS 9. US GAAP accounts in the local subsidiary doesn't really mean much, because it's the Group IFRS 9 basis that's the most important. You mentioned CCAR, and that's where it will have an effect, and that's probably the most important effect.

There are two things I'd point out. Firstly, there are still some discussions as to exactly how it will be implemented, but my understanding at the moment is that it doesn't apply in the same way that IFRS 9 covers drawn and undrawn balances. I don't think it covers undrawn balances, so I don't think it will be quite as pro-cyclical, or quite as conservative, as IFRS 9. We run the company on IFRS 9, so for all forms of stress testing and capital allocation, everything is done on an IFRS 9 basis. For local ICAAP and stress capital requirements, it's all done on IFRS 9 already. As I say, we think IFRS 9 is probably going to be more conservative than CECL as we understand it. Secondly, we think CECL will impact CCAR in 2022, so it's a little bit further out. Because we've already adopted IFRS 9, so our stress tests, rather than the regulator's stress test, become the binding constraint in many cases, so at the moment I don't think it will have a significant effect, if any. But it's three years out so it's something that will evolve over time.

Robert Sage, Macquarie

A quick question following some of the comments from RBS, which talked about slowing demand on the commercial side and relating it to Brexit. Looking at your numbers, it wasn't scintillating, but it had positive growth in UK Business Banking nevertheless, and the Corporate Banking numbers were also up, so I was just wondering if you could comment on the demand dynamics you're seeing within this sector at the moment?

Tushar Morzaria, Group Finance Director

On Corporate Banking, I would say that asset growth isn't quite where we would like it to be. We would be prepared to lend more than the demand we're seeing. On the flip side, we're probably growing deposits quicker than we may have expected as well, and that may be a mirror image of what's going on in those businesses, where there's perhaps some delay in putting their cash to work. Having deposits is still good for us, and we are seeing some asset growth, but it's too early to tell whether the delay in Brexit, whatever kind of delay it is, really has an impact on the way corporate and small businesses behave. Obviously, that delay really came about towards the end of March/ early April, and then you've got the Easter weekend, so it's a slowish commercial quarter in that regard. I think maybe in the next four to six weeks, we will have a better sense of whether there's a pickup in activity. It's steady, but slower than we would like. Conversely, cash balances are probably growing a bit quicker than we would expect.

Jason Napier, UBS

My first question is on IFRS 9. There are c.£13bn of stage two loans in Corporate, £12bn of which are still completely current in terms of their payments. I wonder if you might be able to give us a sense of the risks in the book – why are they in stage two, and what does that say about the outlook?

Secondly, on the cost flex in CIB. Would you mind giving us some sense as to how much flex you exerted on the business in Q1? I appreciate it gets circular, if revenues are really weak people may not leave, but there are questions as to how much you can actually hold costs back to a future quarter. It would be helpful if you could give us a sense as to what you managed to do in Q1.

Tushar Morzaria, Group Finance Director

IFRS 9 is a journey we're all on. Sometimes the complexity of the models can crowd out what's actually going on in corporate and consumer behaviour. One number that may be helpful is the net write-off in any one quarter, and for Q1 that was about £500m for us, which was slightly above the impairment charge – and that goes to the seasonal effect. Assuming activity levels stay where they are, I expect impairment charge to be a little bit higher than that, maybe by Q4, but that gives you a sense of what's really going on underneath in terms of the cash effects of impairment.

With regards to stage two, it's a function of the change in probability of default, which is quite sensitive. Even though everything's going well, no delinquencies, nothing goes into stage three, a slight change in client behaviour can change the probability as well, and these are very tight ranges, so it can slip backwards and forwards between stage one and two. There's nothing to say that they might not slip back into stage one if we go into a different sort of economic environment. Maybe the net write-offs would give you a better sense of what's going on under the covers as you get used to the models.

On cost flex in CIB, I'd say for Q1 the majority of the cost flex was through variable compensation. As you go through the quarter and as you see where things are shaping up for the quarter, I think the first place you would go is variable compensation.

Having said that, you have an outlook for the rest of the year, and that's where you can start speeding up spend or avoiding spend in other areas. I think we've already made some of those decisions, and we don't think it impacts income levels this year or next year necessarily, or even beyond, as more medium and longer-term investments will pick up some of the slack. If the environment gets more buoyant, we can always re-phase them and turn them back on. As you get later on in the year, particularly if we have a difficult Q4, then I think it always ends up being a variable compensation adjustment. I think what's really important, and the employees in the company understand it, is that we've got to have continued profitability. I don't think there's much doubt in people's minds as to what that means in terms of variable compensation levels. If profits aren't improving, then we will not have any qualms about using the full flexibility that we have there.

Jonathan Pierce, Numis

Can I ask you about capital generation? I suppose if you managed to get to 9% returns, we're probably looking at something in the order of maybe 120, 140 basis points of capital generation before any of the drags that are outside of the P&L account. Could you maybe give us a bit of a feel as to what your aspirations are for capital generation over the next year or two? And within that, can you talk in a little bit more detail about some of the non-P&L drags that are coming through? Pensions, redemptions of AT1 later this year etc.? And finally, alongside that, it would be helpful if you could give us an idea of the effects of risk-weighted assets inflation next year.

Tushar Morzaria, Group Finance Director

I think you're right in terms of capital generation coming from profits, that's pretty straightforward. I think from this point on, it looks like what I would characterise as a normal year for Barclays, where we either go flat or slightly backwards in capital in Q1, and then have a progression in Q2, Q3, Q4, so you should expect to see our capital ratio steadily increase from this point on for the remainder of the year. An important priority for us is that we think banks should be generating a lot of the free capital, and a lot of that should find its way back into shareholders' hands, that's a priority for us and we'll talk more about that as we go through the year.

In terms of calls on that capital that are inside the capital account rather than show up in our EPS, you're right to point out pensions. We have a pension [deficit reduction] contribution in April and another one in September, and that's articulated in the annual report. Regarding AT1 redemptions, I can't comment on whether we will or won't be redeeming an AT1, but were we to redeem at current exchange rates, I think the impact would be about 10bps on our CET1 ratio. I think those AT1s are due for call in September, so were we to call them, I don't know if that will fall in Q3 or Q4, there would be a 10bps impact. It may be different by the time we get there.

In terms of other RWA headwinds, we've talked about IFRS 16, that has come and gone, so the next one on the horizon is probably mortgage risk weights next year. I think that will be at the back end of next year. I haven't got a number to give you, but just looking at the comparisons to our UK peers, our risk weights are slightly higher, our loan to values are at the lower end compared to others, and we're on a through-the-cycle model already, so I think it would be relatively less significant versus our peers, but it all depends on how we model and what the PRA approves. That's not a number I worry about at the moment.

Beyond that, it's Basel IV. We will give guidance on Basel IV as best as we can, but again it feels a bit too early. There is a lot of things that affects national discretion, operational risk is a good example. We've been talking about the fundamental review of the trading book for two or three years already. At the moment, I think in CRR2 it's a disclosure-only requirement in [Pillar 3 report] on a standardised basis. All these things need to be fine-tuned and firmed up, and that feels more like a 2022 type guidance, so we will give guidance in good time for that.

Jonathan Pierce, Numis

Is there not a £4-5bn worth of risk-weighted assets coming through early next year on securitisation?

Tushar Morzaria, Group Finance Director

Again, I won't quote a number, but yes that will be a small headwind as well. We will give a number out nearer the time, but it's not on the worry list for me at the moment. There are a lot of things that are happening inside the bank on a day to day basis that you don't see, like tweaks and changes to methodologies. This is something all banks face, and it's something that just goes on. Some of them are just a little bit more in the public domain. There are things that would have happened last year that we haven't really talked about, as would have been true for all banks.

Raul Sinha, JP Morgan

Following up on the discussion on some of the RWA dead weight that still sits in the bank, I was wondering if you could talk about the Head Office. It has almost 10% of the equity allocated of the Group now, and the division is obviously loss-making this year, probably slightly more so than what you thought it would be, so could you comment on the Italian mortgages, and some of the other things inside Head Office? Is there anything you could do to optimise that? And how should we think about the drag from Head Office? Is there a sense of urgency to fix that drag from Head Office, or have you resigned to having a long-term fight? Please could you address that both from a P&L and a capital perspective?

Tushar Morzaria, Group Finance Director

There are three discrete components to Head Office RWA. There's the Absa component – to answer your question that will go when the Absa divestiture is complete. You're probably aware we have a lock-up on that position, which I think expires next summer, so that will give us the opportunity to divest of that if that feels attractive.

We have the Italian mortgages, which we would like to get rid of. The natural buyers of that are Italian banks. These are quite low-margin, relatively high-quality mortgages and they do nothing for us, really, but because they're relatively high-quality and low margin, the usual kinds of buyers in this space, private buyers, sponsors, etc. find it a less interesting asset. So a bank with a franchise there, with deposits, would find it more attractive. The Italian banking system's got its own things going on, but that would be the natural buyer. We would love to divest of them at the right price, for sure. But they're relatively high-quality at the moment.

The bulk of the remainder actually is the leftover from operational risk-weighted assets. As you're probably aware, we're on a basic indicator, or standardised approach, for setting operational risk-weighted assets. We have our Pillar 1 component frozen at about £56-57bn, and has been ever since I've been here, and probably before me. I'm not sure whether total capital for operational risk will really go anywhere because there's obviously a Pillar 1 and a Pillar 2 component.

I think there's a question to be had as to why it is in Pillar 1 and not Pillar 2. All [a switch will do] is optically increase our Pillar 1 reported ratio, and it would increase our MDA with it, so there's no real change in terms of distance to MDA, but optically it would look like you have a higher ratio and a higher requirement, which is consistent with some other banks. But that, I think, is going to be around for some time, at least in total capital.

So in terms of the equity allocation, it would be nice if it was only operational risk-weighted assets, the sort of leftover bits, that were in Head Office. I think that's a function of getting rid of Absa and getting rid of the Italian mortgages. With both we have an action to do and we'll do it whenever we can.

In terms of P&L, the RCI has obviously come out, so there won't be much left in legacy funding costs. Then you're just left with the hedge accounting unwinds predominantly, actually going back all the way from Non-Core. By the end of next year that should be pretty much done as well, so I do think there is a reasonable decline. If you look out with a crystal ball, if you don't have Italian mortgages, you don't have Absa, if your hedge accounting drag unwinds with the passage of time, I think you're just left with a chunk of operational risk-weighted assets, or maybe that moves to Pillar 2, but that is sort of left arm, right arm.

Raul Sinha, JP Morgan

On Barclaycard UK – that line was seasonally quite regressed compared to my expectations. There might have been a bit of seasonality in its tick-down, but you've flagged a very cautious appetite since the referendum. I wonder whether that book will go up from here, or are you reducing your customer base and your balances actively, or is just your existing clients drawing down less and they will come back and spend more?

Tushar Morzaria, Group Finance Director

We've taken, as you rightly pointed out, a relatively cautious stance in the UK. That's very much the case for unsecured, less so for secured, and I think it will be a continuation of where we've been for the last two or three years – I don't expect unsecured to move much at all. You'll see us active in advertising and branding, but I don't think you'll see significant balance growth, given our risk outlook. We would, however, expect to see secured grow. We talked about it a little earlier, we would like to grow business banking assets as well, to the extent there's demand for them.

Mortgage applications are actually pretty healthy in the first quarter, and I would expect to see that balance sheet grow for the remainder of the year. You can see it quite visibly, it's a relatively forecastable business in that sense, we do see the asset growth coming. We would expect to see income growth off the back of it as we get through the rest of the year, but again we are focused on the secured rather than the unsecured side.

Raul Sinha, JP Morgan

Maybe just a specific question on the unsecured side, do you look at the revenue margin of that business? Should we expect that to contract, given the changes coming through from the overdraft?

Tushar Morzaria, Group Finance Director

We had already switched, so our overdraft pricing schedule hasn't really changed for some time now. I think we were the first mover to move away from charging overdraft fees and make it an interest-focused calculation, that was probably five years back. It will just be demand-driven, I don't think we're any more cautious now than we have been, so I don't think you'll see us reducing risk appetite any further.

We would like to grow mortgages slightly more than what we are doing. In Q4 pricing was getting very punchy, and demand was seasonally low. In Q1, we've seen a reversal of both of those trends, so we feel a bit more optimistic about that.

Chris Cant, Autonomous

Coming back on the discussion you were having around the cost flex. In the first quarter it was primarily through the variable remuneration line. I just want to understand how you're practically managing this, now that you do have this flexibility. If we have good quarters in the Investment Bank for the remainder of the year, would there be a catch-up, in effect, on compensation that was foregone in the first quarter? How are you thinking about total remuneration for the full year? Or are you managing quarter to quarter? Is your first quarter compensation accrual based on your presumably revised lower expectations for the full year, which could then be increased again? I'm just thinking back a couple of years, I can't remember which fiscal year it was, but you had a year where you had a surprise catch-up in the fourth quarter in Investment Banking remunerations.

Tushar Morzaria, Group Finance Director

Yes, that was in 2013.

Chris Cant, Autonomous

Is that off the cards, or could that happen again?

Tushar Morzaria, Group Finance Director

That is off the cards. You're right to point that out, in 2013 that was exactly what happened. I go back to my earlier point, it is extremely important for us to show profits increase in the CIB and variable compensation is going to be a lever that will be applied to ensure that. If performance improves and profits go up, we will balance that accordingly. Now, not under every single environment will you be able to bring down variable compensation to just show profit, we'll have to be sensible about it, but that's our guiding star and everybody understands that.

Chris Cant, Autonomous

So when you set your first quarter compensation accrual, is that just based on the first quarter performance, or is that based on your extrapolations for the full year? How do you manage that practically?

Tushar Morzaria, Group Finance Director

It's both, for sure. We have an eye to full-year all the time, but it's less forecastable than some of our balance sheet orientated banking businesses. We have a sense of what the fee pool will look like, we have a sense of what sales in trading etc., will be like, as well as balancing what the quarter shaped up to be. I'm not sure you can say it's one or the other – you have to do it with both things in mind. I think if everything goes according to plan, then you'd expect us to go back to normal accrual rates. If things improve, maybe there will be a scoped increase, and if things deteriorate, we will reduce them. But the guiding star is improved profitability over the course of the 12 months, that's the most important thing.

Andrew Coombs, Citi

Subject to everything you've said about the revenue outlook, what does that mean for compensation accrual? If you take the Q1 cost base, annualise it, add the bank levy, I think you're looking at about £13.3bn. Obviously you've given quite a lot of bandwidth in your guidance – you said you can go below £13.6bn without quantifying; but if we do that simplistic exercise, is there any big investment plan for Q2, Q3, Q4, that we should be aware of that would knock that out?

Tushar Morzaria, Group Finance Director

No, I don't think so. Like with everything, just be a little bit careful annualising it because we brought down variable compensation in the first quarter so you're assuming that times four, which may or may not turn out. We don't know the answer to that. But there's no big bulk of investment that's coming that we haven't talked about that's going to skew up a quarter, or even the remaining three quarters, from here.

We gave a range at the time we talked about the cost flex, to ensure that we have enough latitude to get to our current target. Like with all other things, there is a lot of things that are just different – the rate environment is different, unemployment levels are different, GDP is lower, Brexit hasn't really happened, tax rates are better. It just feels that we need slightly more cost flex to ensure that we can achieve our profitability objectives under most outcomes, but probably not under every outcome.

We certainly haven't told you how far below we'll go. We'll probably have to talk more in detail about that as we go through the year, as we know how the full-year is shaping up.

Andrew Coombs, Citi

If it's a function to Q1 – as you say it was predominantly compensation flex that drove it down, I guess it's a case of you lowering the cost base below £13.6bn this year. Should the revenue environment improve next year, presumably that cost base can then start accreting again?

Tushar Morzaria, Group Finance Director

Maybe. The anchor we have is a 60% cost income ratio. I think we really wouldn't be comfortable going materially backwards in the cost income ratio. We want to keep on progressing towards the 60%. I think we were at about 62% in Q1, so we're not quite there yet. We've been as low as 59% in one of the quarters last year. Seeing the cost income ratio glide down is also very important for us. If revenues were to bounce back a lot, you wouldn't expect costs to increase by the same amount. You would try and capture that in positive jaws.

Andrew Coombs, Citi

You're very much thinking about cost income as a target, as opposed to an absolute cost number then?

Tushar Morzaria, Group Finance Director

Yes, but to help you out and give you a sense of how we're thinking about income as well, at this stage we're giving you absolute cost numbers, and we may have to continue to do that. It's a little bit hard to have full visibility of the top line.

Alvaro Serrano, Morgan Stanley

In terms of when you think to pull the trigger on capacity adjustments, clearly the Q1 environment has been very tough. Would you wait until the second-half of the year, given the first-half is typically better? When you think through it in the current environment, and looking at competition, why have you held back? And what would make you change your mind?

Tushar Morzaria, Group Finance Director

We've made some of those decisions already. The Executive Committee of Barclays gets together for one or two days roughly every four to six weeks, and those sessions are away from the day to day management of the company, to make sure that they're looking at it with a longer-term view. We've already had those sessions, and we've already made some decisions to slow-down and re-pace some of the investments. This won't change the medium, long-term outlook, it's just there are some things you want to pace appropriately to your current level of profitability. We've made those decisions already.

I think as you get to the second-half of the year, any decision you're making are probably affecting the following year rather than the current year. We probably have a very small window left of current year impacts, should we choose to take them, otherwise it's really going to be beneficial to next year. But we've made many of those decisions already.

Alvaro Serrano, Morgan Stanley

I was actually thinking more into next year, when you think about the 9% and 10% RoTE targets.

Tushar Morzaria, Group Finance Director

We could probably go into Q120 to make a 2020 effect, so we've got a bit of time. As I say, we review this monthly just to make sure we've got the pace. Now that we are away from restructuring and legal entity vehicles and getting ready for CCAR etc., we have a lot more discretion on our Capex, and you can choose the pace at which you roll things out and prioritise things. Housing everything in Barclays Services, BX, as our services division is called, means that because it's all centralised you have a much better grip and handle on what's being spent where and what the pay back periods are.

Oddly enough, in some ways we find it perhaps slightly easier to make those decisions in a post-ring-fencing world than when we were much more decentralised. But yes, we could probably go another three quarters and still make decisions that would impact 2020 if we choose to do that.

Ian Gordon, Investec

In terms of RWA evolution by divisions, I think you've been fairly explicit that the Q1 moves were nothing more than the usual seasonality, i.e. US consumer down, UK not much and IB up. If I'm missing anything, let me know. Last quarter when we met here you kind of characterised your ongoing objective as IB flat and then growth elsewhere, primarily US. Consensus does its maths based on that guidance and gets to numbers that are quite materially below Group targets, which I think Jes fairly firmly reaffirms in his

Bloomberg interview, how do you think about the pace of evolution? Clearly the guidance you've given points to IB slowly shrinking as a proportion of the Group, but how radical a change do you think you would get to on a five-year view?

Tushar Morzaria, Group Finance Director

When you say it's different to where the market is, do you mean returns?

Ian Gordon, Investec

Yes, returns.

Tushar Morzaria, Group Finance Director

It's always tricky to forecast out five years, but the objective here is definitely not to grow the CIB. We feel the CIB has the right quantum of capital and our market positions are sufficient for us to have a competitive business. It has to earn a level of profitability that is sensible, and therefore we wouldn't be putting any more capital into it until it's at least able to do that. And when that is, everyone will have their own views on that.

Regardless of that, we would want to grow our consumer businesses anyway, just to have a slightly better balance in the Group. Unfortunately, these are changes on small numbers on the consumer side, so it takes time. I think we're coming close to something like 10% in our UK bank, and something like 20% in CCP, but relatively small levels of capital in absolute terms. I think if you can grow it at those kinds of paces, and I'm talking year on year, that will be quite a bit. If we do that over five years, I think the needle starts moving.

In terms of returns objective, I think someone has asked a question around consensus is somewhere around low 8%, but we're still targeting 9%, so what's driving the difference? Again, without trying to go through line by line – you have your own views on outlooks and forecasts, as do we. I would say that on the income side, I think I'd be cautious in encouraging people to just annualise Q1 income. I think the seasonal shape might be a little bit different. IB fees, for example, is probably at the low end in Q1. We would expect to see the UK income grow year on year.

CCP should continue to grow. You'll have your own views on how much growth that is, and how likely that is, but that's how we think of the income shape. There were also some headwinds that may or may not repeat, so for example we had portfolio management hedge losses in our Corporate Lending line of c.£50m. Again, I wouldn't annualise that. It may recur, it may not, it may go the other way.

On the impairment line, it feels pretty benign, at least for the short-term indicators, so I'd be a bit cautious extrapolating that too far out. But at the moment I look at our corporate watch list, delinquencies, affordability, spend behaviour, it all feels reasonably benign. You'll have your own view on what that yields.

On the cost flex, depending on how the year shapes up, we will match our costs where that's appropriate to do so. The only other line item that is a bit more complicated this time around is the tax line, because of IAS12. In new money terms, post IAS12, an effective tax rate of somewhere around 20% feels about right for the year. Remember, this accounting change doesn't make any difference to reported returns, so it's just an accounting funny rather than an economic change.

Ivan Zubo, HSBC

I have a credit related question. If you're thinking about the cost of your credit capital stack, so AT1, Tier 2, MREL, we've seen that Q1 has been extremely benign, so spreads have compressed quite a bit, but clearly that wasn't the case in Q4. I think it's probably fair to say that for UK banks a lot of that was related to headlines about Brexit – when there are negative headlines, the spreads widen, and vice-versa. Are you thinking about potentially prefunding some of your plan for this year, or maybe even next year, given the low level of spread? How are you thinking about it especially given potentially more volatility with the Brexit deadline now being pushed over to October?

Tushar Morzaria, Group Finance Director

We've actually been a reasonably consistent issuer over the last couple of years, issuing about £12bn of MREL. This year, we're targeting £8bn, because we thought funding markets will be a little bit choppier, given Brexit. I guess that was the case, particularly until we got further into Q1. We've never yet regretted over-issuing, so we normally try to target about £10bn and manage to do £12bn. I still think spreads are at very attractive levels, but I think what's really important for us is to only issue where there's investor demand, and not over-issue, to match demand with supply.

To the extent the market is receptive to that, and to the extent it makes sense for us as an issuer, then I think we'll always be open-minded in satisfying that demand. I think we feel pretty confident that we'll get £8bn done, whether we'll do any more than that, I don't know. And some of it will be driven by you guys, if you have a demand that makes sense for us then we'll look to satisfy it. If you don't have the demand then I don't think we'll go there.

David Lock, Deutsche Bank

My first question is on the UK business. You made some comments around income being higher year on year, or expect it to be higher year on year for 2019, and you're also sticking to the first-half being with negative jaws. This implies that it's going to be quite a big jump-up in costs in Q2 – I just wanted to check whether that's correct. And is there a particular programme you've been working on?

And then just looking a bit further out at consensus, the bank levy is obviously coming down in 2021, I just wanted to check that you thought the £230m, which I think is what consensus has in for 2021, is reasonable?

Tushar Morzaria, Group Finance Director

On bank levy in 2021, we'll have to wait until closer to the time to find out the UK Governments' intentions. I won't make a comment on 2021, but yes, substantially lower than where it is on today's level is the right of to think of it.

David Lock, Deutsche Bank

That's the point I was trying to make – I think it's £260m or something in 2020, so it's not substantially lower at the moment.

Tushar Morzaria, Group Finance Director

I would agree. Assuming it's just applied to the UK balance sheet, then it's a fairly meaningful reduction.

Back to your other question on Q2 UK. There's nothing other than just seasonal effects that we can see. A good example would be the pace of branch closures. We know when there are certain costs that we'll experience. It's reasonably visible, and nothing more than that. You've also seen us take some charges at the back end of last year, and we had some quite meaningful headcount reductions and closed certain centres. We get the benefits of that in the second half of the year, so that's why you see that shape being what it is.

James Invine, SocGen

Could you just say a little bit more about the management changes in the Investment Bank? You've clearly had a bit of a renaissance thanks to Tim, and now he's gone. I know Jes said that he wants to be closer to the people on the ground. If you could just outline what that actually means, and what wasn't quite optimal when he was in-post?

Tushar Morzaria, Group Finance Director

It wasn't to do with that as much – it was actually a little bit more of a by-product. Ashok Vaswani had run the UK bank for some time, having a much broader role, looking at all of our consumer businesses. One of the consequences of ring-fencing is that you have very adjacent consumer businesses split across the ring-fence, for example, our acquiring business and our debit, credit card business, UK retail, small business. That's just one example. We also want to use some of the technology there, maybe with our US Cards business. We want to keep the intellectual property centrally. It was very important to give Ashok that responsibility – the Board and Jes were very keen on doing that. As a consequence of that, Tim may have felt that his job was a smaller job than the one he had, and that wasn't something he wanted to persist with.

I think Tim did an excellent job of, like you say, resetting the management team in the Investment Bank, and we've seen that in the improvement in the relevance that we have with our client base. I think that has a pretty good momentum and will outlive Tim, so full credit and respect to him for doing that. I think Jes wanting to get closer to the CIB is the natural by-product. It's really, really important that we continue to drive profitability of the CIB up, and having more proximity to enable him to implement something was important. But it was really driven by the objective of trying to give Ashok a broader consumer reach than anything else.

Ed Firth, KBW

Coming back again to this week's AGM, the Board and the strategic discussions, I guess you've talked about this any number of times in the past, but if I look at your valuation today, it's difficult to know how much equity is in the Investment Bank because you don't tell us. I assume, based on price to book etc., it's valued at zero, or arguably somewhat less than zero. And if I've got your arguments right, the argument against reducing it is the cost of doing that would be more than the benefits that you might achieve in terms of the mathematics.

It's very difficult for me to get any sense as to how we can test that. Are we talking about redundancy costs? Is it the level three assets? You've got almost £20bn of level three assets – are these things that if you try to reduce them they'll go down? There must be some sort of spectrum; I'm sure you could take a billion of risk-weighted assets out of the Investment Bank without any cost at all, I assume. So is there a level at which it suddenly starts to ramp up the costs? Or is it genuinely that is the absolute minimum you think you can run with?

Tushar Morzaria, Group Finance Director

It's an important topic. There are judgements involved here. It's hard for this to be super scientific – at this point things don't work and at this point they do work. It's never going to be as black and white as that. It's a business judgement as to what scale and size you need to be to generate a level of profitability that justifies the scale and size, and whether it's a ratcheting-down effect if you start shrinking.

Our judgement is that you ratchet down significantly from here – again, significantly is a qualitative. I don't think £1bn would make much difference, and you see a flex of £1 billion here or there in just the regular course of business. But we do think it will be quite difficult to execute any significant ratchet down and free up capital. Now that's a judgement; a lot of people have tried to do this and there aren't many cases, if any, of being able to do it very successfully, including our own. We had a non-core unit for over three years. You can go back and look at the costs of exiting that and what it did to our earnings per share and how much capital it generated.

Of course, when you start off with a big number, it's easier to do the first step, second step harder, third step harder, fourth step harder. So I think you can't even extrapolate, it probably has a kick-up to it. Other banks have tried it, and you can see how difficult they found it as well. The thing with the business, in simple terms, is revenues can dry up very quickly but costs, if anything, magnify, rather than decrease. For example, you'd have to start charging off intangibles, real estate, onerous leases, let alone severance costs and stuff like that. At the same time, your revenue, unlike a balance sheet orientated banking business, or branch banking business, where you've still got net interest income coming through the door that can help manage that part; I think in an investment banking business, which is much more of a human capital business, it's a much trickier thing to deal with. But these are judgements that we've engaged lots and lots of people and looked at it from lots and lots of different angles, poring over as to what to do and what's the right strategy.

Ed Firth, KBW

So it's more about ongoing losses it would generate, in the sense that it's a revenue dry-up and the continuation of costs, rather than balance sheet asset write-down that you'd have to take.

Tushar Morzaria, Group Finance Director

You should go back and look at some of the non-core profiles – it gives you a sense of how quickly revenues dry up, and then the costs of exiting that non-core, let alone exiting the assets as well, which usually changes the price of that asset quite quickly.

Ed Firth, KBW

The way you're looking at it is whether the losses would be more than, broadly speaking, 13% of your risk-weighted assets. Is that broadly the way you look at it?

Tushar Morzaria, Group Finance Director

At the end of the day, you're reducing your earnings so to make that equation work, you need capital out that can justify that earnings loss. You have to look at it with that equation in mind.

Martin Leitgeb, Goldman Sachs

Could I just follow-up on the growth ambitions and the comments made earlier on UK mortgages? Specifically, on the outlook for UK cards, Barclays hasn't grown balances since around 2016. I was just wondering what would make you more positive here in terms of the outlook for growth, obviously being a high return on equity platform for the overall Group? Could that change in economic outlook make you more positive, or is it because your share in cards in the UK is relatively high compared to your share in current accounts, and you're comfortable where you are now? Could this improve going forward, or is this something you would expect to last?

Tushar Morzaria, Group Finance Director

No, I think it could improve going forward. It turned out we were too early, or even wrong, but we thought the UK would have a more difficult economic environment post the EU referendum back in 2016. And unsecured credits is obviously where you get hurt most, so that was the area that we were most cautious about. It turned out that hasn't happened, which in some ways is okay. It's hard to feel that it was still the right call, based on the risk-rewards. But things worked out better, which is a good thing for us as well. So we still have either the largest or at least top equal largest card business in the UK, and it is incredibly profitable.

I think if we were to go through a cycle, or go through something that could tell us that we could look to good stable economic growth in the UK over a period, then we would absolutely grow unsecured balances, but the geopolitical environment just makes that a bit trickier. There are two things we did not quite get right when we made this call – one was the currency adjustment, which was more orderly and provided a sort of monetary stimulus that most people underestimated; the other thing was both Europe and the US had above trend growth after 2016, particularly if you remember Donald Trump was elected in November. I think it turns out that the UK, because it's so connected to those two largest trading blocks in the world, it gets pulled along. And I think, when we look at it now, the US looks fine and actually still feels like it's above trend. Europe is more questionable – you've got Germany almost at zero, and I think Italy may be in a technical recession, so that just feels a little bit more of a worry for us at the moment.

I think we'll continue to be cautious on the unsecured side, but that's not a permanent call. We will look to change that when it's appropriate.

Guy Stebbings, Exane

Can I come back to some of the comments on mortgages? You suggested that pricing pressures had eased somewhat in recent weeks, which is quite a stark contrast to comments from RBS a day later, so I am just trying to understand where you're seeing that pricing pressure ease. And if we bring that back to Barclays UK NIM outlook, it has obviously fallen regularly in recent quarters – are we at a point now where you think it starts to bottom out if that pricing pressure has eased, and we can offset the mix effect that's been coming through in the past?

Tushar Morzaria, Group Finance Director

I wouldn't overstate the pricing improvements. It wasn't a massive rebound, but it did tick up slightly. Again, it may be a product mix; we're all operating in slightly different parts of the mortgage market. For us, the higher component of the market share is the re-mortgage market through the broker channels, and that's what we look at first and foremost. I think up until the first quarter, we saw a little bit more pricing compression in the more high-margin products. That may be where other competitors are more sensitive than we are. It's good business but not something we're as visible in.

In terms of NIM, I think if we continue to grow our secured relative to unsecured, you will continue to see some slight compression. It's just maths, it's nothing more than that. Even if mortgage margins were to improve, you're still diluting your NIM because they're never going to be as wide as unsecured margins. Sure, the gradient will be less, but I think it has a mathematical effect coming through that would offset that. The only way that would also stabilise is if deposits grow above expectations; that would be the other offsetting effect, which we saw a little bit of in Q1.

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