

**Barclays PLC 2015 Interim Results****Analyst breakfast Q&A transcript – 06 November 2015****(amended in places to improve readability only)****Tushar Morzaria, Barclays Group Finance Director**

Let me start off with some introductory comments. I have the usual five points that I touch on every time we get together, so the four or five things that I look at to see if we're making progress in our strategy; first and foremost is our Core bank, the future of Barclays and are we able to make a double-digit return on equity in the Core bank. And again, on a year to date basis, we were 10.5% return on equity, or just over 11.5% if you ignore CTA charges. And ignoring CTA charges we'd be in double digits in the third quarter as well.

And that's important for us - that's the look-through, forward view of Barclays. It's good progress for us because obviously the equity allocation in the Core bank does increase as we run down the Non-Core, so to keep that double-digit return going we do need to increase profits of course, and profits were up in the Core bank again for the third quarter compared to its previous-year comparison. And that's been the case for some time now. Every quarter we're able to keep on nudging up profits so that our returns stay healthy there.

The third quarter was quite pleasing in that regard. We had a strong operational performance in all four of those divisions; profits up in all of those divisions, in fact. Africa profits were up in local currency, not on a sterling basis, obviously there was a fairly significant weakening in the Rand.

The other thing I'd just point out in the Core bank – most people do ignore it and you're right to ignore it in the sense that we try and keep it very small – is Head Office, which is relatively small but did have a negative income for the first time in some quarters. So I'd just remind you, I did say that in the second half; just watch out, it can go negative. And some of you chose to not to pay that much attention to it, which is fine because it's quite small, but it does go negative and it does go positive so just watch out for that.

The second thing is Non-Core; Non-Core needs to shrink in almost any which way you measure it, from

our perspective. We had a modest improvement in Non-Core; RWAs were down a bit, leverage was down actually a reasonable amount. The underlying trend there is still intact. You'll have quarters where there'll be some fairly significant reductions. We've had quarters where, I think, as much as £20 billion of risk-weighted assets have gone out in a quarter; this quarter was obviously far less.

But the trend's more important; it won't be a linear thing. It will zigzag around a bit but if you look forward in two/three quarters' time, you'll see that the trend's been as it has been historically; a relatively controlled progression towards shrinkage both on leverage and risk-weighted assets.

We had a good activity in the third quarter of underlying M&A; we sold our Portuguese bank, we announced the sale of that; we sold the First Plus mortgage portfolio, that's got into the press; and there're a few other things going on that you don't see the capital effect of necessarily or the asset reduction effect of in the third quarter itself. But the activity levels we were quite pleased with so the trend is reasonable there.

We have given a little new guidance on Non-Core. You'll be familiar already with the £20 billion of risk-weighted assets that we're targeting for the end of 2017. We've also guided towards a cost way-point at the end of 2016 for Non-Core, just to give you a checkpoint of what we expect our cost run-rate to be at that point, though it'll be lower again in 2017.

The reason for that is twofold really, to give guidance in that way. Of course our real objective function here is to shrink Non-Core to the point that when we fold it back into Core it's a minimal dilution effect on the Core businesses, and of course the dilution effect will be driven by the amount of capital that'll still be consumed in Non-Core at that point as well as the negative P&L that it will exhibit. Capital we've always been guiding on in terms of risk-weighted assets as the proxy for that. The cost way-point just gives you a sense of how you should expect to see the Non-Core cost component of that negative P&L track down. It is a way-point – don't necessarily think of that as a run-rate for 2017 – as you'd see it continue to glide downwards.

Third thing on my list is capital. It was flat as we expected, 11.1% CET1, slightly up on leverage by 10 basis points. Again, it's been measured progress for us. We've had good capital progression for six, seven, eight quarters now, where we've accreted about 200 basis points, as well as put a lot of large one-off capital items behind us – be it FX provisions, be it quite sizeable provisions in PPI and various other related matters.

So the way in which we're able to navigate through capital earnings releases as well as capital hits, if you like, has been a good journey for us. Again, it won't always be linear. I mentioned that at the half-year, and this is an example of such a quarter where it won't be linear but we still feel confident in our

ability to continue our progression, probably on a slightly more measured trajectory than we've had to up until now, but still targeting to get over 12% as our next important milestone.

Just to give you an example of the ability that we have in terms of navigating our capital position, if you look at the Q3 itself, we didn't touch too much on this on the call, but there was quite a significant number of adjusting items which had negative capital effects. We had the RMBS and CDS settlements, we've had a UK conduct charge and we did sell our Portuguese bank. You add all those three up – because you don't get the capital benefit of the sale of Portugal until it deconsolidates – you add all those three up, you get c. £700 million negative. And then we had a large PVA move, about £500 million, so you get to about £1.2 billion. £1.2 billion as a capital matter for us is about c. 30 basis points, so it's important that we're able to absorb that kind of headwind, if you like, in any one particular quarter and not go backwards in capital. So we feel good in our ability to continue to navigate this relatively effectively.

Fourth thing is costs; costs of course need to go down progressively and as you know, for the last couple of years we've given quite hard specific cost guidance, which is still something that we've continued to guide to in 2016 although we've revised guidance and I'll come on to that.

It's worth just reminding where we've got to on cost and then talk about where we're going to go. Costs in 2014 were lower than 2013, costs in 2015 will be lower than 2014, and costs in 2016 will be lower than 2015, and this is all in, any which way you want to measure it. We've got a menu of cost line items that we publish for you and you can add up whichever variety of them you like, whether it's Op Ex, conduct and litigation, bank levy, CTA and now we'll open up a new line for SRP.

But take your pick, add them all up, add a subset of them up. We've historically tended to look at it as Op Ex, conduct and litigation and bank levy, but you could throw CTA in there as well, and from now on you'll be able to throw in ring-fencing costs. But when you add all of that up in whatever total you want to do, costs are down every single year and that's really important for us. So no matter what things come and go our way, whether FX moves for us or against us, whether the bank levy rate increases, whether we need to take additional cost to exit businesses we didn't anticipate closing, whether we've got intangible write-offs, software cap write-offs, or whatever; putting all of that into the mix for Barclays, costs will be down. This will be the second year in succession, next year will be the third year in succession, any which way you measure it.

In this year we have had a number of things go against us which I haven't spent a whole load of time calling out because I think you'd probably just expect us to manage most of these things. There'll be swings and roundabouts. We've had some things go for us, as we did in 2014, which I'll come back to, but in 2015 we closed the US Wealth business – that's due to close in December and some of those

costs are in CTA and some of those are above the line so that's taken out cost capacity.

We have written off intangibles. We called out the closure of our Bespoke offerings in Barclaycard but there's also, for example, things we haven't called out historically and probably won't do going forward but for example, software capitalisation as we consolidate things onto a single stack. We've obviously had the bank levy rate increase quite materially; it's gone up 40% and you get a full-year effect of that next year.

So if I was to call all that stuff out, and just give you context, we're probably running closer to £16 billion if you strip all of that out, but we haven't revised guidance. So the only point I wanted to make really was that as a discipline in terms of wanting to drive down costs year after year, it's still there, [absorbing] things that don't go our way as much as we can.

In 2014 I did mention that a few things did go our way; foreign exchange rates were particularly helpful and when that's material we'll revise guidance downwards, as we did in 2014. You'll recall we started at £17.5 billion [cost guidance for the year], we dropped it down to £17 billion and finally came in a little bit underneath that. We probably don't [mention it enough] but the £16.3 billion [2015 cost guidance] actually was originally £16.8 billion – but again, just wanting to remind folks that we'll try and be as straightforward as we can about this. Lot of things, I think, will just be swings and roundabouts, but where we see things go particularly in our favour we'll try and be [transparent] about that and when things go against us we'll do everything we can to absorb it.

In terms of where we go from here, we obviously had guidance out there of £14.5 billion [for the Core in 2016]. We have in some ways revised that. We still want to get to £14.5 billion, but we'll call out ring-fencing [implementation] costs separate from that. The reason why we did that – it was our full intention coming into 2016 to actually absorb ring-fencing costs – we now have a lot more, obviously, precision than we had in 2014 when we were initially projecting it out over the three years.

The thing that changed as we got closer to 2016, a couple of things, one is the sequencing of it. A lot of that's going to happen in 2016 so a little bit different to how we were projecting it from when we were originally setting up our targets. And to absorb that we would have had to ask two of the businesses that we'd like to protect as much as we can from costs down-draughts, like Barclaycard and parts of PCB, would have had to take up some of that slack. There's only so much we could take out of, for example, the Investment Bank in a calendar year.

Now, we had the choice. We could have done that but we felt that that would not have been in the company's long-term interests for 2017 and 2018, so the Board decided we should call them [the SRP implementation costs] out, itemise them separately so investors are aware of what we're doing, how

much we're spending. They are one-off in nature, they're not run-rate. A run-rate will be included in Op Ex, so think of it like a CTA-type concept; CTA doesn't revert back up the line, once it's spent it goes and Op Ex stays down at the reduced levels. Ring-fencing costs will have that same characteristic; they're not run-rate expenses. And just to stand back again and reaffirm, costs will be down next year on an absolute level, just as they were this year and the previous year. So that's costs.

So number five on my list are legacy items of the past that we want to put behind us. And obviously you've seen us take a few items in the third quarter. In some ways this has got two components to it. One is we do want to work through the long list of items we have as relatively quickly as we can, but at the same time do it in a way that's constructive to our capital position. So again just to remind you that we have a list of items, we do need to work through them. We've worked through them relatively efficiently over the last couple of years. I was just totting up as I was preparing for the third quarter; you know, we raised about £6 billion of capital in 2013; I think I've mostly spent that already and it's quite eye-opening when you look back, how much has gone through the books but yet our capital position has inched up quite well. So more to do on that but the other important thing is we don't need to add to that list so the continued reduction is important to us.

So to wrap up those five points; double-digit returns [in the Core], Non-Core shrinkage, capital improvement, cost control and working through our legacy items.

Just a couple of other things before I hand over to Q&A. I did give some guidance for the short-term and it's just worth reminding you of that. I did call out that October results in the Investment Bank were weaker than this time last year. I think that seems to be something that's consistent with quite a few others that have commented. And we had our own US bank analyst, Jason Goldberg, who looked at US filings, 10Qs, that have just recently filed and he noticed that a few banks called out a similar effect to us in their outlook section. So I'm sure you've probably already picked that up but it's worth reminding you of that.

Credit card impairment; you'll recall this time last year we had a tick-up in impairment to do with recalibrating our models to our time series. It's actually a regular thing for us, it's about this time of the year that we always recalibrate our models and you should expect to see a similar effect as you saw last year into Q4, so as you think about how Q4 looks just watch out for that.

I'll remind you once again, Head Office can be negative as well as positive so take that in the spirit it's meant to be.

And the final thing is – well, final two things – don't forget about the tax rate. The levy comes in and is booked in the fourth quarter and that's non-deductible, so just watch out for the effect that has on the

effective tax rate on the quarter. And the only other thing I'd say is, as we continue to drive down costs, we're on the hunt for opportunities to do more where we can. Now, in CTA we are guiding towards a £700 million budget for this year. Included in there, as I say, is a component of the [US] Wealth exit costs. Now, that's obviously consumed up some capacity so we're thinking about whether if we see other opportunities, whether we keep going because this will obviously be accretive to ROE next year and lower our costs next year. But that's something that's in our minds at the moment but we haven't made any decisions on that yet.

I think that's probably it. I'm sure you'll have some other questions around the numbers; I'll probably leave that to Q&A.

**Jason Napier, UBS**

Morning. One detail and one, perhaps, more general question. The first was the FX provision in the UK, the £290 million in the last quarter. I'm not sure whether I caught a discussion as to which customers are affected, how we think about adequacy of that and just the nature of that provision please.

And then secondly on ring-fencing, I appreciate that you have a lot more precision now in being able to scope the number and seeking to protect capex in the divisions that are growing and so on. But I guess if you could give us some sense, even at a really high level, what the buckets of spend are because the numbers are gargantuan, I mean, in absolute terms. We get dulled to the billions of things. What is it that you actually get for all of this money spent? How many people are devoted to the project, how much can it really cost to have independent access to payment systems and so on? If you could just help us understand how it is that it's one-off and why we don't expect any of this to result in an asset on the balance sheet, which are kind of below the line charges, and there's nothing really to show for it in three years' time.

**Tushar Morzaria**

Yes, so on the FX provision you haven't missed any detailed commentary on customer cohorts or anything like that, we haven't called that out. It's not at all related to provisions that we took earlier in the year with regard to the Department of Justice action and the civil cases around that, it's completely separate and distinct from that, it's a discrete set of issues.

It's still something we're working through with the regulators as well and it's really helpful to give a running commentary on this but in terms of helping you with the adequacy of the provision, we're trying to be prudent in taking this provision. I don't think of it like PPI where every single quarter there may be a revision or something like that. This won't have anything like those characteristics. It's a reasonably prudent provision but there's not much more I can say about that at this stage, given the dynamic nature of the discussions that we're having with the regulators.

Again, put it this way, it's not in the Investment Bank, how you'd think about the provision that we had for the Department of Justice action. It's customers as opposed to clients but – I don't want to get too specific in the nature of it – it's a very defined cohort actually. It's not across our entire customer base, it's a slice of the customer base, a very precise slice and it's from a specific time period, 2005-2012, so in many ways in that sense it's isolated and boxed. Of course there's a number of transactions that have gone through over that seven-year period and that's why it's quite a data exercise to make sure that we've captured everything and got it right, and we've been prudent in the way we've provided to ensure we're managing that appropriately.

On ring-fencing, these numbers are eye-catching and you're absolutely right, you get a little bit numb to it these days; a few hundred million here or there is not extraordinary. It covers ring-fencing globally so really the United States and the United Kingdom and it's a bit more front-loaded into the US and back-loaded in the UK.

In the US it's really reorganising our operations in the US to fit underneath an intermediate holding company, which is going to sit like a US bank holding company to ensure we are compliant with all the requirements that a US bank holding company needs to do from a regulatory standpoint. The most significant aspect of that is CCAR and the stress-testing. This is something that is an immensely detailed, complicated process for us so you have to reconfigure everything such that you have an entity lens, in fact an intermediate holding company lens, so it's even slightly more completed than that. You've got to project out very detailed, what's called PPNR, pre-provision revenues. You get sets of scenarios that are going to change every single year. You have to give very granular projections of how your revenues will look using quite sophisticated econometric models. You then need another set of econometric models that is independently used to validate that and challenge the business' projections, and then there's an even more, very detailed commentary around why that's an appropriate extrapolation.

On top of that you need to submit very detailed risk management information along with each of those scenarios and stuff that we and all banks didn't do until the requirement of CCARs. I think there are trillions of data fields that need to get sent over. In terms of the number of people working on it we have hundreds, up to 1,000 already working on this project. I mean, it's a very scalable project. It's a build, you don't need only 1,000 people building models and validating them and testing them and regression.

And we have a dry run in 2017 and a public run, if you like, in 2018, so the build work is really in advance of the dry run and then any fine-tunings we will need to do. The Fed will give us private feedback then for a public run in 2018. The intermediate holding company itself, as a physical matter, will be incorporated in July of next year along with the statutory provisions so then it's a legal form

reorganisation of our businesses...

It has other things which aren't particularly expensive but time-consuming. You've got to have an independent board, you've got to have independent risk committees and that kind of stuff. So not necessarily bucket loads of money on that kind of stuff but nonetheless quite important to get all that in place and right.

The thing with CCAR that is quite interesting is that very few banks seem to fail the numeric requirements but do fail the qualitative requirements, so the bar in terms of the quality in which management can stress their books and forward-stress their books and deploy theoretical management actions etc. is a very high bar and that's why it's a lot of detailed systems build to do this for the first time for us. And of course the US banks have been doing this for a number of years and, you know, they still occasionally slip up.

The UK is quite different. In the UK our challenge is that we have a single banking licence under Barclays Bank PLC and in post-ring-fencing world we need to have two banks so we'll have to create a brand-new bank which is getting a licence and separating out the customers, clients, products and systems into a brand-new legal vehicle that needs to meet all the sort of regulatory requirements that such a legal vehicle will require.

Now, for us it'll probably mean moving retail and small business customers and card customers to a new bank. That'll be done through a court-appointed process, a Part 7 transfer. We have about 15 million retail customers and then more Barclaycard customers and more small business customers. They'll all broadly be getting new sort codes and various other things that behind the scenes will be new to them but hopefully seamless to them. So the separation costs – just things like printing new debit cards for everybody and things like that – these will be costs that you would otherwise just roll through, but we may need to give a fresh set out for those that haven't renewed by a particular time. You can just imagine all of the – on an enormous scale – amount of testing that we'll need to go through before we do a live cut-over weekend. It will be quite significant.

So we'll line item out the costs and to the extent we can give a bit more granularity on specifically where we are in a project or some things that are happening, then we'll do that as best as we can.

**Chira Barua, Bernstein**

Morning. One fluffy one and a couple of specific ones. Given the CCAR process, everything that's coming up in the US, I'm sure you guys have thought through whether the Investment Bank sits in the broader Barclays Group entity or is there any chance whatsoever of splitting this off? The total debt and regulatory regime; compensation makes no [sense]. It would be great if you give us your views around

whether that has changed because your cost views have changed, capital has changed, US regulatory, lots of attention on Europe and broker-dealers right now, so how do you think about that? That's one.

Two specific ones, one on Op Risk. Last meeting you told us about the advanced models coming through, I haven't heard from you on that, if you could update us.

And the second one is the specific news item's been floating around that there's a US Government study saying European broker-dealers fudge their end-of-quarter reports like lending books. How do you report, do you report average end quarter and is there any truth there? Thank you.

### **Tushar Morzaria**

So on future strategic choices we may have around the US broker-dealer or US investment bank, I think it's one of the things that I guess no-one would put their hand up and want to ring-fence their operations voluntarily. Obviously it's a lot of work, it's quite hard to justify.

The only silver lining to that cloud is you do get actual legal perimeters in place in a way that Barclays has probably never had. So at the moment, as I say, we've got a single legal vehicle, Barclays Bank PLC and everything essentially hangs off that. You have a Barclays brokerage in the US, there's a broker-dealer but this really puts in much more coherent, if you like, legal perimeters where the entire operations of what we would previously call the division sit inside legal perimeters.

Now, that's not a prediction that we do anything with them, but it certainly gives options at around 2018, 2019 of strategic flexibility that we just don't have at the moment. So previously, to take a very theoretical thing, possibly people have said, well, why doesn't Barclays just sell its Investment Bank? Well, before you even answer that question, have you got anything you can sell, have you got a legal perimeter, can someone actually take a share in something?

So at least in the future we will have clean legal perimeters. In fact, to the extent that because they're going to have to have independent boards and their own governance operations associated with them, they genuinely are "available for sale". That's not a prediction that we're going to do anything with them but that is some flexibility that we just don't have and very few banks have.

In some ways, as painful as the ring-fencing is going to be for Barclays, it probably means that we have more strategic flexibility in the company than we possibly ever had but the Board will take that on at the right time.

Op Risk – this is the disadvantage of trying to be helpful. So Op Risk, as much as I've been predicting it's going to come in any quarter it doesn't come in, which I guess is not a bad thing. But it won't come in

the fourth quarter. Again, I'll give you, as best as I can, a quarter's notice of significant model changes as and when they're coming in but not due yet.

Repo lending and balance sheet, to use bad terminology, 'window-dressing' – there's no truth to that, we don't dress our window, dress our balance sheet, you'll be hopefully not surprised to hear. But we will, along with other European firms, be reporting average into 2016 so people can get a disclosure on that. So not for 2015 but it will be adopted in 2016 and I think that's for all the European Banks.

**Michael Helsby, Bank of America Merrill Lynch**

I've got loads but I'll just ask a couple. Clearly Mr Carney yesterday flip-flopping again but rates are not going up next year and it's questionable whether they'll go up the year after. The curve is extremely flat so PCB revenues are challenged, more challenged at the moment than they have been, so can PCB revenues go up next year in a no-interest-rate-rise outcome?

And if you could just give us a little bit more detail on what the hedge contribution was in Q3 and what that technical drag might be if there is no rate rise.

**Tushar Morzaria**

Yes, so on PCB there are a few things to call out. Obviously a relatively low, flat curve has been in place for a little while now and you're right, it feels like, if you believe Governor Carney, it's going to be around for a little while longer.

As you look to income next year, the US Wealth business leaves so you'll have that slightly more noisy comparison. And we'll do what we can to help people see what the underlying trends are so it doesn't mask any hidden trends that are important.

I'd look at the three businesses, the three components of it a little bit separately – Personal, Corporate and Wealth – as they're probably all slightly different effects. I think on the Corporate side, asset growth has been more resilient than I thought it might have been. If anything, perhaps it was a bit underwhelming historically but we can see that there's good demand for assets, working capital lines, very straightforward corporate lending, to actually increase cash management. So I think the Corporate business going into 2016 has quite reasonable momentum and we're trying to free up risk-weighted capacity from other parts of the company – obviously Non-Core's a key component of that – to try and fuel what feels quite reasonable growth. Not stellar growth, it's low but it's quite profitably growth for us. It's always a bit difficult to give a full-year view on the business environment like that but it feels quite good going into the year.

Wealth is going to look the most different because obviously US Wealth leaves but we feel actually quite

confident on UK Wealth as well. It's been in quite a rebuild mode behind the scenes as opposed to a customer reset. One of the things that Ashok Vaswani has done by running PCB is try and get everything on single platforms. It's amazing when you have different people managing businesses how they build everything for themselves. It's almost embarrassing to give you all the warts-and-all, but Ashok's consolidated it all together so you should see operational improvements there. I think top-line is a little bit harder to call but I would say again a bit more like Corporate, it's a little bit more resilient than you would think.

Personal's probably where we've felt most of the challenges in the sense of mortgage margin pressure, which obviously has been well-trailed and well talked about – and still feels pretty pressurised. Different banks will do this in different ways – we're less keen on chasing pricing down. It's an NII maximisation objective that we have, so it's volume versus the NIM really, and we think holding back volume for slightly larger NIM is probably the best thing for us. But I think we'll have to see how the mortgage market plays out. We're not really big into buy-to-let so with the margin compression, we're not trying to look for higher-margin products very aggressively so it will be what it will be.

On the personal lending side it's quite a small business. It's actually doing okay but the numbers are relatively small, mortgages is by far the biggest lending business it has so that'll be the one that drives that. On the deposit side, I think in Personal there's limited repricing flexibility that we have now. We've repriced our ISAs, we've simplified it down to six product sets and repriced everything over the summer so you'll see a bit of that feed through. I don't think you'll see a lot more; probably a little bit but not a lot. And we've changed our overdraft pricing structure and things like that so we'll send out a text message now before people go overdrawn. That's a good customer outcome but means you earn a little bit less fees on that, but obviously less impairments as well.

So I think it's a mixed bag. I think the one that perhaps is probably least impacted by flatter and lower for longer is probably Corporate; it just feels like it's got a bit of momentum and probably followed by a little bit of Wealth and then Personal.

On the hedge, now, the hedge is in some ways – because we've already been flat and low for a long time – I don't know what word to use but caterpillar. So they have an average duration of about five years and they roll off one year at a time and roll on one year at a time so after about five years, it evens itself out.

So the real interesting thing is, would you have a delayed transmission if rates rally or do you shorten duration? And I won't talk about that, that's something we won't talk to publicly until we've done something. But that's probably more the interesting question – rather than is there a drag from the hedging, it's more, if rates rise are you locked in at a fixed rate so you don't get the full transmission

effect of a rate rise, a too-long duration. But I don't really want to comment on that until we've done anything different.

### **Michael Helsby**

One more, just on the ESHLA portfolio; clearly there's still quite a lot of revenue volatility that's coming through that line and you got the big PVA in Q3. Can you just tell us a little bit more about the underlying portfolio, can you remind us on the size of it from a leverage and RWA perspective? If you could tell us the PVA that is specific to that, if you could tell us what the underlying yield is on the portfolio and just remind us how you're actually calculating the mark-to-market, i.e. is it a true mark-to-market or is it a model that's got no reflection of the actual costs you're getting liquidated for?

### **Tushar Morzaria**

So ESHLA, for those of you who don't know, is Education, Social Housing and Local Authorities. And it's business that we still do today actually, it's a very good business so unfortunately this is one of the sins from the past, when it was done at that time – it's about a decade old now – it was done on a mark-to-market basis rather than on an accrual basis and everything we do now is on an accrual basis and that's why you'd have no idea what – or it's just not that interesting to talk about – the new origination in ESHLA.

It's a zero-delinquency business that's never had a delinquency so it's a very low risk-weight but it's a sizeable portfolio in terms of just the mark-to-market component of it. It's in our disclosures I think it's in our fair value disclosure. I'll get IR to point it to you but it's about £16 billion, £17 billion. So it's sizeable relative to the bid for these assets in one shot, that's why banks lend rather than be a securitisation or insurance-driven business.

So it's a very low risk-weight entity, it's super-high-quality credit, considered quasi-sovereign really and no impairment whatsoever so the capital is really from a PVA rather than our risk-weighted assets and it's a slightly peculiar situation. We only have a PVA because we do mark it to market so it's really the potential uncertainty that you may have as a regulatory matter from spreads, not as an accounting matter. In accounting, you're trying to assess fair value rather than what value could possibly be in a very wide range of uncertainties.

The yield on it is, we swap it out so in some ways the deal is a bit of a – it's not as relevant, it's not a carry asset, it is an accrual asset. As I say, it's fair value accounting so it is at a level which we believe is reflective, so if someone had a bid for those assets that's where they would model them. They are in many ways modelled because some of these are very long-dated and they don't trade at all as some of them go out to 60 years in fact, so there's no two-way market for those kind of things.

So when you're holding them at par and accrual accounting them it all feels very straightforward and obvious. When someone says, can you present value, say, 60 years, you're just scratching your head as to what interest rate and credit spread do I use. So we have a model around that for those very long-dated ones. Some of them are shorter-dated and quite straightforward and it's like with any other long-dated structured derivative, similar sort of technology that we would deploy.

So the real answer here would be, it would be very convenient if we could actually put them on an accrual accounting basis because you actually lose the PVA and you don't have this potential volatility because you can't really – the reason why you get a little bit of P&L noise is you don't hedge it perfectly. It'd be very expensive to hedge this portfolio and some of them have these things called lender options, borrower options, so the ability to call the loan at our request and the borrower can also refinance at their request so it's like a put call. So you're now getting into quite a complex derivative which again you wouldn't have to worry about because it's an accrual account.

Now, under IFRS9 we may have the opportunity to switch the accounting basis and that's a few years out, of course, so there's something about, depending on how that portfolio looks in two or three years' time, that might be the best way to manage it. But at this point in time we're obviously looking to wind it down as sensibly as we can but it's a big portfolio. Most of the PVA is from ESHLA, we haven't called it out specifically. You do get other bits of PVA bid offers in the IB; there's various other IB-oriented things but the bulk of what we have, £2 billion or so aggregate, comes from ESHLA, not all of it but most of it.

#### **Chintan Joshi, Nomura**

If we talk about the Core Investment Bank £120 billion RWA target, on the Q2 call you had mentioned that if you need to pull the capital lever you will pull it, and profitably is still challenged, even if I give it the benefit of the deferred bonuses. Can we expect in the next three or four quarters for the Core IB RWA's to go down as you manage and pull the capital lever? And then two kind of detailed ones; Group tax rate next year if you could guide us? It was raised, I think, three or four quarters ago with the tax changes if you can help us there. And then you mentioned Head Office [income] was negative; are you saying that you expect it to remain negative?

#### **Tushar Morzaria**

Let me answer in reverse order; no I don't say Head Office income will be permanently negative, just to remind you it can be negative. For about three or four quarters it was positive, and then of course everyone assumes it is positive, whereas it oscillates around zero with a negative bias. So if you see a run of positives, probably a good guess it will be negative; if you see a run of negatives, probably a good guess it will be positive, that was really all I was trying to say. It oscillates around zero; actually they only have two components on there. We have about £12 billion of net interest income in the company in any

one year, very, very round numbers, and if the funds transfer pricing component is left in Head Office in any quarter we transmit that through to the businesses – so £100 million or £200 million plus or minus is typical for a quarter when you've got £12 billion of NII; it oscillates around zero. The other thing we'll have in there is structural reform costs; it probably won't make a difference for you but whether we just leave it in Head Office and call it Head Office or do we allocate it to the business? I'm still in two minds how we'll present that but we'll let you know before we get there.

Regarding the Group tax rate, I won't give you precise guidance yet; we're still doing some planning work on it. Think about in the low 30s and as we finish some of the planning work we'll try and give you more precise guidance. There are things, you try and look at all opportunities. Some of them are quite aggressive and we won't do, some of them we may do but in conjunction with the tax authorities so when we've got something meaningful to tell you on changes in the ETR we'll communicate it to you. Yes, so blend it all in. So obviously in the UK it will be 26-28 % depending on how far out you want to be projecting. You've got South Africa at about 30% and then the US at about 40%, so put that into the mix.

As I say when we've got something a bit more precise, we'll share it with you. The other thing with the ETR, it's actually quite a technical thing too because as you recall we do a statutory and an adjusted, and some statutory items are non-deductibles – you get a different statutory rate to the adjusted rate, which is a clean look-through rate so you get that effect going on as well.

Regarding the question on IB RWAs and projections, we won't give you precise guidance but the bias will probably be to the downside. So you won't see IB RWAs grow materially, certainly not above £120 billion, it might bounce around because of FX rates but the look-through trend will have a downward bias to it.

**Chintan Joshi**

Actually the heading question there is, should it be going down towards £100 billion?

**Tushar Morzaria**

We're not giving you revised limit guidance, but there will be a downside bias. As you saw in Q2, it's not untypical that we're several billion below the £120 billion and we'll try and bias it towards the downside.

**Chris Manners, Morgan Stanley**

Good morning Tushar, I had a couple of questions for you. The first one was on the competitiveness of Barclays versus US Investment Banks. It seems that Barclays' return on leverage exposure seems to be a lot lower than where the US banks are, and capital allocation may not be quite as high; just trying to work out how you see that playing field and if there's any skew there? The second question was on

capital; obviously 11.1% should be flat in the fourth quarter. If we look at; Standard [Chartered] has done a rights issue, RBS and Lloyds are much higher, HSBC adjusted for the Brazil transaction will probably be in mid-12% by the end of the year, that leaves you 150 basis points shy of other UK banks; how do you think about that? Is that a problem for you or are you still sticking with a 12%-ish target by the end of next year? Thanks.

### **Tushar Morzaria**

So on the IB question; one thing obviously the US IBs have that the Europeans have less of is access to the US market so the biggest fee pool in the world with the biggest margins are in the US. And it's interesting, it's almost like an oligopoly in some ways; there's the bulge bracket cadre of firms and most of the fee pool goes to that bulge bracket bias towards the US banks. So in some ways the irony of it is in the US, where you've got the biggest fee pools with the biggest margins, you have the fewest competitors. When you come to Europe margins are much thinner; you do an IPO in Europe relative to the US you just earn less fees in terms of margin, and you'll have more banks that want to be on that ticket. You'll have US banks as well as European banks as well as domestics. And it's probably even worse in Asia in some ways; the margins get a little bit thinner and you've got even more fierce competition. So I think in that sense the US will always have a slight advantage just because the capital markets activity in the US is so much steeper. On top of that, those that have commercial banks in the US, of course, it sits very nicely and it's very hard for someone like Barclays to compete; we don't really have a meaningful commercial bank in the US, and it wouldn't be profitable for us to try and develop that. So I think in that regard we are just a different type of business.

The other thing I would say is we're all probably, unlike pre-crisis, trying to do different things. So certainly the Europeans over time are becoming more focused on picking areas where they feel they can compete successfully and generate good returns, and where they can't, not try and compete. So I don't think you'll see, for example, European firms trying to be the top three or four league table fee earning position in the US; it's a very expensive thing to try and do that so I think they'll try and pick their sectors and industries and like for us, natural resources, healthcare and TMTs, those sectors have worked well for us but there are other sectors that have just not. We have a level of diversification that gets you through one year to the next but you don't try and cover the whole world.

Regarding leverage, I think European banks have traditionally been more leveraged, just because US leverage rules have also been in place longer so in some ways it probably goes to the business model as well. That's changing as leverage ratios become much more biting, I guess, in Europe so that's probably really just a catch-up.

In terms of capital, it's a good question; we gave an 11% milestone for the end of next year and we achieved it and you sort of feel good for about a day then everybody says have you got enough capital?

It's a point in time; it was never our resting point, it was never our end-state, and there's no way Barclays can run an 11.1% capital position and feel that that's the end-state. When fully phased in, we'd barely be above MDA triggers by about 50 basis points; that's nowhere near going to be substantial enough. We've got to continue just to progress upwards and navigate through, and I think you've seen the measured approach from us to continue to accrete capital on a measured basis really, releasing capital out of Non-Core, maybe a negative bias in IB RWAs as well as taking our below the line items as we go along. We will cautiously navigate through that.

The next milestone for us is to get over 12%, then I'm sure there will be another milestone after that; probably all banks will hover around a similar capital level at some point and people get there in different ways; some people raise capital to get there, some people sell big businesses to get there, we've done our own way of getting there but feel confident we will get there, but in a measured way.

**Arturo De Frias, Santander**

Thank you. Probably this is a question that you should ask us rather than we asking you. I wanted to ask you about your views on cost of equity. Precisely talking about capital; capital [levels] have doubled or tripled or more, and the same with liquidity, and leverage is now lower than ever and the bond yields are lower than ever, almost, and most of us keep using pretty much the same cost of equity as we did ten years ago, around 10%, 25 bps up or down. What do you think needs to happen for both analysts and investors and rating agencies to accept that banks should be valued with cost of equities of perhaps 8% instead of 10% or 11%? Thank you.

**Tushar Morzaria**

I think it's a good question; I honestly don't know the answer to that. Obviously the investor community will be the people that really know the answer. My sense is probably a bit of stability and I imagine there's a premium because we're still in an evolving regulatory environment, business models are still adapting so there's probably a premium that investors want because the execution risks or perhaps the regulatory uncertainty as things continue to evolve. But for us we don't spend an awful lot of time trying to figure out what cost of equity is because obviously we don't set it, and it's a historical measure in some ways; you get to a lower cost of equity once the investors decide to give it to you. There's not much you can do in advance apart from just running a nice, simple, transparent business that's predictable and hope investors reflect that in the way they value us. So yes, I don't have a great answer; it's definitely more one for you and the investor community.

**Arturo De Frias**

A quick follow on; what is, in your view, your current cost of equity?

**Tushar Morzaria**

Well we publish it actually, in our annual report. We don't spend a lot of time talking about it but we published it at 10.5%, and it's using just standard corporate finance methodology, such as CAPM models, so it's a pretty transparent calculation. The reason why I don't spend an awful lot of time thinking about it is there's a gazillion ways in which you can do that as well and that in itself can be its own science which I suspect is probably a bit futile for a management team to be worrying too much about whether it's 10%, 11%, 12% or 13%. We just need to keep double-digit returns and become predictable and easy to understand and then hopefully that gets reflected in our valuation.

**Peter Toeman, HSBC**

You mentioned that obviously the performance on cost is something that has been very credible and you believed in that, but when you come to give the market guidance about, say, costs in 2017, are you likely to do that in terms of the nominal absolute cost target or are you likely to do that in terms of the cost income ratio going forward? Because I believe that having a nominal absolute cost target has been actually very beneficial in the way that investors perceive the company.

**Tushar Morzaria**

Yes it's probably one for our new Chief Executive. A lot of people ask me for guidance beyond 2016 and I'm obviously reluctant to give that until our new Chief Executive arrives. It's probably something that person needs to own as much as me. So I don't know the answer to that, we're probably one of the early adopters of hard cost targets and I've now seen it's becoming a little bit more fashionable with the recent reviews that other banks have done. It's something we will reflect on, but we're a restructuring story and I think it probably makes sense when banks are restructuring; I think if you feel you're less of a restructuring story I wonder if it's better to go to more traditional measures and cost income ratios is probably a more relevant measure once you're beyond the restructuring component of it and you're in a steady state. We're not quite there yet but that's probably one more for the new CEO.

**Ian Gordon, Investec**

Morning, this is a more general question in terms of tone. A lot of the feedback I hear from your owners over the last three or four months, it seems to me they've been in a different meeting from me. They've heard your team talk much more enthusiastically about revenue growth, I don't think we've touched on that subject this morning, so could you fill me in on the piece of the story I'm missing, which hasn't yet made its way into my model?

And just continuing that more seriously, I say 'what is this story' and they say 'well, it's Cards and then other stuff'; just coming back to the Cards piece, is there anything in terms of recent developments which causes you to reflect on pieces of that story?

**Tushar Morzaria**

John MacFarlane is the catalyst around making sure we don't forget to grow the top line as much as manage all the other things we can. It's a nuanced conversation in the sense that when he came in he did simple things like just ask bankers how much time do they spend with clients and didn't feel we were getting that proportion right, so to make sure we don't lose sight of that.

So that we're building a business for the future, a little bit of that, perhaps the cost-free revisions that we made is in that spirit as well. In terms of where revenue growth realistically can come from; Cards, I'll come back to Corporate Banking, it does feel like a good business at the moment. It's one of the best businesses we have in the company actually. We don't talk about it as much as we talk about credit cards, for example, but it's a tremendously good business for us. It doesn't have quite the compound growth rate the Card business has, particularly in the US, but it's a really nice business that chugs along reliably and has a relatively low risk profile. Africa, probably not now – the macro environment for Africa I don't think is conducive to growth at the moment, particularly for South Africa which is where we're biased – but in a different macro environment that could feel quite different.

The other one I would say is Wealth, even though we'll be disposing of our US Wealth business; Wealth is another growth business. We're the second-largest private bank in the UK, for example, and we don't really talk about that too much. There's pretty good positions there and I think with Mr Staley coming in, who used to run JP Morgan's Private Bank, it wouldn't surprise me if that's an area he spends more interest in, given his background. In some ways the UK Card business and our Corporate Bank are quite similar; they have quite big positions in the UK, very reliable businesses, good risk controls, and throw off very attractive returns. The turbo growth has been in the US where we're much smaller and it's been through partnership deals; we signed up JetBlue last week and there are various other ones that don't always hit the headlines that we sign up. And it's been a pretty good story for us, about a third of our revenue now is from there, getting a third of that in receivables – it's a meaningful business.

To put in context how quickly that business has grown, there's an industry survey that comes out, Nielsen's survey on what the industry uses to assess market share. And if you look at spend on cards, they just ranked banks and we jumped above Wells Fargo in the US, and I think most people will be quite shocked about that. They don't quite often even realise they're using a Barclaycard; we're not brand proud, if you like, over there. The open market offering is quite small but more people spent money on a Barclaycard in the US than they do on a Wells Fargo card and obviously that's a dominant bank over there. So it shows what can be achieved in that kind of business. The only thing I would say with Barclaycard is in the US is the pricing around some of these partnerships is getting quite aggressive and we've passed on as many deals as we've bid on and won. So we'll keep our price discipline; these are quite long term contracts and if you price them wrongly you can sometimes get locked into a ten year contract with a sub-par return; that could be quite a problem. So price discipline is important so we won't chase growth for the sake of it because it can turn pretty ugly if you get it wrong, but where we

see good opportunities we'll continue to take them where we can.

**Ian Gordon**

Any comment on regulatory developments in the UK?

**Tushar Morzaria**

Yes you probably saw the Competition Commission; there wasn't anything there that felt hugely concerning for our business. Some reasonable comments but nothing that I think would fundamentally change the way we'd look to run that business. The thing that has evolved in the UK – that is also turning into quite a competitive business – there's the zero balance transfer product that is turning hyper-competitive and we used to be what was called top of the table; we would have the longest and the best offer. That has the huge advantage of you get to see all the underwriting first and then everybody else getting your rejected underwriting if you like, which is an [advantage]. We're no longer top of the table; we're not going to match some of our competitors who want to extend beyond us, as our models don't suggest the economics are there for that. But you do get the risk of more adverse selection, so people who went to someone else and didn't get accepted might come to you. And you never get to meet your customer in a card business, it's a very much models-based underwriting, you can get adverse selection and you have to be a little bit careful.

The UK market is competitive, more competitive than perhaps people think. All the companies are fighting to be your choice of credit card in your wallet, but still a good business for us as we've been in there many years and there are good economies of scale and good econometric models.

**Fahed Kunwar, Redburn**

I had a couple of questions. Just thinking about your cost base, how much is terminal versus how much is one-off? In the Non-Core, one of your peers got to around £20 billion derivative RWAs and then stopped running it off because the tangible value was too big, the hit was too big. So if I look at the £125 million quarterly costs run rate I'm guessing most of that is derivatives. You've also got a c.£50 million revenue drag as well. Are you going to basically think at that point, let's just let it mature and that drag we should think about being quite terminal? Or will you take tangible book value hits and do those trade unwinds and bring that derivative balance down?

And the second question is on your SRP costs. I think one of your peers said the IHC, around 20% of that would be ongoing. I took from your earlier question that the £1 billion costs you have for the ring-fence and the IHC is a one-off, so just to be clear is none of that going to be ongoing?

**Tushar Morzaria**

So on Non-Core our objective is to do better than the £125 million; it's a way-point not an end-point, so

the terminal annualised effect should be lower than that and we would be disappointed if it wasn't lower than that. And we're looking at the end of 2017 as the time at which we should consider folding it back in. So for a way-point of £125 million [from Q4 2016], we would expect it to be much lower than that [when the Non-Core is folded back in]. Our exit rate out of 2017 ought to be much lower, that would be our objective.

In terms of when we would stop trying to release RWAs, the tangible book value is less concerning especially when you get into those kinds of numbers, it won't be that significant. It's more capital I think. A good example would be the Portuguese transaction with just the cost of a penny in tangible book value, you do go backwards in tangible book but you stay neutral in capital. So I think where those options are available we'd trade on them.

I think we'd be a little bit reluctant to trade on capital. But there's going to be some parts of that capital that are going to be super hard to move out, there's no magic wand like a deferred tax asset. So capital is more sensitive than book value. We don't want to torch our book value either but we are far more inclined to lose a few pence on book value than 10-20 basis points on capital.

On ring-fencing, so for us this is the build costs, again think of it like CTA. Once that ring-fencing cost goes away all you're left with is Op Ex and you'll see the Op Ex line, that will be the Op Ex line post-ring-fencing work and you should see a move downwards. Included within that Op Ex line will be the run-rate costs of administering the ring-fences post-creation of them. So the CCAR costs in the IHC will be in the OpEx line and it will be incorporated in there.

So you don't expect to see a blow back; the £1 billion is no longer recorded here and we're going to inflate our Op Ex by a billion; you should not expect to see that.

**Manus Costello , Autonomous**

Can I just follow up from that because I don't understand why you're putting the ring-fence build costs above the line and why you're not putting it in CTA or why you're not putting it below the line, because your peers are all putting it below the line. Also, the way you talk about capex decisions in the rest of the business makes it sound confused with BAU cost. If we hadn't done this we would have had to cut back on BAU costs in PCB, and I don't understand where that confusion is coming from because if these really are one-off costs, I would have thought it just gets lumped into CTA or below the line?

As a follow on from that, we've been in this meeting several times and asked you about the impact of ring-fencing costs and you said very clearly it's included in our guidance. Can you just clarify what you meant when you said – that you expected it all to hit in 2017 and therefore your guidance was out to 2016 and it wasn't included? From my perspective, and certainly from a lot of investors' perspectives, it

was disappointing to see that number come through and if it really was just that you were expecting it in 2017 then the communication of that was somewhat misleading, I think.

#### **Tushar Morzaria**

In some ways we'll call out where we record it so people can form their own view as to where they record it. We'll isolate it for you, so a bit like CTA. Presentationally, we don't put it below the line, we do leave it above the line and some people leave it above the line, some people take it below the line. To be honest, I've seen some of you do conduct and litigation differently in your models. So in some ways I'll leave that to you. We'll call it out for what it is and you have the freedom to think of it how you want, and so can investors. That was really the objective here; we're not trying to be cute in terms of telling you how to think about it. We'll call it out, explain it to you; you want to strike ROEs before or after then you have the freedom to do that. As I say, I've seen several of you did do it differently for both CTA and conduct and litigation and that'll be with you, but hopefully it will be transparent to you.

In terms of the disappointment, my full intention was to include it in the hard costs guidance that we've given, that was our going in assumption. The sequencing, obviously we know more about a little bit earlier than we thought, but it was a combination of factors. The sequencing definitely we knew more about and therefore the quantum of that sequencing, how much was going to be in 2016 versus 2017, but also the implications of having to make that capacity.

To your point, we tried to think of it as we're giving specific hard costs guidance and roping everything in there, we put conduct and litigation, bank levy, Op Ex. We tried to be as fully encompassing as we could and at that time in 2014, structural reform costs which we had less visibility about obviously, we included it in those three categories in our Op Ex line. So as we do real granular bottom up budgets so we know how next year will look there were decisions that we had to make; do we find the capacity for that, and will that have some implications to other businesses, or do we just call it out and not impact those businesses and that was the judgment that we took.

So just try and be as transparent and as open as we can about that. Hopefully the transparency will allow you to model it in the way that you want to model it and I'll leave that to you and to your judgment.

#### **Jonathan Pierce , Exane BNP Paribas**

I've got two questions. The first one is just a follow up on the question on costs that Manus just put to you. Pressing you a bit more on the sequencing, presumably all of this structural reform stuff, by and large, at least has got to be done by, say mid-2018? You talked us through the complexity of the logistics half an hour ago now and it is clearly very complex. Things like Part 7 transfers, I think, take 12-18 months. I'm just wondering what changed in your mind with regard to the sequencing? We

would always have expected a big bulk of the costs incrementally to have come through in 2016, so what's changed from management's perspective in terms of that?

**Tushar Morzaria**

We never called out in 2014 how much we expected in 2015, 2016, 2017 or 2018 for that matter. We had a shape in our mind, some of that was a bit earlier than we thought but that's life in a very big project; you're going to have those things and no doubt there will be some things that will happen that we can't accurately forecast this time round. But the full intention was let's just manage a big project and we just need to manage those things. But it was the consequences of creating the capacity that's really the judgment that we took, even in the second quarter the full intention as we were drawing up budgets was to absorb it in our Op Ex line. But the consequences of that led us – when you talk about it at the board level – to make a different decision as to how we'll report it.

On the legal effect of the Part 7 transfer, there are some costs but most of the cost is outright operational moves as opposed to legal form changes. The corporate finance aspects of it are relatively less expensive than the systems migration and rewiring, reconfiguring systems with different ledger codes, different branches need to have different sort codes routed in, and your payment system needs to be reconfigured and tested. You can just imagine, no-one has done anything like this before.

I guess the only thing that people have done that is similar is maybe when TSB was extracted out or Williams & Glynn, probably a version or something like that. Perhaps even more complicated because we don't have a banking licence to start off with – this is a greenfield build for us.

**Jonathan Pierce**

Thank you. Coming back to Michael's question earlier on structural hedge, I know you don't want to talk too much about this, but if we look at how the five year swap has moved over the course of the last five years, actually Q1 2011 was a particularly good quarter in terms of the reinvestment; I think it was over 3%. Now the gap down in Q1 of next year, if swap rates remain broadly where they are, is close to 2%. Is there any non-linear roll off of the hedge that we should be thinking about in terms of quarters and on the basis that you've just told us your hedge duration to be put on at five years? Is Q1 of next year a particular problem?

**Tushar Morzaria**

Not really, I mean, there's always going to be some discontinuity in different directions with the capital so it's not like the entirety of your hedge was put on in one quarter. It's a thin strip of quarter by quarter swaps. So you will get bounces going up and down but it's not like the entire hedge is put on at one point in time on one point of the curve. The average duration is five years but it rolls down, we're not just putting on five year swaps all the time. I don't know if that explains it to you but just the midpoint of

the caterpillar that's your duration.

You get a lot of smoothing effect as a consequence of that, that's the whole reason we do it that way, and again to the extent that if there is something funny that's going to happen, we'll try and call it out in advance but at this stage you shouldn't expect it.

**Jonathan Pierce**

Could you tell us, like the Royal Bank of Scotland now disclose, what the yield on the hedge is?

**Tushar Morzaria**

Well I think actually we used to and we've decided not to, partly because it was a lot of disclosure and we got very few questions on it, to be honest. And I think it was done at a time when there was a lot of large moves in rates, especially downwards so people really wanted to understand. Lately, rates have been a little bit more stable. If you go back only two years ago we had it in terms of disclosure but we don't have any plans to put that back in.

**Raul Sinha, JPMorgan Cazenove**

Most of your competitors seem to be trying to give us some estimates about FRTB or Basel IV, plus all of the regulatory change coming in 2018, probably because they are making business plans, they look forward to that and you haven't so far talked about it. I think there was a paper recently which talked about the industry-wide impact of FRTB and the impact that that would have on the capital and that was quite large. So I was wondering if you have, without giving any new guidance, any more clarity on your side on how disruptive or how much this deviates from what you're expecting it to be?

As a second question, John McFarlane talked about a potential new plan in full year results on the new strategy. Is that just your normal new CEO, think about it through the Christmas period and then come back in the New Year and tell us about 2017, or is there something more fundamental? People have talked about refocusing the IB to the US and the UK, can you talk about what you think?

**Tushar Morzaria**

We have a number pencilled in our projections for Basel IV. The reason we haven't shared that with you is it would probably be a bit misleading as I just don't feel I've got that level of precision around it that if I share it with you, it will almost feel like I'm giving you some form of accurate guidance which I just don't think I know enough about yet. When you look at the three components, the one that is the hardest to model is the trading book review. It would be very hard for anybody outside of the bank to really model that because these are fundamental rewrites of complex equations already. Standardised credit risk and operational risk are quite straightforward calculations and the disclosures are there so you could probably calculate it as quick as I could so I'm not sure I'm adding more to it unless I've got

the inside track on what the standardised risk weight will be, which I don't. So I'm not sure there's a huge amount of value to do that. I think once the rules are in place and we know what they are we will of course share with you what our best estimate is. And of course when they come in that's another slight unknown, whether it's 2017 or what have you, some banks think later, there are different dates out there.

It's something that we have in our projected models. The headwind we're going to have to absorb, we've been quite clear that a lot of that will hit the IB. But the capital allocation for the IB at the very least is a proportion of the group but preferably as a quantum as well, we'll try and absorb it within there, but it's very hard to be precise about it until we know the effects. If our calibration is wrong, and it's more than we thought, that may require some business adjustments and we'll be honest with you about that at the time, but it's hard to project too far out with a degree of specificity.

Jes Staley starts in December, so he'd have been in the company probably about three months or so by the time we announce our full year, although there'll be a Christmas bit in the middle so not a typical three months. I think you'd expect him to give his thoughts on any modifications and I've used the word modification rather than a rewrite. I don't think he's coming in with a blank piece of paper, with the Board having no idea and expecting him to tell us what to do. It's more, here's a plan, sign up to the direction and the objective of it. I'm sure he can improve on it and I'm sure he'll put his own personality and style into how it gets done and it'll be more of an update on that. To the extent he does want to modify it and it's meaningful, then I'm sure he'll update folks around about that time, but we'll keep you appraised on that. He hasn't started yet so this is quite speculative and I don't want to pre-emptively lock him into anything. If he comes in and has a separate session to update people on his thoughts we'll obviously let you know about that in good time.

#### **Sandy Chen, Cenkos Securities**

Looking at costs and just drilling down a bit more in terms of retail versus the IB, one of the thoughts that I thought was really quite interesting was that digital is Barclays' biggest branch, because I was quite surprised actually how low the penetration was: digitally active, 1.5 million of 15 million customers. Has that been a good driver for costs and is that a good indicator for the ability to cut costs? Related to that, if you look across at the Investment Bank is there a similar component that you could use to drive costs or is it just much more difficult to convince human investment bankers to cut their bonuses?

#### **Tushar Morzaria**

It's a bit like a credit card, not all of the 15 million customers are permanently active and transacting every single day. So the penetration rates are high for those that are very active customers that we have daily operational relationships with. The cost of running that digital branch is a fraction of our

physical branch, in terms of transactional, real estate and paper trails and everything like that.

The trick is, of course, not to double up your cost base. A good example which someone like Antony Jenkins was really quite focused on, he would say to the retail guys 'I want you to be offering online account openings', and they'd come back and say 'we've got it and we're getting about a third of our people opening accounts online'. Meanwhile, in Barclaycard you can't open an account any other way but online and we seem to have the biggest UK card business around, so why can't you make it 100%?

And Ashok is that way inclined. The real trick here is the digital bit in itself is fine and interesting but you've got to strip out the old way of doing it as well. A real life example would be the unsecured lending where we're doing more in the phone now and online than we are in the branches. At what point do we say you can't get a loan in a branch but you have to do it on an iPad or a phone? With the Digital Eagles, if you do go in and try and get a loan in a branch now almost certainly there'll be someone that will do that transaction with you on an iPad and that's how we've got to re-pivot ourselves.

The IB in many ways is intensely automated. For example, FX algorithmic trading and cash equities are intensely automated. Some things just aren't as automated, for example corporate finance type work and the advisory business, but on the trading side of it, it's way more automated than people think. There's still obviously a long way to go. The swaps market is still a big market that is probably more voice traded than electronic traded, unlike the FX market which is very little voice traded. So I think you'll see that start to happen to the more traditional fixed income asset classes in the way that's happened to foreign exchange and equities as we go on.

So I think we're pretty much out of time so we should wrap up there. I'll leave you with just my usual five points; it's got to be double digit returns, Non-Core shrinkage, capital increase, costs need to come down and put legacy conduct issues behind us. And that's what we'll try and do quarter in quarter out.

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