# Virgin Money UK PLC Full Year Financial Results 2023 - Call Transcript

**<Video introduction plays>**

**David Duffy, Virgin Money UK PLC**

Good morning everyone, and good evening to those dialling in from Australia. Clifford and I will take you through the presentation and a detailed update on our performance, and then we'll move to questions. But before we go through the presentation, I thought I would share my own perspective on our commercial performance in 2023, which is, if you recall, the second year of our three-year plan.

And from my perspective, I'm very pleased with our resilience and our performance momentum and that's really important. Contrary to market trends, we have been able to expand our NIM, we have increased our income, we're continuing to grow our deposits, and we've also delivered good growth in our targeted lending segments.

On top of that, our cost-income ratio, our capital, and our distributions are all meeting or exceeding guidance, and despite the macroeconomic pressures, our asset portfolios are performing well, with no material arrears. I think given the challenging environment that we've been operating in, this is a robust performance, and I'm confident that we're building really good commercial and digital momentum going into 2024.

So let me turn to the specifics of the performance on slide 3. If you look at the left-hand side of the slide, you can see that our NIM has increased from 1.85% to 1.91% year on year, and we're guiding to a resilient NIM of between 1.90% and 1.95% in FY24.

Our NIM stability is underpinned by a variety of factors, including our hedge position and our proactive deposit management, as well as our growth momentum in target segments in FY23. Deposits have grown 2% year on year and growth in target lending segments reached 9%. We're confident that these underpins will continue to drive momentum going into 2024. In mortgages, we have traded resiliently and we remain focused on managing tight spreads, but keeping our market share of around 3.5%.

Our pre-provision profit has increased by 9%, and our cost-income ratio of 52% is in line with guidance. We have delivered £130m of the targeted £175m of cost savings and are now planning to increase the savings outcome to £200m. Clifford will provide some more details on these savings in his section.

As in previous years, our balance sheet is robust with strong liquidity and, as you can see, a low arrears profile. And although we have increased our provision cover, this is mostly based on modelled ECL and prudent macroeconomic assumptions and is not driven by any material increase in arrears.

Now, given our robust statutory profit of £345m and our strong CET ratio of 14.7%, we are pleased to be able to announce a buyback of £150m and a dividend of 5.3p for FY23. This brings our total distributions to £272m for the full year and £539m for the first two years of our plan. As I think you know, and we've said before, we remain committed to reaching our CET1 range of 13% to 13.5% by the end of FY24. Achieving this outcome would deliver more than £800m in distributions to our shareholders.

So, turning to slide 4 and the macroeconomic backdrop. As we develop our economic guidance, we use Oxford Economics analysis for our base data, and then you will see we adjust for our own views as appropriate. As we all know, the UK economy has remained remarkably resilient, despite inflation

remaining higher for longer than forecast. We are now starting to see the impact of 14 consecutive base rate increases, with inflation reducing from the peak levels seen earlier in the year to 4.6%, following the most recent update. Now despite the improvement, we believe it will take some time to return to the target range and so we are therefore assuming a more stable, higher-for-longer rate environment in the coming months and have applied this to our economic analysis overlay. The outlook, I think, from everything I'm hearing, is consistent with the recent Bank of England commentary, but remains a little bit more prudent than the latest OBR forecasts.

UK GDP has remained resilient, and whilst growth is expected to take time to improve significantly, we believe that the UK is now likely to avoid a significant recession. And finally, compared to a year ago, the forecast for unemployment has reduced, and this employment outlook has supported consumer spending patterns to date. We are also optimistic about growth potential in our core specialist sectors, however, we do expect new purchase mortgage activity to remain muted in the short term.

Let me now turn to slide 5. So overall, I think we have delivered really good commercial momentum in 2023. When we set out the original three-year plan, our goal was to grow in our target sectors and to maintain our market share in mortgages and I think you can see we're delivering on that goal, and our digital investments in these areas have been a great support for that delivery.

We have built a business bank which is focused and has a defensive sectoral bias. It has a deep sectoral expertise and is both margin and brand accretive. Our Marketplace digital platform is contributing to our growth capabilities, and our relationship-driven model on top of that has delivered 11% growth in business lending and positive net BCA inflows for the past 22 months.

Our unsecured business also continues to grow, albeit at a rate of 5.8% due to adjusted credit scoring. We have delivered an 11% increase in general card balances and a 21% increase in Virgin Atlantic balances, leading to a market share of 8.5%. It is worth noting that the Virgin Atlantic growth, which contributed to 540,000 overall new card sales, is a great example of how the combination of Virgin Money, the Virgin Group brand and a great digital product can deliver strong growth for the bank.

Our primary current account, with the linked saver account, continued to develop well. Linked saver innovation has been the key driver of a 4% growth in personal relationship deposits. In mortgages, we have continued to trade well tactically, and as I said, we have maintained our market share. And although the environment is still difficult for customers, our portfolio is performing very well and we're not seeing any material arrears appearing.

Our commercial strategy originally included an intention to broaden our product offering for our customers. And I'm pleased to say we are now launching a range of new products. We have relaunched Virgin Money insurance and investments products, and to date, we have seen really strong growth in insurance sales, and our investment business is starting out life with £3.5 billion assets under management.

We are now launching our new digital personal loan proposition, and we have made great progress on the development of a single app for Virgin Money. And this app will deliver a single interface for all products, cashback, and loyalty schemes. We're also in detailed discussions with Virgin Group to include all discounts and benefits offered by the broader Virgin Group, including Virgin Red, to our customers. And finally, our wallet functionality is now live with a closed group of Virgin Atlantic customers, and as we develop this payment functionality further, it will be integrated into the single Virgin Money app. So, overall, I'm very happy with our commercial progress, and as I said, I expect this momentum to continue into 2024.

However, whilst we have been investing in our digital capabilities, the world is changing rapidly, and no more so than in the area of AI-driven fraud and financial crime. So let me now turn to our strategy for future-proofing our bank and customers from risks in this area on slide 6.

By way of background, in the first two years of our plan, we have achieved Tier 1 status, and this means that we are viewed by the regulators as a systemic bank and are being regulated with a level of intensity that comes with being a Tier 1 firm. Consequently, our obligations in terms of resilience and regulatory compliance are also being assessed at Tier 1 levels, so too our responsibilities to our customers under the new Consumer Duty regime.

As I mentioned, our team has been extremely focused on understanding the emerging risks associated with the impact of AI on fraud and financial crime in particular. It is clear that the combination of AI and quantum computing will lead to significant increases in the sophistication and impact of fraud and financial crime. I am sure probably many of you in this room have personal experience of the sophistication of these fraud attempts, and if not, I'm pretty sure you will quite soon.

As part of our risk assessment process, I attended a Microsoft CEO conference on AI in Seattle and was able to see, first-hand, the unprecedented nature of the advances in both AI and quantum computing. And in our discussions, the key theme was that the developments in this area are happening faster than at any time in history, and that the consequences in this area of fraud and financial crime could be severe. And this is a concern, especially around fraud in the digital space, given the fact that 80% of fraud in the UK originates via social media platforms, and it is expected that new UK legislation will require banks to fund most consumer fraud losses. Our conclusion is that the cost of fraud for the bank could materially increase without the right detection and prevention systems and strategies.

Now, we also see that these technologies are driving a material increase in the complexity and power of cyber interventions. And if we are to achieve our goal of becoming the UK's best digital bank, we would need to be able to protect our customers from all of these escalating fraud and financial crime risks.

So, we have therefore decided to invest an additional £130m over three years in the area of fraud and financial crime. Now, this investment will deliver a new, best-in-market fraud platform which is also used by a number of our larger Tier 1 competitors, a materially upgraded financial crime platform and much stronger resilience and protection by futureproofing our customers against these threats. We expect these advanced platforms to materially reduce the cost of fraud to both our customers and the bank.

So, I think the nature of this investment is that it's fixed term, and when we combine that with the impact of higher rates for longer, there will be a temporary impact on the timing of our double-digit returns. Now, to balance the cost of the investment we're making, we are taking a number of additional cost actions, which will increase the savings that we are making from our existing cost programme from £175m to £200m and Clifford will provide more details in his section.

So let me turn to slide 7 and what we will deliver in 2024. Now, in this final year of the strategic plan, we will seek to deliver around £270m of distributions to our shareholders. And as I said, this three-year plan will see us deliver a total of around £800m of distributions to our shareholders. The final numbers, of course, will be subject to the normal Board and regulatory approvals.

We expect also to grow our business and unsecured segments by 5 to 10% and to keep a broadly stable market share in mortgages. And as I mentioned earlier, we'll be launching a single Virgin Money app, bringing together all of our products, loyalty and cashback programmes, as well as providing our customers with access to loyalty benefits and discounts from the broader Virgin Group.

In addition, we will be launching our new personal loan capabilities, we will be expanding our investment and protection product range to include pensions, and we will begin offering longer-duration mortgages to customers. And we plan to deliver a further £70m of annualised cost savings next year, and we are guiding to a stable cost-income ratio.

Continuing to improve customer service in all areas will be our top priority. To date, we plan to have digitised more than 50% of our customer journeys end to end and may exceed that. We are focused on delivering a high quality, stable service to our customers and have already reduced call wait times by 65% from their peak. We are continuing to drive digital-only engagement rates higher and are targeting an increase from 61% to 67% during the year.

We have successfully delivered Consumer Duty phase one, and we will deliver phase two during 2024, and as we embed Consumer Duty, we are conscious of the need to align all of our digital innovations and progress with the requirement to focus on protecting our vulnerable customers.

Now, I think if I stand back, we have reached a level of performance momentum where I'm confident that we will deliver growth in target segments. We'll continue to diversity our product profile and maintain a cost-income ratio of around 52%, and we will continue to deliver innovative, new digital solutions for our customers in 2024. This performance will deliver an underlying double-digit RoTE in 2024, and we are committed to delivering a double-digit statutory RoTE during our next three-year plan.

So that concludes my overview. Let me now hand you over to Clifford.

**Clifford Abrahams, Virgin Money UK PLC**

Thanks, David, and good to see you all. As you've just heard, we're showing good momentum as we start the third year of our digital strategy. We think our equity story and outlook is positively differentiated to some of our peers, as we've set out here.

We're confident in our balance sheet, with strong liquidity, good access to wholesale markets and improved provision coverage. Our capital position is strong, so we've announced another buyback today and given clear guidance on distributions for this coming year.

Alongside this, our digital transformation is well underway. Our underlying business is performing well, enabling improved NIM and further cost savings. And finally, we're growing our relationship customers and targeted lending, enabling us to open the jaws and improve returns over time. You can see how our strategic execution is driving improved financial performance on the next slide, ten.

Since 2021, we've materially grown our relationship accounts and margin accretive products, shown across the top. This, alongside the rate environment, has driven the sustained expansion in our net interest margin, and we expect to maintain this momentum into FY24, despite peaking rates. Consequently, we're generating capital, enabling sustainable shareholder distributions through dividends and buybacks, continuing into FY24.

Now turning to the details of our FY23 performance, commenting first on profitability, then balance sheet, capital, and finally, our forward guidance.

I'm pleased to report here, on slide 11, good underlying performance, with continued top line momentum. We delivered good income growth of 8%, reflecting early management of deposit migration alongside higher rates. Costs were 6% higher, reflecting wage inflation and temporary costs to safeguard customer service. Together, this resulted in a stable cost-income ratio of 52% as we opened the jaws, driving strong growth in pre-provision profit of 9%. Meanwhile, underlying profit was down, year on year, as impairments increased from last year's lows.

Now moving to statutory profit on slide 12. You can see here, we've delivered another year of statutory profit, despite higher below-the-line items. Restructuring costs were higher this year, as we guided, at £131m, as we accelerated activity in the second half, following that service recovery. These include costs from reducing our property and store footprint.

In FY23, we also incurred £29m of non-cash acquisition accounting unwinds, and with this acceleration, we now anticipate a final charge of around £15m in FY24. As we flagged at interims, we exclude hedge ineffectiveness from underlying performance to give a clearer picture of trends in non-interest income. The £16m charge for the year was mainly in the first half.

Within other items, we incurred around £45m of non-cash write-down of intangibles, after deferring the implementation of our mortgage digitisation platform. And here, we prudently fully wrote off the work in progress. We do intend to implement the new system but want to ensure we fully review and test the IT architecture, following the leadership changes during the year.

From FY24, we'll no longer report below-the-line adjustments. Instead, we'll exclude notable items from underlying performance, those items that we consider to be one-off and outside the normal course, in the same way as a number of the big UK banks. These notable items will include the adjusting items you see here as well as our Financial crime prevention programme and we've added details in appendix slide 52 of this presentation change, effective from FY24.

And finally, we declared a 5.3p per share dividend for the year, keeping our 30% dividend pay-out policy, but looking through the specific non-cash charges I flagged earlier, so a statutory pay-out of around 37% for this year only.

I'll now talk through the key balance sheet items from slide 13. I'm proud of our deposit franchise and pleased with our decision to proactively manage deposit migration this year, supporting our resilient margin outlook. I'll comment first on customer deposits, then explain how we are positioned differently to the big UK banks.

Over the past year, the market has seen a higher flow into term deposits as savers searched for higher yield. We saw this early and increased our participation in the market for term deposits, enabling us to lock in term funding at pricing below swaps. We've also grown our relationship deposits this year, despite accelerated market deposit migration. This is a particularly strong performance and reflects the strength of our value oriented PCA and BCA propositions, including our linked savings.

This combination has enabled our margin resilience this year, particularly in the second half. And so now, looking ahead, we're less exposed to further deposit migration compared to the big UK banks since we've already absorbed a substantial shift in mix to term, and our current customer pay rates are already materially higher.

During the year, we also accessed wholesale markets, despite tricky markets. And alongside this, we repaid around £1bn of TFSME and will continue to do so ahead of contractual maturity, whilst maintaining our robust liquidity that we've positioned throughout the year.

Moving now to lending on slide 14. In lending, we've traded well over the year, against a mixed backdrop. Overall lending finished broadly flat, as good growth in our targeted areas of business and unsecured was offset by a modest reduction in mortgages. The mortgage balances were around 1% lower, which is a good performance in a challenging market with slower activity.

We performed particularly well in business, despite the slower market and the headwind from reducing government-backed lending, with our total balances in business increasing 6%. In unsecured, growth in credit cards was slightly offset by a reduction in personal loans, and as you

heard from David, card balances were up around 11% during the year in a strong market, with our market share increasing somewhat to around 8.5%.

Now looking forward, in mortgages we expect market activity to remain muted and new business spreads to remain pressured, so we'll continue to trade tactically and aim to maintain our market share in mortgages, roughly stable in balances, in the medium term. In business, we expect to grow further balances for FY24, continuing to grow our share and in unsecured, we will target measured growth. And I'm pleased with our early trading performance this year.

Moving now to margins on slide 15. I'm really pleased with our net interest margin performance, shown here, a major driver of our improved income. This year, we've added a further six basis points to NIM, with stable performance in the second half.

You can see here that lending has been a modest headwind to margin in the second half, reflecting mortgage spread pressure, mitigated by our growth in higher-yielding lending areas. In Q4 this year, we have seen pressure on deposit margins, reflecting a catch-up of rate pass-through, but this has been largely offset by our structural hedge, contained within the deposit column in this chart.

So looking ahead, we expect net interest margin in FY24 of between 190 and 195 basis points, assuming base rates remain stable from here. Our structural hedge underpins our margin resilience, given the reinvestment benefit at much higher rates, and we are targeting growth in higher-yielding unsecured and business lending, which will give us a mix-driven margin benefit. At the same time, mortgage spread pressure is a reducing headwind. As the book rolls, we now only have a narrow gap between front and back book spreads.

So while we expect some further deposit margin compression, we're less exposed to deposit migration, going forward, since we've already executed the shift to term, and our existing customer pay rates are higher than the market. So, overall, we have a benign NIM outlook, notably more positive than UK peers.

I'll now talk through our structural hedge and rate sensitivity on slide 16. I mentioned that our structural hedge supports our margin. We reintroduced the structural hedge when the rate environment was substantially lower and so now continue to benefit from materially higher reinvestment rates.

You can see on the left, we expect the structural hedge to continue to support net interest margin, even before reinvestment hedges already written, will deliver gross income in FY24 above FY23. In addition, as the structural hedge rolls, it's reinvested at current rates, significantly higher than the average 1.4% redemption yield in FY24. And given this reinvestment benefit, we expect the average yield on balances in the structural hedge to continue to increase, supporting the margin.

On the right, we set out our usual interest rate sensitivity, using our pass-through assumptions at this point in the rate cycle. You can see that we're less sensitive to some of our peers, which is helpful as rates come down.

I'll now move to non-interest income on slide 17. Non-interest income was £7m higher in the year, so down around £10m year on year, when excluding fair value and one-off gains. The main driver of this reduction was business fee income due to lower merchant services income after the group changed its merchant services provider to Global Payments. Personal income was also modestly lower in the second half, following changes to our packaged current account, Club M. Following Consumer Duty regulations, we made it easier for our customers to select their individual benefits, while at the same time reducing their monthly account fees.

Now going forward, we expect OOI growth to be muted short term, given changes to packaged accounts, as we build back merchant services income over time. But looking further ahead, we see targeted growth in OOI as we see contributions from the various initiatives set out on this slide.

Turning now to costs on the next few slides. I'll comment first on our cost performance since we announced our strategy in FY21, before discussing current year performance and outlook on the next slide. Over the last two years, I'm pleased that we've contained growth in our underlying costs to around 4% per annum, despite double-digit headline inflation.

This performance reflects our restructuring activity which continues to deliver, with around £130m of savings earned through the cost base since FY21. These savings have more than offset the impact of cost inflation, while we've continued to invest back into the business. Of course, higher inflation has been accompanied by higher rates, allowing us to drive positive jaws, demonstrated by the sharp reduction in the cost-income ratio from 58% to 52%.

Now turning to cost performance, specifically in FY23, on slide 19. I'll first update on costs and then on our restructuring activity. Our underlying costs of £971m were around 6% higher, year on year, albeit with cost-income stable at 52%. On the left, we set out the cost bridge from FY22 to FY23. As I mentioned, our cost programmes are delivering those savings as we digitise the bank. However, this year, these savings were more than offset by higher salary costs and losses to fraud, higher investment, including costs of Consumer Duty readiness, digital development, and regulatory investment, and also customer experience costs to safeguard service as rate volatility, earlier in the year, drove a spike in customer contacts. Now, with service fully recovered, I'm pleased to report that most of these costs are now gone.

We set out our multi-year restructuring programme at FY21. And you can see here, on the right, we've made further progress this year, delivering a total of £130m of annualised gross savings at a cumulative cost of £213m. We expect most of the remaining £60m of restructuring costs will be incurred in FY24. Now, at the same time, we're increasing our targeted annualised savings from £175m to £200m, reflecting our further actions on property consolidation, outsourcing and digitisation. And these initiatives will support cost delivery in FY24, which I'll now pick up on slide 20.

On the left, we've set out expected underlying costs for FY24. We see further cost savings earning through from restructuring, including the store closures we announced in August. Also, with service now stabilised, we've exited third-party resources, which gives us a £25m year-on-year benefit in FY24, already locked in. Despite these savings, we see pressure on costs from persistent inflation, including salary rises from January 1st. And given this, we now expect a stable cost-income ratio in FY24, excluding notable items, that's above our medium-term ambition of less than 50%.

You've heard from David that we've chosen to increase our investment in financial crime prevention. And here, we're investing £130m over three years, with £40m in FY24. These costs will be ring-fenced and excluded from underlying performance, given the discrete term-bound nature of this programme, and instead, we'll present these costs as a notable item from next year, in line with the presentational change I mentioned earlier.

This investment is critical to safeguard the bank and our customers in the rapidly evolving environment, and we've added further detail on the key outcomes of our investment in the appendix slide 30.

Now moving to asset quality from slide 21. I'm pleased to report that our asset quality has remained resilient. You can see that during the year, our modelled ECL increased, while we broadly maintained overall management adjustments. The increase in modelled ECL relates mainly to cards, reflecting our prudent macros, with a weaker economic outlook and our latest bureau data.

Both these factors have driven significant migration of card balances from Stage One to Stage Two, resulting in a mechanical provision build as we move from 12 months to lifetime expected loss for these balances. Our overall credit quality indicators remain benign, and while we've seen some pick-up in our card arrears, this mainly reflects our recent balance growth.

And in cards, the substantial majority of Stage Two balances, that's 97%, remain less than 30 days past due, with 95% of these balances fully up to date with payments, and our Stage Three balances here remain low and stable. So while our credit quality is resilient and overall arrears low, we're well positioned for uncertainty that lies ahead.

And you can see the effect of the high ECL on our provision coverage on the right, which we've strengthened further to 84 basis points. Included within this is significantly higher credit card coverage at 7%, reflecting the higher modelled provision I mentioned earlier.

And the net impact of all this is that total provisions have increased from FY22, resulting in a £309m impairment charge, equivalent to a cost of risk of 42 basis points, modestly above our previously guided range. Looking ahead, we expect a lower cost of risk of between 30 to 35 basis points in FY24, having already digested the more negative economic outlook this year.

I'll now move on to asset quality on the next slide, 22. We've set out here the strength of our portfolio and why we're comfortable with our credit quality. Overall, our total portfolio is defensively positioned, with balances strongly weighted to mortgages, at around 80% of loans. That mortgage book is low risk, weighted towards owner-occupied and originated within strict affordability assessments, largely on fixed rates. And this has supported affordability headroom at higher rates and our continued low arrears performance.

Our business portfolio remains well diversified, with strong collateral levels and skewed to lending to resilient sectors, with minimal commercial real estate exposure. And in unsecured, our underwriting criteria are prudent, and we've tightened these further this year to reflect affordability stresses on our customers. Our customers here are generally more affluent, and this has supported our good credit quality, with our card arrears typically inside the industry for recent cohorts.

This year, the arrears rate on our overall cards book has risen, albeit from very low levels, and that largely reflects the age profile of our book, that is, with a higher percentage from recent originations and a lower percentage of more mature balances, where arrears are lowest, given our balance transfer model. And as such, arrears emergence for us is more evident than some of our peers, even though our arrears performance, by cohort, is typically better, and we've provided this detail on slide 47.

I'll now move on to capital generation on the next slide, 23. Our capital position is very strong and capital generation continues to be resilient, with 145 basis points of underlying capital generation. Capital distributions consumed 70 basis points of capital in FY23, comprising the total dividend of 5.3 pence per share for the year, the £50m buyback announced last November and the further £50m that we announced in August. The £150m buyback we announced today will consume around 60 basis points of capital in Q1 24.

So altogether, this resulted in a 14.7% CET1 position, considerably above our target range, as you can see on the next slide, 24. We've set out here our expected CET1 path in FY24. So even after the £150m buyback we announced today, we have a CET1 ratio of 14.1%, pro forma. That's £160m of surplus above the top of our target range of 13% to 13.5%.

Importantly, our capital position is resilient since it already reflects the impact of the hybrid mortgage models, no requirement to make further pension contributions, with our latest triannual showing a substantial surplus, and no material expected impact from Basel 3.1.

On this chart, we set out our capital drivers for this coming year. And as you can see, we're generating capital through profitability. We do expect RWAs to increase somewhat as we grow in our target lending segments. We also assume some mortgage RWA migration, with prudent assumptions on HPI. We see modest capital utilisation from the financial crime prevention programme, with £40m to be incurred in FY24. And here, other movements reflects mostly the phase-out of IFRS 9 transitional relief.

So net of all of this, we still maintain significant surplus capital, and so we're comfortable guiding to shareholder distributions in FY24 of around the same level as FY23, at around £270m, clearly all subject to conditions and approvals at the time. I'm confident that this balanced approach to capital management will improve shareholder value whilst also safeguarding the bank and our customers.

Finally, I'll conclude with a reminder of our guidance on the next slide, 25. I set out here our updated guidance for FY24 on the left and our medium-term outlook on the right, and we've mentioned the various details through the course of our presentation.

So in FY24, we expect net interest margin of 190 to 195 basis points. We anticipate underlying cost-income ratio for FY 24, excluding notable items, to be broadly stable. We expect cost of risk in the range of 30 to 35 basis points. And we expect to operate in our target 13% to 13.5% CET1 range, with shareholder distributions at around the same level as FY23. Given all of this, we now expect to generate an underlying RoTE, excluding notable items, of around 10% in FY24. That underlying RoTE expectation excludes the cash flow hedge from equity to give a fairer reflection of underlying performance.

And for notable items next year, we expect £40m in relation to the financial crime programme, the majority of the remaining £60m of restructuring charges and the final £15m of residual IFRS 3 fair value charges. So after notable items, we expect statutory RoTE of around 8%, so lower than our medium-term ambition, but very much in line with consensus for the year.

Now, turning to the medium term, we remain committed to our double-digit target for statutory returns, and this will be supported by profitable growth in our target lending segments and our resilient margins. And alongside this, our cost savings and lower inflation will enable us to deliver a cost-income ratio of less than 50%, albeit in the medium term. So, overall, our strategy remains very much on track, we're generating good business momentum, and our outlook is positive. I'll now hand back to David.

**David Duffy**

Thanks, Clifford. As we enter into 2024, this will be the final year of our three-year plan, so let me just close out with some reflections on the likely plan outcomes.

So in the past two years, we know we've experienced an extraordinarily volatile environment on many fronts. But despite these challenges, Virgin Money has achieved Tier 1 status in the UK and has successfully delivered, as Clifford said, on the Bank of England's stress test in each of the past two years. And these outcomes confirm that we have built a strong and resilient balance sheet, as you've seen, that is well funded and will allow us to deliver around £800m of distributions to our investors within that three-year plan.

Going forward, we're targeting digital growth of 5% to 10% in our target segments. We will keep our market share in mortgages broadly stable, as this year. And, of course, we will continue to invest in protecting the bank and its customers from the emerging risks in the fraud and financial crime arena.

As I mentioned, we will continue to diversify our products and all of the services we have for our customers, and we will launch our new single app. This app will help us to leverage our relationship with the much broader Virgin Group. Now this performance will be underpinned, as you've seen, by an improving cost-income ratio as we accelerate the cost reduction initiatives which we already have underway and identify new opportunities for efficiency.

Now, as of today, Virgin Money is a profitable Tier 1 bank, with a robust balance sheet. And I believe we now have the necessary capabilities and momentum to compete effectively and to deliver double-digit RoTE returns. With a strengthened leadership team now also in place, our goal is to deliver that 8% statutory RoTE in FY24. And I, as Clifford said, am completely committed to delivering statutory double-digit returns during our next three-year plan.

In late FY24, we will present our strategy for the next three years, and I am confident that we will be able to show that we're moving into the final stages of delivering the UK's best digital bank, with the UK's most innovative bank brand.

That concludes our presentation, so thank you for your attention. We'll now open for questions. And I think for those of you in the room, please press and hold the button on the microphone to talk, and Richard will co-ordinate the questions. Thank you.

**Benjamin Toms, RBC**

Morning, it's Ben Toms from RBC. One of the positive points from your results today is the NIM trajectory going into next year, driven partially by a younger structural hedge and a better outlook for deposit migration. Can you just give us an idea of the cadence for NIM for next year? It feels like it might be up a little bit in each quarter, which means that the exit rate for the year will presumably be towards the top end of the range that you've set out for the whole year.

And then secondly, on your investments in financial crime, by the time you've finished doing your investments, do you think you will have a fraud prevention and deterrent system that is better than other UK banks, or are you basically keeping up with peers? And for the £40m underlying run rate, roughly for the investment, how much of that do you think falls away once you get outside of the three years, because presumably, the sophistication of financial crime is unlikely to dissipate? Thank you.

**David Duffy**

Thanks, Ben. Maybe I'll take up the financial crime and the question around the underlying run rate, and Clifford will pick up the cadence on the NIM question. So, with regards to where do you end up in this territory, we're not catching up, I suppose, if that's the phrase. We're looking to be ahead of the threat level that we perceive to come, and that threat level is far greater than the threat level today.

What we're looking to be a part of is a club that has literally the best in class, so if I use fraud as a specific example, we have signed a contract for a fraud platform, but it is basically the level that is being deployed by one of the world's largest banks, so with all of their complexity and needs, that will serve us to an extremely high level, given our product profile. So we are stepping beyond what could be a normal step-up, we're stepping beyond that level, into a space where we believe we are ultimately futureproofing against that rising and very different threat of the future.

If you look at the spend and then you just keep on spending, is it, as somebody put to me, an arms' race? I think what we're saying here is that if we go to the best-in-class platforms for this, for financial crime and so on, we will then be at a maintenance level of spend and that is a very different order of spend than an investment in a platform. So I think we'll be looking at maintaining a profile.

The other commentary to make is that we're looking at a level of engagement in these platforms as beneficial not just for the protection you get, but because the bigger and more complex Tier 1 firms have these types of platforms, and we benefit from the issues and challenges they face in terms of the resilience and protection the system offers. So I think it's a win-win for us, but it's very much predicated on the future rather than catching up, and it's going to be a much lower order of cost in the future. So, Clifford, on the NIM cadence?

**Clifford Abrahams**

Yes, and just building on that, to give you a feel for the numbers, so we typically spent around £40m on what we call reg, regulatory investment, maybe three years ago. You can see in FY23, more or less an extra £20m or so on regulatory - you can see it in the bar charts - so we stepped up in FY23; now, this investment of £40m is a step-up to that, to three figures.

So you can see that that stepping up in tech and systems is above a very considerable run rate and that gives us confidence that we'll go back to those more normal levels. And alongside this, we also frankly, have a lot of resources committed in our business as usual, on fraud and financial crime - that's really people and systems - so that gives us confidence that it is very much a one-off. We don't know exactly where we'll be in three years, but it's very much a step-up from here, so I would expect it to taper after that.

In the case of NIM, yes, agreed, I think one of your peers talked about the swoosh? So we have that, we have an extremely modest downtick, and then we expect really the structural hedge to drive that higher, albeit modestly higher NIM over time, and with some of those headwinds still present, but much more attenuated than you've seen in some of the other banks.

**Andrew Coombs, Citi**

Morning, it's Andrew Coombs from Citi. I have one follow-up and if I could ask a couple of fresh ones as well. So firstly, on the follow-up, just on this investment in financial crime, obviously it is a big investment, and it comes after quite a substantial previous investment, things can drop away, and then there's always something additional. So could you just explain to us, with this investment in financial crime, how much is this your active decision versus how much have you been discussing this with the regulators, now that you've stepped up to being considered as a Tier 1 bank? So that would be my first question.

The second question is just in terms of the loan loss. Again, it's a similar message to the interims, where you talked about a very low arrears trajectory, but you've taken a conservative approach. Part of it is this bureau data; no other bank that we cover talks about this bureau data in the same way that you do, so do you think your methodology is different to peers?

And then the final question just on capital return. The dividend today is perhaps slightly lower than the market was expecting, and also, if I look at your guidance for similar capital return next year, it's below market expectations. But I'm more intrigued on how you think about the dividend versus buyback split going forward. You've talked about that 30% pay-out, but how did you determine that was the right figure to come out with? Thank you.

**David Duffy**

Thanks, Andrew. I'll pick up on the financial crime aspect. I think I'd just characterise this as a CEO decision. So let's be clear on that. I don't have the luxury of thinking just quarter to quarter, it would be an easier job if I did, I could just decide not to say anything about this. But over the past year, I think there's been a lot of chat in the industry, a lot of concern about these topics, but we were very

active in our research, and I spent time as I said, in Seattle but in many other places and looking at many other elements of this and the threat of escalation is what I really focused on, and the level of authenticity, sophistication, complexity that is being laid out in practical terms today and will deploy at scale. I can go all the way down the anecdotes if you want, you can go to the dark web, and ChatGPT Fraud is an app you can access and deploy for the unsophisticated practitioner to engage in fraud. So, there's a real world today that's only going to get a hell of a lot worse.

So I took the view that we could incrementally approach this, or we could recognise it for what it will be in the future. As Clifford said, we're investing heavily in what we have today, but let's invest in the future and future-proof the bank, particularly as you're gearing up to be mostly digital. So I think nobody is pushing us to do anything, it's really a call I had to make, and I have to take the accountability for that. Clifford?

**Clifford Abrahams**

Just a couple of themes. I think on bureau data, what's going on there, so that's the credit bureaus, and we use input from the credit bureaus, in particular regarding customer indebtedness. And the way our models have worked, which is really it triggers SICR - a significant increase in credit risk – is we get inputs from credit bureaus, so if customers are taking on more debt, that will trip that trigger.

Now, other banks may be modelling things in different ways. It is a trigger from stage one to stage two, so it's a provision. If arrears don't emerge, obviously we would release that over time, and you get this 12-month lifetime effect, so we've called that out. But I think it should give comfort that, at this stage, our ECL build is very largely a mechanical macros, bureau-driven factor, rather than arrears. We're not complacent, but we feel comfortable, given that step-up in coverage that you see, and we've called out, from 4% to 7% and so on.

I think maybe I'll just comment generally on our approach to capital distributions and how we've applied it this year and into our guidance. So, we've set our 30% pay-out ratio and 13% to 13.5% target a couple of years ago, and I think at the time, and still now, we're trading where we are, which is substantially below book, so we targeted that pay-out ratio to be maybe at the low end, certainly low end of peers, to provide headroom to do buybacks, frankly, where we're now responding to corporate finance analysis and what investors are telling us. And frankly, we've consistently delivered that, including today, and we've passed two stress tests and so on.

We've been a bit pragmatic this year at 37% pay-out ratio, because we recognise we've taken some of those non-cash items below the line, as you know, intangibles, we've already taken the capital hit, so it just seemed right to look through that to 37%, so I would see that as the Board being pragmatic, but we maintain our policy. In terms of buybacks, I think we're now developing a good and consistent track record of doing what we say in terms of on time, and those buybacks obviously all require PRA approval, and so that should telegraph comfort there.

And actually, for the first time, we've announced our guidance on capital distributions one year ahead. So not many banks do that, and I think that should give you comfort that we feel good about the strength of our balance sheet. Obviously, that gets reviewed by the relevant people, and we'd be committed to doing that, not in all circumstances, but that should give you comfort.

**Grace Dargan, Barclays**

Morning, it's Grace Dargan from Barclays. I think maybe coming back on NIM, note your commentary around the term deposits and the higher pay rates than elsewhere in the market. But, I guess where we're standing today, those rates have probably moved even higher than where your back book is,

with spreads narrower than your back book, so what kind of term spread assumptions are you assuming into next year?

So I think both in terms of those spreads, because you will have those term deposits maturing, but also, I know you're saying a more limited migration, are you expecting any further migration from here or not, I guess, what's in your NIM guidance?

And then secondly, probably again on NIM, just on mortgages, some of the other banks have steered a little bit more detail on the roll-off of those headwinds. Maybe you could give a little bit of colour on that, do you think that's a linear progression next year, is there any lumpiness there? That would be very helpful. Thank you.

**David Duffy**

Thanks. I won't try to answer that, I'll let Clifford do that.

**Clifford Abrahams**

So I appreciate drilling into the detail. I think I talked about headwinds and tailwinds. And it's clear, frankly, our tailwinds are quite similar to the other banks, so the structural hedge. It's just our headwinds are more modest, so you get this sort of leverage effect, so I can understand it's quite sensitive to modelling.

It's quite striking; we look very closely at the other banks - if you look at their Q3 bridge, you can see the very considerable deposit migration, it's double-digit NIM in many cases. Now, we don't have that, because of the effects that I talked about, and we'd expect those trends to continue. By analysing Q4, which is why we broke it out for the first time, comparing to other banks, should enable you to get to the positions in line with our guidance.

In terms of your specific questions, now we made that shift to term, so that's now about a third of our book. Those spreads were positive to swaps, so we could all see it at the time. Right now, it's more like zero, effectively, in line with swaps.

So you think, well, that's a bit of a dilution as they roll off, but it's a very considerably less dilution than rolling off current accounts or general balances. So that's on term. We've also got about 10 billion of non-linked, which we expect to also roll, to deposit migrate. So, I think we've been realistic about the headwinds, it's just the balance that's the difference.

In terms of mortgages, we talked about our book spreads of around 100 a few quarters ago, that's come down further. We've seen some recovery in application spreads in the last few months to being more or less in line with our book, much closer, but we are seeing some of those favourable spread two-year fixes and five-year fixes rolling off, so at the margin there's a bit of dilution, but if you look at book spreads to app spreads, it's really quite close right now for us. And in our case, we failed to sort of, really expand during those go-go years of two, three years ago, so I think that's why we're better off than some of the bigger players. Did that give you a feel for some of the moving parts?

**Grace Dargan**

That's very helpful. Thank you.

**Jason Napier, UBS**

Hi, it's Jason Napier from UBS. First one, and appreciating that you probably don't want to talk about the next strategic plan before this one is done, if you're going to get to double-digit RoTEs in the next plan, you can't have anything like the restructuring charges we've seen in the past. So, if only half of

the bank is on digital journeys, you don't have a single app yet, I wonder whether you could talk to any sense of scale on restructuring burdens to come, below the line.

And then secondly, on the RWA walk-forward, I think we're struggling to get your CET1 down as much as you're saying you will achieve this year. One of the blocks, of course, is pro-cyclicality and balance sheet growth. It looks like about 3% or 4% RWA growth in total, about half of your stat RoTE. If you'd just talk to whether that's right, whether the procyclicality piece is even predictable. We've been fearing procyclicality at a sector level for years, and it's never turned up, so if you'd just talk to the RWA growth in the year ahead, that would be helpful. Thank you.

**Clifford Abrahams**

Yes. So I think you're about right in terms of RWA migration. We're on the standardised approach for a number of our books, so that helps. The hybrid model helps as well. So I think that gets you there. You can see the £160m we've given, so I think you can triangulate back to the buyback that we talked about earlier.

In terms of restructuring charges, we've guided for FY24, we're not going to guide for beyond that. But we're very, very focused on statutory. We call out underlying, but we also quoted statutory, so for us, we're more or less indifferent. We're now talking about adopting the UK banks' treatment, excluding notable items, so you can see we're moving away from underlying and very much focused on statutory. So we'll talk more about future costs, but rest assured, it's that bottom line that we're focused on.

**Raul Sinha, JP Morgan**

Hi, morning, it's Raul Sinha from JP Morgan. Two questions, if I may. Obviously, the cards growth is becoming quite a big feature of your story, going forward. And especially when I look at slide 47, where you show us the vintages and the cohorts, you're obviously very heavily weighted towards the recent vintages, which I suspect at the industry level, are more spenders rather than revolvers, people who tend to hold less balances on their cards.

So I was wondering if you could talk a little bit about profitability within the cards business. Are you finding that profitability is lower than it had historically been when it used to be very balance transfer-heavy driven? Or is it now actually much more profitable because, one, you get the growth, but secondly, also, you're getting a lot of fees related to that? So just the standalone card profitability as you can see it would be very helpful.

And then the second one, just on the longer-term growth prospects for your mortgage book. I don't think you want to be shrinking or leaving that mortgage book stable over the medium term if you're wanting to grow your returns from here. And I would have thought that this would be quite a big opportunity for you, given you don't have the same back book refinancing headwind that a large chunk of your competition has. So, what would you encourage us to think about the medium-term growth rate for the mortgage business? Is it still going to be stable, just given the nature of your deposit base, or do you think we can aspire for something better than that?

**David Duffy**

Thanks for that. Page 47 will be yours, I think, on cards, I think Clifford will cover it. But just on mortgages, I think the way we're looking at that is, we spoke for a few years about originally being overweight mortgages versus our peers, and we're still at 80% today and looking to create a balance of the book by growing in the other areas and we've been doing that steadily, as we've been saying.

What you're dealing with in the mortgage market right now is a obviously much lower volume, more competitive pressures on the pricing, a gearing around retention as a primary, and that's gone extremely well for us, and you're able to hold your market share easier if you do that, a lower turnover of people up to two-year fixes and just holding with their risk profile until they see where this market goes.

I think there are other niches and other tactical areas which we might look at. Our history has always been to tactically trade smart around the margins and I think we're saying, as a position, if we hold our market share and do that in a tough market of lower volumes and greater competition, that's a win, while continuing to grow and diversify. And our business bank, we see, as I said earlier, a lot of opportunity continuously in that and we'll talk about the cards, with personal loans, the investment in pension products, so we're diversifying in addition.

So I think if you look at mortgages specifically, we're saying, really, holding market share over the next period of instability is a good answer and most probably where we'll sit. That's at least a year's horizon, we're not guiding to much beyond that, but we're not going to jump up. If we see an opportunity in the market on pricing or some particular niche, we will, of course, take that and that's always what we've done before. But right now, macro view would be holding market share is a good answer in the current environment. And maybe cards?

**Clifford Abrahams**

We're very focused on all our propositions delivering our target returns, 10% plus, mortgages, cards. And we apply different capital weightings, for obvious reasons, including stress. So in terms of profitability, I don't want to get into too much detail, but those recent vintages, actually a lot of those were balance transfers, so what we see is increasing in revolving, increase in use of cards coming out of COVID, our Virgin Atlantic proposition's going great. Now that will be associated with higher balances, but they're really transactors, and those are, what should I say, fair profitability for us, as well as our partners.

In the case of balance transfer, we took the view that the consumer will be in decent shape coming out of COVID, which has very much been the case. What you've seen is with interest rates going up, the market has lagged a little bit with repricing and in many cases, we've led the market. So the three year, the 33 months, 36 months interest-free periods have come in considerably and we've led that. I think that process still has further to run, but I think for us it's important that the card book delivers profitably as a whole and then we balance the different propositions, depending precisely where the markets are, and the market generally is repricing, reflecting higher rates.

**Aman Rakkar, Barclays**

It's Aman Rakkar from Barclays. I had three questions, all kind of related. I'm just looking at your NIM drivers next year, three of them feel quite mechanical, so mortgage margins rolling over, structural hedge repricing positively. Your term deposit book looks like it's probably got 100bps to digest, if I just look at your current rate versus where your front book business is. I'll save you the maths, but it seems like lending growth is the thing that drives your NIM next year and what kind of asset mix pickup are you expecting on the NIM from your various lending growth, could you quantify that, please? I'm sure I can go away and run those numbers, but it'd be interesting to hear your take on that.

The second is you're re-risking this business, your pivot away from mortgages to targeted growth in higher yielding segments, be it business banking and unsecured. I guess, two questions there, is how are you growing business banking so quickly when, on an underlying basis, the system is not

growing, a la recession? And how comfortable are you about cost of risk through the cycle, because I don't think we can get a clean read on cost of risk at the moment; you've come in above this year, you will be lower next year because you've built provisions and PMAs, but what's a normalised provision charge? It feels like it's probably ticking up on a multi-year view through the cycle.

The third question, the final question, is you obviously talked about the second phase of Consumer Duty, so I think you're probably talking about the implementation of the back book. I think we can see that Virgin Money does have some back book products out there in the market or legacy products that are no longer on sale, so what impact's that going to have on the savings book rates and how is that embedded in your guide?

**David Duffy**

Sure, thanks for that. There's a few things there, so maybe I'll cover pivoting away from mortgages as you put it, and Consumer Duty and back book as well, and asset mix Clifford can cover. To pivot away from mortgages, we have to be careful when we say that, it's very gradual and the materiality is not massive at any point in time and because we were overweight in mortgages, we were comfortable with that migration.

If you look at the business bank and why, to your specific question, are we growing so fast, we're growing steadily. And that's been in the small business area, and it's been in defensive sectors, which are sectors we have three and four economic cycles' knowledge of and supervision of with the same team who have been through those cycles together. In agriculture as a sector, we have five different sectors within that sector, with wind farms as part of that. So if you look at the broad mix, we took away CRE, which is one of the cyclical big swing factors and stands at 1% of our total book. We set up defensive sectors where we had confidence in our knowledge of the customer. We have seen healthcare and were awarded the number one bank in the UK for healthcare lending, so those specialist sectors are quite substantial, they're not just small and we're also seeing steady, continuous growth based on our reputation and our risk management of those customers.

Those customers, because we're small and there's a small SME category, we have deep insight into and through COVID and all the rest of the events that have happened, it's been scrubbed a hundred times. So, the quality is very good and the issues are well-managed. I think we see it's a net deposit gathering business for us with substantial deposits coming in, so that's a very healthy mix for us in that regard, as well. But we have referral business, substantial amounts of referral business in that, and for 22 months with consecutive growth. So it's not that we've become an outlier in one sector versus another, it's the defensive sectors we chose, it's the sector expertise we already have and its referral business and substance, and if you break away the economy, the small businesses are still growing. It's the big corporates that are retrenching, so there's a bit of a bifurcation there, we see that quite well.

The unsecured we've talked about on cards and that type of activity. With what I've referred to as Virgin Atlantic and ourselves, working together on a high affluent type customer to originate substantial growth. That's different than a large-scale player just taking the mass of the market. So, again, more targeted and I feel pretty comfortable there. Then you're looking at personal loans, but they'll be all appropriately credit scored so you're not just piling into scale in that, it's going to be very targeted.

So, you're going to see continuous diversification, the business bank growth, we're very comfortable with the quality of the book and the rate of growth. Cards, the type of targeting of growth we're doing. And I think the mortgages business, as I said earlier, will stay with a reasonable share, so our overriding focus is to risk-manage the book. To create balance, rebalance, and to create substance in each of the other sectors, which is what we're doing.

So, I'm hoping I'm covering the broader round of your questions in targeting that. We can get to the through the cycle cost of risk off the back of that, as well. So, maybe over to you, Clifford.

**Clifford Abrahams**

Yeah, so a few related points, as you say. I think that 100 basis points is just too much. I think I referred to those numbers, in the answer to your question, so if you look at where spreads on term deposits are now, it's close to swaps, I mean swaps are moving around, so I think the spread was tens, it wasn't three digits when we put on those term products, so I think that dilution is less. I think we do have some back book, existing propositions and it's very much in that non-linked savings area, and you can see it's sort of 10 billion or less. We've made appropriate assumptions around that, either further migration or those balances move to different propositions. You've seen that happen this year already, so I think we've made realistic assumptions about that.

I think around tailwinds from lending, the numbers are quite small now if you look at it. We're not looking for outsized growth in those higher-yielding areas. We're really looking to continue the track record, so, business, I think we've got considerable headroom to grow in business, as David indicated, for the reasons he set out. I think on unsecured you'd expect more moderate growth, but still growth that will outpace mortgages and I think that mortgage dilution is becoming over time de minimis. I think if you plug all that in, you'll get close to our NIM guidance and we're happy to work that through with the IR team.

I think for through the cycle cost of risk, our expectation is that is ticking up, and that just reflects the mix. We had a Capital Markets Day 2019, and at that point we set out our very long-term ambition to get to 25% non-mortgage balances, and we're now more like 21, 21 and a bit, so I feel good about that progression. It's quarter-on-quarter, year-on-year we've really delivered and I think mortgages, we've got a good franchise, but it's a well competed sector. We have really great franchises in business and cards, in particular, and further headroom to grow and that will be a tailwind to NIM over time, but also you'll see cost of risk ticking up and I made the point earlier, all our propositions need to deliver target returns after its expected loss and all costs, and that's how we manage the business.

**Richard Smith, Virgin Money UK PLC**

Operator, I think we're going to take a couple from the phone lines, please, if we can have the first question?

**Conference Call Operator**

Thank you. Our first question comes from Ed Henning of CLSA. Your line is now open, please go ahead.

**Ed Henning, CLSA**

Hi, thank you for taking my questions, just two from me, first one on mortgages and then second one on the cost-to-income. Just mortgages, the mortgage platform, again you've talked about it being delayed and I think you've said you wrote off about £45m. Can you just talk a little bit about what happened here, why is it delayed, when it's going to be released? Previously you talked about some costs coming out when that's released, is that still the case? That's the first one.

Then the second one, just on the cost-to-income. It's been flat now for three years; you're still talking about getting it below 50% over the medium term. What gives you confidence that you can get that cost-to-income down? You've been trying to pull costs out, but costs keep going higher, I understand there's a high inflation environment at the moment. Do you keep needing to invest in certain things

or is it revenue growth that's going to get you there? I'm just trying to pull the parts apart here, about where you're going to get that cost-to-income down would be helpful, please.

**David Duffy**

Great, thanks Ed, and we look forward to seeing you on Monday, in Australia. Let me just tackle the mortgages and Clifford will pick up on the cost: income dynamics. On the mortgage platform, the first thing to say is, by the way, it's not affecting our trading, I think a propos the earlier conversation, the trading is fine, it was more about optimisation and/or cost effectiveness. As we were just getting to the final stages of testing, you were not seeing the comfort in the testing data that we would've liked to see, so, rather than take a risk with your customer base, we just said let's go away, redesign or do anything that's required to recut that, so that the data will be something that we can rely upon and deploy with 100% confidence into our customer base.

Sarah Wilkinson, our new COO, who happens to be sitting in the front here, can be accosted after the meeting. But we've asked Sarah to do that checking of that test data, to make 100% sure that we know what we're going to look for in terms of confidence in any redelivery of this. To look to a new solution and to look to use what we can from the existing solution, and to put that timeframe together, such that in 2024, we'll have work beginning. Probably the latter part of FY24, I'm allowing Sarah the time to obviously get to grips with it, to scale a plan for it, and to plan and execute that deliverable timeframe.

So, Ed, we'll talk about it in more depth, but effectively, I want to have confidence in the delivery for the customer. We want to have Sarah, who has put a team together, we'll have really specialised technologists to deliver this and to set the timetable for us, rather than us set the timetable, but, in the meantime, we're trading effectively on it. The timing, I think you should just assume that it's a FY24 science and research project and a FY25 delivery, and thankfully Sarah is nodding at me, which you can't see, Ed. So that'll be the broad-brush strokes on the mortgage business, and maybe on the cost-to-income ratio, Clifford?

**Clifford Abrahams**

I agree, Ed. We set out our ambition of below 50% in FY21 and at the time I think there were a couple of drivers to that. One is our growth ambition, we're a medium-sized bank with a great brand and proposition and we can grow profitability, and we know that. And our cost saving and digitisation programmes, we were planning to open the jaws, now we've done some of that. I think looking back, obviously with the economy weak, we needed to moderate growth to safeguard credit. And it's fair to say alongside regulatory investment, we've had our service issues at the beginning of the year, which slowed our digitisation plans. Those plans have restarted and if I look going forward, we feel we can deliver further growth, like we've done this year.

I think I'd point out our macro forecasts are somewhat more prudent than the chancellors of yesterday. I think the chancellor's again saying no recession, I think that would be positive, but I feel more confident about the tailwinds from the macro in the next two to three years than maybe looking back, so I think that will facilitate top line growth.

But on the cost side, we've very much got momentum back and you've seen stores, as an example. We announced that programme in August, that was 18 months or so after the previous store closure programme, and that reflected our focus on service, and safeguarding the service that wasn't as good as it needed to be. Now that store programme is an example, we're very much getting back on track on digitisation and with inflation, we've got to run up the escalator quicker than it's coming down. So with inflation ongoing, we need to make sure that our digitisation and other cost saving measures are outpacing that and I'm really comfortable with the momentum that we've built up in the past few quarters. So that's really both those things, there's plenty of further cost saving opportunity,

there's lots to do, so for us, it's a question of prioritisation and pace of execution and we'll have more to say about this later in FY24.

**Ed Henning**

Not wanting to take away too much obviously from the Capital Markets Day, but it sounds like from that, that revenue hopefully grows a little bit, as you've mentioned. The big costs, you really just want to, open the jaws a little bit more back to where the original plan was, so costs still continue to trend up, so you don't see any big step changes, it sounds like it's a gradual improvement over time, is what you're hoping at this stage?

**Clifford Abrahams**

Experience says doing many things consistently well is lower risk, for customers in the bank, so expect more of that, and we have a pipeline of that. We feel we've got the growth opportunity, you heard some of it today, but as the economy normalises, we'd expect to see real opportunity for us to gain share. We look forward to talking about that in due course, but as of now, we're really focused on the deliveries that we've set out today and delivering on the guidance that we've set out.

**Ed Henning**

Thank you.

**Guy Stebbings, Exane BNP Paribas**

Hi, morning, everyone, thanks for taking the question, just some brief follow-ups on NIM. Firstly, can I just clarify what you're assuming for base rate in 2024? I think you might've suggested flat, just wanted to double check that.

Then on the 6 billion or so of TFSME, can you talk to how you plan to replace that? I think there's 300 million due in 24 and 2.5 billion in 25 and you've talked to replacing well in advance of contractual maturity, so any colour on what actions or how that informs your wholesale funding and customer deposit strategy?

And a final one on deposits. You've talked to being much further ahead in the journey on both mix and pricing than some of your larger peers. I guess some of those pricing actions would've attracted customers, attracted by the rate, so are you seeing anything in more recent pricing behaviour that gives you confidence that you don't need to be as competitive in terms of relative pricing moves from here versus some of those larger peers? Thank you.

**David Duffy**

Thanks, Guy. We'll pick up those three. Maybe Clifford to start?

**Clifford Abrahams**

Yeah, I'm just reflecting on the questions. We're developing a track record of paying off TFSME, so expect that to continue, I commented on that. I'm not going to target particular bond issues or deposit raising, but you can see we've got really good flexibility, good access to liquidity and will tap the markets where we see opportunity, whether that's retail or wholesale. Expect us to maintain our general wholesale issuance as we've done in the last years, around 2 billion we've said, so 1.5 to 2.5. This year probably closer to the lower end than the top end, but at this stage I think you should take that sort of guidance.

I think you were talking about pricing of deposits. I don't really want to get into specific deposit pricing versus competitors. I think the principles are, we included a chart that looks uncannily similar to one of the big banks, and - not a coincidence - and you can see that our total cost of deposit at 2.5% is maybe 80 to 100 basis points higher than the big banks. We want to provide consistently good value and you can see we've got good access to the retail market when we do that. Our total deposits were up year-on-year. It seems a long time ago everyone was worrying about deposits and deposit flight, and we consistently grew our deposit book quarter-on-quarter. We've maintained, in fact, we've strengthened our LCR, and all that points to plenty of opportunities to manage liquidity and to manage the TFSME, and we're feeling comfortable around liquidity management.

**David Duffy**

Then base rates, I think we're flat.

**Clifford Abrahams**

Yes, so base rates flat, I think I called that out. In our guidance we're not assuming base rates rise from here and then we expect them to decline at the back end of next year, 2024. Then our guidance, I've done these calls for many quarters, and so I know our guidance is based on current interest rates, so curves as of now, that's how we give our guidance, including base rate expectations.

**Guy Stebbings**

Okay, perfect. Thank you.

**Edward Firth, KBW**

Thanks very much, morning, everybody. I was wondering, it's probably slightly related to Ed's earlier question, but I'm just trying to push you a little bit on this double-digit RoTE expectation. Because if I look where we are today, we can argue when it happens, but interest rates are clearly going down from here going forward, which is clearly going to be a pressure in terms of the margin.

I guess we can talk again about one-off costs and what happens, but after seven years as a public company I think you've had one-off costs every year. We can argue whether they're 50 or 100 or 150 a year, but there's going to be something going forward. So it seems to me that the only way you can get that double-digit RoTE is if you make your serious inroads on the cost base and yet, you're saying there's no more restructuring to do or no more restructuring charges to take, let's put it that way. So, what am I missing in that? Because it seems to me that if you can't make a statutory 10% now, I don't see what's going to get so much better without massive restructuring charges that is going to move the needle materially at any time in the next two to three years?

**David Duffy**

Ed, thanks. I don't know if you want to do a full reconciliation, Clifford?

**Clifford Abrahams**

I guess, we talked about Capital Markets Day, I think that's the time to set out those ambitions. I recognise rates peaking, I think that's clear for the sector. We've shown today that looking back our net interest margin is more resilient. You see other banks' NIM coming down, ours is pretty stable and we've given that guidance going forward. But I think you're right in the sense that increasing rates is not going to be the tailwind that it was over the last few years. I think expect to hear us talk about the growth opportunity, I mentioned that earlier with Ed, as well as the cost opportunities that we see. Now we're realistic about inflation and the need to invest in the business, and you'll expect

us to talk about that in a year's time. But what we wanted to set out today wasn't pointing to Capital Markets Day per se, we wanted to set out that milestone where we'll set out the next three-year journey, but we're very, very focused on 24 and delivering on the guidance that we set out.

I think on restructuring, just maybe a little bit of a comment or correction. We didn't say no more restructuring charges ever. What we said was we guided to the remaining restructuring charges in 24, very largely that, £60m, but that statutory ambition is sort of after, after, after. So we are going to move to the notable items treatment, which we hope will be clear, but it's intended to convey a singular focus on statutory returns and then clarify the makeup of the costs, so you can do the modelling and I'm going to commit upfront that we won't have too many notable items. I'm looking at my head of IR, because I've had a page of notable items in another life, and we want to keep things simple.

**Edward Firth**

But just to be clear then, it is a cost story we're talking about. I mean if we take a steadily declining interest rate environment, which is probably consensus of some sort, and we can see UK volumes are pretty flat, generally, it is going to have to be a cost story, isn't it, that is the only way you can get there?

**David Duffy**

Let me just make a comment Ed. I think if you look at the next three years, and we'll get into formal discussions in the latter part of this year, I can see us continuing to drive through our digital efforts the cost-to-income ratio into a better and better place. I think, yes, that's going to have cost effects. It's not all about restructuring, there are other things that you can achieve in costs which don't require restructuring.

So I think what we're saying is that we see a pathway to the medium-term delivery of the double-digit returns when, in effect, in FY24 the underlying business is already delivering double-digit returns. So, I think it's just hard to give you the full guidance ahead of the later part of the year, but that's going to be our focus. You're going to hear us talking about digital delivery, automation, efficiencies, and working with our partners to create further improvements in costs. So I think, if you'll allow us, we'll talk to it then, assume an underlying business will deliver it and that's the precursor to the final piece of the jigsaw, which we'll share late in FY24.

**Edward Firth**

Okay, thanks so much.

**David Duffy**

Thanks, Ed.

**Richard Smith**

Got time for one more quick question, I think we've got one more on the line.

**Chris Cant, Autonomous**

Good morning, thank you for taking my questions. I just wanted to come back on the capital bridge slide and that RWA growth procyclicality component. I maybe misheard your answer to a previous question - are you saying 3 to 4% RWA growth, is that the book growth piece, is that the procyclicality piece or is that both? And I guess I'm interested to understand how you're thinking about how much of that block in your waterfall is procyclicality, because, as alluded to earlier, I think, in another

question, we just haven't seen that. When I look at your ECL scenarios, which I guess are feeding into your view around RWA procyclicality, they are quite, cautious shall we say. So it feels entirely possible that that component of the RWA growth may not materialise next year. I'm just interested in trying to size that within your thinking for that bridge, and if it doesn't materialise, does that just flow back into buyback capacity, given you're still targeting to get down to your 13 to 13.5% range? Thank you.

**Clifford Abrahams**

Thanks for that. On procyclicality, within that number, I think you're reacting to a number that one of your colleagues put out. So, it's that order, sort of middle-ish single digit, it's in our modelling, so underpinning our prudent guidance; I mean there are no numbers given in that chart, but our expectation is that RWA growth will be a headwind. Now we haven't seen RWA growth, really, for the last few years.

I think we should go through, maybe Chris, talk through with IR the RWA modelling basis for each of our portfolios. So we've got a mix of foundation, IRB, standardised and hybrid model, all of which have different sensitivities to macros, but broadly speaking are not highly sensitive, highly geared to the cycle. I think the driver there is mix, so we're growing faster in business and cards than mortgages, so you see that density increase, that's where most of it is. We've also run through our HPI assumptions through our mortgage models, to arrive at some headwind from mortgages, as well, albeit through the hybrid model.

So, you can see, I think we're being quite cautious, it's on that slide, it's more or less 10% over the next few years in our HPI assumption. Now that's a headwind, if that doesn't materialise, obviously there'll be a bit more capital, but we have targeted getting back to our 13 to 13.5% range, so that should help you size the capacity for buyback. We've given you our guidance, albeit one year ahead.

**Chris Cant**

If I could just follow up on that, that's helpful. In terms of guiding to expect some slower unsecured growth from here and not expecting to go particularly wild in business banking, how are you going to get to that mid-single-digit RWA growth? It sounds like most of it is coming from growth, rather than procyclicality, I know you put both on that slide, but from your answer just now, it seems like the majority is really about that growth piece. I'm just trying to square that with the answer you gave a little while ago about a slowdown in cards and continued progression, basically, in business.

**Clifford Abrahams**

I think we're getting into the details here, but slowdown, I think we called out 11% growth in cards, and I'm not expecting that, so, its slower growth, but not no growth. We're happy to pick this up, but underpinning our guidance, I think, is appropriate prudent assumptions around RWA growth and because of the nature of our models, we're not highly procyclical. I think the other thing I'd call out is Basel 3.1. So we're expecting the final rules mid-2024, but increasingly as we go into 2024 all banks, including us, will be thinking about Basel 3.1 and managing capital and any buybacks in relation to Basel 3.1. And we're more and more comfortable that that will not have a material impact on capital for a good few years.

**David Duffy**

And we have the 5 to 10% growth plan for business and unsecured still, in line for next year and beyond.

**Chris Cant**

Okay, thank you.

**David Duffy**

Thank you.

**Conference Call Operator**

Thank you. We have no further questions, so I'll hand back to David for any further remarks.

**David Duffy**

Thank you. Only another 20 minutes, so relax! No, thank you all for making the time today. We have our IR team here, we also have Allegra, who's just joined us, running our commercial business, and Sarah, who is our COO. If you wanted to, you can accost them unfairly here and get all sorts of information out of them. But thank you for the time and the focus, and we can cover any follow-on questions with you, as usual, so enjoy the day. Thank you.

**[Ends]**