Barclays PLC HY 2019 Results

Fixed Income Conference Call Speech

Tushar Morzaria, Barclays Group Finance Director

Kathryn McLeland, Group Treasurer

Title slide: Barclays PLC Fixed Income Investor Call – H1 2019 Results Announcement

Slide 2: Tushar Morzaria, Barclays Group Finance Director

Good afternoon everyone and welcome to the fixed income investor call for our half year 2019 results.

I'm joined today by Kathryn McLeland, our Group Treasurer.

Let me start with slide 3 and make a few brief comments on our Q219 performance and our targets before handing over to Kathryn.

Slide 3: Q219 Group highlights

We generated a profit before tax of £1.5bn in the quarter with a statutory RoTE of 9%, supported by double digit returns for both Barclays UK and Barclays International of 12.7% and 10.7% respectively, despite the challenging income environment

As we mentioned on the call this morning, we continue to target an RoTE for 2019 of over 9%, excluding litigation and conduct, and we called out that cost control will be a continued focus of the management team through the second half.

We have reduced our 2019 cost guidance for the Group to below £13.6bn, which you'll recall was the lower end of our previous guidance range and that's based on 30th June exchange rates

In terms of asset quality, delinquencies remained stable despite impairment being up £197m year on year to £480m, but this was due to the non-recurrence of favourable US macroeconomic updates and single name recoveries. The net write-offs in the quarter were just below the impairment charge at £465m.

Kathryn will talk about capital in detail shortly, but I wanted to briefly mention the increased half year dividend announcement we made today, of 3 pence per share which will be paid in September

Our capital returns policy is unchanged and the announcement is consistent with our progressive dividend intention. It's also our intention to supplement the ordinary dividend with additional cash returns, including share buybacks when appropriate.

Bondholders are, of course, a key stakeholder when we consider our capital plans, and we continue to view a CET1 ratio of around 13% as the appropriate target for Barclays.

Before handing over to Kathryn, I'd like to briefly mention Brexit given the uncertain political backdrop.

As you will have heard us say on numerous occasions, we believe that Barclays is prudently positioned in terms of our conservative domestic risk appetite.

Operationally we were prepared for the original March deadline. We have continued since then with the build out of our EU subsidiary, Barclays Bank Ireland, and the migration of all European branches is complete.

And, lastly, we have as our key tenet the advantages of a diversified business model – both geographically and across our consumer and wholesale businesses. This should stand us in good stead for any market stress events.

And with that, I'll hand you over to Kathryn, who will provide a comprehensive update on our capital, funding and liquidity positions, as well as other areas of particular interest.

Slide 5: H119 highlights

Thank you Tushar and to everyone for joining today's call.

I am pleased to be hosting my fourth fixed income investor call, and to be able to once again report robust balance sheet metrics.

We prudently managed the Group's capital position this quarter, finishing June with a CET1 ratio of 13.4%, marking the eighth consecutive quarter of operating at or above our CET1 target, that Tushar just referred to, of around 13%.

We continued to make strong progress on our MREL build, issuing over £7 billion in the first six months of 2019, out of a total plan for the year of around £8bn. As a result, as at the end of June, our HoldCo MREL ratio stood at just over 30% - at our 2022 requirement.

Today we also announced our intention to redeem three AT1 securities issued in 2014 with first call dates coming up in mid September this year.

Our balance sheet has remained highly liquid, an important credit strength for Barclays, with the June LCR at 156%, and a high quality liquidity pool of £238 billion.

The evidence of our improved, and sustainable, statutory profitability, coupled with the prudent management of our balance sheet, contributed to the positive outlook we received from Moody's for the ratings of Barclays PLC and Barclays Bank PLC in May.

I will now begin with some remarks on the Q2 developments in the Group's CET1 position, which you can see on slide 6.

Slide 6: CET1 ratio progression

We reported an increase in the CET1 ratio from 13.0 to 13.4% over the quarter, driven primarily by strong organic accretion from profits of 38 basis points.

There were also favourable moves in the value of our Absa shares, bonds we hold in our liquidity pool, scrip take-up, and a slight decrease in RWAs, alongside other smaller items which aggregated to another 38 basis points of accretion.

Given our dividend announcement today, the accrual rate was adjusted for the first six months of 2019 and is reflected in the 22 basis points impact we show for dividends paid and foreseen. The scheduled pension contribution caused a negative impact of 6 basis points.

These results marked the fifth consecutive quarter of clean results, and we continue to demonstrate the capital generative capacity of our business model.

The profits we make will help absorb the manageable headwinds ahead. These include in the near term, the FX impact from the redemption of the AT1 securities, another pension deficit contribution in September and dividend accruals.

Of course the AT1 redemptions will also have an impact on our Tier 1 capital position, and therefore the leverage ratios too, of around 25 basis points on a UK spot basis.

Turning to slide 7.

Slide 7: Strong capital position

As I mentioned at the beginning, we have been operating at or above our target CET1 ratio level of around 13% for eight consecutive quarters.

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The calibration of our target to regulatory requirements has not changed, as you can see on this slide. When we also consider with our capacity to absorb stress tests, which I will cover in a moment, we still view around 13% as an appropriate CET1 target.

Jes and Tushar highlighted this morning the current treatment of Op Risk RWAs. We are exploring with the PRA the possibility of removing the floor that was introduced in our operational risk RWAs.

This would have the effect of reducing Pillar 1 RWAs, and would also be expected to lead to an increase in the Pillar 2 requirement. Our reported CET1 ratio would therefore increase, as would our regulatory minimum.

In assessing the adequacy of our capital, we do factor in future headwinds from regulatory changes in RWAs. We are confident that these changes are manageable, and they are of course, taken into account in our capital planning.

Over the next couple of years we have the PRA's proposed changes to mortgage risk weights in Barclays UK, starting at the end of 2020, where there is a change to the definition of default from 180 to 90 days, partially offset by an implementation of a hybrid point in time and through the cycle model.

In the CIB, there are changes to the securitisation risk weightings in early 2020, and changes to standardised counterparty credit risk, or SA-CCR, from mid-2021.

We currently expect each of these three elements to result in RWA increases of low single digit billions.

On a positive note, there is an expected modest leverage benefit from the SA-CCR change, as the new approach gives greater recognition to netting and collateral.

Of course this is based on our current balance sheet and business mix, and does not take into account further mitigating actions.

Beyond these items, we are aware that some of our peers have disclosed estimates for the impact of so-called Basel 4.

We feel, however, that it is still too soon to be providing guidance, not least as the Bank of England has yet to formally opine on how they would implement the new standards. And, we are particularly mindful of areas where there is national discretion such as the op risk multiplier.

We are aware that the Basel committee seeks implementation in 2022. However, we know this would be subject to the European legislative process – a potential CRR III package – and so we may be looking at an implementation date well beyond 2022, and with a five-year transition period to follow.

Slide 8: Demonstrated ability to pass stress tests

Another important driver of regulatory capital is stress tests, and naturally, the market pays closest attention to the Bank of England exercise in the case of UK banks. You can see the results from the last two years on slide 8.

For the 2019 test due to be published towards the end of the year, we note that the stress variables are broadly similar to the last three years.

However, a key difference to last year for us is that our US RMBS litigation settlement in 2018, which accounted for around 40 basis points of the CET1 drawdown, will not be repeated, and so the equivalent drawdown in last year's test would have been around 400 basis points.

We know that a key area the market is focussed on is the interaction of the stress test with IFRS9, as banks and Regulators evolve their approaches.

We have observed that the Bank of England has been consistent with their overarching principle that IFRS9 should not drive a de facto increase in banks' capital requirements.

And, the hurdle framework remains under review to adapt from the test last year.

Turning now to leverage which you can see on slide 9.

Slide 9: Managing evolving future Group minimum leverage requirements

Our UK leverage ratio for the Group was 5.1% on a June 19 spot basis, and 4.7% on a daily average basis.

As you know, the UK is ahead of Europe in disclosing average leverage ratios.

We are required to meet leverage requirements on a daily basis, and so we naturally manage and hold divisions accountable to an average leverage balance sheet measure. As you can see, both the spot and average metrics are prudently above the 4% requirement.

We are also mindful of CRR II requirements that are due to take effect in 2021, and potential further changes by the Bank of England.

Considering the current and potential future regulatory requirements, we remain a Bank that is RWA constrained, with leverage acting as a backstop measure. This is consistent with the Regulator's intention that leverage acts as a secondary metric.

Turning now to the legal entities.

Slide 10: Strong legal entity capital and liquidity positions

The CET1 ratio for the Group of around 13% continues to accommodate the capital requirements of all our legal entities.

As you can see on slide 10, at the half year, Barclays Bank UK PLC, or BBUKPLC, and Barclays Bank PLC, or BBPLC, printed CET1 ratios of 14.4% and 13.4% respectively.

For the US IHC, capital is of course regulated on a standalone basis by the Fed and the required levels of capital are largely driven by the CCAR stress test outcomes.

We were pleased to have passed our second public CCAR in June, demonstrating that the entity continues to be well capitalised and our ability to manage capital appropriately across our subsidiaries. As at 31 March 2019, Tier 1 leverage was 9.3%, and CET1 was 15.1%.

Slide 11 looks at the other elements of our capital stack, and where we are transitioning to the 2022 capital structure.

Slide 11: Transition to 2022 capital structure well established

Starting with AT1.

You will have seen our AT1 call announcement today across all three instruments with first call dates on 15 September.

We have been consistent in our messaging that we review the economics of call decisions - in the round. I explained how we think about this in some detail on our February fixed income call.

The AT1 guidance we communicated at FY18 results remains. Namely, to hold AT1s in the low 3 percents of RWAs. This maintains a comfortable headroom above the 2.4% level, which reflects the Group pillar 1 and pillar 2A capital requirements allowable in this form, and accommodates variability in both RWAs and FX, including under stress.

We also consider our call profile when assessing the appropriate level of AT1, and its secondary benefit of contributing to the leverage ratio.

For Tier 2 - we are incentivised to hold at least 3.2% of RWAs in this form, and again we intend to maintain headroom to this 3.2% level.

We were pleased to have been active in issuing both AT1 and Tier 2 instruments during the first six months, raising almost £4bn equivalent.

We have made good progress in managing our legacy capital too, most recently redeeming our BB PLC issued £3bn 14% RCIs in June.

One question we are often asked is our view on the Bank of England's MREL policy which states that legacy capital instruments not issued from the resolution entity, "could constitute an impediment to resolution"

Our understanding is that, as outlined in the policy, they will consider each bank on a case-by-case basis and that they will look at the presence of these instruments as part of the overall resolvability assessment.

We believe the modest and short-dated post-2022 legacy capital stack is highly relevant for this assessment, as we have only £1.2bn of instruments with first call dates or maturities beyond the end of 2022.

As we have stated previously, we don't view the presence of legacy capital instruments as a concern for Barclays in this regard.

Turning now to our HoldCo issuance plans.

Slide 12: Successfully transitioning to a HoldCo funding model

As you can see on slide 12, we have been active in the primary markets in the first half, issuing £7.1 billion equivalent from the Holding Company.

£3.4 billion of that was in senior form, with £2.5 billion in AT1 and £1.2 billion in Tier 2. This compared to around £7 billion of maturities and redemptions from the HoldCo and the OpCo.

We were pleased with the continued currency diversification of our HoldCo issuance – for example the AUD 800 million senior public transaction we launched in June.

We value this currency diversification in our term funding, and the ability to attract new investors to our credit, and we intend to continue issuing in non-G3 currencies going forward.

As a result, our Jun-19 MREL ratio was 30% on a HoldCo basis, and 32% on a transitional basis – in excess of our interim requirements and at our 2022 requirement of around 30% of Group RWAs.

As many of you listening to this call will know, we intend to hold a prudent headroom above this minimum MREL requirement.

And we expect to continue to be a regular participant in the MREL market, across the full range of AT1, Tier 2 and senior unsecured.

Given that we have issued almost all of our £8bn plan for the year, naturally we have been asked about our intentions should we complete our target well before the end of the year.

If we find ourselves in that situation, we may look to continue issuing modest amounts of MREL-eligible paper should market conditions be conducive, being mindful of the economics of doing so.

Before moving on, I wanted to briefly take the opportunity to cover issuance from other Group entities.

The two main subsidiaries of BB PLC and BBUK PLC have been active in accessing the funding markets across the diverse spectrum of funding streams that are available in both secured and unsecured markets.

One example I wanted to highlight is the four-year covered bond issued by BBUK earlier this year, which marked our inaugural SONIA-linked instrument.

At Barclays we have been proactive in looking at ways we can support benchmark reform, and this is one such example.

Tushar is of course Chair of the Risk Free Rate working group, whose objective is to catalyse a transition to using SONIA as the primary interest rate benchmark in the sterling markets.

Turning now to liquidity.

Slide 13: High quality liquidity position

Slide 13 shows our prudent approach to liquidity, with a liquidity pool of £238bn and an LCR of 156%, representing a surplus of £83bn above our 100% regulatory requirement.

We remain comfortable with the conservative position that we run, and believe this to be an inexpensive credit strength as we navigate an uncertain macroeconomic backdrop.

The decline in the LCR from the December 2018 level of 169% marks the seasonal use of liquid resources, and you should expect to see this ratio move within these ranges, all else being equal.

Subject to a constructive Brexit outcome, you could reasonably expect us to run a slightly lower LCR, whilst continuing to maintain prudent surpluses to internal and external requirements across the Group and its material entities.

We have of course seen the recent implementation of NSFR in CRR II, which is effective from June 2021, and so we continue to run the Group's funding profile with this in mind, and in surplus to the NSFR requirements, based on a conservative interpretation of the standards.

Slide 14: Ratings remain a key priority

Turning now to our credit ratings – which are a key priority for Barclays, with our focus particularly on the outlier, Moody's Baa3 Hold Co senior rating.

We were pleased with the change in Moody's outlook on Barclays PLC and Barclays Bank PLC's senior unsecured ratings from stable to positive, following the downgrade to those ratings just over a year ago.

We know that their focus is on our statutory profitability, which is fully aligned to our Management's goals of continuing to improve our profitability on a sustainable basis, to achieve our Group returns targets. The £1bn of statutory profits again this quarter clearly demonstrates that this is happening.

Importantly, we are also working closely with S&P and Fitch, and conveying the successful execution of our strategy, and our intention to further strengthen our credit proposition, and thereby improve our ratings profile over time.

As for my final comment, I would like to devote some time to ESG, which you can see on slide 15, our first slide on this important topic, though of course we have had ESG disclosures in our Full Year Results and Annual Report for many years.

Slide 15: Focus on ESG

We know that both our fixed income and equity investors have rightly become increasingly focussed on ESG matters.

We have welcomed this interest, and have been very glad to engage with investors on this, talking through the initiatives that we have undertaken, and demonstrating that we take our responsibilities seriously as a global bank.

For instance, in environmental matters we have made a significant effort on climate related financial risk management, working on implementing the PRA Supervisory Statement SS3/19 that includes governance, risk frameworks and MI, and developing our approach to climate related stress testing.

We are members of the Taskforce on Climate-related Financial Disclosures (TCFD), with our first disclosures in 2017, and we are a founding member of the UN Principles of Responsible Banking.

And we have set ourselves clear, ambitious and unequivocal goals to make a tangible difference in this field, committing to providing £150bn of social and environmental financing by 2025. We've pledged to reduce our own carbon footprint by reducing our scope 1 and 2 green house gas emissions by 80% by 2025 and sourcing 100% renewable energy by 2030, with an interim target of 90% by 2025.

Within Treasury, we are focused on meeting our goal of holding £4bn of green bonds in our liquidity pool over time, and we were also the first UK bank to issue a green bond backed by UK assets.

On social matters, we are actively engaged in a variety of important areas, including vulnerable customer support, helping customers manage data privacy and security, and in creating a diverse and inclusive workforce.

And lastly from a Governance perspective, we are pleased to have put many of our legacy cases behind us, whilst strengthening our control environment through firm-wide initiatives.

We know that many of our investors rely on third party providers of ESG ratings, and we will continue to work closely with these agencies to try to ensure our activity and actions are correctly reflected in their models.

For example, ESG ratings can sometimes be based on backward looking information, and reflect legacy issues that are not relevant for up to date scores.

We know that ESG is an evolving field and we would be delighted to continue to engage directly with our investors on this matter.

And so to conclude.

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Slide 16: Conclusion/Q&A

At the beginning of the year I set out Treasury's priorities for 2019 – which were split into two key areas.

The first was to maintain the robustness of the Group's balance sheet, given the uncertain political and economic backdrop. This includes managing the Group's capital position at our target CET1 ratio of around 13%, continuing to build our MREL funding stack, and running a prudent liquidity position.

The second was to support the Group in the achievement of its financial targets.

We are pleased with the progress we are making, but recognise that there is work to do.

Tushar, with that, I'll hand back to you.

Thank you Kathryn. I hope you have found this call helpful. We would now like to open the call up to questions.

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Information relating to:

- regulatory capital, leverage, liquidity and resolution is based on Barclays' interpretation of applicable rules and regulations as currently in force and implemented in the UK, including, but not limited to, CRD IV (as amended by CRD V applicable as at the reporting date) and CRR (as amended by CRR II applicable as at the reporting date) texts and any applicable delegated acts, implementing acts or technical standards. All such regulatory requirements are subject to change;
- MREL is based on Barclays' understanding of the Bank of England's policy statement on "The Bank of England's approach to setting a minimum requirement for own funds and eligible liabilities (MREL)" published in June 2018, updating the Bank of England's November 2016 policy statement, and the non-binding indicative MREL requirements communicated to Barclays by the Bank of England. Binding future MREL requirements remain subject to change including at the conclusion of the transitional period, as determined by the Bank of England, taking into account a number of factors as described in the policy statement and as a result of the finalisation of international and European MREL/TLAC requirements;
- future regulatory capital, liquidity, funding and/or MREL, including forward-looking illustrations, are provided for illustrative purposes only and are not forecasts of Barclays' results of operations or capital position or otherwise. Illustrations regarding the capital flight path, end-state capital evolution and expectations and MREL build are based on certain assumptions applicable at the date of publication only which cannot be assured and are subject to change, including amongst others, holding constant the Pillar 2A requirement at the 2018 level despite it being subject to at least annual review and assumed CRD buffers, which are also subject to change.

The information set out in slide 23 (the "Illustrative Financial Information") is for illustrative purposes only and is subject to change. The Illustrative Financial Information, including indications of total assets, revenue, funding, balance sheet estimations and ratios has been compiled as if the following activities, customers and clients ("In-Scope Business") were comprised in the businesses of Barclays Bank Ireland ("BBIe") as at 31 December 2018:

i. all regulated activity and client base of the European branches of Barclays Bank PLC ("BBPLC") as at 31 December 2018; and
ii. all regulated activity of European clients of BBPLC who were located within the EEA (excluding the UK) as at 31 December 2018.

The Illustrative Financial Information represents a modelled view including estimates based on Barclays' current planning assumptions for the business and operating model for BBIe, and is presented to show the possible effect of the proposed business transfers as if they had occurred on 31 December 2018. In addition to this, certain of the Illustrative Financial Information has been sourced from the BBIe 2018 statutory accounts, management accounts of BBIe up to 31 December 2018 and also the general ledger. The Illustrative Financial Information has not been independently verified. While Barclays' plans for an expanded BBIe in response to the UK's withdrawal from the EU are well progressed, they remain subject to the outcome of the political negotiation, ongoing regulatory engagement and management discretion, and so are subject to changes which may be significant. Among other variables, the actual amount of In-Scope Business that may ultimately transfer to (including, but not limited to, as a result of what activity is finally determined to be regulated activity) and/or continue to trade with BBIe in the future may differ significantly from the assumptions used in producing the Illustrative Financial Information. The Illustrative Financial Information is therefore provided for illustrative purposes only and is not a forecast of present or future financial condition or performance of BBPLC or BBIe. Whilst all reasonable care has been taken in providing the Illustrative Financial Information no responsibility or liability is or will be accepted by Barclays PLC and any of its subsidiaries, affiliates or associated companies or any of their respective officers, employees or agents in relation to the adequacy, accuracy, completeness or reasonableness of the Illustrative Financial Information or for any action taken in reliance upon that information by any party whether customer, client, counterparty, investor or otherwise. Nothing in the relevant slide should be taken as (or is) a representation or warranty, express or implied, as to any of the matters presented.

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This presentation includes certain non-IFRS performance measures, such as income statement and financial performance measures excluding litigation and conduct. These measures are defined and reconciliations to the nearest IFRS measures are available in the appendix to Barclays Group's interim results announcement for the period ended 30 June 2019.