Virgin Money Q1 2016 Trading Update

Transcript

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Preamble

Good morning everyone. I am here this morning with Dave Dyer, our CFO, and Anth Mooney is also here with us. I know you will have some detailed questions on our mortgage portfolio later, and there is certainly no one better to answer them than Anth. I will give you a short update on our performance in the first quarter, and then we will take your questions.

Overview

I am pleased to say that we have had a really strong quarter and we have delivered against all of our targets for growth, quality and returns. For me though, to start with it is important to emphasise the stability of our business and of our profitability. We continue to see strong asset quality across all lines, and we uphold rigorous underwriting standards. We continue to enjoy a legacy-free business. During the quarter intermediaries voted us their number one mortgage partner, and only last week we were independently assessed as one of Britain's most trusted banks, second only to Nationwide. I think that all of this puts us in a unique position in the market. We are not a specialist lender, we are not an incumbent bank, but we are a sizeable and trusted alternative, with a brand that cannot be copied and which achieved almost 4% growth in customer numbers in this quarter alone.

Mortgages

The story of the first quarter is one of strong asset growth funded by equally robust retail deposits. We had a record quarter in mortgages which were up 30% year-on-year. To be clear, the majority of that growth came from residential mortgages, and they grew about twice as fast as buy-to-let. Buy-to-let was less than 25% of our front-book flow and it remains at just over 17% of our total portfolio. Mortgage asset spreads remain below the level of the back book of course, but slightly ahead of our experience in the second half of 2015; or, as Dave would say, we are seeing them flat with a hint of up.

Cards

Our cards business continues to exceed my expectations, with strong growth in customers and balances and a low cost of acquisition. We are confident of reaching our accelerated £3bn target by the end of 2017, and maybe we will get there a little bit earlier than that. However, please do not get too carried away based on our current run rate, because that is of course affected by normal market seasonality. I know that many of you joined us for Michele's Spotlight on Cards very recently on 20th April, and so you will know our confidence in the NIM growth that the cards book can deliver.

Retail

All of this asset growth has been supported by an equally strong performance in retail deposits. Price and volume were in our favour, and we did really well in the Cash ISA market where we have grown our market share to over 4%; and that is up from only 3% at this time last year. There is further to go on deposit pricing, as we are currently going through another back-book reprice of around £5bn worth of deposits, and I think I mentioned that when we spoke at the year-end. Once again, through the reprice attrition is lower than expectations. The rate reduction will not be effective until the end of this month, and so it has not impacted on our NIM yet.

As you know, we have also had two successful RMBS offerings this year, and they have totalled £1.3bn worth of funding. Both priced well in currencies including the dollar and euro, and both were multiple times over-subscribed. As a result, our loan-to-deposit ratio increased marginally in the quarter. Taken together with our strong retail deposit position, we are currently long in liquidity, which is our preference as we go into the referendum uncertainty. Current accounts, although small, grew well during the quarter, and we actually saw an almost 20% increase in current account balances year-on-year. Travel and home insurance performed especially well but we have more work to do on our other insurance lines, especially after the conclusion of our partnership with Friends Life. However, the opportunity here certainly remains significant. Our pensions business grew well, although income from this and from our other investment businesses is strongly affected by the performance of the FTSE, of course. In summary, OOI is doing okay and there is much further that we can go.

Costs

Our costs of course remain a key part of our story. We have done more mortgages than we planned in the first quarter, but our costs have remained flat and on budget. The reality of our operating leverage really does continue to come through. In fact, we have held costs pretty much flat now quarter-on-quarter for the last six quarters. So although we are not disclosing our jaws this quarter – we only disclose it at the half- and full-year – they remain strong. As one of the analyst community said to me only recently, 'They are in a place where James Bond himself would be proud of them.'

Asset quality

Our asset quality also remains strong, and that is as a result of both the benign rate environment that we all enjoy and, I think more importantly, as a result of our stringent affordability and underwriting criteria. We stress-test our policies regularly and we make changes as necessary, so you will not be surprised to hear that at the moment we are currently reviewing our rental cover requirements for buy-to-let lending, given recent movements in the market.

Net Interest Margin

Let me turn to net interest margin. NIM for this quarter was 160bps, and we continue to expect to hold it at this level for the year. It is affected, however, by the relative growth of our mortgage book compared to our cards growth. Obviously a higher proportion of cards means higher relative NIM, but we will not hold back growing mortgages if they are available within our risk appetite, where marginal returns meet our mid-teens hurdle. Whilst accelerating mortgage growth might dampen NIM, it will of course enhance and advance our returns. To be clear, we remain absolutely focussed and confident in delivering mid-teens returns by the end of 2017, as we have previously and consistently guided.

Looking ahead

Looking ahead, we expect strong mortgage growth to continue. We expect, subject to the outcome of the referendum, a mortgage market of around £240bn and we continue to expect to take towards the top of our 3–3.5% market share aspirations. We expect, again subject to the referendum, asset pricing to remain stable, especially given Lloyds' comments in this area. As I previously said, we are confident of cards growth and we expect full-year NIM of around 160bps.

We do see uncertainty ahead around the referendum, but we are of course a UK-only retail bank. We are not exposed to Europe or beyond and so will be affected only by the impact on the UK economy, where we see a Brexit resulting in higher asset pricing for customers and less certain incoming investments for businesses.

For our own business we continue to focus on the growth of our existing business lines, and also the development of our other income lines, and the build of our SME business, and the analysis of our PCA development opportunities and the continued development of our very strong customer culture. It is very much, for us, steady as she goes. A really good and strong quarter delivering on our promises, and we look forward with confidence to being recognised as Britain's best challenger bank. Thank you very much. We look forward to your questions.

Q&A

Rohith Chandra-Rajan (Barclays): Hi, good morning, a couple if I could please? One on the mortgage growth, which you have partly addressed, and the other one is to clarify some of the margin outlook. On the mortgages, volume in the quarter was obviously strong year-on-year, up 30% in terms of gross. However, that is lagging the market [which was up] about 40%. I think you just clarified in terms of what your expectations are for the year so, £240bn at 3-3.5% is maybe £8–8.4bn. I just wanted to check that you are still expecting the run rate that you saw in the first quarter in terms of gross mortgage lending to continue for the rest of the year? I would be interested to know your thinking on why the Virgin Money growth has lagged the market? Is that due to a strong quarter in Q1 last year, which I think was above the target range in terms of gross lending? Or is it more around risk appetite? That is the first one, thank you.

Jayne-Anne Gadhia: Thanks Rohith, and good morning. It is unfortunate; we tried to get the Bank of England analysis on the balance of buy-to-let and resi in the market, to be explicit about the answer. However, for us we absolutely focussed on residential mortgage growth rather than buy-to-let mortgage growth. My expectation when the analysis comes out is that a lot of the overall market positions will have come from buy-to-let, and we have not seen a bubble in that. We consciously aimed not to see a bubble in that. I did not want to be sat here saying to you that we are delighted about our mortgage growth but it is all dependent on the risk that the world is taking on buy-to-let. We have not done that, so we are very pleased that that growth has come from twice as much acceleration on the residential book than the buy-to-let book, and a diligent focus and continued focus on, as you rightly say, our risk appetite.

We are delighted with the performance, delighted with the mix. It is exactly where we wanted it to be. In absolute terms of course, it is ahead of where we expected it to be. As we have said on this call previously, the way in which we try and run our operations effectively is to establish the number of applications that we will be able to take a day. To get to 3.4% market share of a market that was bigger than we expected, actually because of the buy-to-let blip, we have been able to do more than our target number of applications a day consistently for the quarter. We have done it whilst holding costs flat.

All of that together: we have over-delivered absolutely in volume. We have hit market share targets. We have done it without increasing costs. We have done it within our risk appetite and we have done it predominantly through residential. All of us here feel very pleased about that.

Rohith Chandra-Rajan: Okay, thank you. Could I just check on the volume expectations for the year: is that similar run rate to the new business written in Q1? Is that roughly what you are expecting?

Jayne-Anne Gadhia: Yes, that is right.

Rohith Chandra-Rajan: Okay, great, thank you. Then secondly on the margin, I think you ended last year at 164/163bps; obviously a bit of attrition in the quarter I guess driven by the strong mortgage volumes, but some benefit from deposit repricing coming through. I just wondered if you could talk about the positives and negatives for the rest of the year, and why you think you can hold it flat at 160bps given the Q-on-Q decline?

Jayne-Anne Gadhia: Yes, as I was trying to say really in my opening remarks, for us the really good news is that mortgage asset spreads remains flat with a hint of up. Hearing António and Lloyds talking about their view on stability of asset pricing is obviously good for the whole mortgage market. Our cards position you know well, you personally having come along on 20th April, and we remain very confident about our cards yield and the prudence of our EIR calculations. Just to reinforce the point, as far as retail deposits are concerned, we are able to grow that deposit but actually slightly ahead of our overall expectations at the beginning of the year. We have set that pricing well.

The only reasons for any dampening of our NIM is the acceleration of mortgage growth. When we sit and think about, 'Should we, as a growing challenger bank, be restricting our growth in order to protect our NIM?', it does not seem to be doing the right thing for shareholders. Because actually, what we want to do for shareholders is to get to mid-teens ROE. We feel that, while the market is available for us to do that, we can do that at the margins by increasing mortgage volumes, and we think that we would be negligent not to do that. We have talked a lot about which our priority should be, NIM or returns, and to be really clear we are prioritising returns. We are not going to do that willy-nilly at the complete expense of NIM, but it is our view that the right thing to do with our capability, our funding and our capital in a market where we can grow within our risk appetite confidently and within our operating leverage position, is to take market share while we can at the right price and drive our returns position accordingly.

Rohith Chandra-Rajan: That is great. Thank you very much.

Jayne-Anne Gadhia: Thanks, Rohith.

Andrew Coombs (Citigroup): Morning, a couple of follow-up questions on the net interest margin, especially from the asset side. You made the point that pressure on front-book spread is less than you anticipated given the move year-to-date, but that you still expect pressure overall given the move from the back-book rate to front-book rate. Perhaps you could elaborate on what the aggregate back-book rate is that is rolling over onto new front-book rates?

Then the second question which is with regards to the deposits that you have managed to take on board in Q1; a very strong result, £1.2bn of growth. I think you said 70% of those relate to ISAs, so perhaps you could elaborate there on the cost of those deposits; what is the split fixed versus variable, and how does that compare to your existing deposit base? Thank you.

Jayne-Anne Gadhia: Gosh, that is a detailed question, Andrew, thank you very much indeed. Who wants to answer that, Anth or Dave?

Dave Dyer (Chief Financial Officer, Virgin Money): I am happy to start. Andrew, we do not give out the complete detail of that front-book/back-book point but you will appreciate, understanding the market, that three years ago spreads were a lot higher than they are now. You are looking at a book that is tens of basis points different back-book to front-book, and that effect continues to roll through for everybody in the market. That is why we talk about continued pressures; the take-on of new business at spreads below what we have enjoyed in the back-book.

On the deposit side, the ISA success is notable and we are very proud of the scale of that achievement in terms of the volumes. However, we have actually done it inside our budgeted expectation for pricing, and we have seen the front-book pricing perform better than it did last year this time. Again, we are not generally giving out the specifics of that mix, but you can expect that trend to be an improvement on the rate at which we were acquiring deposits last year.

Jayne-Anne Gadhia: If it helps as you all think about your models, part of the back-book/front-book position for us: only 13% of our portfolio is on SVR. So despite the fact that we are seeing that as a dilution between front-book to back-book, compared to the big banks with very big SVR exposure clearly the position for us is stronger, because of the relatively small SVR position. That is 13% percent of our total portfolio.

Andrew Coombs: Okay. I guess the broader question would be that, given some of the pressures that you had anticipated have been less acute than you had previously expected, is the sole reason that you are maintaining the guidance of a dip to 1.6 purely on the basis of the faster mortgage growth than anticipated? Is that the sole change versus your expectations at the start of the year?

Jayne-Anne Gadhia: Yes, absolutely.

Andrew Coombs: Okay, very clear.

Jayne-Anne Gadhia: The acceleration of volume is the only difference we are seeing. In fact, as you rightly said, there are some improvements on some of the individual components of our overall NIM.

Andrew Coombs: A final one on this before I let you move on, on savings repricing. You talked about the savings that you have that were repriced at the end of this month: are there any expectations that you can reprice further?

Anth Mooney (Director of Financial Services, Virgin Money): As Jayne-Anne has described, we have got that further repricing to take effect during May. Given the softer market pricing environment that we are seeing, if that were to sustain then there is a possible further opportunity for us to look at certain segments of our back-book. We will continue to keep that under review.

Andrew Coombs: Right, thank you.

Jayne-Anne Gadhia: Thanks, Andy.

Guy Stebbings (Exane BNP Paribas): Good morning. First question from me, back on NIM again. I just wanted to pick up on the trajectory for this year. I think previously at the full-year you said down slightly from full-year last year, but the exit rate for this year ought to be ahead of where we are at the first half of the year. Is that still the case? I appreciate the comments about being long liquidity at the moment ahead of the referendum. Then a second question on balances.

Dave Dyer: In terms of the NIM trajectory, at the moment we are holding to the view that we will be flat to the Q1 answer you have seen, 160bps. Obviously that is very dependent upon the evolution of mortgage volumes, and indeed the evolution of cards volumes. Until we understand the outcome of the referendum and how the market will play in H2 we are sticking with the 160bps view, which at the moment is our view on our current volume run rate, as Rohith pointed out, with an outcome on the referendum which is Remain and therefore not disturbing that market expectation.

Jayne-Anne Gadhia: I do think, just to try and repeat what I said in answer to Rohith's question: it seems to me wrong, to put it bluntly, as a challenger bank growing as we are, to constrain our growth because of a NIM expectation when we can drive returns. However, the additional point I should make, because I think you are reaching for it, is there is no deterioration in the quality of any of the components of our NIM make-up. Anything that you are seeing that has got downward pressure on it is to do with increased volume. I just want to be really clear on that, because we struggle with this a lot. There is a market expectation for us to hit a NIM of *X*. That would be daft if it would mean an ROE that is lower than we could otherwise achieve. I want to be really clear: we are prioritising ROE but that is not to the detriment of pricing and margin quality. It is just for the acceleration, if possible, of volume.

Guy Stebbings; Okay, great, thank you very much for that. Then, are you able to give any additional colour at all on experience so far this quarter on mortgage balances? Clearly you have said it has been the owner-occupier space rather than buy-to-let where you have concentrated. So, whereas at a sector level we might have had a degree of pull-forward in Q1 from Q2, would you say that is less likely to be the case yourself in terms of experience thus far?

Anth Mooney: Yes, as Jayne-Anne has described, the residential lending at Virgin Money is up 35% compared to 17% in the buy-to-let space. Based on comments from the CML, we think that up to £5bn of buy-to-let balances have been brought forward into quarter one to support the strong completions number that we saw in quarter one.

From a Virgin Money point of view, our focus throughout the quarter has been on residential. As we have entered April I would describe what we have seen in the buy-to-let market as a normalisation. We have seen the proportion of our new business level back down to 16–17%, which is broadly in line with 2015. Based on the feedback and intel that we see across the market, we would expect that to be broadly true at a market level. The only notable change that we have really seen is a shift from purchase business back into remortgage, and the splits that we are seeing in April remain broadly in line with the splits we saw in 2015. I think we have definitely seen a jump in lending during quarter one, particularly in March, but in April so far we have not seen the level of decline in buy-to-let lending that some had predicted.

Guy Stebbings: Okay, thanks a lot.

Jayne-Anne Gadhia: Thanks, Guy.

Chris Cant (Autonomous Research): Good morning, a couple from me please. I just wanted to follow up on this series of questions on margin. Obviously full-year guidance you are pointing to a 165bps target for 2017, and you are now guiding for a flat 160bps NIM throughout the course of this year. I am just interested in what you think it is that happens in 2017 to kick the margin higher? Do you at that point expect to be mix shifting even more aggressively towards cards to offset faster mortgage growth during the course of this year? If I can put it in a slighter different way as well: if the plan for this year played out throughout 2017, i.e. faster growth in mortgages; to your point Jayne-Anne, would you then abandon that 165bps target for 2017? That was the first question.

The second on buy-to-let. 18% of the book now; I cannot remember where it was a year ago. I think it may have been 16% in Q1 of last year from memory. You have expressed in the past the target of around 19% I think, so you are getting up towards that level. I am just interested in what you think the risk appetite there is going to be going forwards? Would you flex that again in order to protect your margins if necessary? Thanks.

Jayne-Anne Gadhia: Okay. Thank you, Chris. On NIM guidance, the other point to make of course is that, you will know much better than me, we have been very clear that in all of our expectations we are expecting a flat base rate environment. I just wanted to remind everybody of that in everything that we are saying. To your point: as you know, the sweet spot for us is as cards growth gets to a position within our overall balance sheet whereby the acceleration of the cards yield compensates for the lower asset spread on mortgages. It is that trajectory that gives us the growth from the 160bps to 165bps and, as things currently stand, we still see that the 2017 growth expectations that we have of both asset classes would get us to 165bps of NIM for 2017.

Now, all of that said, and I am not in any way meaning to temper that guidance, but where we are re-guiding if you like, although I have not thought about it like that until this very moment, is we will prioritise returns. We do not expect that to give us an issue at all on the 165bps, but to be really clear we will prioritise returns. I think that is what I should be doing as a CEO of a growth bank. However, we do still see that our plans definitely and confidently get us to 165bps of NIM in a flat base rate environment in 2017. I hope that helps. We tend not to abandon targets. I do not thing we have ever abandoned a target, so do not worry about that.

As far as buy-to-let is concerned: what I think we have said, Chris, is that we would not expect our books to be over-exposed to buy-to-let in comparison to the market. We think that we have been pretty consistent both in saying and doing that, and we would continue to expect that to be consistently where we end up. That is our risk appetite. There is nothing at the moment that implies that that is too high or too low, and Anth and his team have very diligently focussed on making sure, as I said, that we do not take too much buy-to-let given the focus on it over recent months. Indeed, you might remember last year that we did have a higher share of buy-to-let flow in the first half of last year than we did in the second half of last year, and it will be one of the reasons for some of your questions on comparative mortgage growth. We pulled back on that given the focus on it, and we have continued to do so. Managing risk and growth of all asset classes is something that we consistently do, and at the moment we are doing it pretty well.

Chris Cant: If I could just follow up, though? 25% of your flow in buy-to-let in the first quarter, obviously that is ahead of the previously guided 18–19%. I appreciate the comment that, by product, spreads are flat to a touch up. However, if you are mix shifting away from buy-to-let going forwards in order to not go through that sort of 18–19% of stock level, it feels like that, even absent further downwards pressure on broad product spreads, would lead to further asset margin pressure. If you combine that with the faster mix shift towards mortgages – obviously you have got the deposit repricing actions which you are hoping to take during the course of this year, which gives you some support to your NIM going forwards given the step down in 1Q. However, if you are going to be flat on 160bps by 4Q, which is I think what you have effectively just guided in response to a previous question, I am still not sure how much card growth – it would have to be pretty stellar card growth coming through in 2017 to get from a 160bps entry run rate to a 165bps average for 2017. It feels like quite a big ask, if that is what you are looking for.

Jayne-Anne Gadhia: Anth is keen to answer on the buy-to-let side I know, so over to you Anth. Then we should probably not go through too much more detail on the NIM. We are clear on our guidance and we will leave you to work that through in your models. However, I should say our models are equally clear that that is where we will be coming out. Anth, over to you on buy-to-let.

Anth Mooney: On buy-to-let, just to reiterate the point, we have seen around 24% of lending in the first quarter on buy-to-let. I think we will see something very similar at a market level when we get the Bank of England data through, because of that pull-forward of buy-to-let lending from quarter two into quarter one. In terms of our buy-to-let mix going forward, we are not changing our risk appetite. We are not intending to materially change the mix of our new business lending that we deliver on buy-to-let. As Jayne-Anne has described, we will manage that broadly in line with the market. I do not think there is a change in our intent or a change in our outlook in that regard. We just intend to manage buy-to-let prudently as part of our overall mix.

Jayne-Anne Gadhia: Do not forget, Chris, whilst I am talking about the acceleration of the mortgage business, quite clearly the relative acceleration of the cards business within its own asset class is always going to be much faster in the short term because of where we started from.

Chris Cant: Sure. Okay, thank you.

Jayne-Anne Gadhia: Yes. Thank you very much.

Nick Baker (Goldman Sachs): Good morning. Just two from me quickly, one on other income and one on deposits. On OOI it seems as if that has been relatively tougher going than on the volume side, and I am just curious as to your comments about it inflecting in the second half. What sort of actions are you looking at taking to really improve the OOI piece?

Then the second one on deposits. I take the point that you are looking at potential for incremental reprice exercises; would you also consider looking at your deposit mix, and thinking again at potentially SME or accelerating PCAs to an extent as well? I know you said they are up 20% in the quarter, but obviously that is off a small base. In terms of thinking about how to manage down costs of funds, is that something that you are considering in the near term? Thank you.

Jayne-Anne Gadhia: Thank you, Nick. On OOI, the truth of the matter is that the way in which the Virgin Money business has developed – we acquired Northern Rock, focussed very hard on mortgages and savings. Then we acquired an MBNA portfolio and we focussed very hard on cards – we are now turning our attention to all of the OOI lines. As I said earlier, we have been very successful in some, particular travel insurance and home insurance, and there is a lot of opportunity to go in others. The straightforward answer is much more management focus from now on OOI as the other big lines are starting to, if you like, motor more within the engine room of the business, if that is the right way of putting it. We will turn our senior management attention to the OOI lines. We have started to do that this year anyway, and we would expect therefore to see an uplift by the end of this year.

On deposits, I will ask Anth to answer the incremental reprice point. Just at your general point, of course we are always focusing on the weighted average cost of funds. We have driven that down very, very materially over the course of the last several years. We hope to carry on doing that. As far as the deposit mix is concerned, you are absolutely right: as we develop our SME and PCA businesses, on PCA obviously we would bring in that sort of funding position but we are thinking about our ability and capability to do that on the SME side too. It is not going to be a short-term material benefit to us, but building now will give us a medium-term benefit for sure.

Anth, did you want to answer on the incremental reprice?

Anth Mooney: I think on the incremental reprice, the process that we will go through is looking at our more recently acquired retail funding, so the funds that we have brought to the balance sheet during the last 12 months. If we look at our funding in 2015 and the price points at which that new money was acquired, and compare that to the open market pricing today for new money, then there is circa 10–20bps differential. We would need to believe that that current pricing for new money would sustain at the current level before we would pull that additional lever. However, it is certainly something that we are looking at very closely and we will continue to focus on during quarter two.

Nick Baker: Okay. Just one follow-up on that 10–20bps: that presumably is incremental to all of the dialogue we have had about NIM earlier this morning?

Anth Mooney: We do not have any further changes baked into our existing plans.

Dave Dyer: To be clear, we are not talking about the entire book. We are talking about a portion.

Anth Mooney: It is on a segment of our back-book.

Nick Baker: Okay, thank you.

Jayne-Anne Gadhia: Thanks very much, Nick.

Ivan Jevremovic (UBS): Good morning, thank you for your time. I was hoping to ask a couple of questions on pricing. One on the asset side; whether you are still seeing the difference between buy-to-let and residential at around 100bps as you previously said?

On the funding side: I was wondering with the RMBS, beyond the simple benefit as it were of diversification, what the relative attractiveness is of RMBS funding versus deposit funding whilst you work through the currency swaps and so on? Thank you.

Jayne-Anne Gadhia: Anth, do you want to start on the pricing front? Dave, perhaps you can take RMBS? Thanks.

Anth Mooney: The price and differential between buy-to-let and standard resi has narrowed slightly over the past six months, but that is not because we have seen a material change in the margin available on buy-to-let lending. It is more to do with the fact that residential spreads have strengthened slightly. It is still within that 85–100bps ballpark, but we have not seen any material deterioration in buy-to-let spreads. However, we have seen a strengthening in resi application spreads of around 20bps.

Dave Dyer: On RMBS: broadly, if I look at term money from RMBS – and the last two issuances we have done have been up to three years – and compare that to retail, I am safely inside the retail marginal price of acquisition. It is not just a diversification point; it is also an efficiency point to have RMBS in the funding stack at current pricing.

Jayne-Anne Gadhia: To build on that, Ivan, the reason that some of you, in the same way as I did really, may think, 'Why did we do two RMBS issuances in four months? and the second one was entirely EU referendum-driven', it was actually in the plan for later in the year. We brought it forward simply to be certain of the funding pre-referendum, to be honest. It was more of a risk management point than an absolute funding point, but we were still able to achieve it with economic certainty.

Ivan Jevremovic: Thank you. If I could quickly just follow up on that final point; as you said, you are also then going long liquidity into the referendum. Assuming we get through that without too much disruption, would you expect to be able to optimise the balance sheet a bit in the second half then, and what the NIM benefit from that might be from that? Thank you.

Dave Dyer: Certainly, if everything goes as we expect it to and there is no interruption from a referendum result, the current long liquidity point would be burnt through by the mortgage pipeline by roughly August. We tighten the liquidity relatively quickly after June. That expectation is built into our plans, so that would not give us an incremental benefit versus the guidance we have given so far.

Ivan Jevremovic: Thank you, that is really clear and it is helpful to understand that saving. Thanks again.

Jayne-Anne Gadhia: Thank you, Ivan.

David Wong (Credit Suisse): Good morning, just two hopefully short questions from me. The first one is: could you tell us how many customers you now have? You referenced above three million, but I wondered if you could just be a bit more precise on that number. That is the first one.

On the second one: clearly you referenced the fact that you are stepping up mortgage lending. I am just wondering how we ought to think about, in particular, your leverage ratio; how has that moved in the quarter? How is the acceleration of mortgage lending affecting your thinking about the kind of leverage ratios you intend to maintain over the short to medium term? Thank you.

Jayne-Anne Gadhia: Thank you, David. The answer on customers is about 3.25 million. On the leverage ratio obviously it is a binding constraint on us, and in planning our mortgage volumes we would not be at this point considering going below our risk appetite of 3.75% leverage. We are not close to that yet, but we certainly feel that we can trend in that direction given the regulatory environment at the moment. Some people might say that we are actually still quite prudent at the 3.75% level and, as you know, we like to be prudent in all of our ratios. That is how we are thinking about it at the moment.

David Wong: Many thanks.

Jayne-Anne Gadhia: Thank you.

Michael Helsby (Bank of America Merrill Lynch): Yes, morning all. It is just building on that last point actually, Jayne-Anne, because you have been very, very clear on your mortgage appetite and how that might build even more. However, there are two ways to build your ROE, and I think one way your shareholders will thank you for and that is by improving the operating leverage. The other way is by introducing more financial leverage into the model, and that is not something that shareholders will necessarily pay for. Do you see your skew and appetite to grow mortgages to boost the ROE coming more from operational leverage, because you think you have got more cost control in the franchise and you are not gearing up the balance sheet? Thank you.

Jayne-Anne Gadhia: Yeah, entirely that, Mike. For us, as I say, the only way that I have thought about it, not from any financial engineering point, is: how much capacity have we got in ops, assuming we have got the funding to support it and the capital to support it? Therefore, we are writing mortgages properly at the margin as opposed to, as you say, extending either the balance sheet or our fixed cost base to do it. The mortgage growth is mortgage growth at the margin that produces marginal returns in the mid-teens.

Michael Helsby: Okay, thank you.

Jayne-Anne Gadhia: Thank you. Thanks, Mike.

Ian Gordon (Investec): Yes, morning, just two quick ones from me please. Firstly, thank you for your comments on the outlook for other income, which are encouraging. Just to confirm though: I assume that, given the NII strength in Q1, other income as a proportion of total income would have been down in percentage terms in Q1; can you confirm or correct that please?

Then secondly, just on costs: can you just remind me of any guidance relating to the FSCS charge you are anticipating in Q2? Thanks.

Jayne-Anne Gadhia: Right. So you are correct in your assumptions on OOI; because of the strength of NII, it is a lower percentage than otherwise it would have been. It has not grown in the same way, is probably the best way of putting it.

Dave Dyer: It is marginal. It is marginal.

Jayne-Anne Gadhia: Okay. You answer the second one, Dave, as well then, yes? Which is any guidance we have given on FSCS.

Dave Dyer: We have not given guidance on FSCS. I think it is safe to say that our current expectation is an improvement on last year. We think it will be single-digits.

Jayne-Anne Gadhia: Ian, I am sorry if this is unhelpful. I do not intend it to be. As you know, in our re-guidance at the end of the year we said that we would achieve our 50% cost:income ratio now including FSCS, and we continue to see that path clearly including FSCS. I do not think we have guided specifically to this year, but in terms of your view on the total cost position for the business you should be including FSCS in your 50% cost:income position.

Ian Gordon: Thank you, but if it comes out in single-digits that is a major positive towards delivery of that objective.

Dave Dyer: It is helpful, of course.

Ian Gordon: Yes. That is great, thank you.

Jayne-Anne Gadhia: Thanks, Ian.

Gary Greenwood (Shore Capital): Hi, just a question on buy-to-let. Obviously, where you have been cautious relative to the market growth. If I look across the specialist buy-to-let lenders, they are growing at reasonable rates and generating fairly strong front-book returns, or at least they claim, on their buy-to-let business. I am just trying to understand your relative caution on that market. Is it because the areas that you are operating in, which is more towards the amateur end of the market, is more competitive and the pricing is less attractive than the more professional end? Or is it just general concerns around regulatory risk? If you could give us a bit more colour on that, that would be really helpful.

Jayne-Anne Gadhia: It sounds like you have been reading the *FT* this morning, Gary!

Gary Greenwood: I have not had a chance yet.

Jayne-Anne Gadhia: The truth of the matter is that I have always felt that, of course, the specialist lenders generate special returns because they have taken much more risk than we are prepared to take. To be really, really clear, I have said it right from the beginning of listing, and much before that when we took Northern Rock: I want to be able to sleep at night. We all agree with that. We want to build the best quality mortgage book in the UK and we want to be confident about asset quality, particularly at a point where we are in such a benign interest rate environment at the moment that as we look forward through the cycle we want to be equally confident in these sort of updates for the future.

Asset quality, to be clear, is a very, very significant and primary driver for our business, our performance and my mental health. As a consequence, we have never wanted to get into any risky asset classes. We have never wanted to be over-exposed in the market to anything that is ahead of market norms, as it were. As soon as the buy-to-let question started to be raised at the macro level we wanted to make sure that we are very clear on what a sensible and risk-managed, as opposed to risk-averse, approach is in the buy-to-let market.

At the moment, we continue to think that that is to do with amateur landlords. We do think that there will be firms that are advising normal people, as it were, how to put together portfolios corporately in order to manage tax positions. I think that is an accident waiting to happen. We would much prefer to support individual people that want one additional house rather than people that are trying to put together a portfolio and get burned in the future. It is a case of being cautious, being sensible, trying to read the runes and not being exposed in any way to unacceptable risk, whether that is market risk, product risk or person risk, as it were.

Gary Greenwood: Presumably from what you are saying, you do not think the pricing in the buy-to-let market appropriately reflects those risks?

Jayne-Anne Gadhia: From our perspective the risk-adjusted return on capital that supports the buy-to-let portfolio is still significant. My point is not that the returns on buy-to-let are not attractive, because they are. My point absolutely is that you can get carried away in the short-term by that attraction, and we want to get that in the right place, if you see what I mean.

Dave has just passed me a note rightly which is to say – and of course, you touched on it earlier – we do think that there are some regulatory risks that are a 'known unknown' on the buy-to-let world at the moment. So I would not be sleeping at night if I had 90% exposure to buy-to-let, and if most of that was in a non-amateur sort of play. I think there is a lot of risk in that.

Gary Greenwood: Okay.

Jayne-Anne Gadhia: To sum up, you should definitely think of us as very much trying to balance risk and return. We will be delighted with mid-teens returns on such a low-risk business, and that is something that will give me a lot of pleasure, frankly.

Gary Greenwood: Okay, thank you very much.

Jayne-Anne Gadhia: Thank you, Gary. Thank you all very much indeed for your time. I look forward to catching up with you all again soon.

[END OF TRANSCRIPT]