Metro Bank H1 Results 2019

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Vernon Hill (Chairman), Craig Donaldson (CEO) and David Arden (CFO)

Presentation

Vernon Hill

Sorry I'm a few minutes late. We have people with us today in London, we have people on the phone and we have people online. Is that correct? Well, welcome to the half one 2019 presentation of Metro Bank. Next week is the ninth anniversary of the creation of Britain's first new retail bank in 100 plus years. The creation of a revolution in UK banking, providing consumers and businesses with a real, differentiated, value-added choice. Yes, in the first half of 2019, we had some bumps, a few things went wrong. Not abnormal when you build a major business from scratch. Yet, none of these problems affected the world-class customer service we deliver every day. Our team rose to these challenges and I have complete faith in Metro Bank, its model and its team. As we progress through 2019 and on, we will continue to strengthen our foundation and, daily, continue to improve the Metro Bank experience. Our thanks to our customers, our shareholders and our friends. I'll now turn it over to our Chief Executive Officer, Craig Donaldson, and David Arden, our Chief Financial Officer. Thank you all.

Craig Donaldson

Thank you, Vernon. Thank you everybody who is here today, thank you for those in the room who've travelled in the heat. I'm sure the Tube was not pleasant, so thank you. Thank you for being here in the evening. We decided three times ago to move to the evening to allow us to speak to our colleagues, our customers and our shareholders on both sides of the Atlantic in daylight hours. Therefore, that's why we continue to do this announcement at 4:45 to 5:00, and then presentations at 5:30. We will continue to do that.

As Vernon said, we have had a challenging first six months, a number of challenges which we faced into and are addressing. The RWA adjustment was the start, we've implemented a detailed plan that we're following through on now. Following the RWA adjustment, we saw a period of intense speculation that spread through February, through May. During that time we did see outflows of deposits, in fact, we saw about £2 billion of outflows in deposits. What we've seen though, over the last seven weeks, from the beginning of June, is a return to growth in Metro Bank. Our deposits have grown over £700 million in the last seven weeks, showing the return to form which you would expect from Metro Bank. As you would expect, when we saw the outflows, we took actions to manage the balance sheet and some of those actions did impact on the profitability in the first half of the year. The profitability, when you look year-on-year, was more heavily impacted by the adoption of IFRS 16 and by the Tier 2 debt costs. David will talk to us more about that in a few minutes. The actions we took to manage the balance sheet have positioned us with an extremely strong balance sheet as we enter half two.

By raising £375 million of equity, for which we were oversubscribed almost threefold, and by the sale of the non-strategic loan portfolio, we now have a CET1 ratio of 16.1%, up from the 13.1% at the start of the year. We have a higher liquidity coverage ratio, we're now up to 163 up from 139 at the end of 2018. As well as having a very strong capital base from which to grow, and being highly liquid, sitting on significant amounts of cash from which we will grow, we continue to have a strong and robust asset quality on the back book, with our cost of risk down at half one 2018 of 8bps to 6bps at the end of the half one 2019. We have had challenges, we are addressing them and the actions we've taken deliver us into the second half of the year with a very strong balance sheet from which to grow. We continue to invest and spend time on the platform from which we will deliver the profitable growth.

We've announced today some changes to our board. Vernon has decided to start the process to appoint an independent Chair. We've appointed a new independent NED, Michael Torpey, who we're very much looking forward to joining us in September. I've also announced, earlier this week, that we are strengthening the management team with the appointment of Cheryl and Dan, who will join us as Chief Information Officer and Chief Transformation Officer, making sure that we deliver on the commitments that we made in February around our strategic initiatives. As well as governance and leadership, we've also continued to invest in the momentum. The momentum and the resilience of the momentum have really come through. We've grown by almost 200,000 accounts in the first half of the year to over 1.8 million customer accounts. We also have grown our current accounts by 21% year-on-year. For me, something I'm really proud of is we won 18% of business switches in London and the South-East in the first half, up from 15% previously.

I can't not mention, although it's not in here, around the momentum in the core franchise. We are number one for personal service in CMA surveys and number two for business, delivering on the promises we made when we set the bank up nine years ago. As well as dealing with the challenges, focussing on making sure the momentum is there, we've also, as a management team, been extremely focussed on our strategic initiatives. There is no doubt that we have gathered real traction with our bank-wide efficiency programme. We'll be announcing today, earlier today, sorry, that our cost efficiency programme is on track and, in fact, will deliver at the upper end of the range this year on the cost savings and we will increase the upper end of the ranges in outer years, and we will achieve that at lower cost to achieve.

Fee income, up 61% year-on-year, a very strong performance, achieved because we delivered what we said we would do and it worked the way we said it would. This will be accelerated further with the money that we'll be using from the C&I to build out the digital services that really will differentiate us as we go forward to win more SME customers and offer them more services to make their lives easier.

Finally, we're on with the rebalancing and we will continue with the rebalancing as we move away from commercial real estate, do more small business lending and do more consumer unsecured lending. It is a year of transition. It has been a challenging half one, but we are addressing those challenges and we enter half two with momentum in the business and a strong platform for growth. David, may I hand over to you?

David Arden

Thank you, Craig. Good afternoon, everybody. As you know, we experienced a modest deposit reduction in the first quarter, after our January update to the market. Headline deposits were further impacted by intense speculation ahead of our equity raise in May. Net outflows in the half were £2 billion and in Q2, £1.4 billion. The adverse sentiment we saw primarily impacted commercial customers and a meaningful proportion of the deposit outflow came from a limited number of larger commercial accounts. As Craig said, June has returned to growth, £400 million in June. July, to date, has been over £300 million so far of inflows. As we stand here today, deposits are back above £14 billion. We're really pleased with the resilience shown in key parts of the customer base. As you can see, retail continued to grow, up £400 million in the half. Retail partnerships were broadly stable and, for the first time, we've broken out SMEs, which we see, obviously, as a key customer segment. They also proved to be very resilient, showing the underlying strength of the customer proposition.

Costs of deposits were 71bps in the quarter. We've taken pricing action to drive deposits and support the brand. As that flows through into the second half, we should expect costs of deposits to be around base rate in the second half. We've continued to see strong growth in total accounts, to 1.8 million. Personal current accounts, business current accounts have continued to grow. Our total current account deposits are now £4.3 billion, which is 31% of the total customer base. We're winning significant share of BCAs. Our share of switches in London and the South-East, i.e. the core market in which we operate, is now 18%, up from 15% six months ago. We think that's an incredible statistic.

Our balance sheet remains strong and we've taken action in Q2 to maintain that resilience. Firstly, clearly, we completed our equity raise. We've elevated LCR to 163%, principally through the sale of £1.5 billion non-LCR treasury assets. We've also, today executed a £500 million portfolio sale. It's a non-strategic asset which we sold back to the same counterparty we bought it from at the same price. We've managed our lending volumes by scaling back high RWA lending and increasing mortgage pricing. We've continued to focus on low-cost business. Our cost of risk is now 6bps down from 8bps. We've driven deposit gathering initiatives by offering competitive fixed rates which drive deposits and also support the brand as we move into new markets. We do recognise that the loan to deposit ratio is elevated at 109%. Given the momentum we've seen in July, as we stand here today LTD is 107%. As we head towards the full year, you should expect it to be around 100% and, thereafter, we'll bring it back to in our stated guidance in a controlled way over the medium term.

Following our equity raise, we are now one of the most well-capitalised banks in the UK with a pro-forma CET1 ratio of 16.1%, which provides substantial headroom for controlled growth over the medium term.

The balance sheet remains highly liquid, with an LCR of 163%, up 22 points year-on-year. To achieve this, we've divested of treasury assets. As we said at Q1, we've also utilised some repo. Looking ahead, we anticipate issuing MREL debt in the second half in order to meet our MREL requirement by 1st January 2020. To do so, you should expect for us to issue a credit rating to support that issuance in the second half.

You've seen this slide many times, but it's worth reiterating that our lending book remains high quality. Cost of risk is 6bps, NPL ratio is 17bps and, just to reiterate, we will not go up the credit curve to drive NIM. We do not think it would be a prudent thing to do given the current macro environment.

Given the challenges in H1, we have prioritised balance sheet resilience over profitability. That said, income has been resilient with solid growth. We're particularly pleased with fee income, growing 61% year-on-year. We've talked about this last year and it has come through and it will continue to come through. Operating expenses have continued to grow as we invest in the business. As Craig said, in line with our strategy, our cost transformation is a key focus for management and Craig will talk about this in more detail later. Underlying profit before tax is down overall, principally due, on a year-on-year basis, to IFRS 16, Tier 2 debt costs and the ongoing challenges in the mortgage market. These had a direct impact on NIM, which is down to 1.62% at the half. However, strong fee growth served as a counterbalance to NIM pressure. Below the line adjustments reflect restructuring, transformation and remediation costs. The balance sheet actions that we've taken in H1 aligned with the issuance of MREL in the second half, we do expect to impact on H2 profitability.

Before I hand back to Craig, I wanted to highlight the expected trajectory on some of our key metrics. We don't normally provide near term guidance, but we do think it appropriate on this occasion. Given current momentum across June and July, we expect deposits, at year-end, to be broadly in line with December '18. There will be headwinds on NIM, most noticeably from the anticipated MREL issuance, but that will be partially offset by continued fee growth. You should expect that operating cost growth will moderate in the second half and we anticipate low single digit growth in absolute terms half two on half one. In fact, the only cost growth that we're expecting in the second half is from new stores. Excluding new stores, you should expect BAU cost to be flat, half-on-half. Given the H1 challenges, we expect our cost to income ratio to be above the 90% guidance range. Finally, expect continued strong credit metrics. We see no signs of credit stress in the book.

In summary, we do recognise it has been an extremely challenging first half. We have, though, been addressing those challenges. We are, though, very pleased with the resilience of the business and the underlying momentum in the core franchise. We could see that demonstrably in some of the numbers. I'll now pass back to Craig who will talk about how we intend to take the business forward. Thank you.

Craig Donaldson

Thank you, David. Absolutely spot on. David talked about the challenges and now we're going to talk a little bit about the strategic initiatives that we announced in February. We announced that we would be balancing controlled growth with profitability and capital efficiency, but that we wouldn't compromise on the integrated customer experience. There's been significant management focus on delivering that during the first half of the year. As we said, we have a significant focus on our cost-efficiency and we will deliver the top end of the range in 2019. We're already well on with the restructuring and the cost takeout of this year and that will continue. Dan Frumkin, who will join us on 2nd September as our Chief Transformation Officer, a significant part of his role will be on ensuring that we keep the focus and the delivery on this and make sure it comes through appropriately whilst delivering the service. We've also delivered on the fee income, as we said.

One thing that we haven't talked about, but was in the prospectus for our May capital raise, is we have concluded a significant T24 upgrade. T24 is our core banking platform and a few weeks ago we upgraded the system. This is one where I couldn't be happier that nobody knew about it, it's a real positive when you do an upgrade and nobody talks about it. Delivering that means that the things that we've been working on, that have been caught in the change freeze of that upgrade, will now be delivered in Q3 and Q4. You will see a renewed delivery around our digital offering and the service and fee offerings that we have for our customer base. That's also supported by the C&I. C&I, as you will remember and David mentioned, we won the top award, £120 million, that we're using to actually create competition in the SME market. Some very exciting things that we're working on, the programme mobilised fourteen weeks ago and we are on track for the deliveries of this year, including significant digital investment and also we are starting the work in Manchester and Liverpool stores, which will open later this year.

Looking at rebalancing the lending mix, well, we've seen movement there. We've seen a reduction in our commercial lending and that will continue. We've started the build-out of our unsecured SME lending platform and also our 'Mcard' platform. Exciting things that will come into play in 2020.

It is about growth and, as David said, we've finished half one with momentum in deposits, with momentum in current accounts and with momentum in our brand. We're going to take that as we go into the second half of this year. We're going to open four stores in Birmingham, our first store will open on 9th August opposite the Bullring in Birmingham. Please come along, it will be a good day. We will also open, as I said, in Manchester and Liverpool towards the end of this year, fulfilling the commitments we made to the C&I this year and we've already got Sheffield, which is well underway. By entering these new markets, new regions, these aren't just stores we're opening as we move into Birmingham and the Midlands and as we use the C&I money to move into the north earlier than we would have. This is opening significant new market opportunities. At the moment we currently cover 30% of the SME market, and by entering the Birmingham and the M62 corridor, we open that, we expand that into 66% of the SME market. Expansion into new markets plus expansion of our service offerings using our digital offering wins us the customers, wins us the deposits and drives our profitability and that's what we're doing. That's how we're taking this forward.

Now, to support the expansion we'll continue to work on the shoe leather, we'll be out in Birmingham. We're already out in Birmingham talking to customers, talking to SMEs. We'll increase our brand promotional work because it's new regions we're entering, not just new store locations, and we'll also, as we go into next year, take the learning that we have from the 67 stores to date to look at how we adapt the store format to fit with the communities that we'll be serving.

That's how we go through the growth, on delivering of the run rates, as I said, we'll deliver savings against the top end of the range that we announced in February, so we'll be up towards the £19 million. We've already delivered 60% of that to date with the actions we've already taken and some of those actions can be seen in the P&L. We've just set out here, I'm not going to go through them, some of the things we've already delivered or are delivering and these will all be done this year.

We're also upgrading our expected ranges as we look out, increasing to £80 million the expected run rate reductions in 2022 and to achieve that, we're actually lowering the amount we'll have to spend. We said in February it will take about £150 million to deliver the savings on the run rate, we now believe it'll be more like £125 million. We are very, very focussed on delivering this and, as I said, bringing Dan in will help us to continue to keep that focus and to make sure that we deliver on these savings.

Forgive our subtlety on this slide, in case you hadn't picked up on the 61% increase year-on-year in our fees, you know us, there would be flashing red lights around there if we could make it happen. We have delivered on what we said we would do and we will continue to deliver growth in this area. We have a number of initiatives and it says here 'to drive fee growth' but actually what we're doing is we're broadening out our service offerings and by broadening out our service offerings we're delivering more benefits to our customer that they want to purchase. The SME market is a real, real opportunity for us in this space. We've delivered the things in half one and, as you can see, they have come through and delivered the benefits that we expected, and the second half of the year we will deliver the things that you can see here.

We'll be delivering some business debit card improvements, which will allow us to charge a higher interchange rate. We'll be launching our trade finance and FX enhancements that we spoke about last year. We'll be launching 'Mcash', I'm told that's not the trading name yet but I keep trying to force it through, and we'll continue to work on addressing fee leakage and there will be some price changes in part where we believe the market can carry it because we are a business. Looking out to 2020, there are some very exciting things that we're working on and in the first half of 2020 I would expect us to launch the ability for us to open business current accounts online using the current account initiatives we launched last year working with our fintech partners. Really exciting opportunities as we move forward on our digital propositions.

This slide is to bring to life what we are doing using the C&I money. We're investing in real digital innovation, working with a number of specialist fintech companies and it's all focussed on launching services that we believe will make an SME's life easier. By making a small and medium enterprise's business life easier, we drive productivity for them, and that's why they're willing to pay us. What we've set out here is, across the life of a business, the services we will be launching to make their lives easier with our support. These digital innovations that we will be launching on this page, remember they're built on the foundation that you see on the bottom of this page. That foundation has us number two for service in the UK and that's before we launched these digital innovations that will help us to really drive the business forward and deliver on the commitments that we've made to the C&I.

Finally, rebalancing our lending mix. As you can see, we've had a 2% reduction in our business and commercial lending in the first half of the year. That will continue and I expect, over the course of the years, you will see a significant reduction, that 29% will reduce to below the 20-25% that is shown on this slide. What will happen is, though, the rest of that will be filled up by the delivery of the new platforms that we'll be delivering, starting in the next year. We are already on track building out our new small business loan platform and that will launch, hopefully, in the first half of next year. We're also developing our SME enhanced overdraft and we're working on our new 'Mcard' offering for SMEs. A number of things, that even though we're taking the commercial and business lending down, will really drive that forward and be at an attractive yield, driving our return on equity to a different place. Also, as we see, the risk in the right place and the right risk reward of consumer finance and consumer lending, we'll also do more of that and we are still on train to deliver that as we move forward over the medium-term. So, we've started the move in the lending mix and we've started to build on the platforms to really drive that forward through next year.

So, our model remains strong, Metro Bank is delivering the model. The deposit flows have returned. We've talked about the challenge, you know, two words you've probably picked up a lot in this presentation 'challenge' and the 'transition' but that's where we are. We're facing and addressing the challenges and we're driving through the transition, and in doing that, we've seen a return to growth in our deposits that David and I have both spoken about, with over £700 million back in the last seven weeks, £700 million of inflows in the last seven weeks. Rebalancing the asset base, that's on track and we continued to have an extremely, extremely strong asset quality, which will be really important as we go forward. We've upgraded our cost targets and we've reduced our cost to achieve them. We've delivered a 61% year-on-year increase in fees and that will continue. I don't want to say we'll be delivering 61% every year-on-year but you will see continued growth in our fee income as we launch more services for our customers and as we win more customers as we expand across the UK.

Our C&I delivery is on track, the commitments we made to win the £120 million are on track for delivery and there are some very, very exciting things that will come out of that over the next 24 months. Part of that is our expansion north. We are paying for the Birmingham sites and we're using the Williams and Glyn money, the C&I money, to move into Manchester and Liverpool earlier than we otherwise would have. Before that, we're delivering the continued growth, 23% year-on-year growth on personal current accounts. 19% year-on-year growth on customer current accounts, 18% of the switches in business in London and the South East coming to Metro Bank. The foundation is there, the model remains strong.

As you go through the second half of the year, that momentum will grow and we will build on the strong balance sheet that we have going into this half, and that's why we remain committed and we reaffirm our medium-term guidance. David gave you guidance on 2019 and how the challenges have impacted on 2019 but it does not change what we see happening as we head towards our medium-term guidance and we reaffirm that guidance. So, thank you, we've taken half-an-hour of your time. May I now open it up to questions, please?

Q&A

Aman Rakkar

Thanks, guys. It's Aman Rakkar from Barclays. Yes, just regarding the loan sales. Two questions really. First of all can you give us a sense of the kind of associated earnings impact, loss of earnings you'd expect to give up or, you know, whatever earnings impact from the £521 million sale. I guess the second question, I was keen to interrogate the logic behind the sale, you know, I think the maths suggest it's risk weighted at 35%, so it's not the kind of problematic loans that were the source of the RWA increase at the beginning of the year.

Vernon Hill

It has nothing to do with the problematic credit.

Craig Donaldson

David, do you want to start and then we'll...

Aman Rakkar

Alright, sorry. I'll correct the words there. It wasn't problematic loans. The source of loans that are now risk weighted at 100% that perhaps is...

David Arden

The portfolio we've sold is a non-strategic portfolio that we acquired two years ago. It was bought tactically to elevate our loan to deposit ratio at the time. We sold it to the same counterparty who we bought it from at the same price to tactically bring down our LTD. It has no impact on the core customer base that we have because we've not really cross-sold to them and to the customers that have been transferred there is no impact on them because the servicer remains the same. So, it's a tactical sale to drive the LTD and maintain our balance sheet metrics. In terms of the income give up, they are broadly in line with the mortgage pay rate that you would normally expect, so that's what you would expect to be lost through the sale.

Aman Rakkar

So, is it reasonable to expect that you're still in the market for loan sales then regarding the loans that are now weighted at 100%?

David Arden

We have consistently said that there are a number of portfolio options available to us. We will do that, or not, at the time that's right for Metro Bank, so they remain an option for us going forward.

Craig Donaldson

Thank you very much.

Benjamin Toms

Hi, afternoon. Ben Toms from RBC. The inflows of £700 million that you saw in the last eight weeks, can you just split those between retail, retail partnerships, SME and commercial, and whether the commercial are coming back that you'd lost in the previous months?

David Arden

It's a broad mixture really of new existing customers, some chunky deposits coming back but supported by the FTD rates that we've been going out there in a very competitive way. So, I wouldn't point to any one particular segment. It's a broad range of deposits that we're bringing back and it's very much back to BAU. I don't know if you want to add anything, Craig.

Craig Donaldson

That's fine. For me that's the positivity out of it, you can see it's that return of momentum that we would expect from Metro Bank, and it is that broad church where we're seeing it, with continued resilience and growth in the retail, the SME and some of the commercial customers coming back, and some new commercial customers that the guys have been working on for some time but just take a little bit of time to land.

Benjamin Toms

Thank you.

Craig Donaldson

Thanks, Ben.

David Arden

Should we go to John at the back?

John Cronin

It's John Cronin from Goodbody. Can you give us anymore guidance on the funding costs that's expected in H2 and I suppose related to that, are there other options here for you to resuscitate NIM? Look, you're still at £4.3 billion of current accounts, which could be higher as a proportion of the overall deposit base. You see Tesco Bank selling a mortgage book that's going to have excess funding. Are there other novel ways you can win current accounts or do you see your own organic growth trajectory as conducive to getting to where you want to be? Then secondly, on the various governance changes you've called out in recent days, I know you need to be very careful about what you say on this, but do you think you've gone at least most of the way at this juncture in terms of addressing the PRA and FCA's concerns in the context of their review, and what kind of repercussions do you think there could be, if any, from a Pillar 2A requirements perspective?

Craig Donaldson

Thank you, John. David?

David Arden

On cost deposits, John, as I said in the presentation, we would expect in the second half, cost deposits to increase to around base rate. We have taken some pricing action in this quarter that will wash through and then you'll see that playing through in Q3 and Q4. Great question on driving current accounts. It is a primary focus for us and we're focussed on primacy as opposed to just winning current accounts. That's the core thing that the store network and colleagues in stores really drive for and we see that coming through on a consistent basis. Novel things on the balance sheet? I just point to the response on further the portfolio sales, we may consider them. We have optionality and we'll retain that optionality going forward. Craig, do you want to pick up on the governance?

Craig Donaldson

Yes, you know, the governance changes have been a refreshing of the board. Vernon has obviously started the process to appoint or to find an independent chairperson but the bottom line is we've been refreshing the board. We said in February that we would continue refreshing the board. That will continue as part of business as usual, and I would expect us to talk about that as we go forward because it's the right thing to do. With regard to the PRA, I have no insight. There is nothing to say on that, John. I'm afraid there is nothing to say on that, so forgive me for my obtuseness. I would say on the current accounts, I'm genuinely excited about moving into the new markets. I do think that the momentum we have, especially in the business markets and moving into, you know, doubling our market coverage will be huge for us and very exciting in the second half of the year. So, entering Birmingham on 9th August and then moving into Manchester and Liverpool. With the services that we're building and some of the digital innovations that we've got coming, actually I think that's how we drive our current accounts and, you know, our deposit base at the moment is 31% of our deposits are current accounts and I think that's a strong position. Of course I'd love it to be more but we'll do that through winning customers and getting the right customers with the right fee income opportunities as well because that's also very, very important. Thank you, John.

Michael Perito

Hey, good afternoon guys. Thanks for taking my question.

David Arden

Hey Mike.

Michael Perito

Okay. I wanted to ask you just on near term, it's kind of a two-part question here. The deposit growth has obviously rebounded in a big way in June and July and, you know, when you think about that plus the loan sale, it would seem like there's quite a bit of liquidity that's being deployed. I was wondering if you can maybe just give us a little more colour about the plans around that. Then also secondly, if you look at the concentrated rate of deposit growth in those two months, it's obviously very high, it's higher than I think the longer to medium-term guidance you gave. I guess I was wondering, do you think that that is kind of just some catch up and some pent up demand from some of the volatility of the spring or do you think there's still, kind of, actions or further actions that need to be taken to make sure the growth rate is moderated to the 15% to 20% range that you guys had discussed previously?

David Arden

Shall I take the first part? So, from a liquidity perspective, Mike, you're right. We have got an elevated liquidity level today. Two reasons for that. One is the particular challenges that Metro Bank has experienced over the half and secondly the broader macroeconomic backdrop as we head into H2, given the uncertainty we face. I think, on both, we need to let that play out before we start to think about bringing liquidity levels down but I would hope that would be the case at the back end of this year. Craig?

Craig Donaldson

Yes. As for the continued momentum and the mix, I think there are some deposits coming back, Mike. I think that's certain but actually it's really strong momentum. What I'd like to do is let that momentum play through because I think that at the moment, you know, it was tough on some of our colleagues in the first half because people are so proud of what we do and genuinely our colleagues believe in what we do, and genuinely believe in what we do. The inflow of the deposits has really given everybody that pep that lift, and also the delivery of T24 and the huge success with so many people involved. Aisling and her team and in fact the teams across the whole bank did a superb job in delivering that and you can feel the lift in the organisation when that was delivered. I'd like that to continue because I think momentum is good, the growth is good as long as it's at the right price, to David's point.

So, we will take some pricing but we'll let the momentum continue, we'll continue to let our colleagues have the support and we'll continue to grow that and take the pricing actions at an appropriate time. I do think that we're growing well. It's great to see the last seven weeks and how we've just got back on the momentum and what's also, like you said, is great is how many of our customers who are joining us are new and how many customers who never left us, they took some of their deposits and are bringing it back. Thanks, Mike.

Michael Perito

Secondly, if I could on the TFS scheme. Can you just remind us the near term unwind of that and any potential impact it could have to your near term liquidity and margin position?

David Arden

Sure, Mike. It's a four-year funding scheme so the repayable is out to 2022. I think the bulk of it is 2021, so there's plenty of time to think about the repayment schedule. We have a number of options from deposit growth, MREL issuance that we will do, or indeed the higher levels of liquidity that we're running today, we've still got a substantial treasury portfolio. So there are a range of options for us and it's not something that we are unduly concerned about in the short-term because it's a four-year repayment programme.

Craig Donaldson

If you have a look we're still sitting on about £1 billion of investment that actually don't feature in our LCR number and so we have a very strong portfolio there we can draw on at the right time as well. Is that okay, Mike?

Michael Perito

Very helpful, thank you guys. Appreciate it.

Craig Donaldson

Thank you, Mike. Next question, please.

Joseph Dickerson

Hi guys. Thank you for taking my question. Sorry I couldn't be there in person, I couldn't get there fast enough. Just a couple of questions around the NIM. Have you estimated or can you share what you believe the drag either to interest income or net interest margin is from the higher liquidity levels, and secondly, what do you think after we get through company specific issues in the near-term and, say, over the next six to eight months, however long it's going to take, a bit more clarity on the macro situation? What's the optimal LCR that you would like to operate at? As I sit here today, there is quite a bit of onus on the net interest margin to get you to your 2023 ROE targets and so I'm kind of struggling to see how you get there without material base rate hikes or material pullback in liquidity, given the extension of the mix into mortgages. Then the second question I have is around the new stores that you're opening in the North. How are you staffing those? Are the staff coming locally or are they coming from existing stores? Just some colour. Is it consistent with how you've extended in the southern part of the country or are you doing anything differently there? Some colour would be useful and maybe we'll come up to Birmingham for a field trip.

Craig Donaldson

David, do you want to take the first question and then I'll cover the second one?

David Arden

So, you're right, Joe. The high liquidity levels have dragged on NIM. We have, as I said in the presentation, prioritised in the first half balance sheet resilience over profitability. It's at 163% at the moment. I plan to keep it at that level for the foreseeable future until we can demonstrably show, and we need to print Q3 numbers with positive deposit momentum but thereafter you should expect us to bring LCR back to within where we normally are, which is a 130%, 140% level and that will improve profitability in and of itself.

Craig Donaldson

I'd also suggest with the blend on the rebalancing of the lending that we've talked about. As we do more consumer finance and as we do more of the SME finance, unsecured, both on loans and on credit cards, and the overdraft facilities we'll be launching, that will drive up the yield which will drive up the NIM. So, you'll have a reduction in the liquidity levels as we return to normality but we will also see a mix of the business change as we go through 2020, which will drive up that NIM as well. On your second point, I think culture is so important to us. How do we maintain and build a culture as we move into the North West? Well, people in the North West, as you can tell from David, are very smiley people and they're up for good service and-,

David Arden

I hope that's a compliment.

Craig Donaldson

I know what we're doing is, by opening in Birmingham first, we're opening in Birmingham in August. We'll be opening towards the end of the year in Manchester and Liverpool. We will recruit our colleagues there a little bit earlier. We will engage them in supporting in the Midlands for an extended period of time. What we also have is a number of our colleagues who come from the north, North West and a number of them are going to take this opportunity to go home for their life stage, life decisions, and so we'll be moving a number of colleagues. I know we've already done that in Birmingham, so we'll be moving colleagues up there and recruiting new but making sure we give them support and the grounding to deliver the culture that delivers Metro Bank because we have to get that right and we're not going to compromise that. Is that okay, Joe?

Joseph Dickerson

Great, yes. Thanks.

Craig Donaldson

Thank you very much.

Robert Sage

Yes, thank you very much for taking the question. It really, sort of, goes back to some of the earlier questions with relation to the deposit growth outlook. I think you've been quite specific about where you expect the year end 2019 figure to be ending up but you were also saying that your medium-term objectives are unchanged, which I understand it is around a 20% growth in deposits. I was wondering how we should look upon, in particular, the year 2020 with respect to the definition of medium-term. Whether you think once we get beyond this year we're straight back into a 20% deposit growth or whether that would be too aggressive at this sort of stage? The second question is really just one of the words that David used in terms of this presentation, talking about a more controlled growth in loans. I was wondering whether you are signalling by this possibly a slightly lower ambition in terms of future lending growth than you've talked about in the past, or whether that's reading too much into it.

Craig Donaldson

David, do you want to answer that bit first?

David Arden

I think it is reading too much into it, Robert. Being naturally CFO cautious in terms of controlled lending growth, we need to demonstrably prove to the business and to the market that indeed our deposit growth is sustainable. I genuinely believe it is given the two months we've had and I believe that getting back to flat year-on-year is eminently achievable. Thereafter, because that implies in and of itself in the next six months a £2 billion deposit increase, which in all intents and purposes is back to normal run rates for this business, and thereafter I would expect 2020 to be back to normal run rates.

Vernon Hill

Robert, this is Vernon. Let me just say one thing. When you look at deposit growth, we've given you this new target of £4 million a store a month. That's a better way to look at store growth than this percentage rate.

Craig Donaldson

I would also say, and just to do the whole trio. I can't remember if it was John or Mike who asked earlier about moderating the savings growth we were seeing as we go through the rest of this year. There's no doubt we'll be above the 20% if we deliver what we said and I believe we will, as David and Vernon do, in our deposit growth in the second half. Therefore I think we should go into next year with strong momentum, and whether it's 20% or 23%, you know, I would hope and expect that we will be back on 20% or possibly better as we go into next year because of the momentum we'll exit this year with, and then we'll take the right actions to manage the deposit growth at the right price, and also the right liquidity cost to make sure that we're building, to John's point earlier, on the personal current accounts and the business current accounts that are the life blood of a transaction bank and that we continue to win very strongly. Thank you, Robert.

Robert Sage

Thank you.

Christopher Cant

Good evening, thank you for taking my question. Hello. Could I just ask on liquidity, please? You've shown a marked improvement in your LCR in 1H despite a sharp reduction in your cash and investment securities and I appreciate that you can shift the mix of the latter to exclude LCR ineligible assets but I think you only had £0.7 billion of assets which were not eligible as collateral at the BOE at the end of the full year '18. If I assume you've pledged liquid assets against your repo funding, which has obviously gone up quite a lot in the first half, and you had been doing as at full year '18, your unpledged liquid assets as a percentage of deposits has fallen from 39% at full year '18, or 34% if I exclude the BOE ineligible securities at full year '18, to 24% as of the first half. How do I square that with the change in the LCR? Is the repo funding you've got on the balance sheet from the central bank, which would use whole loan collateral and thereby support the LCR? That would be the first question, please. To what extent is this decision to sell loans driven by liquidity considerations?

David Arden

On the first question, Chris, we wouldn't comment ever on the counterparties for repo, suffice to say we have taken appropriate action to maintain a strong and resilient, highly liquid balance sheet, as you would expect prudent management to do given the challenges this bank faced in the first half. Your second question, Chris? Sorry, I've lost my train of thought.

Craig Donaldson

So, was it about liquidity?

David Arden

Oh, the book sale, as I've been very clear, the book sale was all around, we tactically bought it two years ago to expand our LTD. We have sold it to the same counterparty for the same price to reduce our LTD and it's as simple as that, Chris.

Craig Donaldson

If I may just to add, obviously David was very clear that we are looking to bring our loan to deposit ratio down from 109% at the half year, the 107% today, down towards circa 100% by the year end. As well as doing that, we want to be lending to new and existing customers. We want to build relationships and we are a bank that is looking for relationship lending, so we want to be doing our mortgage lending, we want to be lending through private banking, we want to be lending to our business customers and to our commercial customers, and we will continue to do that. In order to do that, we would rather sell, say, a strategic book and win deposits to allow us to do more of the relationship lending, which will be more profitable and more structurally sound for the organisation long-term than holding a non-strategic book. So, that plays into it as well to help us achieve 100%, whilst also helping us help our customers. Sorry, go ahead Chris.

Christopher Cant

If I could just push you a little bit on that. If your underlying liquidity position, and I appreciate you don't want to comment on where that repo funding has come from, but if the underlying liquidity position is as robust as your LCR suggests it is, why do you feel the need to bring down the loan to deposit ratio? I know you've said you want to bring it down over time but you also said on the 1Q call you wouldn't take any drastic actions to bring it down sharply, it would fall very gradually. So, what is it that's actually prompting you to bring down the loan to deposit ratio, which will obviously impinge upon your profitability, in theory, if your liquidity position is as robust as your LCR would suggest it is?

David Arden

Because, quite simply Chris, you know, the reality is we had some deposit outflows in this second quarter, more than we would have anticipated or hoped for, given the intense speculation that existed before our equity raise, and this was a non-strategic asset that allows us to realign our balance sheet metrics, and I think, for the long-term of the bank, it's the right thing to do.

Craig Donaldson

As I said before Chris, I would prefer us to be able to use, as we bring the loan to deposit ratio down and win more deposits from our customers, to be able to do more lending to make profit by building relationships across private banking, commercial banking and our retail customers. This was a non-strategic asset that frees up a £500 million on to the balance sheet that allows us to continue to support our customers and lend into the real economy. Thank you very much.

Christopher Cant

Given the composition of your deposit book and how it's behaved in the last two quarters, are you at all concerned about how it would behave in the event of a liquidity stress following a hard Brexit? If that happens.

Craig Donaldson

Well, the deposits that we experienced the outflows from, as we said today, was principally from a limited number of commercial customers. The reality is those deposits were of low liquidity value and we were holding high liquidity for them anyway. Going forward, would we allow those customers to come back? Of course. We're a broad church and if a customer wants to come and experience our great customer service, then we would never say no, for the right price.

Christopher Cant

Okay, thank you very much.

Jennifer Cooke

Thanks for taking my questions. First of all actually I just wanted to come back to Chris's point on liquidity. We've had two consecutive quarters of deposit outflows, I just wanted to understand a little bit more about what customer stability assumptions you're making around your deposits for liquidity coverage ratio purposes, particularly amongst those partnership deposits. Secondly, I appreciate the guidance on the H2 outlook but, quite simply, given the headwinds you're facing, do you expect to be profitable in H2? Thanks.

David Arden

So, the liquidity outflow scenarios we run are entirely consistent with the behaviour we see on the book. We have had some learning in the first half, one or two deposits behaved as we wouldn't expect and we've taken that learning and we will run it through our liquidity metrics, but in the main, Jennifer, our deposits have behaved exactly as our liquidity stress scenarios suggested they would. We have taken a bit of learning but in the main they behaved as exactly we would expect. Looking forward to the second half all I would say is that we have given very clear guidance on how we would expect our key metrics to behave in the second half and I'll leave you to draw those conclusions in your model.

Craig Donaldson

Jennifer, thank you very much for your question. It is 6:30pm, the heat awaits those in the room to go outside into. Can I just say thank you very much? I think that, to sum it up, we have had a half of challenge, but we are addressing that and we have momentum in the business as we move forward and we will build on that momentum with delivery and it's the delivery which is the key as we move forward and we will continue to do that. Thank you very much for your time, thank you to everybody on the call. Thank you.