Chief Executive's Statement

We have the right model to thrive in this environment and are confident in the opportunity it creates for us to lean in and support consumers and SME businesses

Adrian Sainsbury,
Chief Executive

We have performed well in the second half, with an acceleration of loan book growth, strong margins and a stable credit performance in our Banking business. We continued to attract new client assets in CBAM, with strong net inflows, although Winterflood's performance remains impacted by subdued trading activity. Despite the second half momentum, our financial results for the full year were significantly impacted by provisions in relation to Novitas announced in our Half Year 2023 results in March.

This year has been marked by a challenging market backdrop, where mixed economic conditions in the UK have created substantial uncertainty for our consumer and SME customers. Although demand levels have remained robust, the uncertain external environment led to higher forward-looking impairment provisions and difficult conditions for our market-facing businesses, CBAM and Winterflood.

Whilst headwinds facing SME firms have abated somewhat, uncertainty and challenges for these firms persist, with interest rates rises and cost of funds remaining a key concern for many business owners. We recently published the Close Brothers Asset Finance Business Sentiment Index, which provides insights about our core customers' plans for the future. The research shows that SME business confidence continues to recover, and we are reassured to see a reversal of 2022's downward trends, with a cautious optimism continuing to return. Overall, the appetite to invest remained stable, with three-quarters of the firms aiming to seek funding for investment in the next 12 months.

We are confident that we have the right model to thrive in this environment and are confident in the opportunity it creates for us to lean in and support consumers and SME businesses.

Our through-the-cycle business model and financial strength mean we can support customers even during these uncertain times. By leveraging our long-term relationships, the deep expertise of our people and our customer-centric approach we can deliver disciplined growth and are well positioned to resume our long-term track record of earnings growth and returns, building on the second half's momentum and a good start to the 2024 financial year.

Financial Performance

The financial results were impacted by a significant increase in provisions in relation to Novitas incurred in the first half, as we have taken measures to address the issues relating to that business. As a result, statutory operating profit before tax decreased to £112.0 million (2022: £232.8 million). While we are disappointed with these developments and the impact they have had on our performance this year, the financial strength of the group leaves us well placed to move forward on the delivery of our strategic priorities. We evaluate continuously our businesses and initiatives against a set of criteria, our "Model Fit Assessment Framework", to ensure they are aligned with the key attributes of our model that have and will continue to generate long-term value. We are confident that there is no read-across from Novitas to other books in our portfolio and our prudent underwriting continues to be reflected in the asset quality and performance of the rest of our loan book.

In Banking, excluding Novitas, profit performance primarily reflected good loan book growth of 6% and strong net interest margin of 7.6%, more than offset by higher impairment charges to take into account the uncertain macroeconomic outlook and increased costs related to our investment programmes and inflation, including wage awards. Our Asset Management division delivered strong net inflows of 9%, although profit reduced, reflecting wider market conditions and costs related to our successful hiring strategy, as we accelerated our efforts to grow CBAM. Although performance at Winterflood reflected the continuation of challenging trading conditions, we remain confident in the track record of our trading business and are well positioned to retain our market position and benefit when investor appetite returns. Winterflood has made good progress on the diversification of its revenue streams and is exploring growth opportunities to balance the cyclicality seen in the trading business.

Our capital, funding and liquidity positions remained strong. The events impacting the global banking sector earlier this year highlighted the benefits of our prudent approach to managing financial resources, with our diverse funding base enabling us to adapt our position, based on market conditions and demand. Our funding base was further strengthened by the successful issuance of a £250 million senior unsecured bond in June 2023, and we maintained our prudent liquidity position, with the 12-month average liquidity coverage ratio ("LCR") of 1,143% substantially above regulatory requirements. Our common equity tier 1 ("CET1") capital ratio was 13.3% at 31 July 2023 (31 July 2022: 14.6%), significantly above the applicable minimum regulatory requirement of 9.5%. We remain committed to optimising further our capital structure, targeting a CET1 capital ratio range of 12% to 13% over the medium term. This will allow the group to maintain a buffer to minimum regulatory requirements while also retaining flexibility to grow the business. We remain encouraged by the available opportunities to deploy capital to deliver disciplined growth, which remains a key strategic priority. We will continue to assess the potential for further distributions to shareholders based on future opportunities.

We are pleased to propose a final dividend of 45.0p per share, resulting in a full-year dividend per share of 67.5p (2022: 66.0p). This reflects our underlying performance and the Board's confidence in the group's outlook. We remain committed to our dividend policy, which aims to provide sustainable dividend growth year-on-year, while maintaining a prudent level of dividend cover.

Well Placed to Resume Our Track Record of Earnings Growth and Returns

We have made good progress against our strategic priorities and remain committed to resuming our track record of earnings growth and returns.

Our investment programmes are progressing well and enable us to protect the key attributes of our business model, maintain regulatory compliance and enhance efficiency, as well as future-proof our income generation capabilities. We continue to see tangible benefits from these investments. We advanced our strategic cost management initiatives, including our technology transformation programme focused on the rationalisation of IT infrastructure, as well as making operational enhancements in Retail. These actions aim to create capacity to accommodate growth, inflation and investment to support our business. We continue to evaluate additional opportunities for efficiency with a view to achieving positive operating leverage over the medium term. Furthermore, we undertook work across our businesses to ensure readiness for the implementation of the FCA's Consumer Duty, which came into force on 31 July, completing product reviews and enhancing frameworks to incorporate the new requirements.

We remain focused on delivering disciplined growth and continue to review a range of opportunities in line with our model, with our growth initiatives delivering a significant contribution to loan book growth in the year. Our recently hired agricultural equipment and materials handling teams in Asset Finance have written healthy levels of new business and are building strong pipelines. In Invoice Finance, we participated in our first syndication deal and the newly hired team, providing bespoke term loan structures to SME clients, closed their first deal this year. We saw good demand for the new offerings in Property Finance, including our specialist buy-to-let proposition to existing bridging finance customers. We are delighted to have recently announced our agreement to acquire Bluestone Motor Finance (Ireland) DAC, which is aligned to our commitment to Ireland as a strategic market and provides a platform for us to build our Irish Motor Finance business. Following last year's announcement of our initial green growth ambition of providing funding for £1.0 billion of battery electric vehicles by 2027, we are pleased to have funded £164 million in the first year.

In CBAM, our hiring strategy is proving successful, with a strong pipeline of new hires and significant contribution from new portfolio managers to the inflows. We also continue to build our pipeline of in-fill acquisitions to support the long-term growth potential of the business. In addition, WBS exceeded the targeted £10 billion of total AuA and is well positioned for further growth, both organically and supported by a solid pipeline of clients. We expect WBS to grow AuA to over £20 billion by 2026.

We continued to make progress against the group's sustainability agenda. We set our group-wide climate commitment, becoming signatories to the Net Zero Banking Alliance and Net Zero Asset Managers initiatives in September 2022, and I look forward to sharing our initial intermediate 2030 targets for the most carbon-intensive sectors in our loan book over the coming months. We remain focused on improving the quality of our emissions reporting, including our financed emissions.

Our People

We consistently focus on employee engagement to support the wellbeing and needs of our colleagues. I am delighted with the positive scores achieved in our most recent employee opinion survey, reflecting our teams' strong sense of belonging and our distinctive culture. I am particularly impressed that we have retained our high engagement score of 86%. Our colleagues play a key role in driving our organisation towards lasting success, and I would like to extend my gratitude to all our people for their dedication and resilience, especially in the face of the financial pressures brought about by higher inflation and the cost of living. Together, I am confident that we will continue to deliver on our purpose to help the people and businesses of Britain thrive over the long term.

Outlook

We are making the most of opportunities and are encouraged by the momentum generated in Banking in the second half. We have seen a good start to the 2024 financial year and our underlying business is well positioned to maintain stable returns this year, as we sustain growth momentum and pricing discipline, with a resilient credit performance, despite the near-term cost pressure.

Our proven model and financial strength leave us well placed to resume our track record of earnings growth and returns by focusing on disciplined growth, cost efficiency and capital optimisation.

Adrian Sainsbury
Chief Executive

26 September 2023