Barclays PLC Q2 2020 Results

29 July 2020

Results call Q&A transcript (amended in places to improve accuracy and readability)

Joseph Dickerson, Jefferies

The first question is do you expect any benefit on capital in the second half from the recent changes around the treatment of software intangibles?

And then secondly, from a top-down standpoint, everything that you're saying suggests that you have reached an inflection point on margins. It sounds like volumes at the system level are picking up [based on] what we saw from both the BoE data today and your own commentary, and provisions [are expected to come] down in the second half. It seems like there's a fair amount of earnings momentum available to you in the second half, would you agree with that?

Tushar Morzaria, Group Finance Director

Let me take both of those questions, and Jes may want to touch on the operating environment in the second half as well. In terms of tailwinds to our capital, with regards to potential rule changes around software intangibles, to the extent they go through, it's in the order of around 20 basis points for us. Let's see if it goes through. If it does, that's what it is, but we'll see how that evolves.

In terms of the operating environment into the second half of the year, in many respects you are right in the sense that we should see some mechanical benefits coming through in the second half of the year, particularly in our consumer businesses. For example, if you take net interest income, for both BUK and indeed CC&P, there'll be the mechanical effect of lower deposit rates coming through in the third and fourth quarter in the UK. Obviously under UK rules we're not able to pass on lower base rates for a period of time, so our deposits reprice in July onwards, and you get no effect in the second quarter but a full effect in Q3 and Q4.

In CC&P, for example, we have dropped our deposit rates in the US from about 1.5% to 1%, but that reduction was very much towards the back end of the second quarter, so you'll see the full effect of that come through in Q3 and Q4. In addition to that, we've noticed some peers have lowered deposit pricing yet again. We'll take a look at that and there's a reasonable chance we may follow suit, given how strong our funding position is.

I think the other thing on the consumer businesses that's worth bearing in mind is obviously the decline in income that you saw in the second quarter. That quarter was characterised by both the UK and the US being principally in lockdown for the entirety of that quarter, and therefore you've seen continuing decline in spending and balances.

As we exited the second quarter, those lockdowns were being reduced and therefore we've seen spending pick up. In fact in the UK, spend levels are down only single-digit percentage points from pre-lockdown levels, and we've seen material pick-up […] in the US as well. Another data point to tell you how quickly spending seems to be recovering: if you look at SMEs that we have in our acquiring business, less than half were actually open during the lockdown. More than 90% are now operating, so this stuff transmits to income relatively quickly.

And on the back of that, in the US it transmits into income through your transactor balances both on the card interchange, as well as in the UK on the acquiring fees that we earn. If spend continues into the third and fourth quarter as we've seen at the moment, anywhere around these levels, you would expect to see interest-earning balances on the unsecured credit side also begin to recover, and that would be helpful both to margins and indeed net interest income.

And the final point, on impairments, we've tried to be conservative where we felt it was appropriate. We'd encourage folks to look at coverage ratios to give a sense of how much protection we have against a downturn in credit. Of course, these coverage ratios are principally driven by the provisions we have against non-defaulted credits, and these are sort of anticipating losses.

If we don't feel the need to increase those coverage ratios any further, absent the significant changes in the macroeconomic outlook, then you would expect our impairment charge to be lower. But that is a difficult thing to forecast with a high degree of certainty, given we're going into a post-lockdown environment in most of those economies, and the next few months will be critical in that. But absent any changes, yes, I would expect impairment charges to be quite a bit lower than we've had in the first half.

Joseph Dickerson, Jefferies

That's helpful. I think that you had guided on the roundtable following Q1 for c.£5bn impairment charge for the year. I think the consensus that you sent around was for around £5.7bn, which looks like c.£2bn incremental charge in the second half. Are you still comfortable with that guidance? Or how would you position the current outlook now, versus to what you saw coming out at the time of Q1?

Tushar Morzaria, Group Finance Director

Yes, […]. If you think about the charge we had in the second quarter, [there are] three building blocks for that. If you look at the underlying baseline run rate, absent any changes or updates to economic forecasts, we called out £400m. In addition to that, we had single-name charges of £200m, giving you a total of £600m. That's the kind of [baseline] run rate that we're experiencing at the moment, absent any changes to macroeconomic forecasts. If economic forecasts don't change much from here, let alone improve, then obviously the impairment charge ought to be a lot lower [than H1].

If economic forecasts deteriorate, the thing that's most relevant to us is long-term unemployment, and you see we've increased the levels of long-term unemployment going into 2021 quite materially, particularly in the UK. The other thing to bear in mind here is what happens when the government support schemes come to their natural end, whether they're the furlough schemes or various other things. We'll just have to see how the economy responds to that. But I think all things being equal, as we see today, those kind of underlying impairment levels that we're running at the moment would be how it looked in Q2, and you can build from there as appropriate.

Jonathan Pierce, Numis

Two questions please. First on impairment, then second on risk-weighted assets. The first question on impairment is more qualitative really, and it's the same question as Q1: I'm just interested in how your thoughts have developed since then on how these models are going to work. I guess the general expectation is that genuine {defaulted] impairments will pick up into the back end of this year and next year, but how do you think the models will react to that?

On the forward-looking provisions you've taken so far, are you expecting those to start releasing fairly quickly as we actually get the pick-up in stage three [balances], or is there going to be this period of almost double-count where the reserves remain elevated but the stage three charges pick up sharply? I'm interested in how your thoughts have developed on the working of the models into higher stage three charges.

The second question on risk-weighted assets. I wonder if we could just press you a bit more on where we may go in the second half, because in Q2 there was obviously a 2% fall in risk-weighted assets, but there were lots of big moving parts contributing to that. Maybe you could give us your thoughts on the book size and the credit portfolio, that fell £8bn in the quarter, but I guess the RCFs movement and credit card balances may level out, so perhaps those are flat in the second half?

Counterparty credit risk was down c.£4bn in the second quarter, should we assume that levels out as well, so that the second half movement in risk-weighted assets is really all about procyclicality? Maybe give us a feel as to where we could end the year in risk-weighted assets terms?

Tushar Morzaria, Group Finance Director

With impairments, this is a really good question in terms of how the models behave. […] The way I think about the book-up that we've taken, the anticipated expected loss over the cycle of £2.4bn, [there are] two things you've got to believe. One, our models are perfect at forecasting. No models have gone through this particular unusual scenario, so you have to put a bit of a caveat on that. And secondly, that we've forecast the economy perfectly as well. We may be too conservative, we may not be conservative enough. Again, we'll find out.

On the assumptions we've got the call on the future economy right and our models, indeed, are perfect, in principle we've already taken the loss associated with future expected losses. However, I think your question is a good one, because the timing of that will be important.

Typically what will happen is you'll have some credits that go all the way through to default, and we would write them off ultimately, and some credits won't go through to default and will cure back into lower stages. I think what will typically happen is on the defaults we would be conservative, and maybe recognise them sooner […]. I suspect they will happen earlier on in that cycle, and on the other hand] we're probably going to be conservative in curing the undefaulted credits back into lower stages [with reduced impairment provisioning].

So I think the net P&L charge, if we're right, is going to be around that sort of level, but you may see a mismatch in terms of timing with defaults happening slightly earlier than cures. It remains to be seen, of course. We've got government support measures going on here, so that might delay those credits that are going to default until much later, and maybe that gives time for good credits to cure back [into lower stages]. It's a little bit uncertain, but hopefully that gives you a sense of how we think about it.

On RWAs and guidance, I'm always a bit nervous to say this now, after the first quarter showed just how quickly things can change. But things feel very different now to how they did at the back-end of April, when there was quite a meaningful degree of procyclicality, and draws on revolving credit facilities, and economies going into lockdown, etc. Economies, and asset markets, have calmed down a bit. You've seen very strong capital markets activity, which is a good representation of that, and we continue to see RCF draws reverse even since the end of the second quarter, so that trend has continued.

I do expect that it will be difficult to forecast the economy over the short to medium term. You have got the difficulty in knowing exactly how governments and economies will respond if there is another wave of infections. I don't have a crystal ball on that, but that's a level of uncertainty. We've got elections in the US, we've got geopolitical stuff going on, so there may be some choppiness in markets, and if there is some choppiness in markets then there may be some procyclicality that comes through. And we should be fine with that, with a jumping-off level of 14.2% [CET1 ratio]. If we do get that procyclicality and capital goes back a bit, I think we'd be quite comfortable with that. Absent any choppiness in markets, and if it's more of a normal year, then you've seen that we should continue to be profitable hopefully, and that would be reflected somewhat in our capital ratio as well.

The final thing I'd just say, which I don't know if you're aware of, is that our MDA level may move as well. It's now a variable actually, in a positive light, because it's a fixed quantum Pillar 2A inside our capital stack. This does mean that as a percentage of RWAs it may go up or may go down depending on where RWAs are. And of course you've got the re-evaluation of Pillar 2A at the back-end of the year, so that will come through as well.

Jonathan Pierce, Numis

That's really helpful, because it is extremely difficult on the outside to model RWAs, as I'm sure it is within the bank itself. Would it be as good a guess as any at this stage just to bolt on another couple of quarters of maybe £5bn procyclicality to leave the year-end at around £330bn? Accepting it could be miles away from that, is that as good a guess as any?

Tushar Morzaria, Group Finance Director

Yes, it's tough. At best, if markets are choppy, the models, the whole framework is designed to be procyclical, so we will respond to that. If markets aren't choppy, then you've probably got previous quarters that you can refer to as to how we normally fare in the second half of the year. I think for me to give a number out, it's very difficult to forecast given I don't have a crystal ball on how choppy or not markets may be.

Andrew Coombs, Citi

If I could ask a couple of follow-ups please relating to slide seven. The first question is on the weekly spend data that you provide. UK looks almost back to normal, but the US is still lagging, down 25% year on year. [Are] you seeing divergence between the northern and southern states within that? And if you could elaborate as to how Barclays US credit card splits out regionally, as obviously the consumer card spend will drive the balances and the revenues from here?

And the second question relates to the right-hand of the chart on slide seven, looking at digital versus branch engagement. The branch engagement is starting to come back, but it's still running 40% below where it was, and it may never fully recover. At what point do you take another look at the branch footprint, when do you review that as a potential further cost-saving opportunity?

Tushar Morzaria, Group Finance Director

I'll get Jes to talk about the digital and branch footprint, and why don't I talk about some of the UK-US spend trends. The first thing I would say [on] the graphs here, […] the UK is a measure of debit and credit spend, whereas for the US we've only measured credit here. Now, in the UK what we have seen is a pick-up in debit spend. As spending has improved, it's been more skewed towards debit card, so that's probably why you're seeing a difference in those two graphs.

Coming back to your question on the US and the differences by state, a few comments from us. One is, as you know, in our business we are probably overweight in the airline and travel [spend]. We've been watching whether the spend on our cards, relative to industry spend levels, is any different, and actually it's been remarkably consistent.

We are slightly lower in travel spend itself, to the extent people were booking in the second quarter for flights and things like that […]. On the flip side, on other types of spend, we were bang in line, or sometimes slightly better than the industry, so that's very positive.

In terms of by individual states, the large economies like California, Texas [and] the Tri-state area are important to us […]. We're not very clustered by state though, it's relatively representative. It's more clustered by partner rather than by state. If we look at our data, we're not like a nationwide, open-card business. [We are] tied to the [partners], so we don't get an index view of the US in the same way we do in the UK, but on our spend at least, we're not seeing any discernible differences between those states that are having higher infection rates and talk of maybe some sort of restrictions coming in, for example like Texas, versus other states which are probably not experiencing those levels of infection rates.

For the moment, it feels quite balanced from our perspective and card spending is improving. You've seen it down almost 50% and recovered quite sharply, and looks like it's got some momentum still going into the third quarter. We'll obviously see how economies perform further into the third quarter. Jes, do you want to talk more about the use of branches and digital?

Jes Staley, Group Chief Executive

A couple of trends coming out of the pandemic. For sure, the use of digital networks from our consumers and small businesses across the UK has been increasing, and the use, for instance, of cash [contracted most] during the pandemic.

While in the short term that clearly impacts our transactional volumes, particularly in the branches. In the long term, the more we can get consumers migrating to our digital offering and using the mobile banking app and online to manage their transaction volumes, the better for us. That's a higher margin way to engage with our consumers.

We are running some 800 branches now. We've been slowly decreasing our branch footprint over the last couple of years. The branches are very important during this pandemic though. A lot of customers and small businesses that are under stress, and that are concerned about their financial future, and having the ability to go in and to talk to someone physically in a branch is very important for the wellbeing of our customers. We see it in the engagement scores we have with our customers.

I think the impression that Barclays has remained open for business through its branches and has been providing support to the communities where we live, there's clearly value there. The other thing that we did as a response to the pandemic, the call volumes of customers with issues, with concerns, at some point in time were up four to five [times] what they were this time last year. In order to give relief to our call centres, we actually began to re-train a lot of people in our branches. As of now, we are fielding about 200,000 incoming consumer calls every week with our personnel that are resident in the branches. So rather than just being there, waiting for someone to walk in the door, we're actually re-positioning the branches to do much more than that. Take incoming calls, make outgoing calls, to keep that engagement with our consumers in the time of this crisis as high as we can.

In the longer-term, as finance increasingly digitises, I think we will always be evaluating our branch footprint, and I would imagine the trend that we've seen over the last couple of years will continue.

Chris Cant, Autonomous

One on costs and then a follow-up on RWAs please. The cost: income ratio across BUK and CC&P, and I know you've shuffled some stuff between divisions, but if I just […] ignore that, was 67% in the second quarter after adjusting for the Visa preference share impact.

I understand that you expect some topline recovery there, but if I look at H1, which obviously includes the first quarter when you didn't have the impact of the rate cut tucked in and COVID wasn't in full flow, it would be 62% across those two divisions, again adjusted for Visa. You've still got your target of less than 60% for the Group over time, including Head Office which is a drag, and CIB which would normally be above that level. What do you expect the cost: income ratio for your retail-facing businesses to be? If you think about BUK and CC&P, what do you expect the cost: income ratio to be next year and looking into 2022?

And on a related point, the cost: income ratio for the CIB at 49% looks unsustainably low. It looks low versus what the CIB divisions at other banks have printed. Could you comment on your [compensation] accruals policy please? What is going on there? Because it looks like you're not really reflecting the very strong performance in the bonus accruals, and I'm just not sure how your year-end conversations will go, given that you're also flagging the strongest ever capital ratios. Should we be worried about a Q4 comp catch-up again?

And just one quick follow-up on RWAs please. On Jonathan's question, I understand you're reluctant to guide, but it does feel like this is a bit of a random number generator from the outside. First, do you have any more model change impacts in your back pocket to come through in the second half? And what is the quantum, presuming you do have visibility on management actions? And you said to look at prior periods' movements. Last year we saw a £14bn reduction in CIB in the fourth quarter, are you suggesting we might see the same this year, absent a big spike in volatility?

Jes Staley, Group Chief Executive

One, we stand by our target of a 60% cost: income ratio for the bank over time. The first half we delivered 57%, so those are the numbers. Obviously, in an environment like this, when spend just literally fell off the table in our two principal consumer businesses, UK and US, you're going to have a move in your cost: income ratio [in the consumer businesses].

We felt it was very important that this bank stays open for business and stays engaged with our small business and consumer clients, and maintains the employment head count for us to do that. We also publicly came out and said that we were going to cancel any redundancy moves in our consumer businesses until we get through the end of September. During a moment of crisis like this, it just didn't seem appropriate to us that we start laying-off a lot of people. I don't think the current cost: income ratio in our consumers businesses are reflective of what it will be in a normal state. They have been comfortably below 60% in the past, and I think we'll comfortably get below 60%.

In terms of the CIB, that cost: income ratio is obviously very, very strong in the first-half of the year. I would expect that to go up as markets progress. You essentially have the pandemic creating a distortion on one level in BUK, then creating [positive] distortion, to a certain extent, in the CIB. Our anticipation is, in the third and fourth quarter of next year, you will start to normalise those cost: income ratios and our target remains the same.

In terms of accruals for compensation, again the ultimate decision around compensation will be made at the end of the year and beginning of next year. We are very aware that we are in an industry with competitors, and we have to recognise what the industry is doing. We want to compensate our people fairly, but also we have a very uncertain economic environment right now and we need to be mindful of that. We are accruing, and I'm not worried about being able to keep the very talented people that help us in the wholesale side of our business.

Tushar Morzaria, Group Finance Director

To round that off, […] our costs have been declining in absolute terms for a number of years now. I think regardless of size, shape and any environment that we're operating in. Cost discipline is an important thing for this management team, and perhaps now even more so, given some of the uncertainty we have on the topline.

Your question on RWAs: I think your question was on whether we've got any model changes or something like that in the back pocket. Nothing I would call out. There are the rule changes that may or may not happen on software tangibles, there are SME factors that we didn't put through. These are relatively small, and I wouldn't call them out as big drivers of our capital ratio. I think what will be [is] just whether volatility in markets goes back to anything like they were in March/April - that will transmit some pro-cyclicality if it does. RWAs will inflate and we're okay with our capital ratio going back a bit. If it doesn't, then it may be more of what you're used to.

In terms of the fourth quarter, […] because you've got Christmas and New Year right at the back-end, the trading book settlement balances just tend to be very low at that point in the year, so you do get an additional tailwind if that remains the case this year, which I think we've seen in most years now.

Alvaro Serrano, Morgan Stanley

I have a follow-up question on provisions. You've done a good effort topping up the reserve build on the credit cards, but quantitatively your balances in credit cards are down 18% in the UK and more than double-digit in the US. From a qualitative point of view, can you give us an impression how that has de-risked your book? What kinds of clients are paying down the balances? I don't know if you have any colour on the rating of those clients? Is it good clients who are paying it down or is it across the board? Is it high balances, small balances? Something that can give us a qualitative impression of if that is really de-risking your book or the riskier clients are still there? Obviously payment holidays have almost reduced to zero, but what quality is on the balance sheet.

Related to that, obviously in Q1 you had a big oil reserve, I think it was £300m. The oil price is now much better. [Relative to] your Q1 wholesale exposure, what areas of the portfolio are you more concerned about? Would you say retail is now the major concern? How do you see the reserve building up in the wholesale in the second half? Not just in the second-half, but [perhaps also] medium-term from a qualitative point of view?

Tushar Morzaria, Group Finance Director

In terms of the balance reductions, I'd almost characterise it as a vertical slice. We didn't see a particular skew towards riskier or less riskier credits, both in the US and UK. I think the reduction in balances was as much driven by just people spending less and that finding its way into lower balances, rather than those that could afford to just pay off their cards and those that couldn't were leaving their balances running. We didn't really see that at all.

What we did see at a very marginal level was on payment holidays, those with riskier credits have a higher propensity to take payment holidays. But looking at the numbers now, I'd say that's behind us and these are back in the books, rather than in a special payment holiday category, as you can see in our disclosures.

For example, you'll see our FICO scores in the US are, broadly-speaking, what they were before the pandemic, so we haven't really deteriorated there either. The other thing I would say is to ask everybody to take a look at coverage ratios. Provisioning is something that is difficult, given that we're making quite long-range estimates based on uncertainty around the economics, uncertainty around government support schemes, [uncertainty around] customer behaviours. What we've tried to do is to be as prudent as is appropriate, and have what I would consider strong coverage ratios on some of our riskiest part on the books.

On the retail side, UK cards, we're at 16% provision rates and US cards at 14%. These are pretty high by any historical measure. For those of you that will have this data, the last financial crisis, our UK cards business had cumulative NPLs of 6.9%, so we feel appropriately provided, given the credit profile of the books there.

Your other question, on wholesale, the areas we're most focused on we called out on a slide. It's about £20bn of exposure, and it's in the sectors that you would expect - transportation, retail, hospitality, etc. We're 4% covered there. You've got to remember, most of that is non-defaulted, so these are [forward-looking] book up provisions.

We do quite a bit of hedging there. We're 25% synthetically hedged across those sectors. We obviously have collateral levels, covenant triggers, we're insiders to the company, and these are much more of a bottoms-up, name-by-name assessment of what is the right provision level. You will have the numbers there in the slide, but we think we're well provided and relatively modest in terms of exposure to us.

Rohith Chandra-Rajan, Bank of America

Just to follow-up on Alvaro's question, just in terms of behavioural activities that might give us some indication of credit quality going forward. I think the comments on the cards book and the payment holidays were helpful. Are you able to expand that at all in terms of the corporate business?

You referred earlier to what your acquiring business is telling you about SMEs open for business. [Can you comment on] activity levels or types of activity for SMEs? And then on the large corporates, the fact that primary capital markets have been opened is presumably helpful in those large corporates [and their ability] to refinance? So that was the first one, just in terms of any lead indicators on credit quality.

The second one on BUK NIM. The guidance reiterated the 250 to 260bps NIM for the year as a whole. It looks like a spread of 230 to 250bps in the second half, just wondering what the uncertainties are that will drive that 20bps range in that margin for the second half?

Jes Staley, Group Chief Executive

I'm going to start to give some colour on the first question, and Tushar will pick up on the second one. On the consumer side, I think what was a little bit of a surprise to us on receivables was that historically going into an economic downturn, you see consumers and small businesses actually increase their reliance on short-term credit in order to maintain a lifestyle or to keep a business functioning. And then, as you come out of recession, they normalise. In this event, what clearly was driving consumer and small business behaviour was fear. And so [among] people of good credit quality, and even [among] those businesses that stayed open, use of short-term credit declined. They wanted to get their balance sheets in shape, less worried about their own personal income statement.

[…] We've done hundreds of thousands of payment holidays. In the mortgage payment holiday portfolio, we're actually seeing a slight uptick in requests for extensions of payment holidays as the holiday periods come to an end. In the cards side, as we showed, people are not asking to extend or roll their payment holidays. So the consumer is acting rationally in terms of, "okay, I will roll my debt which is at a very low interest rate number, like a mortgage, but I'm not going to continue with the payment holiday on something that's got an interest rate in the high teens." So they're acting rationally, and I think it is resulting in a book which is maintaining its overall credit quality.

On the corporate and the SME side, what we're seeing emerging is a pretty dramatic recovery in spend. At the trough of this crisis, spend was off anywhere 30 to 40%. You take away cash spend, and spend numbers are almost getting back to where they were a year ago this time, which is quite a reversal. That's very encouraging in terms of what we see for SMEs. And then on the SMEs, and to a certain extent the corporates as well, two things are having a market impact on our credit risk to SMEs and corporates, and those are the government programmes.

We put £21bn into small businesses and large corporations [through] government programmes to provide them liquidity and funding at extremely attractive rates. We've done close to £11bn of commercial paper issuance in the UK through us to Treasury. That's a lot more attractive funding than going to a bank revolving line of credit. Both corporates and the SMEs have been actively using government support mechanisms for credit, and that's clearly had an impact on the credit profile of Barclays.

And then, as you said, [there's been] an unprecedented injection of liquidity into the capital markets, as well as central banks around the world using their balance sheets to actually buy credit in the capital markets. Those markets reopened with an extraordinary amount of volume […]. We participated as a manager in three quarters of a trillion dollars of debt issuance around the world, most of it in the second quarter. That's £3tn of funding for corporates that is not going to find its way back into a request for [banks'] balance sheets. So on the one hand, we are open for business. We believe, it's an obligation of this bank to keep our balances open and to have those facilities available to our customers. Between the government programmes and the robustness of the capital markets, quite frankly, the demands aren't there.

Tushar Morzaria, Group Finance Director

On NIM, the trickiest thing to gauge there is balances and just how quickly they recover. It's quite early on in post-lockdown environment and quarantines […], but we've seen a plateauing of balances. We've seen a fairly decent recovery in spend levels, and I think if those spend levels stay anywhere near where they are at the moment, let alone continue to recover, you ought to see balances growing shortly thereafter. But there is some uncertainty there. We don't have much to model this stuff off, and it's only a small number of weeks post-lockdown, and that's why there's a broad range.

Rohith Chandra-Rajan, Bank of America

So it’s really about loan mix in terms of BUK NIM uncertainty? I guess you have a clear understanding of what the deposit impact is, but the asset side of the balance sheet is the uncertainty?

Tushar Morzaria, Group Finance Director

Yes, you’ll probably see mortgages continue to grow, but it’s the unsecured card balances - how quickly they come back is a little bit harder to forecast. It’s good signs, but we need to see that momentum continue.

Guy Stebbings, Exane BNP Paribas

First, a quick follow-up on BUK and then a question on CC&P. I just wanted to check, on the Barclays Partner Finance move, whether that was then captured in the Barclaycard consumer line? If that’s the case, the balances would have been about £9.5bn, down from £13.6bn in the first quarter. So underlying decline in balances would be roughly double the industry level, so I don't know if there’s anything you’d call out there, which obviously feeds into the prior question on the NIM outlook?

And then on CC&P revenues, you’ve talked about a gradual recovery and some of the better spend trends in the US more recently. I’m just trying to gauge what you expect a gradual recovery will look like and how it will be achieved? And clearly, sat here today, having delivered just over £1.8bn in the first half if we add back the visa headwinds, and the balances is down to £33bn, we’d need to see quite a strong recovery to get back to market expectations for the £3.9bn this year and north of £4bn thereafter. Should we assume a fundamentally different outlook to prior market expectations given the environment? Or if not, what sort of revenue margin expansion and balance growth are you targeting?

Tushar Morzaria, Group Finance Director

Let me do the second one first, and I’ll come back to your first question on BUK. There are three things on CC&P that will be tailwinds into the second half of the year. I’ve talked about net interest margin on the liability side, the 50bps margin pickup towards the back-end of the quarter on our [US Cards] liability balances, and we may drop deposit rates again. That is a tailwind, and obviously very different from where we were in Q2.

Second thing is payments. The transmission effect on payments is relatively quick. In our acquiring business, now that the bulk of those businesses are actually open, you’re seeing spend levels almost back to pre-COVID levels. That quickly transmits back into fees, particularly in the UK where our acquiring business is most important. And in the US, interchange fees are still quite attractive. The spend recovery in the US will translate back into fees there pretty fast as well.

The harder one to gauge is balances, particularly on US cards. If spend levels continue, then balances will follow, but there is a delay effect there, and that’s a little bit dependent on how the economies perform in a post-lockdown period. Do they continue as they are at the moment? To all intents and purposes, even though there’s a lot of concern around infection rates, we’re not really seeing any tail-off in consumer strength at the moment. At which point, we would expect to see balances and card openings increase.

I can't give you numbers on that. It's a bit too early in the quarter to start extrapolating, but those are meaningful tailwinds that we'll have from this point on, and we've talked about a steady recovery. We'll see how strong that is as we go further into the quarter.

Just to answer your first question […], the Barclays Partner Finance business is recorded in the Personal Banking line. If you want to make sure you know what we're calling what out where, then we can spend a bit of time behind the scenes to point you to the right places and to the disclosures that we've got.

Guy Stebbings, Exane

I don't know if I could just push you a little bit on the CC&P revenues? If those three items all do come through, and I appreciate [the balances] is hard to gauge, but if that were to come through nicely over the course of the second half of the year, are you hopeful we can get back to a c.£1bn quarterly run rate revenue?

Tushar Morzaria, Group Finance Director

I know you're keen on trying to get me to give a range, and I'm reluctant to do that, only because it's quite a fair old extrapolation. All I would say is, I'll be disappointed if there isn't a recovery into the third quarter that has momentum into the fourth quarter and beyond. It's a momentum business, so once things start moving in the right direction, they will be followed through.

How strong that follow-through is, the signs look pretty okay at the moment. Spend levels are improving, margins improving on the liability side. If that all continues then, we're cautiously optimistic, but it's early days in a post-lockdown economy to give you too much precise guidance.

Ed Firth, KBW

[Bringing] you back to costs, […] you're talking about income up 8% and costs down 4%. I've followed banks for a while. Those numbers are almost unbelievable, and looking at the share price reaction today, I'm not alone in that concern.

If I look into the second half consensus, the consensus seems to be looking at revenue falling c.£2bn, and costs actually going up a little bit. It's almost like there's a complete disconnect between what's happening to your costs and what's happening to your revenue. Could you help me a bit with that? I'm not asking for a number, but if the revenue environment stays very benign, should we expect costs at the current level or should they grow quite substantially from here?

If we see a big fall-off in investment banking revenues, have you got flexibility? Could that -4% be -6% or -8% at the full-year? What are the levers you can pull? What sort of comfort can you give us on that?

Tushar Morzaria, Group Finance Director

First of all, the backdrop I'd start with is [to] look at the trend over the last two or three years. We have been reducing our cost base in absolute terms, regardless of size/shape of the company and the economy we're operating in. Cost discipline is very important to us, and that's something that's a constant focus of this management team, and I'd like to think that we've got a track record of reducting our costs year on year.

This year is obviously much more complicated, because […] when we went into lockdown, plans that we had in place [were] put on ice. For example, we were very public that we wouldn't lay anybody off until at least September. [For] people that we did lay off before we went into lockdown, we gave them [the same terms as those that are on government furlough schemes, but paid for by ourselves]. This was completely discretionary on our part, but just to try and do the right thing for people, […] so now that comes at a cost.

Obviously attrition levels fall quite meaningfully. The job market dries up, so we've got a higher headcount on both levels - lower attrition and staff reduction programmes that we didn't implement. And then just the costs of keeping businesses open with social distancing requirements, cleaning and all the various other things that go alongside that. It is an unusual cost shape, but as we go into a normalised operating environment in a post-lockdown environment, we will absolutely examine all the new ways of working that we've learnt.

One of the things that is absolutely eye-opening in lockdown, there are some things we've been able to do as an industry, and certainly as a bank, that we thought were unfeasible previously. I'll give you an example. Some of the largest capital markets transactions that were done quite early on in lockdown, you had the issuer working from home. You had the investors working from home. You had the research analysts working from home. You had the syndicate desk, the traders, the salespeople. Even the settlements engine, the folks driving the mechanics of settling these trades. Everybody at home, and yet we [did] three quarters of a trillion dollars of capital market issuance.

None of us would have thought that would have been possible on 1st March, so that's a really interesting new way of working that we will examine and understand and look to take the benefits from. That's probably more looking into next year and beyond in terms of opportunities.

For this year, it's just a slightly unusual year. We had good momentum in the back-end of 2019 that's come through in the first half, but we put on ice a lot of the plans that we would have otherwise had. That will be a slight headwind going into the second half, but cost discipline is super important. Jaws are very important to us. Cost income levels are very important to us, and that's something we are focused on.

Jes Staley, Group Chief Executive

Putting in rank order the priorities we focused on in this unprecedented medical crisis, leading to an unprecedented economic crisis, leading to an unprecedented government and central bank response. First and foremost is the financial integrity of the bank, so tracking the liquidity profile of the bank, tracking the capital level of the bank, and making sure, if at all possible, to remain profitable each quarter. We accomplished all three of those in the first half of the year - record level of capital, record level of liquidity and profitable through each quarter.

In that profitability story, there's a 27% improvement in pre-provision earnings year over year. We take a hard look at that, and we're encouraged by the move forward led by the CIB. But then the next thing you look at is, what can we do to give back to our communities? And we have [88,000 employees], we can move that employment number up and down.

When I got here four and a half years ago, we were about c.120,000 employees, so we will make the move when we need to make it. We used to have c.1,400 branches, now we're running 800 branches. So we can manage costs, but we're going to do it with a focus on the challenges that particularly the UK is going through, and we're going to be there with payment holidays, overdraft fee waivers, bank fee waivers and keeping people employed.

You're going to have distortions in an environment like this, which will settle down as the economy starts to settle down, and we hope to see that in the third and fourth quarter. So big positive jaws movement led very much by the Markets businesses, which hit all sorts of records, but know we have our pulse on what's going on in the bank. We're serving the communities and the consumers that we need to. We're partnering with our regulators and the central bank and government. The bank is in a good place.

Ed Firth, KBW

Could I just come back quickly on that? […] A lot of the things you highlighted from the first half are things that I thought would have increased your costs, not decreased them. You're stopping redundancy, relocating people, etc. It's still a struggle to me to see why people seem to be expecting a big fall-off in revenue in the second half, but costs to be up slightly. I'm just trying to think, is that a sensible type of forecast? Would you feel that that's the right way of looking at it?

Tushar Morzaria, Group Finance Director

Another thing I'll say is we were on a declining cost trajectory as we came into 2020. You've seen that momentum in the first half. That momentum will be frozen a little bit by deliberate actions that Jes called out [just now]. We don't have the same momentum going into the second half. That's just the way it is, for all the good reasons we talked about, but there are new ways of working and new ways of doing things that none of us thought were possible.

There are some really interesting opportunities that we'll start examining. That's probably more a 2021 conversation. Income-wise, we'll see where the CIB goes. We talked about us expecting the consumer businesses to start recovering, so there'll be some different trends in the different businesses there.

Jes Staley, Group Chief Executive

Just two anecdotes, the technology spend of moving 60,000 people to work from their kitchen tables, where we have compliance, controls [and] insights into our systems that are dispersed around the world, that's a lot of money to set all that up and track it. We gave pretty much carte blanche to our technology people to allow us to work as remotely as we have. Now the flipside of that, there aren't a lot of people jumping on airplanes right now, so our travel and leisure expense absolutely collapsed in the first half of the year.

What's incumbent upon Tushar and myself is, as the economy begins to normalise, we look at the spend and technology and ops. As we bring people back into offices, does that decrease? Do we think about rationalising the real estate footprint? On the flipside, we'll probably start to let people go out and visit a client every now and then. We will keep our hand on those cost levers to ensure the financial integrity of the bank, the profitability of the bank and the capital strength of the bank.

Tushar Morzaria, Group Finance Director

With that, we'll close the meeting here. Thank you very much.

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