CYBG PLC Interim Results – Analyst Breakfast Call

Hosted by: Ian Smith (CFO) and Andrew Downey (Head of Investor Relations), CYBG PLC

Andrew Downey, CYBG PLC

Thanks very much, everyone, for joining. As you know, we've set this session up to do a bit of a wash-up of the interim results. Obviously, we're conscious it's the first time you've seen the combined set of group numbers, you might have a few questions to follow up on so we thought we could just use this as a bit of a Q&A. We haven't any prepared remarks to kick off with so we'll kind of hand it over to you guys and take Q&A from there. We'll come to the phones a bit later on, so we'll take questions from the group first and then we'll pick up on the line.

Ian Smith, CYBG PLC

This is being recorded and transcripted so the usual protocol on giving names and things just so we have that for the transcript. Okay.

Ed Firth, KBW

It's Ed Firth from KBW. Yes, I'm just thinking about the margins, just trying to get some sense of some of the drivers. Can you tell us what the—I understand you've changed all the accounting on the credit card book, etc. Is it possible to just give some idea of what the current yield is on the credit card book, under your current accounting procedures and processes, if you like?

Ian Smith

Yes, so I guess there's a sort of back book yield and front book that I think is if I've understood it? Broadly speaking, the back book and average yields is on slide 12, which is about 7.6%, and that's really a sort of the mixture of the mature cash flowing balances that we get through Virgin Money, the CYBG cards business which is quite small, as you know, so sort of 350 million post to post outstandings so, you know, that's the key driver there. In terms of the sum of the business, it's a shade over 5% and that's, as I say, we talked about this over the last few months in terms of trying to bring both the life over which we measure EIR and the rates back into the pack, so about 5%.

Ed Firth

The 7.65%, I guess includes the unsecured loans, as well as the credit card?

Ian Smith

Yes it does. Broadly speaking, the unsecured loans are a wee bit lower on average.

Ed Firth

Right. And what portion of today is on a cash 0%?

Ian Smith

So what we talked about last week was about 35% of the Virgin Money hedged portfolio is post promo, therefore yielding cash.

Ed Firth

So to be clear about the maths, 65% has a 0% cash yield?

Ian Smith

Yes. A 0% headline interest rate, and clearly there are fees and any costs on further customer drawdowns.

Ed Firth

Are you out of that business now completely, in terms of offering 0%?

Ian Smith

We're still in it, but it's a much smaller proportion of the portfolio and the average offer now is somewhere around 24 months rather than the much longer period. So it was altered throughout the market, I guess, 12 to 18 months ago, so that's certainly brought in the duration of the interest rate period.

Ed Firth

So say your new business today in the credit card book, will broadly speaking be around 24 months, 0%?

Ian Smith

Around about—just under half of the new business flow is on that straight balance transfer offer. When we look at, say, the growth in balances over the last couple of halves, a good proportion of that has been Virgin Atlantic. Virgin Atlantic is a straightforward purchase and revolving credit card that earns the market rate of interest. So let's say it's less than half of front book business is on those teaser rates.

John Cronin, Goodbody

John Cronin from Goodbody. As a follow up to Ed's question on the credit card, two separate questions. One is you mentioned the back book yield at 7.6%, and you've also separately indicated that we should model at £300m fair value adjustments over five years which incorporates the write-down of the EIR assets. I'm just wondering if that happened on Virgin's books at acquisition? I'm just wondering how that dovetails with NIM and the consequent compression in that 7.6% rate; presumably some back book compression will already be captured through fair value adjustments by virtue of writing off the EIR assets over time - is that the correct interpretation?

Then my second question is you mentioned 65% of balances around—is it 65% of the outstanding balances relate to the zero balance transfer cards specifically? I understand that Virgin did get customers to transact so just trying to understand the variance difference between the 65% upon the balances or within that 65% some of those customers pay the rate on some of their outstanding balance.

Then I was—on a separate note, I've seen the news from Tesco this morning about the sale of its mortgage book and various speculation of various other similar books for potential sale in the market. I understand you're still very focused on bedding down and integrating Virgin Money, but would you potentially opportunistically look to put some excess capital to work in terms of opportunistic acquisitions on these loan books or other?

Ian Smith

Okay. So there's a couple of quite big questions in there. Let me deal with the second one first up. So, to be clear, around about 65% of the Virgin Money card book is still in its promotional period. What that means is that it could be something that was written on close to January 2017 and is probably, on that basis, a few months later on coming out of the promotional period to something that was written a couple of months ago.

And to your point, over the life of those customers, we'll see further drawdowns, we'll see fees, all those sorts of things. I'm not saying 65% is not cash yielding, but it's still within its promotional period. So 35% post promo, having gone through that, I guess that opportunity for the balances to attrite away but also critically starting to earn sort of the full rate of cash interest. So that's that.

The Tesco mortgage book. I mean, we saw the news the same time as you guys this morning. It illustrates some of the challenges that are there for smaller mortgage players at the moment. I know nothing about the book in terms of its composition, its rate, those sorts of things. I think we'd always be open to looking at portfolio acquisitions that make sense, but I know nothing about this other than I'm sure someone will come and talk to us about it in due course.

Then your first question which was about sort of, interplay of EIRs, customer situation and fair value. So, to be clear, what we did through the fair value exercise was to essentially eliminate the EIR asset that was being carried on Virgin Money's standalone book. We did then recognise the fair value asset which has, on the face of it, a sort of—you might think it has similar characteristics to the EIR asset, but they're actually quite different.

So the fair value exercise requires us to look at the balances on the books not the customer relationship if you like, but the balance on the books and estimate the income to be earned from those balances. Now, of course, if you're looking at a balance that is earning 0%, your estimate of future income on that is pretty low in a fair value context. You have to look at this as what would I pay to acquire that balance?

So, we've done this in some detail, as you would expect. The composition of the fair value asset that sat on the books of Virgin Money, was very heavily weighted to newer vintages and income still to be earned in cash terms. The fair value asset is very heavily weighted to that portion of the book that is cash earning at the moment, because that's where you can impute a fair value of the income to be earned from those assets. So a very different composition and so, while on the face of it they might look like sort of similar approaches in concept, the weighting is different. So that's, I guess, the first point on that.

What we sought to do in relation to how we present our underlying results and our net interest income, is to reflect what's going on out in customer land, if you like. So that impact of unwind and fair value adjustments, all those sorts of things, is being taken below the line because those are sort of financial or accounting impacts rather than what we're seeing at the customer level.

What you see going through our net interest income, what's the components of the net interest margin that we declare, and importantly what we talk about in terms of the yields on the book, on slide 12, are what the customer sees and therefore, what you're seeing through there in that sort of 7.65%. First of all it's a composition of two CBYB PLs and cards, about sort of £800 million or so of the £4.5 billion balance, the rest of that being the Virgin Money cards and it's a mixture of, in that 7.65%, if you like. If you sort of ignore the impact of PLs and that sort of thing for the moment, what you're seeing in there is a mixture of that portion of the Virgin Money heritage book that is post promo and cash yielding and we're recognising as cash yielding because when we acquired it, it was only cash. That element that is EIR and some of the other sort of mix effects and things in there, but that's a customer rate.

Robert Sage, Macquarie

Can I ask a question about, it's Robert Sage from Macquarie. Can I just ask a quick question on looking at mortgages, a number of the other banks have sort of given us a feel for what they consider even returns; what they seem to generate is around 10% to 15%, and I was just wondering whether you could comment in terms of absolute returns that you see on residential mortgage lending?

Ian Smith

Yes. So thank you, Robert. Certainly, in terms of—we've never typically given disclosure of those lines and I'm not going to sort of change that practice today. We've indicated that we're much more interested now in managing margin rather than the pursuit of volume in our mortgage book and that really relates also to our view of returns.

And so there are certainly some parts of the mortgage book where returns are less attractive than they used to be. We still have a higher risk-weight density than some of our larger peers. That's really a feature of us being relatively new, certainly on the CYB side to the IRB landscape and a degree of conservatism and other things in our models there. Part of that equation as being more circumspect about where we play in mortgages relates to an analysis of returns. There are some parts of the mortgage market where we find those less attractive.

Nicholas Herman, Citi

Nicholas Herman, Citi. Just want to ask a follow-up question on mortgages. Your LTV ticked up, particularly on new book, just below 69%, almost 70%, 69.5%, something like that. Over the medium term, is that something you expect to continue, how much more runway do you have to further increase LTV?

Ian Smith

So, thanks, Nicholas. It is a feature of mix. We've got more first time buyer which is sort of typically 80% to 90% LTV that's in that. And first time buyer is still relatively attractive from a rate perspective. We've got, as you would expect us to have, is caps on the proportion of the book that relates to high LTV lending. So I don't expect us to expand that dramatically over the next few months. It is a feature of having done as I say, in a market where purchase is very much focused on first time buyer and the bulk of the market is re-mortgage. It's a matter of consequence of that.

Nicolas Herman

You are still below peers, a lot of peers, so there's a fair amount of runway if you wanted to, but it sounds like you're not going to be?

Ian Smith

Yes, but we do have capacity left in our risk appetite settings but we don't expect to spend that capacity certainly in the near term. You always have to manage to the mix of the book.

Aman Rakkar, Barclays

It's Aman Rakkar from Barclays. A couple questions—first of all, on mortgages again. So appreciate the second half is a period of acute redemptions which will eat away at net interest margin. I was just trying to think about can you give us some indication of what growth rate we can expect from this business? Particularly, if, I guess, pricing in the second half could be problematic in terms of the re-pricing of the book. Are you minded to kind of take a step back and cede share? I mean, more broadly, just any sense of kind of growth rate we can expect from this business as well, as a combined entity. I know historically you have talked about single digit growth, is that the kind of thing we can expect?

Ian Smith

Okay. Do you want do your second one now or?

Aman Rakkar

Yes. Actually, do you know what, this is leading on from the questions on the call last week. It was regarding RWA inflation. You did mention definition of default which is potentially on the Virgin Money book. Any sense on how to—the size, essentially how to estimate that in terms of what the effect might be? And if there are any other risk weight inflations we should be aware of?

Ian Smith

Yes. So in terms of aspirations for growth in the mortgage book, we don't expect to grow very much in the second half of this year. And I think you might even see circumstances where the odd month we might go backwards. That's really a feature of us, say going back to the point we were discussing earlier, picking our spots a little bit.

I think in the medium term, we would expect sort of through—sort of, over time, to grow pretty much in line with market, but we'll do a bit more at Capital Markets Day about where we'd see growth of balance sheets and that sort of thing. But some of our sort of thought process around mortgages is ensuring that we're pursuing the right kind of growth, the stuff that is return enhancing and that does require us a little bit to undertake a bit of a churn and a mix shift in the mortgage book and we were very heavily weighted in the VM heritage, to some of the lower margin business.

Then the other thing, I guess, that's sort of a feature there is we've talked a little bit about what we think, and we'll say more about this on Capital Markets Day, but we've talked about what we think our balance sheet shape ought to be and in conversations with analysts and investors, we talked about sort of reshaping a wee bit from where we're about 83% mortgages now and, over time, shifting that more towards or certainly a higher proportion of SME and unsecured, and we'll talk about how we think about the absolute shape of that on Capital Markets Day.

Aman Rakkar

Do you see yourself as kind of underweight in any particular parts of the mortgage market, maybe geographically, or sounds like first time buyers is something that you're quite happy with?

Ian Smith

There are some small pockets, as I say, let me let Hugh talk about that on Capital Markets Day, just to talk about where would expect to grow.

Then RWA inflation. Yes, as I said, last week as part of transition to IRB, the CYB heritage dealt with the change in the definition of default. That's still to come in the Virgin Money mortgage book. There are sort of puts and takes in other directions and, again, that sort of direction of travel, I've talked a little bit about us being, having a degree of conservatism in the mortgage models. So, again, a trajectory for RWAs and RWA density is a topic we'll pick up on Capital Markets Day. So while we see a bit of RWA inflation coming from that particular feature emerging, there are some items that help offset that.

Ed Firth, KBW

Can I ask another question? It's Ed Firth again from KBW.

It's just a slightly broader cultural question because, and I guess when you bought Virgin Money, one could have gotten quite excited about the potential of the brand and growth and, I guess, the sector, as a whole—

Ian Smith

Some did.

Ed Firth

Yes, including me, and I guess the sector as a whole, is seeing a lot of players who are going for big market share grab, you have all the digitals etc., etc., and, yet, the sort of messages we're hearing now more is sort of maybe holding market share, maybe surrendering a bit, focus on the margin, we didn't get anything in the government's innovation fund. It's sort of like maybe we just—the two of you together is just the two of you together.

I'm just trying—as we approach the Capital Markets Day, how should we be thinking about the sort of culture you're trying create? Are you trying to create some sort of market share grab and growth culture or should we be thinking more about sort of a traditional, small, incumbent bank trying to protect its current returns and enhance as best as that they can in next three to five years?

Ian Smith

I think that—as you would expect, we think that we have the opportunity to do something quite special here. I think that the brand allows us to be meaningful throughout the UK and an enormously valuable brand, we think, that plays very well with consumers and businesses, a bigger customer base from which to deploy a full range of products, etc., etc.

What you're seeing at the moment, though, is it's impossible, other than through pulling some levers on cost, for us to sort of demonstrate the value of the acquisition until we get through Part 7 because until we can actually start to put the businesses together and to really make a difference with customers and those aspects of the business that we expect to deliver differentiated growth and performance, we can't actually demonstrate that.

We're also in that position of—you'll forgive me if I allow David to talk a bit about that on Capital Markets Day, about where we really see the potential here. So let me reassure you that in the short term, where we see some particular challenges in relation to the mortgage market, we're circumspect and I think that we're right to do so. I don't see that as something that persists in the medium term. We think that the potential for the brand and the business across the UK to offer something completely different to what you see with many of the players out there is substantial, but we will—we're not going to show our hand on that until we get to Capital Markets Day.

I think the point you made about us not winning funds on the SME side. You know, I think you know my feelings on that. It absolutely is a disappointment. Having said that, we have a very clear view of how we can still deliver growth in the SME business and I think SME is a real sort of jewel in our portfolio if you like, in terms of our ability to grow market share and to do that at a better margin with stronger fee income, all of those sort of things. No, you should absolutely not be thinking about us as a dull, small incumbent and we'll talk a bit more about that in June.

Ed Firth

When does the integration with Part 7 take place?

Ian Smith

We expect to get the Part 7 by the end of this year. So we're still on track with that. As I said before, that allows us to really make a difference in terms of, first of all, rebranding the business and secondly, able to offer the full product suite to the full set of customers.

Jenny Cook, Exane

Jenny Cook, Exane. Can I come back to some of those things that you talked about, on asset RWAs going forwards? If I look at your mortgage risk-weight density it is considerably above peers which is driving primarily from the CYBG book, do you think there's any ability to inch that down over time as you prove the use of your IRB models; even if I look at peers on a fully loaded basis at CRD IV, they are still going to be operating on a risk weight density considerably below yours. Do you think you're going to be able to pull that down a bit?

Ian Smith

No question. That's—but the key is over time, so we—as you can imagine, when you go through a process like IRB accreditation, both we, in terms of just wanting to be comfortable with the operation of the models, both we and the PRA are always pleased to have a bit of conservatism in the risk weights that those generate so I think there is potential to work with that there.

I think, while we will see some of those larger peers with very low risk weights get pushed up a bit, I still think we have some capacity to bring our average risk weight density on mortgages down and we'll sort of, give a bit more colour on that in due course.

In terms of the bits and pieces that sort of move and offset, I suppose one of the key features of our portfolio is we have Virgin Money heritage credit card book that is still on standardized, but it stands that we will take that to IRB and the credit quality on that is so strong that we would expect to see a risk weight improvement from moving that to IRB. Those are some of the things that, as I say, help offset the general or the sort of puts and takes that will manage through this, so I think there is plenty of opportunity out there and I'll cover those again next month.

Jenny Cook

Just on MREL, as you drive forward you actually have quite a weighty Pillar 2A at the moment which I assume is incorporating integration risk?

Ian Smith

Yes.

Jenny Cook

As you kind of think about that, if you double that, then it puts you on quite a high final MREL stack. How might you think about that going forward with the potential for it to potentially come down a bit from your interim MREL funding position through to your final MREL position if that was to come through?

Ian Smith

Yes. You're right, Jenny. We have some stuff in Pillar 2A that shouldn't require us to match for that amount, if you like, so for those temporary things like integration add-ons. One of the biggest components of Pillar 2A individual components, is pension risk and as far as we're aware, that won't require us to be matched with MREL. The eventual total will be, you know, sort of lower than what's indicated by the current Pillar 2A requirement.

We've guided before Andrew in terms of what we think are our sort of landing point will be on MREL, could you remind me?

Andrew Downey

In terms of issuance we need to do?

Ian Smith

No, in terms of where we expect to get to.

Andrew Downey

I don't think we've given a percentage just because of that Pillar 2A delta. So we've always said that we would expect that Pillar 2A to come down and that's the only real bit of guidance in there.

Ian Smith

But we've given the range in terms of what we thought the total ought to be?

Andrew Downey

Ah right OK, I'll have to go and check that.

Ian Smith

Yes. We'll get that back to you afterwards in terms of where we're heading to and it's a range because of not yet having full clarity on where the Pillar 2A requirement will end up.

Jenny Cook

Any timing on when you will actually get that through?

Ian Smith

To get what through?

Jenny Cook

In terms of your Pillar 2A update coming through.

Ian Smith

So the Bank of England won't confirm our final MREL requirements until some way into next year. It's after we sort of get through the interim hurdle. But I think the range will specify this has got a sort of £600 to £700 million delta on it.

Aman Rakkar, Barclays

One more question. This is Aman from Barclays again. So thank you very much, you've provided some very helpful slides on the structural hedge, so I was just looking at one thing that I wanted to get your view on. Basically, if I look at your gross income, so slide 34 in your half year slides, gross income, £111 million. If I just compute that as a yield, it just looks quite low, so I think it comes in at about 90 bps or kind of 95 and maybe to 1%? So that yield hasn't really changed year-on-year to bench setting, even though you've got have higher base rates. Also, it looks relatively low versus some of your peers, so if I look at Lloyds they're just on full year, so I appreciate it's a bit of a quarter mismatch, their gross yield looks like something 170 bps.

I was just interested in do you think that yield is low and do you have any reason as to why you think that's low? Is that just a kind of heritage of the Lloyds book having been around a bit longer? Presumably your current account base has been around for quite a long time, so?

Ian Smith

Yes. Aman, I'll come back to you on the sort of absolutes, but I haven't actually looked across at Lloyds and understood what they're doing versus what we're doing, I mean I think they do stuff differently, but I haven't focused on that.

Aman Rakkar

I know they're a lot more dynamic in terms of putting hedges on. I guess it is a bunch of, you have a fairly mechanical approach to managing the hedge?

Ian Smith

Yes. We tend—I think some banks work quite hard at managing the impact of their structural hedge. We don't—it's a hedging tool to smooth volatility of income.

Aman Rakkar

Do you consider it as a management team? Do you observe that yield as being a bit lower than you'd like, in which you'd—is there any action you can take in terms of extending the duration or trying to extend the value of the assumptions on your balances or anything?

Ian Smith

We don't start from the point of view of maximising the impact, I guess. We start from the point of view of ensuring that we capture the balances that need to be hedged, and you know, as I say, use it as a tool for smoothing volatility. It's not something we focus on particularly, but I'll take your question away.

Rohith Chandra-Rajan, BAML

Rohith Chandra-Rajan, Bank of America, I wanted to ask about SME lending, I mean you were very clear that the redemptions were higher because of business disposals but the new flows actually held up very well, which is quite different I guess to what we're hearing from other banks, which are kind of saying that businesses are quite reticent about levering-up in the current economic uncertainty. So, I'm guessing that your new business flows are really the result of market share gains, and is that something you'd expect to continue, given this going uncertainty we have at play?

Ian Smith

Thanks Rohith. Yes, you're right. This is about winning customers. It's about—I suppose you take a step back, that atmosphere of lower confidence and reluctance to invest and hire, and that kind of thing, and therefore to lever up. That's a real feature. We do see that amongst the broader customer base and so, I think the growth of SME credit is relatively low system-wide.

The reason that we're taking market share and we're winning customers is I guess really a feature of where we are in the evolution of our business. For those that know our history, we essentially came out of that market for a bit of time, say 2010 through to 2014, and have been slowly rebuilding, I guess, our market presence there. We always used to talk about having about 12% to 15% share of liabilities in our sort of key markets in SME and more of a 5% to 7% share of assets. We're kind of working to rebuild that balance if you like, so this is about yeah, the new lending is winning customers, and that is still in what I think is quite a difficult business environment.

Rohith Chandra-Rajan

Thanks. Can I just ask on the funding side, how do you expect the funding mix to evolve in the second half and I guess, in particular, when you think of the full year, you anticipate refinancing about £1bn of TFS and you've obviously done £150 million in March so is that £1bn still the right number and what's the sort of mix, I guess, that you would look to refinance that in?

Ian Smith

Have we given that number?

Andrew Downey

Yes, we did say that.

Ian Smith

I sometimes forget what I've said and what I haven't said. Funding plan, there's a degree of flexibility with TFS. I think that one of you guys last week said why would you in the current environment, so I think we'll retain our flexibility and still have a plan to get ahead of the game on refinancing. And it's a mixture of—we've always said we would do 50/50 wholesale and customer deposits, that's still the broad plan, and so I'm not expecting to see a sort of dramatic change in mix.

Ed Firth, KBW

Ed Firth again, so just relating to that, your funding costs have spiked in the back end of last year along with the whole sector, but yours is, I guess it's quite a standout in terms of the extent. I mean, obviously it's come back now, but have you got a good sense as to what was driving that, and given that there's quite a wall of refinancing you've got to do over the next two to three years, how confident can we be or can you be, I guess, that we're not going to go through that again? What do you think was driving - so I guess it's pretty difficult for me to understand quite the extent of the spike and because of that, it's quite difficult to know why it's not going to happen again?

Ian Smith

Base rates. Really when you consider the sensitivity of our deposit book to -

Ed Firth

Yes but I'm thinking of things like AT1.

Ian Smith

Ah I see what you mean.

Ed Firth

The AT1 was 8 point, the AT1 was the most expensive AT1 anybody's ever done. I can't—looking at you, I can't quite see why that should be, and I should obviously speak to some fixed income people but I still don't have a good sense as to why that is, and what are the risks that people seem to be worried about?

Ian Smith

Yes, okay, I understand. You're focused on the headline rates of recent wholesale issuance, rather than the sort of broader cost of funding.

Ed Firth

And relating that to what that might cost you for MREL and re-financing for a TFS and all the other stuff you've got to do.

Ian Smith

Yes. AT1 was simply regarded as that was the market rate. That's kind of what we expected to be paying.

It's not a lot different from the extant AT1 that Virgin Money had issued some time ago, and so to see the cost of that creep up over the last two years, given what's happened to the cost of money in wholesale markets in general, I'm not particularly seeing a disconnect there. From recollection, I think the Virgin Money AT1 was 8.75% or something like that.

Ed Firth

Now, you're trading at like 150 basis points, 200 basis points tighter, and if you'd done it the first half of last year I guess it would have cost you 300 basis points less, something like that. It's not a criticism, I'm just trying to get a sense as to if we're looking out over the next two to three years you've been very clear that there's a lot of refinancing to do. That's obviously the sort of thing that people get very nervous about in terms of what it might cost you, and how that might impact the margin, and what are some of the drivers. I'll be honest with you, I'm just not clear in my own mind what is driving them. Is it Brexit, or—

Ian Smith

What's driving the broader—

Ed Firth

The cost and the volatility in the—

Ian Smith

Sorry Ed, I'm just trying to make sure I'm understanding the questions a little bit. So, I think if we accept that broadly wholesale cost of funds is increasing, so you would expect to see some general pressure on that. An AT1 issuance that is about 40 basis points to 50 basis points higher than something that was issued a good number of years ago in that environment isn't particularly a surprise.

Would it have been different at a different time? Don't know. I don't particularly focus on the cost impact of £250 million of AT1 issuance. You'll know that we have a call date coming up in July for a chunk of the Virgin Money AT1, so I'm not—I kind of don't think about it terribly much. It came in at what we expected it to be.

The Tier 2 issuance that we did in early December last year was, I think, just sort of particular circumstances. We wanted to get that Tier 2 done ahead of the end of 2018 for a number of reasons and given that markets were quite turbulent given what was happening on the Brexit front, and essentially there was quite a lot of the world having shut up shop for the year, we expected to pay a little bit more for that, and we did.

But I was pretty comfortable that we did it because we wanted to ensure that we had filled the, I guess the gap in the capital stack before what we thought was a period of potential further uncertainty and potential market closure. We had done—we'd been out of the capital and hybrid issuance market for pretty much most of 2018 because of the transaction. So, you just accept that in order to get it done you have to pay up a little bit. I'm not seeing that as a read across anywhere else. I think the sort of MREL market, the unsecured senior, the issuance that we're going to be doing on an annual basis is a much better read, I guess, of what we think our sort of wholesale funding costs are going to be, so I'd focus on that going through this year.

John Cronin, Goodbody

John Cronin, Goodbody, can I just come back on a couple of points? Firstly on the, I just want to labour the point of RWA density just in terms of the mixture that's going to Virgin's low margin business, presumably that will drive up risk weights and I know you've mentioned that there are some offsetting factors in the context of the definition of default and I presume the wider points.

What I'm also wondering about is you have called out previously that you have certain opportunities within niche segments of the mortgage market. Just trying to get a sense of what you think about that on a broad market level. We hear a lot of commentators talk about that, or at least lending into retirement, shared ownership, or what not, so just to get a sense of do you see an opportunity on that and actually would it drive an uplift in risk weights too. And then look, secondly just on the – actually you've said that.

Ian Smith

Okay. Look, John, we're not proposing to take a particular strategic fork in the road that will make a big difference in terms of the type of lending that we're doing to average risk weight densities. That's much more a sort of regulatory discussion, I guess, with the direction that we're going to take there. While we—so for example, we've developed bridging loan capability over the last wee while. So it's nice to have, and you'd like to see yourselves doing a few hundred million pounds business over the next three years on that. Definitely margin enhancing, but isn't really going to move the needle on risk weighted assets on average. Not flagging a particular change from mix of business however.

Andrew Downey

Shall we go to the phone and see if there are any questions on the line? Operator, can you ask for any Q&A on the line?

Coordinator

Thank you so much. [Operator instructions]. There are no incoming questions in the queue.

Andrew Downey

Okay.

Nicholas Herman, Citi

It's Nicholas Herman, from Citi again. Firstly, I know that you're somewhat limited to what you can say on the ISS, but you did say on the call that it was a good take-up so far to your offer. Are you able to say if there's any particular reason why you've seen particularly good share, or any reason you've done better than expected? Then, the second question just on the mortgage book, would you be able to provide any detail in terms of how much of the book is variable and SVR of the stock, that would be helpful.

Ian Smith

In terms of incentivised switching, yeah, I said we'd seen good interest in the offer. I'm fairly limited in what else I can say because that information still belongs to RBS if you like, until customers walk across the road. It felt like a decent start, albeit probably a bit slower than everyone expected.

In terms of just regional splits, I don't have that information in particular, but given that the vast majority of this customer base is the Williams and Glyn's heritage which is sort of Midlands and the North-West, it's a regional UK book, and that's one of the reasons why we think we're well-placed in that, because it's the kind of customer base that we work with in the regions so we're at least well-known and that sort of thing. In terms of the split of the book?

Andrew Downey

I'll come back to you on that one.

Any other questions in the room? Okay. Can we just give one last try on the phone? Any final questions on the line? Otherwise we're going to end it there.

Operator

There are no questions in the audio queue.

Andrew Downey

Okay. Okay, we will end it there. Hopefully that was useful everyone. See you at Capital Markets Day. Thank you.

[END OF CALL]