BofA 27th Annual Financials CEO Conference: VMUK Fireside Discussion – Meeting Transcript

Hosted by Rohith Chandra-Rajan (BofA, Analyst) and Clifford Abrahams (VMUK, CFO)

Rohith Chandra-Rajan, BofA

Thank you very much for joining us and for your stamina. This is the penultimate session, so thank you. Very pleased to welcome Clifford Abrahams, CFO of Virgin Money UK. In terms of the format of this session, Clifford's going to present to you. We'll then have some Q&A as usual, as you're more than accustomed to now. There are some tablets on your seats which you can submit questions through, and I'll very happily ask those as long as they're polite. Clifford, it's a pleasure to have you here.

Clifford Abrahams, Virgin Money UK Plc

Great to be here. I will say a few words; we thought having been where you're sitting on a few occasions, it would be useful to give you a few words about where we are as a business, something about the economy, and how pleased we are with our strategic execution. I'll only take five to ten minutes, and then we'll get into what I think will be a great Q&A with Rohith.

These slides are available on our website. If I turn to slide 2, you can see here an update that we gave at our Q3, which is August this year - we have a September year end. You can see at Q3, we were pleased with our strategic and financial momentum as new propositions dropped and we're delivering on our digital transformation.

This progress meant that we delivered and printed a year-to-date return on equity of nearly 10%, so we were pleased with that strong performance and good momentum. Now turning to our strategy, I've set out here the themes around our equity story. This reflects the update that we gave in November last year; really our post-COVID strategic recalibration.

That story, that strategy is around consolidating our resilient balance sheet, progressing our digital transformation following the integration of Virgin Money, and delivering on profitable growth. We feel we're making good progress on each of these elements, and I'll update on each of those over the next few slides.

But first, I just want to comment on the economy, which is a topic of much interest to all of us at this conference. You can see here, our latest economic outlook. We rely on Oxford Economics for our macroeconomic projections, but it's more or less in line with consensus. As we all know, the outlook for inflation has picked up over recent months. We can debate whether it's peaking or peaked, but it's certainly elevated. This has led to tightening of monetary policy, notably today, and in particular, increasing interest rate expectations. I've set out here on the top right interest rates that we saw at Q3, so in August, and currently and you can see quite some step up. As we all know, interest rates picked up further today, and that's a tailwind to the guidance that we gave at Q3, which reflected interest rates at that time.

Now, I think consensus and certainly our view is that unemployment will remain moderate through this cycle, and that underpins our confidence in asset quality, and I'll talk about that a little bit more in the next few slides. But also, we expect in the next 48 hours or so, further action from the new government led by our new prime minister, which will, again, I think make the really severe outcomes that we were worried about a few quarters ago less and less likely.

Now, turning to our balance sheet, there's quite a lot of data on this slide, but I think the highlights are clear enough. We have a defensive balance sheet with 80% comprising of mortgages with loan-to-values of just over 50% on average. Clearly, we're monitoring our customers for signs of stress given the cost-of-living issues, and we're not seeing increases in arrears as yet, which I know you've heard from many CFOs and CEOs here.

I'd highlight our CET1 ratio of nearly 15% that we printed at Q3, and that sets a very strong foundation for our recently announced capital distribution framework; a dividend pay-out of 30% with scope for buybacks. I'm pleased that we announced our first buyback in June this year of £75 million. We're making good progress in execution, and we said in August that we would consider a possible top up at the end of our financial year, and we'll update clearly on that in November.

Now, moving on to our progress on digitisation. I think in common with many banks, we're digitising at pace. We set out our clear goals in November last year, and we're making good progress. I've set out here our progress and also our ambitions for '24. That's on track and underpins our cost savings target of £175 million; we're making good progress on that. This digital investment also underpins our proposition delivery as we're very much focused on our digital customer strategy.

On the next slide, I've given the highlights of our pipeline of products. Following the merger, we substantially integrated a little over a year ago, we've launched a series of new, refreshed digital propositions. A number of them have landed and a number of them are landing now. We find this a really exciting development and should give us profitable growth momentum, notwithstanding the uncertain macro environment.

We're pleased with our buy-now-pay-later proposition which we announced over the summer. We've talked a lot about our digital wallet. You'll see the first iteration of that this calendar year.

Finally, guidance. I'm sure we'll talk about guidance during the Q&A. I've set out here our guidance for the full year, that's full year '22, and also our medium-term outlook where we're focused on delivering our targets for full year '24, and in particular, our return on equity target of double digits. Thanks for your attention. I'm happy to take questions from Rohith.

Rohith Chandra-Rajan, BofA

Thank you very much for that, Clifford. I guess starting on strategy, as you said, it was refreshed November last year, but essentially, it's been pretty consistent since 2019. And it's really about balance sheet mix to improve profitability as well as cost and capital efficiency. The macro environment, as you just discussed, has not only changed since 2019 many times, but it's also moved very quickly since November last year.

What does the impact of higher rates and higher inflation and arguably a weaker economic outlook mean for Virgin Money's profitability in the near and medium term?

Clifford Abrahams, Virgin Money UK Plc

Thank you. We set out in November our commitment to 10%+ returns, and we were looking to deliver that by growing in unsecured and business, delivering our cost savings, in particular our 50% target cost-to-income ratio. That was really the north star that we set out in November last year. We've seen clearly increasing rates since then, and we've been a beneficiary of that. Our NIM has performed above our expectations that we set out in November.

We recognise that the economy is weaker than we'd considered, but we feel confident about the defensive nature of our balance sheet, still 80% mortgages. We retain much of the provisions that we set aside during COVID and in particular on costs, we're benefiting from the program of investment we announced in November. We targeted £175 million of cost savings. We're on track to deliver that. So, notwithstanding inflation, we do expect costs to come down in nominal terms over this period. That, all together, gives us the confidence, that we reconfirmed our targets are on track when we announced our trading statement in Q3 earlier this year.

Rohith Chandra-Rajan, BofA

Thank you. We turn then to balance sheet mix which is a significant part of the strategy. There's been a lot of progress on the funding side of things, particularly the deposit mix has improved substantially, largely reflecting the broader trends in the market. In fact, the market in terms of mix seems to have stabilised. In terms of your own funding mix, how do you see that evolving from here?

Clifford Abrahams, Virgin Money UK Plc

We set out our strategy at the time of the merger, coming together to develop what we call relationship deposits, so these are personal current accounts and business current accounts and related balances. We're really pleased to see that, having developed over those three years from around a third of our balance sheet to just over half.

That had benefited from the COVID liquidity benefit, but we've seen some structural shift during that process and that's delivered our cost of deposits of around 50 basis points in Q3. That's a lot less than swaps and base rates at that time. We're seeing good growth in both personal current accounts and business current accounts since then. I would say we are a long way through the transition to maturing the balance sheet on the liability side, but we still have some headroom to go.

Rohith Chandra-Rajan, BofA

On the asset side, that's proved a little bit harder in terms of changing the mix, and arguably economic conditions really haven't helped in terms of credit demand and quality credit demand. Do you still anticipate a material change in the loan mix by 2024? And I guess breaking that down, credit cards seems to have been going very well, but how do you move the dial in terms of business lending, and perhaps digital is an important part of that?

Clifford Abrahams, Virgin Money UK Plc

We have, as you say, we're looking to increase the mix of unsecured and business and reduce the overall weight of mortgages on our balance sheet really to make our capital work harder. We've been pleased with unsecured. The personal sector has been strong through COVID, and spending has continued in a robust fashion since the lockdown came off.

The business side has been a bit more difficult to deliver growth. We've been working against the headwind of guaranteed balances coming down, so we, like other banks, lent money with the government guarantee; a little over a billion for us, and many of those customers took on those loans as a sort of liquidity buffer and have looked to pay that back. What we've managed to do over the past few quarters is, as that shrunk, as the guaranteed portion shrunk, we've grown our franchise business, broadly offsetting that. I'm confident that, that unwinding of the guaranteed portion of the lending has largely slowed, so you'll see the benefit of franchise growth coming through.

It's fair to say that the market for business lending has contracted in the UK over the last few quarters and business confidence is clearly suffering somewhat from current uncertainties. What gives me confidence that we can grow that business book for the mid-single digits is the strength of our specialised lending franchise. We have a market share of 2 to 3%, but we have much higher market shares in our specialist segments, agriculture being one, nursing homes. There we have real expertise, a real franchise, and a brand. Our relationship managers have been back on the road since early February this year and the pipeline is building nicely. So, we think we can grow that profitably in coming quarters and you'll see the benefit of that as we print in due course.

Rohith Chandra-Rajan, BofA

Thank you. And then, credit quality's been a key feature of so many discussions here over the last three days, and broadly in the market much longer than that. You're not flagging any near-term deterioration in credit quality. When I look at your IFRS 9 disclosure, your downside scenario again indicates very little need for additional provisions.

Given that we've got a weaker macro picture and usually one that would result in a spike in loan losses, what gives you confidence that we won't see that this time?

Clifford Abrahams, Virgin Money UK Plc

Overall, we are defensively positioned, so around 80% of our balance sheet is mortgages with very strong collateral. I think the number of questions I've had have been primarily on the unsecured side and to some extent on business. I think on unsecured, I think you guys would be aware that we're coming from a background where we've been skewed to the upside in terms of our affluent customer base.

Our borrowers tend to be in their 40s. They're more likely to be homeowners. Over two-thirds are homeowners compared to somewhat less than that for the general market. They tend to have incomes that are higher than market average, over £40,000. And so, we can see looking back that we've outperformed in terms of credit.

I think the metric that I'm certainly focused on is around unemployment. You saw from the figures that I highlighted that unemployment is still historically low despite the weakening economy, but it's projected to remain say around 5%. And I think unemployment would have to spike higher than that to give a genuine cause for concern around unsecured. The business book is resilient, and it was de-risked considerably five or ten years ago as Clydesdale came out of NAB. It has good diversification. It's had defensive underwriting in place for many years.

And then stepping back and looking at our provision levels, I think I mentioned during my remarks that we're still materially above our provision coverage that we had pre-pandemic. Now we'll have to obviously look at that, the full year, but that should give a confidence in cost of risk in coming quarters.

Rohith Chandra-Rajan, BofA

Let's dig into a couple of those areas a little bit more. The credit cards book has been growing very nicely, probably a little bit ahead of market.

You commented that it's an affluent book and people have mortgages, etcetera. Has your underwriting criteria changed at all over the last 12 to 18 months?

Clifford Abrahams, Virgin Money UK Plc

Yes, it has. We tightened up on our underwriting in the early days of COVID. We measure that, we give percentages, we tightened it up by around 40%[1]. So, we did that going into COVID. We were quite early doing that. Nonetheless, we grew the book quite strongly during COVID because the personal sector was robust, as we all know.

We tightened our criteria further early this year by 10% or so as we saw cost-of-living pressures building up. It's clear that we moderated our underwriting criteria to reflect these cost-of-living pressures. All of that is before the intervention of the new administration. We'll see the details of that in coming days. But that, combined with that low unemployment gives me comfort that these will represent good vintages going forward.

Rohith Chandra-Rajan, BofA

And linked to that there's a few questions coming through from the audience on your buy-now-pay-later strategy recently launched. I guess, concerns around the credit quality of buy-now-pay-later have been rising recently. The question really is, is now the right time to do buy-now-pay-later, and how are you ensuring you're writing the right business?

Clifford Abrahams, Virgin Money UK Plc

Our proposition, you can see it on the website, it's sort of a buy-now-pay-later type proposition, but it will be credit scored and customers will get an app and they'll be able to manage multiple purchases within that app. They and we will be able to see their exposure to all their purchases, not just individually, which I think is some of the weaknesses of the current buy-now-pay-later proposition.

We've announced that. We've actually now got a wait list for that product of tens of thousands. The first customers will be able to use the product in a low number of weeks, and we'll start things off in quite a gentle fashion reflective of the macroenvironment. We'll want to see how customers use it. We want to leverage some of the new developments; we're working with Experian, our credit specialist provider there. They're bringing to the table new and interesting information that's relevant for these sorts of customers, these

[1] Updated for clarity

younger customers. So, their subscriptions, for example, that gives true credit information, but is not something that's typically used for credit scoring. This is an unashamed innovation. We think it's got quite a lot of attention and quite a lot of customer interest already, but we'll take a prudent approach to underwriting and building of balances reflective of the macro environment.

Rohith Chandra-Rajan, BofA

And then, on the business side you mentioned some of the areas of specialism earlier. One of them was agriculture. A couple of the other banks we've heard from previously have said that that's a sector they're watching particularly closely. Obviously import costs there are going up a lot. Can you talk about how you're managing that and how you're seeing customers behave?

Clifford Abrahams, Virgin Money UK Plc

We have a business book of about £8 billion and agriculture represents a little over a billion. So, it's a decent part of that portfolio, and it's also a sector where we have around 10% market share. So, we are a leading franchise. I think it's well known that import prices have risen. Russia and Ukraine being the key suppliers of fertiliser, for example. I think we've all found going shopping much of that import pressure is being passed on in the form of rising prices, rising food prices.

And equally, the government has been quite careful to manage the transition through Brexit to support cashflow of the agricultural sector. I think it's fair to say that the agricultural sector has surprised to the upside in terms of credit resilience over the last 12 months or so. So that's actually one sector I'm not so worried about.

Rohith Chandra-Rajan, BofA

Moving on to income. You mentioned in your presentation that you highlighted at Q3 that the full year NIM guidance has been improved slightly, so moderating decline that you're expecting for the second half of the year. What is it that's made you a little more optimistic on the second half of the year? And I guess perhaps more importantly, how do you see the margin evolving this year if the BOE continues to hike quite aggressively?

Clifford Abrahams, Virgin Money UK Plc

We've consistently upgraded our NIM guidance through the year, and at the half year we set out our guidance of 180 to 185. We got quite a lot of challenge at the low end actually, and at Q3 in August, we reconfirmed around 185 basis points. What had changed over those three months, I think, had been further increases in rates. We're seeing that continue today.

We've seen some recovery in spreads on mortgages over the summer, as swap rate increases moderated, and so customer rates outpaced swap rate increases. You saw many competitors are talking about 100 basis points plus in terms of application spreads, so that was a positive development. And we saw the continuing low deposit betas. That was through, between May and August, and August was the time of our Q3 guidance.

We said at Q3 we expected NIM for the full year to be around 185 and to be sort of stabilising into next year. I think it's fair to say the rates have moved sharply up since that August guidance was given. I showed the figures in my little presentation, around 100 basis points.

Rohith Chandra-Rajan, BofA

I think that's higher again today.

Clifford Abrahams, Virgin Money UK Plc

Indeed. So that will be a tailwind primarily into next year. We've now got less than two weeks for us to the end of our financial year. I think, at the same time, it's fair to say that the mortgage spreads have tightened as swap rates spiked in recent weeks. But I think the experience in the early part of the summer gives me confidence that over time the mortgage market in the UK acts rationally and sort of triple digit mortgage spreads are a reasonable basis to assume going forward.

Rohith Chandra-Rajan, BofA

On that last point, as you say, we had swap rates move up very sharply in the second half of August. If I've understood you correctly, you think it's just a timing thing, that it takes a while to raise mortgage rates and that they will ultimately will catch up?

Clifford Abrahams, Virgin Money UK Plc

I get daily updates on competitor action, and typically you see us and other competitors, when they choose to raise rates they'll do it by double digit basis points, 10, 20, 30 basis points. We've seen 50 basis points[2] today. That will take a little bit of time to digest, I think, by the market. So, you tend to see when rates increase sharply, you'll see that come through in swaps, which you commented on. You'll see a tightening of spreads in the short term, and then gradually widening over time. What that means, in my view, it means that rates have spiked. As that rate of increase moderates and stabilises, that gives the market breathing space to digest swap increases, widening mortgage spreads, and gives me confidence in call it a medium-term outlook in mortgage spreads.

Rohith Chandra-Rajan, BofA

And then something that we were talking about just before this, and the audience have also asked about, is this recent market focus, something that the market has been discussing for a while but re-emerged recently, in particular, I guess ahead of tomorrow's announcements, in terms of remuneration of deposits at the Bank of England.

Just interested to get your thoughts on how that might work as a policy, and then also what the implications for Virgin Money would be?

Clifford Abrahams, Virgin Money UK Plc

We spent a little bit of time talking about that with investors in smaller groups today. The background is Europe where actually the remuneration of deposits and tiering works the other way, where it was a mechanism to support the banking sector. I think the idea here in the UK will be the other way around. It will be an opportunity – I kind of call it a stealth tax for want of a better word. It's clearly up to the administration to propose what they think makes sense.

It strikes me that this will be quite a material development for banking markets, wholesale markets, and debt markets generally at a time when the new administration is looking to lean more heavily on such markets. That any material change such as this, I would expect would come with a period of heavy consultation before and I note that that hasn't been the case. We'll see. I mean, never say never, but it doesn't seem like an idea that would be imminently implemented in my view. I think in terms of how we'd respond to it, we keep considerable balances in the Bank of England. That's a safe place to keep it and has not suffered in terms of financial penalty.

If that changed, we'd have to revisit that, and we would have to look at how much money we'd need to keep there that's strictly needed and how much we could reallocate to other liquid assets. I've seen some of the figures from the sell-side, but typically they would assume, call it no management action in that circumstance. So, I'm pretty sanguine about it and we'll just look forward to seeing what's announced tomorrow.

Rohith Chandra-Rajan, BofA

And is there a cost to reallocating to other liquid assets, so those liquid assets would count towards your leverage ratio, for example?

Clifford Abrahams, Virgin Money UK Plc

We'd have to work through that, but in our case, our capital constraint is our CET1 ratio. Our leverage is pretty comfortable. We'd have to work through all that, but I know from experience the sort of consultation, for

[2] Bank Base Rate

example, the Bank of England has done when there have been changes, and I take comfort from that that we've got responsible authorities.

Rohith Chandra-Rajan, BofA

And then on costs, again, you mentioned the £175 million of gross cost savings which you've recommitted to. You also mentioned inflation. You also mentioned 50% cost income ratio. How should we think about you managing those three things I guess, cost cutting, inflation, and a cost income ratio over the coming years?

Clifford Abrahams, Virgin Money UK Plc

We're really committed on delivering on the things within our control, and in particular our 10%+ ROE target in full year '24. We're very much on track for that. That's underpinned by our target of 50% or less cost income ratio. In November last year, we pivoted to a ROE target and a cost income ratio target as we felt that was more suitable for a growth bank in an inflationary environment.

We did announce a nominal spend and a nominal cost savings of £175 million, and we said we'd reinvest around half of that in growth and inflation. Clearly, inflation has picked up, so we expect more of that £175 million to be absorbed by inflation. We still expect costs to come down in nominal terms. And clearly, with the inflation high, our base rate's higher, we're seeing the benefit of that come through in our net interest margin and that underpins our confidence in the 50% cost income ratio and 10%+ statutory ROE that we expect to deliver in full year '24.

Rohith Chandra-Rajan, BofA

So, the £175 million cost cuts plus the revenue benefits from high rates margin expansion should get you to the 50% cost income?

Clifford Abrahams, Virgin Money UK Plc

Yes, notwithstanding inflation.

Rohith Chandra-Rajan, BofA

Another question from the audience which ties some of the previous parts of the discussion together I guess is thinking about mortgage rates, mortgage affordability, the housing market; there may or may not be a cut to stamp duty tomorrow. In summary, how do you see the UK housing market evolving, mortgage volumes, and mortgage affordability and any credit risk around that?

Clifford Abrahams, Virgin Money UK Plc

I think, clearly, history is important. We've seen strong HPI performance, really since the great financial crisis and right the way through COVID. All banks, including us, are sitting on really quite low LTVs. Right now, it's a little bit over 50%. We underwrite a mix of variable and fixed rate, so we see that recycling over time. Around a quarter of our business is available for repricing and would reprice each year onto higher rates.

The underwriting that we've done, influenced by regulation, has been pretty prudent right the way through the period post-great financial crisis. The stress test that we look at, the limits on borrowing to income are pretty prudent and we've benefited from that. I think the sector has benefited from that. I would say, going forward, I expect house prices to moderate. It's possible that house prices come down in nominal terms. We see that from Oxford Economics.

My view is it's more likely you'll see house prices coming down in real terms as inflation and wage inflation outpaces nominal pricing. I think we'll continue to benefit from a housing market point of view from low supply and first-time buyers, including my children for example, benefit from the bank of mum and dad as the ultimate subordinated lenders. And there's a huge generational transfer that's expected to take place. So, I think that will support first-time buyers and the housing market during this period. I think if unemployment remains low, that will underpin confidence in the housing market and the mortgage market. Certainly, my view is some moderation of house price inflation is a good thing in coming years from a society, generational perspective and even a macroeconomic perspective.

Rohith Chandra-Rajan, BofA

And just in terms of the stresses that you do on origination, I guess mortgage rates that you see on offer today are already three times what they were two years ago and likely to go higher. Potentially, we're looking at 4% mortgage rates today, arguably we could be in a 5 to 7% range at some point in the next year or so. Would that be within the range of stress that you've factored in?

Clifford Abrahams, Virgin Money UK Plc

That's broadly in the range. I mean we had income multiples, there've been limits on the proportion of mortgages on our book and the industry's book, both income multiples, that's an important strain, and in terms of stressing, not just us but the industry looked at stresses beyond SVR, standard variable rate. And those stressed rates are in excess of the numbers that you just indicated. So I think we, together with the industry, prudently managed underwriting during this period.

Rohith Chandra-Rajan, BofA

And the quarter of the book you mentioned refinances each year indicates that your fixed rates are relatively longer-term fixed rates?

Clifford Abrahams, Virgin Money UK Plc

It's a mix. It's a mix of two years and five years is typically what we see. You see a range and that quarter reflects that blend.

Rohith Chandra-Rajan, BofA

Capital distribution, a relatively new thing for Virgin Money and has been taken positively by the market. You still have a 14.8 percent CET1 ratio, well above your 13 to 13.5% target. The market was concerned initially when there was an expectation that you'd start the buybacks, then didn't because of economic uncertainty and a number of other factors.

It still feels like we're in uncertain times. How should we think about, is this the sort of market where you're happy doing a buyback with full year results, for example, and how should we think about dividends and the pace of buybacks, not just for this year, but going forward in terms of distribution strategy?

Clifford Abrahams, Virgin Money UK Plc

We recognise our capital distribution approach needs to season. We need to build a track record. I think at the time of our half year results in May, we talked about our distributions in principle, but weren't in a position to pre-announce a buyback. Reflecting that, in the period leading up to our results was the time when Russia and Ukraine was just flaring up and macro uncertainty was, I think at its highest.

We were pleased to announce the inaugural buyback in June, not long afterwards. At our August Q3 trading update, we said we would revisit a buyback and consider whether a top up was reasonable in November alongside our full year results. And so, we expect buybacks to be a sustainable feature of our capital distribution approach. Our 30% pay-out ratio enables us to continue to growth the business profitably but given our 10%+ returns, we would expect to continue to accumulate capital and that would fuel sustainable buybacks. What we would like to do is to deliver buybacks consistently and given where we're trading - we're trading around half book - represents really an attractive way to return capital to investors and it's something that we would expect to continue.

I can't pre-empt the decision we'll make at year-end, but we were clear from our statement in August that it's very much on the table for consideration at this year-end.

Rohith Chandra-Rajan, BofA

Can we go back to rates, given just how sensitive the sector is and you're arguably less sensitive than some of the other UK banks as a function of your balance sheet mix. It seems that actually most of the sensitivity comes through the structural hedge, which means it takes a bit longer to come through than it might for some of the other banks. Could you just talk us through I guess how you think about rate sensitivity, what the key drivers are? And I think you also assume a 50% deposit pass through? What's been the experience to date, which I think has been better, and how do you see that changing?

Clifford Abrahams, Virgin Money UK Plc

That's right. I think we've been in a situation where we've delivered more interest rate sensitivity than we've guided, frankly, consistently through the year. So, in Q4 '21 we printed 170 basis points of NIM, and in Q3 '22 we delivered 187 basis points of NIM, so that's 17 basis points. And that outpaced our interest rate sensitivities essentially, and that reflects consistently rising rates and we've seen rates continue and also, that low deposit beta. If you look at our interest rate sensitivities that we disclosed, it's around half from the structural hedge, and that earn through over time. And around half from, call it, the interest rate lag, and that's very much a short-term benefit. And what we've seen with the deposit beta as low as it has been, we've seen that interest rate lag really outperforming.

So, that's benefited us in the short-term, but in the long-term, that structural hedge will earn through. We're currently yielding around 50 basis points[3] on the structural hedge of £32 billion and with five-year swaps that are near 4% now, you can see a very strong tailwind of earnings coming through even if rates stay as they are.

I think we all feel the structurally Virgin Money is less rate sensitive than some of the bigger peers, but in practice, we've delivered quite some interest rate sensitivity over previous quarters. I think our approach is to be transparent so people can sort of figure it out for themselves.

We felt that the COVID-related balances would unwind, we haven't seen that. We feel that the deposit beta would normalise to around 50% and we haven't seen that. We felt that rates had gone up and we'd looked at the existing money markets, but actually we've seen rates continuing to pick up. So, we're in this sweet spot where net interest margin has had quite some tailwinds, but we've yet to see, may not see, the adverse consequences of all of that coming through our credit quality.

Rohith Chandra-Rajan, BofA

Is there a level of rates that would cause you concern from a credit quality perspective?

Clifford Abrahams, Virgin Money UK Plc

I think we've talked about rate pressure on mortgage holders. I think it's clear that the business sector and indeed the personal sector has entered this recession with quite strong liquidity buffers. But clearly, if rates spike a lot higher from here, that will stress some of our customer base. I think we take comfort from a few things; one, the strong credit quality across the portfolios that I mentioned earlier, and also the action the government looks like they're taking. So, they're taking action on not just on supporting vulnerable sectors, but also in trying to address some of the drivers of inflation, which is a sort of lead indicator of base rates. So, we'll see. We're not immune to these effects, but we've demonstrated resilience to date, and we feel resilient going forward.

Rohith Chandra-Rajan, BofA

That's been great, Clifford.

Clifford Abrahams, Virgin Money UK Plc

Thanks. Nice to speak to you.

[END]

[3] As at H1 2022