VIRGIN MONEY UK PLC FY19 RESULTS – Analyst Call

Hosted by: David Duffy (CEO), Ian Smith (CFO) and Lucy Dimes (Head of Group Business Transformation)

David Duffy, Virgin Money UK PLC

Welcome everyone, good morning. Thank you to all of you managed to join us in person, and welcome to everyone on the webcast and on the call, and good evening to all our Australian investors. Today is a little bit of a special day because it's the first set of results for Virgin Money, combining both CYBG and Virgin Money under the rebranded Virgin Money UK PLC.

I think we'll split it into four headings today. We're expecting to take no longer than 40 minutes, followed by Q&A. I will walk you through some of the highlights of the past year, then Ian will take you through some of the financial results. Then I'll ask Lucy Dimes, our Group Business Transformation Officer and the newest member of our leadership team, to talk to you about the next steps in our integration, but more importantly, what Lucy is doing, together with Ian and Fraser, to deliver the broader business transformation. Finally, I'll come back and share my views on the outlook for the business in the years ahead.

So, before I address the highlights of the year, some of which you will see here, I would like to take a moment to recognise that this has been a tough year for our investors. We have announced a statutory loss today after absorbing the PPI provision, and our performance has also been hindered a little by a weaker macro environment, and as you know, margin pressures due to ring-fencing and mortgage competition.

Whilst the macro environment is one challenge we all face, I was personally very frustrated at the scale of provisions that had to be set aside for the final phase of PPI. I think that while most banks suffered in a similar manner, I know that's of cold comfort to our shareholders. But as you know, it's something that's outside of our control, but the consequences of the size of the provision are very real for our investors.

Now, we are at the passing of the time bar deadline and we've committed to remediating our eligible customers in a timely manner, and I think we mustn't forget that customers have suffered here too. But this legacy issue, which has been very frustrating for our customers and our shareholders, should now be fading into the past.

With regards to provisions, we have assessed a good proportion of the PPI information requests, which has given rise to the provision in Q4. I think I've confidence in the provisions we have taken, because we're dealing with the results of claims processing that we control. So, it's much more we control, rather than trying to estimate the incoming volume of information requests, which was much more difficult to control. However, I'll leave it to Ian to take you through our detailed assumptions on this subject a little bit later.

We've also taken the difficult decision to suspend our dividend in 2019. Again, this is disappointing for our shareholders, but we felt that this was an appropriately conservative decision to take in the circumstances. That being said, we will reconsider our dividends for 2020, in line with normal practice. However, notwithstanding the provision and the discussion, I believe that our robust capital provision with a CET1 ratio of 13.3% provides us with sufficient capital and resources to deliver on our strategy.

If I can now maybe turn to the underlying performance of the business. Overall, I'm very pleased that we've delivered a resilient operating performance, and that's despite several complex headwinds in the marketplace. Our income has held up well, I think in the face of a very competitive environment, and whilst our NIM declined due to continued pressure from the mortgage book churn, we do anticipate a stabilisation of that NIM as we move into 2020. Obviously, the markets that we're operating in, as you know, still carry a degree of volatility, and therefore uncertainty.

If you look at our three lines of business, they've all performed well, and we've seen good growth across the portfolio with above market asset growth in Business and Personal, as we've highlighted, disciplined growth in Mortgages. And importantly, at the same time, our asset quality has remained resilient and stable.

As you've heard us say before, our Business lending is sector driven, and when supported by 300 plus relationship managers with an average of 14 years' experience and this sector expertise is very important in maintaining the quality of the Business lending that we originate. And it is worth remembering, especially in the context of today's climate, that we do not lend to high street retail or to commercial real estate.

Similarly, most of our growth in unsecured lending is driven by Virgin Money's more affluent higher quality credit card book and in personal loans, we've seen good growth in our salary deducted loan offering through our Salary Finance joint venture.

We've also in the past year, talked a lot about our liability strategy, and it was encouraging to see that the overall deposit growth of 4.6% was strong, and partly achieved through good growth in our lower cost relationship deposits. Ian will talk more about that later.

Apart from the growth and the funding of the business, a key part of our strategy is the ability to achieve this growth whilst managing to reduce costs. We have delivered £53 million in run rate net cost savings this year, and our 2019 costs are within guidance. Encouragingly as well, we remain on track to deliver our overall envelope of our cost target, which is less than £780 million by the end of 2022.

The integration programme is going well. It's on track and I was especially pleased that we're able to complete the Part VII process faster than we had initially expected. And that means that we're now able to move forward on the integration of our customer platforms, which as you know, supports our cost saving and other commercial ambitions.

As I've said, the leadership team and I, particularly, have been quite frustrated by the PPI outcome, but we haven't let it distract us and we remain focused on the strength of our underlying business. I think that we have delivered well on the initiatives this year, where the outcome was in our control. For example, we've completed the process of the acquisition of Virgin Money, including the Part VII approval, we've achieved IRB accreditation and announced, as you know, our medium-term strategy and targets at our Capital Markets Day.

In parallel, we also developed our strong technology platform and product capabilities. For example, we executed joint ventures with Aberdeen Standard Life and Salary Finance and launched the GoCompare utility switching capability. While Aberdeen Standard Life, is still in its early stages, Salary Finance was responsible for around 25% of our growth in personal loans during the year.

Our utility app is interesting. It's proven a demand for what we'd call beyond banking services, and has saved, in the pilot test, an average of £290 per customer. And this GoCompare capability will actually be included in our new Virgin Money app launch in December, which we'll talk about in a minute.

From an internal perspective, I'm actually quite proud of the way the organisation came together to deliver our purpose and values. More than 2,000 of our colleagues have input into this work, which is now being embedded in literally everything that we do. And the success of that initiative has had a positive impact on the critical mission of integrating our two cultures, which we can evidence by our engagement score of 76% for the combined group, and that is after all of the work we did on integration and everything else.

As I said, I think this has been a good year for delivery on key initiatives, but we've also, at the same time, had to address substantial material legacy issues, which as I've said are now coming to a close. In addition to all of that work, we had the Part VII approval and we had to manage two entirely separate banks, plus four brands during that period and the combination of these activities actually drew quite heavily on the management resources. And that being said, I think we're now in a position where the bank is at an inflection point. In the next few years, the leadership team will be able to focus on delivering our targets that we've talked about, rather than managing legacy issues or the complexity of an acquisition.

We'll be, in simple terms, managing one bank with one brand, one technology platform, and a culture defined by our agreed purpose and values, and the overall envelope of a clear strategy to deliver double digit returns for our shareholders. To understand the details of how we'll do this, let me now hand you over to Ian to review our financial performance. Thank you.

Ian Smith, Virgin Money UK PLC

Thanks, David, and good morning everyone, and good evening to those listening in from Australia, it's good to be talking to you again. So I think the snapshot of the first year of the combined business tells a pretty good story of the operating performance of the business, and early progress against the strategy we announced on the 19th June this year.

Now I won't stray too far out of my comfort zone by talking about non-financial measures here, I'll leave that to my colleagues, but suffice to say that we're very focused on winning in the key battleground of customer experience and our people are up for the fight.

We saw good growth in Business and Personal lending, while taking a measured approach to the mortgage market. And we grew deposits faster than lending, supported by good growth in all-important relationship deposit balances.

We hit our net interest margin guidance and delivered positive jaws with a strong performance on costs. We saw higher cost of risk year-on-year - and we explained that at the interims - which was due to a combination of asset mix, IFRS9, and a return to normalised levels of impairment.

However, the surge in PPI towards the end of the financial year was a real kick in the teeth and tipped us into making a loss for 2019. But the KPI that I draw attention to on this page is our underlying return on tangible equity of 10.8%. That's a pretty good outcome from the core business. Now I know that it's underlying, but I think it's a relevant benchmark, given the clear path to converging underlying and statutory profits by 2022. And now I'll take you through the numbers in a bit more detail.

The core business operating performance has been solid. We hit all of our operating targets, and I think that we're more than holding our own in the testing environment. Macro, competition, legacy and the requirement to run two separate banks made for a demanding year. But against that backdrop, we offset income pressure with a good cost outturn, ahead of where we plan to be, and this drove positive jaws.

Impairment charges increased, as anticipated, and that drove underlying PBT below last year's number. And all of our underlying efficiency, return and earnings KPIs are solid. One point I should mention here though is the bank levy, as I won't talk about it anywhere else. The acquisition of Virgin Money brought us within scope of the bank levy for the first time. It's not a number we can really influence; it's a tax, I'm just not allowed to put it in the tax line. And it's going to be with us until either the government decides that the banks have done their bit, or hell freezes over. However, it's not a big number for us, unlike the other major banks, and it doesn't grow much bigger in the foreseeable future.

As you're aware, we have significant exceptional costs related to the acquisition and integration of Virgin Money, and very disappointingly, legacy conduct where we took additional PPI provisions of £385 million at the year-end giving total PPI costs of £415 million for the year. There are some big numbers here, £804 million in aggregate, driving the loss for the year, but if we take a step back, there are more than £500 million of charges here that we just don't expect to see again.

Our TNAV per share reduced by 11 pence. We saw net TNAV build in the year, even after substantial acquisition integration costs that was overwhelmed by PPI.

At the interims, we talked about how a portion of restructuring and acquisition costs are one-off in nature, and as we can see here, the second half was all about restructuring and the unwind of acquisition accounting adjustments. I'll explain later the basis of the restructuring costs incurred in the year. We did more than we planned. And the acquisition accounting unwind was lower in the second half, because we've seen lower attrition in lending, and we've gone a bit faster on TFS repayment. The important thing to emphasise is that for both items overall, or rather the overall cost estimate has not changed, even if the phasing is a little different than planned.

Since we made our announcement on the range of potential additional PPI costs in early September, we've done a great deal of work to settle on our estimate of the provision at £385 million. And I'm going to walk through how we've landed on this number. We think this is a realistic and sensible estimate, and the estimation risk in setting this provision is lower than it has ever been.

In September, we highlighted that there were two key drivers of the costs. One was the rate at which information requests were expected to convert to claims. And two, the time and cost to process the claims and each of those was a major uncertainty at that stage.

The work we've done in the last three months has indicated a conversion ratio of 9% on the circa 410,000 information requests received and that's around the middle of the range we estimated. We deployed some smart technology to eliminate duplicate requests and to sort through more than half of the residual IR population, looking for PPI markers.

This stage is around £25 million of IR processing costs, compared to our original estimate and where we couldn't process the IRs digitally, we undertook further sampling. We've developed an operational plan that's been approved by the regulator to process the requests and resultant claims, between now and the end of September 2020. And that has allowed us to firm up our estimate of operational costs.

So what we're working with now is a fixed number of outstanding claims to process, an IR population that has been well scrubbed to establish a conversion rate, and a clear operational plan to process the claims. The major assumptions that we use to assess PPI claims costs, such as uphold rates, redress amounts, and costs to do, are well understood and stable and we're not baking in any improvements to these values.

The main source of estimation risk in the past where we got it wrong has been the number of complaints coming through the door. That door is now closed and the principal source of estimation risk is a rate at which the 325,000 IRs we're currently working through convert into actual complaints that we have to remediate. So, that's the £175 million bucket.

Now, the digital processing has already identified the number of complaints to be validated for over half of the population, meaning that the estimation risk remains on the 150,000 that we couldn't process digitally. However, our sampling gives us a good level of confidence that our assumptions are appropriate.

Now while the conclusion of PPI has been unexpectedly painful for our shareholders and the company, it feels that we're putting this damaging legacy item behind us and we can focus wholly on delivering the strategy and generating good returns for shareholders on a statutory basis.

So, turning to business performance, deposit growth outstripped lending this year and the funding engine is in good shape ahead of the launch of our new Virgin Money propositions. The blended average cost of deposits increased by 10 basis points, and around half of that was down to the base rate increase in August 2018 and the other half due to mix.

We've chopped a lot of wood on the wholesale funding front this year. We've issued RMBS, covered bonds, senior unsecured and tier two debt and we've paid down £1.3 billion of TFS. And the blended average cost of wholesale funding has increase year-on-year, reflecting higher rates, including 25 bips on TFS balances and a slightly richer mix.

At the interims, and in more depth at Capital Markets Day, we talked about our focus on growing relationship deposits. It's a key part of our strategy, to grow our base of loyal, engaged, lower cost deposit balances and helping to underpin our margin. We set ourselves a target of delivering high single digit CAGR in relationship deposits.

As you can see, and this is before we've launched our new Virgin Money propositions, we've grown our relationship deposits strongly this year with 7.1% overall and a particularly strong performance in Business banking. We've called out the blended average cost of these deposits here, to highlight first of all, that it's around one-third of the total deposit costs and around one-fifth of the current marginal cost of retail term money.

Now, our business deposit growth includes around £160 million of balances, recruited via the RBS incentivised switching scheme. And although we're performing relatively well ourselves, I think it's fair to say that the scheme has got off to a disappointingly slow start. You'll recall that the requirement for increasing competition was to switch 125,000 customers away from RBS in 18 months, so by October 2020. And in the first seven months of the scheme only 18,000 customers have switched. Now we've picked up a decent share of those switches, around 20%, in line with what we were targeting and we're really pleased with the quality of those customers, who have also brought in around £100 million of lending.

And it looks like we're over indexing on the larger, more valuable customers and that makes sense because we have the capability to match what RBS offers. And that's really the critical point, we're focused on recruiting meaningful balances much more than the number of customer switches. While we've got line of sight to further potential switchers in a pipeline of balances, the scheme really needs to pick up the pace, or there's a serious risk that it will fall short of the all-important competition objective. As you can imagine, we're working as best we can with the BCR and RBS to drive the scheme harder.

So, the picture on lending is exactly what we painted at Capital Markets Day. Strong growth in Personal, continued progress in Business lending, and measured growth in Mortgage balances.

The Personal division saw good growth in cards and personal loan balances, levering our strong cards platform, the substantial improvements in digital PL acquisition, and the launch of our JV with Salary Finance. Underlying growth in the Business book, stripping out the balances recruited from RBS via the switching scheme, was 3.3%.

Now turning to margin, the moving parts in our net interest margin are clear. The average yield on the Mortgage book reduced by 12 basis points year-on-year and that's the now familiar story of the impact of mortgage market competition. In contrast, we've seen the average yield on the Business portfolio increase by 23 basis points, a combination of rate and pricing improvements.

Similarly, we've seen a strong increase in the yield on Personal lending, driven mainly by cards, where we've benefitted from acquiring a more seasoned book with stronger cash yield. And as we saw a few slides earlier, we absorbed an increase in deposit costs last year, a function of the August 2018 base rate increase and our deposit mix. And that reduced our net interest margin to 166 basis points in line with our guidance.

So turning to next year, we expect our net interest margin to be relatively resilient through FY20 and let me explain why. The two key drivers of NIM reduction in 2019 were mortgages and deposits, and we don't expect either of these to play such a big part in the 2020 NIM evolution.

Competition in the UK mortgage market and the squeeze on margins has dominated the conversation about NIM for the past few years, and really the key impact has been back to front book compression with new business coming on at lower rates than the balances rolling off and growing a mortgage book aggressively in that environment compounds the problem.

And we've argued for some time that our book is less exposed to this effect going forward and this chart on the left, which shows the impact of mortgage churn on our margin, supports that argument. So, just to be clear, the purple yield line on the top represents the yield on those balances which churned or redeemed in the period and are effectively repriced at the front book rate, which is the red line below.

And this is the most relevant comparison because that's what drives the margin impact. Through 2018 and 2019, the top of bank NIM pressure eased a little because the gap between back and front yield has narrowed, and because net lending growth has been dialled back. In 2020, we expect the gap to be even smaller, and recalling the expression that Hugh used at Capital Markets Day, we're not straining for growth in Mortgages. As a result, we don't expect further significant pressure on our NIM this year from mortgage competition.

In 2019, the biggest delta in our NIM related to deposits, and similarly, we're not expecting a repeat. Half of the increase in 2019 was due to the base rate, and we're not expected to see a base rate rise any time soon. The other half related to mix. We grew strongly in savings and that increased the blended average cost of deposits. We expect the mix of deposit growth in 2020 to be more helpful, with a stronger proportion of lower cost relationship deposits alongside our savings growth.

The third product driver in the NIM evolution is the tailwind of changing our asset mix. Now that had a positive impact in 2019 and we expect to see more of the same in 2020.

Finally, and this is what makes the guidance for 2020 harder to call, is the impact of the rate environment, and in particular, the short end of the yield curve. Right now that's not very helpful. The narrowing of the gap between base and LIBOR that we've seen over the last few months as the market has elected to price in the possibility of a rate cut, has hurt us and in Q4 of 2019, it probably cost us a couple of basis points on NIM.

We think that the outcome of the general election will be a critical driver of interest rate expectations. We're not calling it either way, just to be clear. Our track record in predicting what the electorate will do is somewhat patchy. But whatever outcome we get is likely to set a new path for interest rates.

Accordingly, we're guiding to a range for 2020 NIM of 160 to 165 basis points with a base case somewhere in the middle of that range. And to be clear, that assumes that current market conditions and the interest rate environment persist.

One note of caution for all of you out there, it should be clear that the way we expect NIM to evolve driven by mix, will mean a gradual build over the year. As ever, we're guiding to an annual outcome, and you shouldn't be surprised if the quarterly results are a little lumpy. I've already mentioned the unhelpful impact of the rate environment on the Q4 exit rate, for example.

On fee income, I wanted to draw a couple of key points out at this point. Performance in the year and a reminder of some impacts going on the fee base going into next year. Business fee income is going well. We saw this as a growth area from broadening our offering and growing our customer base, and it's good to see that coming through.

The year-on-year increase is down to a better all-round performance, Gavin's guys have really knuckled down, and the introduction of a new business debit card during the year that's had great traction.

Personal fee income continues to be under pressure, though, and that's a familiar story across the industry. We've reduced fees on a number of items over the years, and last year, we saw significant reduction in charges for returned items alongside lower account fees, although this was partly offset by higher interchange fees from the VAA card base. We also saw lower fees from our investment business, as soon after the acquisition, we reduced our asset management charges and that was really necessary as Virgin Money was somewhat out of the market.

Looking into next year, we'll see Business fees go from strength to strength, but there'll be further pressure on the Personal fee base as we'll reduce our overdraft fees along with everyone else in the industry. And a final heads up, is a reminder that the sale of the unit trust business to the joint venture with Aberdeen Standard means we now recognise our share of the JV profits rather than the full income and expenses of that business.

So turning to costs, we've made excellent progress on costs this year bringing the Opex base down from £998 million to £942 million. We delivered on our market guidance, despite a four-month delay in completion of the investment JV, meaning we outperformed on core costs.

One of the key drivers, of course, was integration synergies, and we outperformed here too, landing £60 million of run rate cost synergies against our plan of £50 million, with net synergies after the incremental brand license fee of £53 million. The costs to do incurred in the year were £156 million. These were higher than planned because we brought £38 million of restructuring costs forward into 2019, while the related run-rate benefits of £30 million were not crystallised last year. They won't be recognised until later in 2020.

The accelerated costs pertain to the announcement at the end of September, 12 months early, of the consolidation of our operating locations and the closure of three major offices, Edinburgh, Norwich, and Merrion Way in Leeds, along with the related FTE exits. We decided that giving our colleagues clarity as early as possible was the right thing to do and announcing the closures meant we had to provide for the costs.

Now that we've completed the Part VII process, integration will switch gears. 2019 was all about going after the low hanging fruit - delayering senior management, reducing investment spend, managing our supplier base. In 2020 and 21, we'll be integrating customer platforms and operations, de-duplicating and refreshing the branch network and at the same time, we'll be bringing the customer proposition to life under one brand.

We'll maintain our momentum, delivering £50 million of additional run rate synergies in 2020. But it's important to note that the initiatives are weighted to the second half of the year, especially the branch cost savings, and that limits the in-year benefits.

We're therefore guiding that we expect our operating expenses to be less than £900 million next year, with a very strong exit rate into 2021. We're also reaffirming our estimate of the aggregate restructuring and rebranding costs at £360 million. And just to remind everybody, the rebrand costs are £60 million all in, and we expect to incur most of that in 2020. So you know our track record on costs and we're off to a strong start with a very clear path to our 2022 cost target.

Our net cost of risk increased to 21 basis points year-on-year, and we talked about what was driving this at our interims and I think the drivers of the increase were clearly understood back then. And helpfully, the full year picture is consistent with what I said at the time. It's really all about Business and Personal. The Mortgage book continues to see negligible losses. In Business, what you can see is a return to more normal levels of gross cost of risk after an unusually benign 2018 and in some respects, compared to the run rate in the first half, was probably still a little underweight in 2019. Our Business portfolio continues to perform well and notwithstanding the more uncertain economic environment.

Cost of risk in unsecured has increased by 83 bases points over the last 12 months and there are several contributors here and none of them are any cause for concern. We've seen a seasoning of the cards book over the last 18 months or so as new business rolls through into more mature cohorts and then there's the IFRS9 effect. Now IFRS9 was implemented in the VM book at the start of 2018 and in the CYB book from 1 October 2018. IFRS9 accelerates the recognition of provisions, especially in the unsecured lending, without changing the overall lifetime losses and we said at the interims that we estimated that more than half of the increase in unsecured cost of risk stems from the implementation of IFRS9.

Asset quality is in good shape across the board and we're not seeing signs of increasing stress in any of our portfolios. We've maintained our tight underwriting discipline throughout, and actually, the quality of business we've been writing in 2019 has been on average, better than in previous years. Credit conditions remain relatively benign, and the macro drivers of credit stress, such as interest and unemployment rates are still quite subdued. But some commentators are worried about a weaker economic outlook, and in response, we've increased our Brexit related reserves and our book is well provisioned.

Turning to capital, we generated 77 basis points of CET1 before exceptional charges; pretty much enough to cover the restructuring and acquisition costs, while PPI accounted for 172 basis points of CET1. Now, we've been clear on the outlook of these exceptional items, and that should help show the path to healthy free capital generation. The leverage ratio remained strong and we're comfortably ahead of the game on meeting our 2020 MREL requirement of 21.5%.

So after absorbing PPI, the group remains well capitalised with a CET1 ratio of 13.3%. We're above our medium-term operating level of circa 13% and hold a substantial buffer to our CRD IV minimum requirement of 11%. Remember, that includes a reduction of 60 basis points to our Pillar 2A requirement, compared to the CMD picture.

Nevertheless, given the substantial absorption of capital by additional PPI costs, the board has re-examined the Group's strategy and capital requirements. We expect to be net capital generative from 2021 as the burden of exceptional charges is substantially reduced and the benefits of cost reduction and other actions are realised.

That's driven a focus on 2020 and the need to conserve capital in the short term, and the consideration of a full range of organic and inorganic options to enhance the Group's capital position. Accordingly, the board has determined that it would be prudent to suspend the ordinary dividend for 2019, but no other inorganic capital action is considered necessary.

After taking this action, the board considers that the Group's capital position is robust and provides sufficient capacity to execute the strategy and deliver on the performance targets for 2022. And all other things being equal, we would expect to recommence ordinary dividends in 12 months' time. However, the board will decide on the resumption of dividends later in 2020, having regard to capital generation and other pertinent factors at that time.

So to finish up, the group remains on track to deliver on its medium-term targets. In 2020, we expect to deliver a net interest margin between 160 and 165 basis points. We will reduce our underlying operating expenses below £900 million and operate with a CET1 ratio of circa 13%. As discussed, we'll reconsider the capacity for ordinary dividends in FY20, and it's our current expectation to recommence dividend payments at the end of financial year 20.

Today, we're also reaffirming the strategy and targets for 2022, including our intention to deliver a statutory RoTE of more than 12%. So, I hope my remarks have helped shine a light on our performance, and I guess I'll find out when we get to Q&A. In the meantime, I'll hand over to Lucy.

Lucy Dimes, Virgin Money UK PLC

Thank you, Ian. Good morning to everyone in London and good evening to those of you joining from Australia. I'm delighted to be here presenting to you today. I joined the group back in July at what is an incredibly exciting time for the bank. To begin with, I'd like to take a few minutes to explain my background, which I hope will reinforce why David appointed me to the role of Group Business Transformation Officer.

The majority of my career has been spent in technology services businesses. I spent a large chunk of my career in British Telecom, and in my last role as the managing director of Group and Openreach Service Operations, I led a transformation programme, which realised £100 million of annualised cost savings and before that, I led the group's strategic partnering programme.

I then held roles at Equiniti as the Chief Operating Officer, at Fujitsu as the CEO for the UK and Ireland, and most recently, I was the CEO for EMEA at UBM where I led the growth strategy, which was focused on digitising and transforming the business.

So, you may recall that at the last Capital Markets Day we talked about our four stages of development since we IPO'd and since we acquired Virgin Money. To simplify, to digitise, to integrate, and to transform. Having exited from NAB, and delivered IRB, and built the new IB digital platform, the initial stages of simplifying and digitising our business are now largely complete. And so our focus has shifted to integration and transformation.

My role is to execute the transformation workstreams, which underpin both the £200 million of net cost savings and our broader strategic growth objectives. The first of these is to leverage the iB platform, our modern, scalable, digital platform, which we have invested in over the last few years.

The second is to support the development of a bigger, bolder Virgin Money brand by bringing the strengths of the two businesses together and leveraging the power and the reach of that iconic Virgin brand. David will talk a bit more about this later, so I won't steal his thunder just now.

Next, to drive those significant synergies, we need to deliver the integration of the two banks. And finally, we need to establish a much more agile, disruptive digital change capability, and take advantage of the unique partnership opportunities available to us through the wider Virgin Group, as well as other innovative complementary partners. And importantly, we will deliver all of this within the cost envelope we've previously announced.

So, as I mentioned just now, the real prize from our business transformation will be delivering leading customer experiences that support our growth ambitions. The foundation for this is our digital IB platform, which is the strategic platform for all of our products and services. And because of its modular Lego brick architecture, we can now take a much more modern, agile approach to innovation.

We are therefore creating a disruption hub in Newcastle, which will bring together multi-disciplinary teams from across the business to rapidly design and deliver new product features and app enhancements. Now this will create a new way of working within the Group, which we expect to permeate the entire bank over time and we'll be launching this in January, and we're building a capability that will scale to around 200 to 300 people by the end of 2020.

We will combine this with our unique partnering model, leveraging the Virgin family that we're now part of, and commercial partners, such as GoCompare and Salary Finance, to deliver an improved customer experience.

Our hub initiative is the icing on the cake of a transformation agenda that underpins £200 million of net cost savings, and as Ian has already mentioned, the £53 million of run rate net cost savings we've delivered in 2019.

I'd now like to take you through the detail of what we said we would do, what we've done so far, and what we're doing next. The first organisational design related to the deduplication of senior management roles, so executives, non-executives, senior managers. We've achieved half of the synergies in 2019 and with FSMA Part VII now complete, we can operate as a single bank, which will release the remaining roles to deliver a further £20 million of savings.

We also commenced the central costs workstream in 2019 and achieved just under half of the expected synergies, for example, through procurement savings and the closure of the Virgin Money London office. And in September, we also announced our end-state location strategy, and are now progressing the three office closures in Edinburgh, Norwich, and Leeds over the next two years. And we'll also progress further procurement and sponsorship savings to complete this workstream.

With Part VII complete, the operational workstream is also now able to progress at pace, and we made a good start on this last year, achieving £12 million of the £45 million of expected savings. And we're now focused on realising the remainder of the 1,500 role synergies across back office, middle office, and functional areas. Now, some of these roles are dependent on technology enablers, such as platform closures and process automation, but a significant proportion will exit in 2020 and then with the remainder in 2021.

The smallest of the integration workstreams is network efficiency, which is the consolidation of the branch network and this is also on track. For the benefit of doubt, there are no changes to our network efficiency programme or our headcount reductions. We are simply progressing with the original plan we announced at the time of the transaction.

The fifth workstream, digital and change, is now up and running, and will see us truly leverage the platform that we've built, supported by disruption hub capability. For example, we will drive digital channel adoption and customer self-service, to significantly reduce printing and postage costs as well as introducing a strategic sourcing approach that will enable us to consolidate our supplier base from 2,000 today to 1,000 over time.

These initiatives will help us deliver a highly efficient cost base, and also, give me the confidence in our ability to deliver our sub £780 million cost base in 2022. And importantly, we will also deliver a faster and better innovation capability and unique supply side and go to market partnerships, creating the platform for us to really disrupt the status quo.

I'll finish there and now hand over to David, who will talk you through the outlook for next year and beyond.

Thank you.

David Duffy

Great, thank you Lucy. There's a lot in there and I think it can be very clear to you that we will maintain the focus on integration and cost management relentlessly. But we also want to transform our business from a customer perspective, so let me talk to you a little bit about our focus on that in the medium term.

We've talked for the last few years, about how we're transforming our technology platform. And as you know, IB is now built, and all of our customers and products and services will soon be on one platform. What that means is we'll soon be able to operate with a single open API technology platform that will support the development of new propositions and the integration of our fintech partners across the next year.

If you look at that, that's a tremendously strong capability. But also, given the competitive dynamics in the marketplace, we need to be able to deliver new experiences and propositions in weeks, not months or years and we need to have the same innovation capability as any competitor, small or large. The creation of the disruption hub that Lucy's talked about will allow us to do this, and it is the investment in our IB platform that has made that possible.

It's important though to do far more than improve processes; we want to create world class experiences. And the acquisition of Virgin Money has given us the ability to deliver what I think are unique solutions, which combine a great brand, which is known for its service, our innovative technology that we've built, and value for money propositions, and national distribution.

But if you stand back, what I think is truly unique is that we will be able to offer access to up to 25 Virgin Group companies. And just to be clear, this is not just theory, we already operate the Virgin Atlantic Credit Card partnership, and that has delivered over 130,000 valuable customer accounts.

And that's the first part of the story, but we also want to further improve the value outcome for customers by combining a group wide loyalty programme with value-based propositions. What does that mean? Not only will our customers get value on the acquisition of a product, but they will also earn loyalty points and benefits across products when they use them.

We are working very closely with the Virgin Group on the development of that group-wide loyalty and rewards programme, and I expect that we will deliver our initial propositions during the first half of 2020. We're also making good progress on a number of propositions for our Mortgage business, as highlighted by Hugh in our Capital Markets Day, and the first of these will also launch in the first half of 2020.

It's also important to remember it's not just the retail business that we're focused on, as part of our launch, we will announce a full capability business current account in the first half of next year, and Gavin's team are busy working on that.

It's also interesting because as we launch the Virgin Money brand nationally, we will benefit from the halo effect of being part of the broader Virgin Group, and specifically, we're going to be taking part in the 50th anniversary of the Virgin brand. Yes, it's 50 next year, it makes us all feel quite old. And we'll be working with a lot of the other Virgin Companies, and this allows us to combine our presence and impact in core northern cities, like Manchester, Birmingham, and Leeds, so when you're in those locations, you have a massive presence as an employer and as a brand.

To give you an example, we'll have a number of joint events and we're talking to, specifically, Virgin Atlantic and others, but they will demonstrate the brand of the company and the diversity of that brand across every one of our key locations, and it will also allow us to market each other's products in many of those locations.

Now, as we go national, we're launching the Virgin Money brand, of course, and it will have its traditional red look and feel. However, we will be deploying a contemporary version of the brand for different segments of the markets, and that will really demonstrate the power and the flexibility of the brand across our business.

It's going to be a pretty busy year ahead, but we're starting to deliver on the benefits of the acquisition right now. So, our first Virgin Money national product launch is next week. The Virgin Money current account will be available and will include all of the B app features, which now has a current NPS of 52, and there are a lot more elements included in it, as well.

We think the combination of the innovative B digital platform and the Virgin brand will be a great start and I would think it's better than most that I can see in the market, if not all. In addition to our product and proposition launches, of course, we will convert three of our flagship branches into our new Virgin Money concept stores in Manchester, Birmingham, and London. So, they will be a very, visible high street brand presence.

In line with the current account launch, the rebranding process will also begin in December with the rebranding of B to Virgin Money and the launch of a new Virgin Money current account app to complement the recently launched Virgin Money Credit Card app. So, a lot of things happening.

One of the most important aspects of this activity is the innovative branding and marketing campaigns that will be delivered, and you will see those start in January and be pretty much on all the time after that. I'm pretty excited about what we'll be delivering, and internally, the whole bank is eager to see us move from the past to the future now that we have permission to integrate this brand.

We are now moving into a phase of delivery. I think we've been planning a lot, but it's now a delivery phase. And over the next couple of years, we will roll out the complete rebranding of all of our products, propositions, technology platform, and physical locations.

So, as we stated at the Capital Markets Day, as a bank we have the trust and the product and service capability of a major bank, combined with the ability to innovate, particularly with customer experiences, like fintechs can. As the market develops though, we're also working with other non-Virgin partners and service providers, because we think there are other propositions with great value for money for our customers that we could develop.

We will update further on those kinds of discussions as we develop them throughout 2020. But at its core, I firmly believe that Virgin Money is unique in the marketplace. We will be the only bank that can offer value through a broad range of banking and non-banking services, with integrated discounts, points, and loyalty-based offerings.

And we'll deliver all of those services as one bank with a single technology platform, one brand, and it's a fintech and partnership friendly platform, and this will be supported by the disruption hub that Lucy discussed, and it will deliver world class customer experiences. That's pretty unique in the marketplace.

In short, it's now time to deliver on our ambitions for Virgin Money. And as I look at all of this, I'm absolutely confident that we will deliver and that our purpose of Making You Happier About Money will guide us in our ambition to disrupt the status quo.

But critically, being successful will allow us to deliver sustainable returns to both our existing and new investors and will ensure great outcomes for all of our broader stakeholders.

So thank you, I will close there and we will now turn to questions. I think we're going to start with questions in the room, and then we will pass mics around and then we'll come on to the call and to the webcast shortly after.

Rohith Chandra-Rajan, BAML

Good morning, it's Rohith Chandra-Rajan from Bank of America. Your revenue expectations for next year are very much predicated on growth, particularly in Business and Personal lending and I guess we've seen some evidence of that, certainly in the second half of this year. So, Business looks like it was growing in the second half, annualised around 11%, consumer at 22% and that's really before the integration takes hold, although in Business, there was some Williams & Glyn or RBS benefit. So I was just wondering if you could scale your aspirations, in terms of volume growth for next year, because that seems to be the key thing in terms of the revenue outlook, both in net interest income and fees?

And then secondly, just to understand, I think it was the left-hand side of slide 16, in terms of your mortgage expectations for next year, I think the margin outlook is pretty clear, relatively flat is your expectation. But then the bottom chart there seemed to imply new lending and refinancing offsetting one another, so a relatively flat mortgage book. So, just really to try and get your sense of growth in Business, Personal, and Mortgages for next year?

Ian Smith

Thanks, Rohith. So, I think you've called the direction of travel correctly. It is my favourite expression actually, that Hugh used at the Capital Markets Day, which is we're not straining for growth in Mortgages and our ambition there is principally to retain our market share. We don't expect to see much growth in the mortgage market next year, so I would expect us to hold our own and not much more than that.

And that, as I say, means that we're going to see that easing of pressure on the NIM from the Mortgage business. As far as the rest of our businesses and the outlook overall, we said that we would expect to grow above market, and that remains our guidance.

I think that I wouldn't read too much into the sort of half on half growth rates in Business. It's a fairly lumpy profile, or has been a fairly lumpy profile, because it depends on customer drawdowns and repayments, those sorts of things, but that broad trajectory of 4.5% is the right number to focus on.

And Personal is important to us, so our guidance is above market growth, and you can see what we think about what we're going to be doing in Mortgages and I think the direction of travel for our other key businesses is clear.

Rohith Chandra-Rajan

Can I follow up in terms of balancing growth aspirations and capital returns? You said that your expectation is to, all else being equal, resume the dividend next year, but you don't expect to be capital generative until 2021, I'm trying to square those two things.

Ian Smith

First of all, what I'd point to is in addition to the generation of capital from earnings, we've shown ourselves to be pretty good at RWA husbandry and managing that side of the book. So, I think the important thing is the board will look at capital generation, a whole bunch of other things, and I'd like to manage expectations at the sort of modest levels, in terms of our resumption, so, I'm not particularly concerned about that.

Fahed Kunwar, Redburn

Hi. It's Fahed Kunwar from Redburn. I just wanted to understand, I think on slide 45 there's a hedge slide where you talk about an increase in your hedge portfolio, but the number of that seems most important, just so I make sure I understand this is, the net NII booked from the hedge is £30 million, is that correct?

Ian Smith

Yes, that's correct.

Fahed Kunwar

So, for other banks, obviously the steepening of the yield curve is a reduction of a negative. But for yourselves, if you do get a steepening yield curve, should we think about incrementally positive NII coming from that hedge portfolio, considering you're basically booking hardly any hedge income right now? That was my first question.

My second question was on other operating income. So, half on half, it was quite a big decline in other operating income. I appreciate you gave some colour, but was any of the kind of reduction that you expected in 2020, did any of it come into that reduction in the second half of the year, or what was behind that reduction and shall we assume that's the run rate going forward?

And the last question. The funding cost plans are a big component to your flat margin guidance going forward. If the RBS incentivisation plan is going slower, from memory, the business current account deposit benefit was upfront and the personal current account were going to come later on in the plan - shall we assume, then, if that's going slower that that funding cost benefit takes longer to come through because the business current account isn't quite going as fast as you expected? Thank you.

Ian Smith

Thanks Fahed. Yes, you're spot on, in terms of your hypothesis on hedge income and the impact of a steepening yield curve would be helpful for us.

The OOI position, half on half, I guess what you saw through the second half, in terms of real business, the impact of the asset management fee, we reduced that from 1st January, so that came through much more strongly in the second half.

And some other bits and pieces in there. We saw a slightly stronger first half, say, from Business. We earn some chunky fees sometimes on customers and business there. In terms of how we see that going forward, the things to bear in mind are the fees from the investment business are now out, and we have the impact, as we flagged, around ten million on high cost of credit.

So, factoring those into your expectations for next year, alongside the full year performance is the right way to look at it.

John Cronin, Goodbody

Thank you, it's John Cronin from Goodbody. Just two from myself. One is, again, getting back to the unsecured lending growth. You've mentioned that much of that is coming through the affluent credit card customer base that was Virgin Money's book that you acquired. But can you speak a little about what's happening in the rest of that book, in terms of unsecured personal lending product and what kind of growth rates you're experiencing there, and also, in terms of credit quality?

Secondly, getting back to Lucy's presentation, on slide 25, you mentioned big tech and fintech partnerships. Just wondering, more broadly, in the context of this disruption you speak about, anything we can be expecting on a near term or medium-term view in terms of such partnerships that would be transformational for your Personal business?

Ian Smith

Thanks, John. I'll waffle on about unsecured growth and then Lucy can come in with the partnership piece.

So cards continues to do well and we understand the quality of that business and the quality of the platform. I think there's an additional feature this year that is important to understand, which is that we've seen, certainly in percentage terms, really strong growth in personal loans. Now, it's off a very low base, so a couple of hundred million on a 750 million base. But that's coming from two places. The first is, as we've talked about, the launch of Salary Finance and we're really pleased with that and the progress that we've made.

And the second is, now we've talked for a long time about lack of capability in personal loans, and that was the thing that was holding us back, both from a cost to acquire perspective, but also, that risk management and the risk of negative selection, If you're not really good with the aggregators, you get some of the poorer bits of business.

So, we've worked very hard at that, and in particular at our aggregator proposition, and we've become much more competitive there in terms of being able to win business via aggregators. So, our personal loan business has gone from strength to strength this year. It's good quality, I mean the asset quality measures of arrears and all those sorts of things are in good shape, but importantly, the things that we look at in bringing that business on, so affordability and customer indebtedness, are all really good, compared to previous years, and that's what we've been looking for, as I say, to avoid that negative selection.

Then finally, we also look at the probability of default in those lines and again, much stronger than business we have written in the past. So, our growth in personal has been both on the cards and on the unsecured personal loan side, but really happy with the quality.

Lucy Dimes

And in terms of the partnerships, we can't announce anything today, but we've got lots of conversations going on. The focus of our near-term activity is the Virgin Group, because obviously, there's some fantastic opportunities there. We have other conversations happening on the supply side and the go to market side.

I guess the key point is probably that we're feeling very attractive as a partner. We've got a great brand, we've got the agility now to do things quickly with the disruption hub, our platform is easy to bolt things onto. So, more to come in this space, but nothing that we can announce exactly at this moment.

Charmsol Yoon, UBS

Thank you, it's Charmsol from UBS. Regarding your NIM guidance, did you assume liquid assets to decrease or increase? So when I look at slide 42, it says you will probably do £3.0 to £3.5 billion of wholesale, and then there will be a £1.8 billion on slide 43 to mature, which will give £1.2 to £1.7 billion in net increase in wholesale funding, and then there will probably be some TFS repayments, so I was just wondering how that will affect your liquid asset position?

Ian Smith

Charmsol, there's lots of detail in your question there; I think the answer's a pretty simple one. So we're carrying quite high levels of liquidity at the moment - two reasons, we ran high on liquidity throughout 2019 because we were waiting for Brexit to happen and so it still hasn't happened, so we're still holding that. And we also have a specific stock of liquidity to manage the risk of the Part VII, so our customers have until the end of January to determine whether or not they want to withdraw. Withdrawal levels at the moment are extremely low, but we're holding some additional liquidity for that. Once that period has passed, we'll iron that out through the course of the year.

Charmsol Yoon

So your NIM guidance doesn't assume that liquid assets position to materially decrease, hence it will rise. Correct?

Ian Smith

No, the NIM guidance, we expect to be able to reduce our stock of liquidity, and we have baked that into our NIM guidance. So, there's no more upside to come there in any material way.

Ben Toms, RBC

Morning. Ben Toms from RBC. PPI seems to be coming to an end, but it turned out to be a bigger problem than initially expected. Do you have any view about the recent Treasury Select Committee paper on push payment fraud? Do you think this is an issue and have you run any numbers internally about it?

Secondly, consensus expects costs for 2020 around £880 million. Are you comfortable with that or would you prefer it if it was closer to the £900 million?

Ian Smith

So, we're not concerned about exposure to push payment fraud, is the short answer. We're not going to talk numbers and things at the moment, but we don't have a concern there. In terms of consensus, look I'll reiterate our guidance, we said below 900, and you know, we've been pretty good at managing our costs down against that guidance through the year, so I'm going to stick with what we've got out there.

Chris Cant, Autonomous

Good morning, it's Chris Cant from Autonomous, thank you for taking my questions. I wanted to ask about EIR. I was looking at your accounting policy disclosures on page 54 of your release, and it's something that's been topical with some of your peers recently. So, I note that you say you assume 83% of SVR customers will fully repay within two months or re-mortgage. If that was to move to 90%, you'd have a £20 million EIR adjustment? I haven't spotted this disclosure before if you've given it previously, but I find it quite interesting - are you trying to flag that there's a potential EIR adjustment coming, which is something that some of your larger peers have been flagging as a feature for them in 4Q results, which would be your 1Q, that would be the first question.

And the second question, also on EIR, you've also given some commentary around the Virgin card book in terms of the EIR again. Is that something that's building up again? So obviously, for Virgin Money standalone EIR and the accrual on the balance sheet became a huge topic, when you acquired it, you essentially wrote that balance off. Is that balance now rebuilding and how large is it today and how large would it be in, say a year's time, just wondering if that's topics going to come back around again? Thank you.

Ian Smith

Thanks, Chris. The short answer on mortgage EIR is no, I mean, the disclosures are there to be helpful. Our SVR balances are both a very small proportion of our book and also, pretty stable now. And the key thing that we look at when thinking about mortgage EIR is you know, what's the average period which mortgage customers spend in SVR, and it's less than two months. So first of all, we think we're pretty prudent on mortgage EIR and we're not flagging a risk of an adjustment, I think it seems to be a bigger challenge for other people.

On cards EIR, yes, the balance will build. We've zeroed it out at the acquisition, but if you continue to write zero rate balance transfer business, it will build again. It is pretty small. It never gets to the levels that Virgin Money had on a standalone basis, so we think it's just de-emphasised now really. And that's because, first of all, in terms of the scale of it compared to our income and our capital base, so very different from the old Virgin Money standalone days. Secondly, I think we've got a much more seasoned and broader book. So we're recruiting customers on the BT product, but also, on all round cards, on retail cards, VAA, all those other things. So, it's, as I say, de-emphasised going forward.

Jenny Cook, Exane

Jenny Cook from Exane. Thanks for taking my question. I had one on your mortgage maturity profile, because I find it quite surprising that for most of this last quarter, you can get a cheaper five-year fixed rate product with yourselves versus a two-year fixed rate product. So, I was just wondering why you've got negative term premium on your mortgage rates. If you can shed any rationale on why this is the case, that would be quite useful, thanks.

Ian Smith

Jenny, let me come back to you on that one. We'll pick that one up offline because you know, I agree with you that it would seem slightly anomalous, but I'll come back to you.

Martin Leitgeb, Goldman Sachs

Good morning, it's Martin Leitgeb here from Goldman Sachs. Maybe a little bit more broadly on the mortgage space, I was wondering if you could elaborate on what kinds of trends you're seeing in terms of competition. I mean, what we can see from an external perspective, some players are trying to increase their share in mortgages, but equally, there's others dropping out. So, it seems to be fairly balanced at this stage, and I was just wondering if this is what you're seeing or if you're seeing any discernible change, in terms of trends?

And the second question is more on deposits and the outlook for the average cost of deposits of Virgin Money UK going forward. I think you highlighted the importance of relationship balances, in order to drive down the costs over time. I was just wondering if you could shed a little bit of light on how we should think about the launch of the new Virgin Money current account product going forward. What kind of pace of take-up or how shall we think about this cost of deposits evolving as this relationship balance hopefully gets a meaningful boost from the new product? Thank you.

David Duffy

Thank you. From a general mortgage perspective, we've seen stabilisation a little bit. We've seen some players losing volume and then cutting their rates, most recently, I think Nationwide did some of that behaviour. But the aggregate behaviour of the scale of the market has stabilised a little bit.

You've seen a number of small players come out, and I think that's a lot to do with having a monoline business. You don't have the diversity of your liability and asset management around different margins and different businesses, so there has been a softening of the market, in terms of those people stepping out. And I think we've seen a calmer, and it seems like the future will be more of that, rather than more of the past.

Then on the deposit side, most of what we do with Virgin will be the same as what we've done before, which is a linked savings account, which drives a lot of that. Do you want to make a comment on that?

Ian Smith

Sure. Thanks, Martin. On deposit costs, you reminded me that I didn't answer all of Fahed's question. The way we thought about deposit costs is first of all, in the shorter term, the real advantage is the recruitment of Business deposit balances. I guess what I'd point to there is the growth of relationship deposits on the Business side have been nearly 15%, without the benefit of RBS. So I think you're right, RBS will take longer. We'll do what we set out to do, but it takes a bit longer, but what's brilliant is that Gavin's guys are out there growing that deposit base without that tailwind already. So, first of all, that gives us a bit of confidence that certainly in the year ahead, with Business being that engine of low-cost deposits, both BAU and RBS, I think that'll be a big contributor.

On the proposition side, when we talked about this, the Personal proposition, depositors get a pretty poor deal from high street banks at the moment and I think that we'll offer something pretty compelling, and that blended average cost of those deposits is going to be far lower than the savings products that we offer, savings and term.

So, I think that helps underpin cost of deposits going forward, which we just don't expect to see the increase that we saw in 2019. I think what's also telling is what's happening out in terms of deposit pricing. Even the famous Marcus products are reducing in price and we're just tweaking some of our pricing on deposits at the moment, bringing some of our savings products more in line with current market rates and that should also provide a bit of a following wind on deposit costs. But the key thing for us, medium term, over the next two to three years, is to really get that engine of growth going, in terms of recruiting Personal customers with a fantastic proposition that will deliver cost of deposits that are lower than the average today.

Shailesh Raikundlia, Panmure Gordon

Morning, it's Shailesh Raikundlia from Panmure Gordon, a couple of questions if I may? Just a follow-up on the EIR, with the credit card book, obviously you had a big write down at the time of the acquisition. I was just wondering behaviourally if that's changed and is there any scope of that, or is it a bit early at this moment in time for the EIR to be written back at some stage, given the fact that you had a seven-year behavioural maturity rather than the five year that you've assumed now?

And secondly, on the cost of risk, I'm looking at the fact that your underlying cost of risk was about 27 basis points, and then you had specific releases of five basis points. I'm just wondering whether the run rate is more like the 27 basis points or where we are with that?

Ian Smith

Thanks Shailesh, in terms of the EIR assumptions, we're sticking with five years. We think that's a much better place to be. But while that sounds much more prudent and in line with the market, and it is, we've also got a real benefit from starting the clock again. If you look at a chunk of our improvement in unsecured yields, is that we were able to recognise that something approaching 40% of the Virgin Money credit card book is now post promo and therefore, earning cash interest, which made for a stronger overall yield. So, I'm very happy that the assumptions are in the right place that we use, not proposing to sort of term that out further or anything like that. I don't think we should do that and I don't think we need to do that. The business is in great shape.

On cost of risk, that delta between gross and net, we don't expect that to close particularly because a lot of that reflects recoveries, and in particular, in unsecured, we see annual recoveries because we undertake debt sales and other things. So, that is what sort of nets us down, and so I'm not concerned that somehow we're exposed to that higher line.

Operator

We have three questions registered. We have Ed Henning from CLSA, Ed, please go ahead.

Ed Henning, CLSA

Thanks for taking my questions. A couple of things from me, firstly, the Capital Markets Day was five months ago, you've talked about the progress, all the guidance is in line. Has there been anything better or worse in your experience, in that five months that you've achieved so far?

Then the second one on that, you mentioned the Capital Markets Day, you're rolling out the new business current account and the personal loan all in the first half, and on slide 28, you talk about business lending and business credit cards. What's the rough thinking on the timing of rolling out those new products?

Ian Smith

Better or worse, Ed, short term, I think we've got as I said in my remarks, a slightly unhelpful short-term interest rate environment. As I say, let's see where that goes when we get into the new year. I think there are many arguments for suggesting that UK interest rates are going to have to rise over time, but let's just see what happens. And I think that just puts a bit of pressure onto the margin environment, but as we've highlighted, we've got good reasons to believe that our NIM will be resilient into next year.

In terms of just what's going on in the rest of the business, I think we're doing pretty well, despite the market uncertainty. One of the things that we look at, coming into a day like this, is our pipeline, and our pipeline in Business banking is really good. And it's kind of odd how customers are somewhat defying the conventional wisdom of uncertainty around Brexit and other things. We're still seeing our customers doing business and that gives me some comfort.

I think the mortgage market is going to be quite quiet next year. Certainly, the roll into Christmas, which is traditionally quite strong, the December reporters pushed pretty hard to put business on in the last quarter of the year, that sort of thing. I think that's been quieter than we've seen for a number of years.

David Duffy

Just on the business current account. We can never be exact, but we really want to have that in in the first half of the year. What we want to have is we start December with the current account, we do the big branches, we roll into hopefully having the Virgin Money loyalty programme, and then we'd like to have the business current account, debit card, and credit card, all launched around that time.

I'm sure some of my team will be hating me saying that, but that is now an announcement, guys, so get on with it. But seriously, I think the issue is we want to tie them together, so the current account and the retail side, and the SME if you recall, our SME is S, it's the smaller side, and there's a fungibility between the Personal and the Business. So, we want to take advantage of that and then deploy the Virgin loyalty programme, so, our ambition is to have all of that locked in in the first half of the year Ed.

Ed Henning

OK that's great. Just one follow-up Ian, you've talked a lot today about Mortgage growth and Business growth, and Personal, and that Business and Personal above system and Mortgages roughly around system. What are your expectations for system next year?

Ian Smith

Sorry, expectations for system?

Ed Henning, CLSA

Yes. Across the three, Business, Personal, and Mortgages.

Ian Smith

We can flick the exact predictions to you, but we are currently expecting to see a flat mortgage market, similar growth in business, a couple of percentage points, and slightly more subdued personal lending. I forget exactly what system growth was for this year, but slightly more subdued.

Operator

The next question is from Victor German from Macquarie. Victor, please go ahead.

Victor German, Macquarie

Thank you very much. I just wanted to ask a question on margins first. Ian started to answer that question, but I was hoping to get a little bit more detail. If I look at product margins, it looks like you've seen a meaningful decline in mortgage margins, which you're hoping to arrest next period, but one of the products that we've seen quite good performance, in terms of margins, was unsecured, where you've seen ongoing increases in that spread. I was just wondering if you could give us a little bit more colour, it sounds like part of the reason behind it is because you're getting less customers in interest free periods and more actually interest paying periods.

Just interested if you can give us some numbers around how this thing has evolved and whether you expect that trend to continue into the next period.

Ian Smith

Thanks, Victor. Good to hear from you. If we look at what drove the increase in unsecured, first of all, you're right, a lot of that was the stronger yield from the credit card books, from the cash interest yield. So we're not going to see a repeat of that going into next year, certainly to that same magnitude, but we are expecting to see some continued improvement, but not of the scale we saw 18 into 19.

Another feature of the 18 into 19 increase that I think is margin accretive, is on the personal loan side. On the one hand, you've got still a very competitive unsecured personal loan market with headline rates around the 3% mark. Where we've seen a good chunk of our growth though is in Salary Finance and that is at much better rates than you're seeing on the aggregator side. To a certain extent, it's kind of twice what we're seeing, in terms of headline market rates. I think we're enriching the mix there, and that's a really good stream of lending for us. So, I would expect to see a better average customer yield on our Personal lending into next year, but not as big a step-up as we saw 18 into 19.

Victor German

Thank you. And also, on the structural hedge, I know that you talked earlier around this issue already, but I'm just wondering if rates were to stay at current levels, assuming no changes from here. Presumably, given that you've got a five-year structural hedge, the rates are still lower than they were over the average of that period. So, I'm wondering, as we go into 2020, is the structural hedge supposed to be a drag to margin? Presumably it is in your guidance, if you can give us any colour on that, that would be very useful.

Ian Smith

Yes Victor, it is, the current interest rate environment is factored into our guidance, so we're not assuming, in that guidance, that the world gets any better or anything of that nature. So definitely, what's happening on the structural hedge impact is baked in. We're kind of expecting, therefore, the contribution from the structural hedge to be flattish into next year, so no major benefit from that.

And that's because, first of all, it's less of an issue for us. Our average yield of structural hedge balances is lower, and we topped up at our lower rates. So, again, it's all about that back to front compression piece. So we think that the impact of structural hedge, baking in the current interest rate environment, is pretty flat through 2020, and that's what we've put into our guidance.

Moderator

The next question is from Joseph Dickerson of Jefferies. Joseph, please go ahead.

Joseph Dickerson, Jefferies

Hi, guys, thanks for taking my question. It's also on the structural hedge, and I'm sorry to bludgeon you with questions on the structural hedge on this call. Incremental to the other two questions, the average balance increased about two and a half billion year-on-year, can you give us a sense for how much more capacity there is to take that up from the current 24 billion sterling? Thanks.

Ian Smith

Thanks, Joe. What lies behind that increase is when we took over Virgin Money, we brought in some of their administered rate deposit balances into the structural hedge, into the scope of the structural hedge, so, that's the increase. We don't see scope for significant increases in what we're structurally hedging going forward, so we should see it pretty stable year on year.

Andrew Downey, VM UK PLC

We've just got one on the webcast, a question from Guy Stebbings from Exane who has asked basically why haven't we adjusted the management buffer given that the Pillar 2A came down. Is this because you want to hold some extra head room for the integration with an eye on stress testing for next year?

Ian Smith

Thanks Guy. So, gosh, part of me just goes, we've just absorbed 172 basis points of PPI charge, let's pause for breath. But it is a fair question because when we were talking about our medium-term aspiration, it was to hold a 1% to 1.5% buffer. I think, Guy, you've called it right. We've absorbed a shock to our capital base, we've you know, turned the business upside down to make sure that we can still do what we set out to do, after absorbing that shock and we feel good about it.

But I think it helps to carry a little extra cushion into next year, just as we work through what, as I highlighted, is a year of sort of flat, in terms of capital generation, before we start to generate excess capital in 2021. So, it feels like a good sort of pause at the moment, and let's talk about it next year.

David Duffy

OK I think we've come to the end of our timing and we've covered all the questions. Thank you, everyone, online, on the webcast and in the room. See you next year, or sooner.

END OF CALL