

# Royal Bank of Scotland Group PLC (RBS.L)

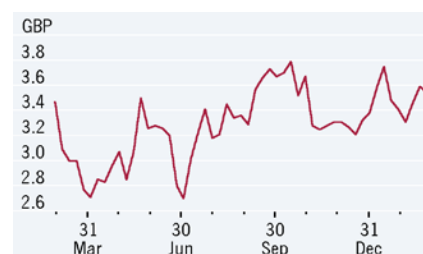
## The Right Strategy; The Wrong Share Price

- **The Right Strategy...** — RBS' geographic focus is set to return to the UK, which is expected to account for c80% of revenues by 2018-20, up from c60%. The business mix emphasis will also be more focused on Retail & Commercial banking, expected to increase from 80% of RWAs (20% Wholesale) to c85% in 2018-20. Markets, International Banking & Ulster Bank will all be sharply reduced in size. This should enable RBS to once again achieve a return in excess of cost of capital in the long-term and eventually, in 5 years+ time, place RBS in a position to return to growth.
- **... But The Wrong Share Price** — However the RBS share price is already pricing in this turn-around and more, in our view, trading on 0.9x last reported tangible book for a c9% RoTE in 2017 (we are at the bottom-end of the company target of 9-11% on our revised estimates) and c10x 2017E EPS. We think a greater share price correction is needed.
- **TNAV Set To Go Backwards...** — We forecast a further 5% decline in TBVPS in 2014 with restructuring, divestments & conduct charges more than offsetting any underlying earnings. We then model a stabilisation in 2015 and recovery in 2016+.
- **... And The Next Three Years Is All About Execution** — The cost-save targets of £2.2bn (ex disposals, run-off), at the same time that the bank is targeting c3% core UK loan growth pa, appears ambitious. RBS also plans to shrink Markets RWAs by c55%, but with only c40% revenue attrition. We see significant execution risk.
- **Sell The Shares** — Management have finally "bit the bullet" and devised a strategy that should return RBS to a sustainable business, with solid returns. However the timeframe over which this can be achieved should not be underestimated — there is a reason the financial targets stretch out to 2020. We see significant execution risks in the medium-term, and believe further tangible book erosion is probable in the short-term. We cut 2014E underlying EPS by 19%, 2015E by 13% and 2016E by 6%. We reiterate our Sell (3H) rating, new target price 270p (from 290p).

- Estimate Change
- Target Price Change

<b>Sell/High Risk</b>	3H
Price (27 Feb 14)	£3.27
Target price	£2.70
	from £2.90
Expected share price return	-17.3%
Expected dividend yield	0.0%
<b>Expected total return</b>	<b>-17.3%</b>
Market Cap	£36,917M
	US\$61,550M

### Price Performance (RIC: RBS.L, BB: RBS LN)



### Royal Bank of Scotland Group PLC (GBP)

Year to 31 Dec	2012A	2013A	2014E	2015E	2016E
Net Income (EM)	1,717.2	-2,750.3	2,166.2	2,909.0	3,271.4
Diluted EPS (p)	15.6	-24.6	19.2	25.8	29.1
Diluted EPS (Old) (p)	15.5	-29.3	23.6	29.6	31.0
PE (x)	21.0	-13.3	17.0	12.7	11.3
P/BV (x)	0.6	0.7	0.7	0.7	0.7
DPS (p)	0.0	0.0	0.0	10.0	15.0
Net Div Yield (%)	0.0	0.0	0.0	3.1	4.6
ROE (%)	-9.1	-15.4	-1.7	1.8	4.8

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See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

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Fiscal year end 31-Dec	2012	2013	2014E	2015E	2016E
<b>Valuation Ratios</b>					
P/E adjusted (x)	21.0	-13.3	17.0	12.7	11.3
P/E reported (x)	-5.9	-4.1	nm	39.9	14.7
P/BV (x)	0.6	0.7	0.7	0.7	0.7
P/Adjusted BV diluted (x)	0.6	0.7	0.7	0.7	0.7
Dividend yield (%)	0.0	0.0	0.0	3.1	4.6
<b>Per Share Data (p)</b>					
EPS adjusted	15.6	-24.6	19.2	25.8	29.1
EPS reported	-55.0	-80.3	-7.7	8.2	22.3
BVPS	570.2	474.9	457.2	462.0	472.6
Tangible BVPS	448.3	365.0	347.3	352.1	362.7
Adjusted BVPS diluted	570.2	474.9	457.2	462.0	472.6
DPS	0.0	0.0	0.0	10.0	15.0
<b>Profit &amp; Loss (£m)</b>					
Net interest income	11,417	10,992	11,086	9,239	8,636
Fees and commissions	4,876	4,518	3,887	2,889	2,720
Other operating Income	5,792	3,932	3,737	3,651	3,443
<b>Total operating income</b>	<b>22,085</b>	<b>19,442</b>	<b>18,710</b>	<b>15,778</b>	<b>14,799</b>
Total operating expenses	-13,854	-13,313	-11,995	-8,998	-7,992
<b>Oper. profit bef. provisions</b>	<b>8,231</b>	<b>6,129</b>	<b>6,715</b>	<b>6,781</b>	<b>6,807</b>
Bad debt provisions	-5,279	-8,432	-2,893	-2,044	-1,597
Non-operating/exceptionals	-8,229	-5,940	-4,344	-3,090	-1,340
<b>Pre-tax profit</b>	<b>-5,277</b>	<b>-8,243</b>	<b>-523</b>	<b>1,647</b>	<b>3,870</b>
Tax	-441	-382	118	-384	-903
Extraord./Min. Int./Pref. Div.	-337	-370	-462	-341	-462
<b>Attributable profit</b>	<b>-6,055</b>	<b>-8,995</b>	<b>-867</b>	<b>922</b>	<b>2,505</b>
Adjusted earnings	1,717	-2,750	2,166	2,909	3,271
<b>Growth Rates (%)</b>					
EPS adjusted	325.6	-257.4	178.3	34.3	12.5
Oper. profit bef. prov.	-4.0	-25.5	9.6	1.0	0.4
<b>Balance Sheet (£m)</b>					
<b>Total assets</b>	<b>1,312,295</b>	<b>1,027,878</b>	<b>964,853</b>	<b>859,582</b>	<b>847,062</b>
Avg interest earning assets	594,062	543,881	450,028	400,123	384,836
Customer loans	430,088	390,825	371,403	285,768	277,097
Gross NPLs	41,140	39,392	25,845	15,507	9,304
<b>Liab. &amp; shar. funds</b>	<b>1,312,295</b>	<b>1,027,878</b>	<b>964,853</b>	<b>859,582</b>	<b>847,062</b>
Total customer deposits	433,239	414,396	423,515	351,877	360,142
Reserve for loan losses	21,262	25,225	16,550	9,930	5,958
Shareholders' equity	68,678	58,742	56,750	57,296	58,488
<b>Profitability/Solvency Ratios (%)</b>					
ROE adjusted	2.6	-4.7	4.1	5.6	6.2
Net interest margin	1.92	2.02	2.46	2.31	2.24
Cost/income ratio	62.7	68.5	64.1	57.0	54.0
Cash cost/average assets	1.0	1.1	1.2	1.0	0.9
NPLs/customer loans	9.6	10.1	7.0	5.4	3.4
Reserve for loan losses/NPLs	51.7	64.0	64.0	64.0	64.0
Bad debt prov./avg. cust. loans	1.2	2.1	0.8	0.6	0.6
Loans/deposit ratio	99.3	94.3	87.7	81.2	76.9
Tier 1 capital ratio	12.4	13.1	13.6	18.2	19.6
Total capital ratio	13.6	15.4	17.7	117.7	117.7

# The Right Strategy; The Wrong Share Price

## Financial Targets vs Citi Estimates

Figure 1. RBS – New Financial Targets

	Targets		Citi Estimates		% Difference vs 2016-17 Targets	
	2016-2017	2018-2020	2016	2017	2016	2017
Revenues	15.0	-	14.8	15.0	-1%	0%
Costs (w/levy; ex-restructuring)	-8.0	-	-8.2	-8.0	2%	0%
Implied Loan Losses	-1.4	-	-1.6	-1.3	15%	-3%
<b>Implied PBT</b>	<b>5.6</b>	<b>-</b>	<b>5.0</b>	<b>5.6</b>	<b>-11%</b>	<b>0%</b>
Cost-Income	55%	50%	55%	54%		
Loan Loss Charge	40-60bps	-	0.57%	0.49%		
<b>RoTE</b>	<b>9-11%</b>	<b>&gt;12%</b>	<b>8.1%</b>	<b>8.9%</b>		
RWAs	300	-	301	299	0%	0%
CT1 Ratio	>12%	>12%	12.8%	13.5%		
Leverage Ratio	3.5-4.0%	>4%	-	-		

Source: Company Reports and Citi Research Estimates

## Valuation & Summary Estimate Changes

Figure 2. RBS – Summary DDM & Warranted Equity Valuation

1. Dividend Discount Model (DDM)	2013e	2014e	2015e	2016e
PV of dividend (by quarter received)	0.0	0.0	8.3	11.4
<b>Total dividend PV (GB pence)</b>	<b>20</b>			
2. Terminal value (WEV)	2016e			
RoTE	8.1%			
Long-term growth	2.0%			
CoE	10.6%			
Theoretical TBVM	0.71x			
TBVPS	363			
Terminal value	258			
Basel 3 CET1 ratio	12.8%			
Capital surplus/(deficit) per share vs 10.5%	74			
<b>PV of adj TV (GB pence)</b>	<b>250</b>			
3. DDM & WEV valuation				
<b>Total PV (1 + 2) (GB pence)</b>	<b>270</b>			

Source: Citi Research

Figure 3. RBS – Summary Estimate Changes

	2014E			2015E			2016E		
	Old	New	% Diff	Old	New	% Diff	Old	New	% Diff
RBS Total Net Revenues	19,920	18,710	-6%	17,360	15,778	-9%	17,038	14,799	-13%
Total Operating Costs	-12,192	-11,995	-2%	-9,706	-8,998	-7%	-9,515	-7,992	-16%
Gross Operating Profit	7,728	6,715	-13%	7,654	6,781	-11%	7,523	6,807	-10%
Impairment losses	-3,096	-2,893	-7%	-2,311	-2,044	-12%	-1,974	-1,597	-19%
<b>Operating PBT</b>	<b>4,632</b>	<b>3,822</b>	<b>-18%</b>	<b>5,343</b>	<b>4,737</b>	<b>-11%</b>	<b>5,549</b>	<b>5,209</b>	<b>-6%</b>
FVOD, PPI, Levy, Amort'n & Other	-2,369	-4,344	83%	-1,085	-3,090	185%	-335	-1,340	300%
<b>Statutory Pre-Tax Profit</b>	<b>2,263</b>	<b>-523</b>	<b>-123%</b>	<b>4,258</b>	<b>1,647</b>	<b>-61%</b>	<b>5,214</b>	<b>3,869</b>	<b>-26%</b>
Underlying EPS (p)	23.6	19.2	-19%	29.6	25.8	-13%	31.0	29.1	-6%
DPS (p)	0.0	0.0	-	10.0	10.0	0%	15.0	15.0	0%

Source: Citi Research

## Summary Financial Model

Figure 4. Royal Bank of Scotland – Group Profit and Loss Account 2010-17E (£m)

	2010	2011	2012	2013	%chg	2014E	%chg	2015E	%chg	2016E	%chg	2017E	%chg
<b>Net Interest Income</b>	14,200	12,313	11,417	10,992	-4%	11,086	1%	9,239	-17%	8,636	-7%	8,709	1%
Net Fee Income	5,983	5,417	4,876	4,518	-7%	3,887	-14%	2,889	-26%	2,720	-6%	2,828	4%
Income from trading activities	6,070	3,313	3,533	2,651	-25%	2,337	-12%	1,898	-19%	1,515	-20%	1,477	-3%
Other Operating Income	1,213	2,381	2,259	1,281	-43%	1,400	9%	1,753	25%	1,928	10%	1,978	3%
<b>Total Operating Revenue</b>	<b>27,466</b>	<b>23,424</b>	<b>22,085</b>	<b>19,442</b>	<b>-12%</b>	<b>18,710</b>	<b>-4%</b>	<b>15,778</b>	<b>-16%</b>	<b>14,799</b>	<b>-6%</b>	<b>14,992</b>	<b>1%</b>
Staff Costs	-8,956	-8,072	-7,377	-6,882	-7%	-6,082	-12%	-4,562	-25%	-4,052	-11%	-3,974	-2%
Other operating costs	-5,992	-5,139	-4,943	-5,170	5%	-4,714	-9%	-3,536	-25%	-3,141	-11%	-3,080	-2%
Depreciation	-1,762	-1,635	-1,534	-1,261	-18%	-1,200	-5%	-900	-25%	-800	-11%	-784	-2%
<b>Total Operating Costs</b>	<b>-16,710</b>	<b>-14,846</b>	<b>-13,854</b>	<b>-13,313</b>	<b>-4%</b>	<b>-11,995</b>	<b>-10%</b>	<b>-8,998</b>	<b>-25%</b>	<b>-7,992</b>	<b>-11%</b>	<b>-7,838</b>	<b>-2%</b>
Other net income	345	0	0	0	n.m.	0	n.m.	0	n.m.	0	n.m.	0	n.m.
<b>Gross Operating Profit</b>	<b>11,101</b>	<b>8,578</b>	<b>8,231</b>	<b>6,129</b>	<b>-26%</b>	<b>6,715</b>	<b>10%</b>	<b>6,781</b>	<b>1%</b>	<b>6,807</b>	<b>0%</b>	<b>7,154</b>	<b>5%</b>
Impairment losses	-9,256	-7,439	-5,279	-8,432	60%	-2,893	-66%	-2,044	-29%	-1,597	-22%	-1,345	-16%
<b>Pretax Profit (underlying)</b>	<b>1,845</b>	<b>1,139</b>	<b>2,952</b>	<b>-2,303</b>	<b>-178%</b>	<b>3,822</b>	<b>-266%</b>	<b>4,737</b>	<b>24%</b>	<b>5,209</b>	<b>10%</b>	<b>5,809</b>	<b>12%</b>
FVO gains	242	1,914	-4,649	-120	-97%	0	nm	0	nm	0	nm	0	nm
Restructuring costs, PPI & other	-2,336	-4,444	-3,580	-5,820	63%	-4,344	-25%	-3,090	-29%	-1,340	-57%	-540	-60%
<b>Pretax Profit (reported)</b>	<b>-249</b>	<b>-1,391</b>	<b>-5,277</b>	<b>-8,243</b>	<b>56%</b>	<b>-523</b>	<b>-94%</b>	<b>1,647</b>	<b>-415%</b>	<b>3,869</b>	<b>135%</b>	<b>5,269</b>	<b>36%</b>
Tax	-663	-1,075	-441	-382	-13%	118	-131%	-384	-427%	-903	135%	-1,229	36%
<b>Post-tax profit from continuing ops</b>	<b>-912</b>	<b>-2,466</b>	<b>-5,718</b>	<b>-8,625</b>	<b>51%</b>	<b>-405</b>	<b>-95%</b>	<b>1,263</b>	<b>-412%</b>	<b>2,967</b>	<b>135%</b>	<b>4,040</b>	<b>36%</b>
Profit / loss from discount'd ops (net of tax)	-28	348	-172	148	nm	0	nm	121	nm	0	nm	0	nm
Minority Interests (Incl. Non-Equity)	-61	-28	136	-120	nm	-12	nm	-12	nm	-12	nm	-12	nm
Preference dividends	-124	0	-301	-398	32%	-450	13%	-450	0%	-450	0%	-450	0%
<b>Net Attributable Profit</b>	<b>-1,125</b>	<b>-2,146</b>	<b>-6,055</b>	<b>-8,995</b>	<b>49%</b>	<b>-867</b>	<b>-90%</b>	<b>922</b>	<b>-206%</b>	<b>2,505</b>	<b>172%</b>	<b>3,578</b>	<b>43%</b>
Ordinary Dividend & DAS Paid Out	0	0	0	0	n.m.	-1,125	n.m.	-375	-67%	-1,313	250%	-1,688	29%
<b>Retained Earnings</b>	<b>-1,125</b>	<b>-2,146</b>	<b>-6,055</b>	<b>-8,995</b>	<b>49%</b>	<b>-1,992</b>	<b>-78%</b>	<b>546</b>	<b>-127%</b>	<b>1,191</b>	<b>118%</b>	<b>1,889</b>	<b>59%</b>
<b>PER SHARE DATA</b>													
Basic, Core EPS	96.7p	55.1p	54.6p	10.0p	-82%	33.0p	232%	33.3p	1%	32.7p	-2%	34.1p	4%
Basic Underlying EPS	7.5p	3.7p	15.6p	(24.6)p	-257%	19.2p	-178%	25.8p	34%	29.1p	12%	33.1p	14%
<b>Diluted Underlying EPS</b>	<b>7.5p</b>	<b>3.7p</b>	<b>15.6p</b>	<b>(24.6)p</b>	<b>-257%</b>	<b>19.2p</b>	<b>-178%</b>	<b>25.8p</b>	<b>34%</b>	<b>29.1p</b>	<b>12%</b>	<b>33.1p</b>	<b>14%</b>
Diluted EPS Reported	(10.5)p	(19.8)p	(55.0)p	(80.3)p	46%	(7.7)p	-90%	8.2p	-206%	22.3p	172%	31.8p	43%
Dividend per share, reported	0.0p	0.0p	0.0p	0.0p	n.m.	0.0p	n.m.	10.0p	n.m.	15.0p	50%	15.0p	0%
Diluted BVPS	641.6p	635.7p	570.2p	474.9p	-17%	457.2p	-4%	462.0p	1%	472.6p	2%	489.4p	4%
<b>Tangible diluted BVPS</b>	<b>509.9p</b>	<b>500.9p</b>	<b>448.3p</b>	<b>365.0p</b>	<b>-19%</b>	<b>347.3p</b>	<b>-5%</b>	<b>352.1p</b>	<b>1%</b>	<b>362.7p</b>	<b>3%</b>	<b>379.5p</b>	<b>5%</b>
<b>OPERATING RATIOS</b>													
Reported NIM	2.0%	1.9%	1.9%	2.0%		2.5%		2.3%		2.2%		2.3%	
<b>Cost-income ratio, adjusted</b>	<b>60.1%</b>	<b>63.4%</b>	<b>62.7%</b>	<b>68.5%</b>		<b>64.1%</b>		<b>57.0%</b>		<b>54.0%</b>		<b>52.3%</b>	
NPL ratio	7.4%	8.9%	9.1%	9.5%		6.7%		5.2%		3.3%		2.0%	
Coverage ratio (Provision / NPL)	47.1%	48.8%	51.7%	64.0%		64.0%		64.0%		64.0%		64.0%	
Adj. ROE	2.3%	0.6%	2.6%	-4.7%		4.1%		5.6%		6.2%		6.9%	
<b>Adj. ROTE</b>	<b>3.9%</b>	<b>0.7%</b>	<b>3.2%</b>	<b>-6.0%</b>		<b>5.4%</b>		<b>7.4%</b>		<b>8.1%</b>		<b>8.9%</b>	
Adj RoA	0.05%	0.03%	0.12%	-0.23%		0.22%		0.33%		0.38%		0.44%	
<b>BALANCE SHEET SUMMARY</b>													
Total assets	1,452,634	1,506,867	1,312,295	1,027,878	-22%	964,853	-6%	859,582	-11%	847,062	-1%	852,143	1%
Net loans and advances to customers	502,748	454,112	430,088	390,825	-9%	371,403	-5%	285,768	-23%	277,097	-3%	277,382	0%
Customer accounts	510,693	502,955	521,279	470,880	-10%	476,686	1%	402,389	-16%	408,128	1%	415,812	2%
Loan to deposit ratio	98%	90%	83%	83%		78%		71%		68%		67%	
Total shareholders funds	70,388	70,075	63,386	53,450	-16%	51,458	-4%	52,004	1%	53,196	2%	55,085	4%
<b>CAPITAL POSITION</b>													
Core tier 1 capital (Basel 2)	49,309	46,341	47,320	42,165	-11%	40,173	-5%	40,719	1%	41,911	3%	43,800	5%
Core tier 1 capital (Basel 3)	46,897	44,218	37,908	36,768	-3%	35,358	-4%	37,050	5%	38,277	3%	40,027	5%
Risk weighted assets (Basel 2)	462,600	439,000	459,600	385,500	-16%	356,788	-7%	269,510	-24%	256,622	-5%	255,429	0%
Risk weighted assets (Basel 3)	675,725	582,035	494,600	429,100	-13%	400,788	-7%	313,510	-22%	300,622	-4%	299,429	0%
<b>Basel 2 Core Tier 1 Ratio (%)</b>	<b>10.7%</b>	<b>10.6%</b>	<b>10.3%</b>	<b>10.9%</b>		<b>11.3%</b>		<b>15.1%</b>		<b>16.3%</b>		<b>17.1%</b>	
<b>Basel 3 Core Tier 1 Ratio (%)</b>	<b>6.9%</b>	<b>7.6%</b>	<b>7.7%</b>	<b>8.6%</b>		<b>8.8%</b>		<b>11.8%</b>		<b>12.7%</b>		<b>13.4%</b>	
Basel 2 Tier 1 ratio (%)	12.9%	13.0%	12.4%	13.1%		13.6%		18.2%		19.6%		20.5%	

Source: Company Reports and Citi Research Estimates

Figure 5. Royal Bank of Scotland – Group Profit and Loss Account 1Q11-1Q14E (£m)

	1Q11	2Q11	3Q11	4Q11	1Q12	2Q12	3Q12	4Q12	1Q13	2Q13	3Q13	4Q13	1Q14E
Net Interest Income	3,203	3,135	2,987	2,988	2,923	2,907	2,811	2,776	2,672	2,770	2,783	2,767	2,740
Net Fee Income	1,460	1,460	1,247	1,250	1,306	1,249	1,191	1,130	1,106	1,142	1,144	1,126	984
Income from trading activities	1,570	1,219	282	242	1,264	929	769	571	1,016	874	599	162	797
Other Operating Income	673	830	505	373	672	435	787	365	367	661	368	-115	350
<b>Total Operating Revenue</b>	<b>6,906</b>	<b>6,644</b>	<b>5,021</b>	<b>4,853</b>	<b>6,165</b>	<b>5,520</b>	<b>5,558</b>	<b>4,842</b>	<b>5,161</b>	<b>5,447</b>	<b>4,894</b>	<b>3,940</b>	<b>4,871</b>
Staff Costs	-2,298	-2,080	-1,949	-1,745	-2,171	-1,945	-1,882	-1,379	-1,821	-1,764	-1,758	-1,539	-1,618
Other operating costs	-1,290	-1,280	-1,318	-1,251	-1,234	-1,307	-1,217	-1,185	-1,221	-1,327	-1,223	-1,399	-1,222
Depreciation	-373	-396	-416	-450	-394	-382	-374	-384	-339	-308	-305	-309	-300
<b>Total Operating Costs</b>	<b>-3,961</b>	<b>-3,756</b>	<b>-3,683</b>	<b>-3,446</b>	<b>-3,799</b>	<b>-3,634</b>	<b>-3,473</b>	<b>-2,948</b>	<b>-3,381</b>	<b>-3,399</b>	<b>-3,286</b>	<b>-3,247</b>	<b>-3,139</b>
Other net income	0	0	0	0	0	0	0	0	0	0	0	0	0
<b>Gross Operating Profit</b>	<b>2,945</b>	<b>2,888</b>	<b>1,338</b>	<b>1,407</b>	<b>2,366</b>	<b>1,886</b>	<b>2,085</b>	<b>1,894</b>	<b>1,780</b>	<b>2,048</b>	<b>1,608</b>	<b>693</b>	<b>1,732</b>
Impairment losses	-1,947	-2,264	-1,536	-1,692	-1,314	-1,335	-1,176	-1,454	-1,033	-1,117	-1,170	-5,112	-807
<b>Pretax Profit (underlying)</b>	<b>998</b>	<b>624</b>	<b>-198</b>	<b>-285</b>	<b>1,052</b>	<b>551</b>	<b>909</b>	<b>440</b>	<b>747</b>	<b>931</b>	<b>438</b>	<b>-4,419</b>	<b>924</b>
FVO gains	-560	324	2,622	-472	-2,456	-518	-1,455	-220	249	127	-496	0	0
Restructuring costs, PPI & other	-685	-1,831	-599	-1,336	-110	-201	-822	-2,447	-170	-510	-576	-4,564	-535
<b>Pretax Profit (reported)</b>	<b>-247</b>	<b>-883</b>	<b>1,825</b>	<b>-2,093</b>	<b>-1,514</b>	<b>-168</b>	<b>-1,368</b>	<b>-2,227</b>	<b>826</b>	<b>548</b>	<b>-634</b>	<b>-8,983</b>	<b>389</b>
Tax	-389	-168	-744	226	-138	-261	-3	-39	-350	-328	-81	377	-101
<b>Post-tax profit from continuing ops</b>	<b>-636</b>	<b>-1,051</b>	<b>1,081</b>	<b>-1,867</b>	<b>-1,652</b>	<b>-429</b>	<b>-1,371</b>	<b>-2,266</b>	<b>476</b>	<b>220</b>	<b>-715</b>	<b>-8,606</b>	<b>288</b>
Profit / loss from discont'd operations (net of tax)	69	133	100	46	93	13	67	-345	129	9	-5	15	0
Minority Interests (Incl. Non-Equity)	1	-18	7	-18	14	11	3	108	-131	14	-6	3	-3
Preference dividends	0	0	0	0	0	-82	-104	-115	-81	-101	-102	-114	-113
<b>Net Attributable Profit</b>	<b>-566</b>	<b>-936</b>	<b>1,188</b>	<b>-1,839</b>	<b>-1,545</b>	<b>-487</b>	<b>-1,405</b>	<b>-2,618</b>	<b>393</b>	<b>142</b>	<b>-828</b>	<b>-8,702</b>	<b>173</b>
Ordinary Dividend & DAS Paid Out	0	0	0	0	0	0	0	0	0	0	0	0	0
<b>Retained Earnings</b>	<b>-566</b>	<b>-936</b>	<b>1,188</b>	<b>-1,839</b>	<b>-1,545</b>	<b>-487</b>	<b>-1,405</b>	<b>-2,618</b>	<b>393</b>	<b>142</b>	<b>-828</b>	<b>-8,702</b>	<b>173</b>
<b>PER SHARE DATA</b>													
Basic, Core EPS	32.6p	13.1p	3.6p	6.2p	11.6p	22.9p	10.1p	10.1p	5.3p	3.4p	7.1p	(5.9)p	8.7p
Basic Underlying EPS	6.3p	3.5p	(1.7)p	(4.4)p	6.8p	2.6p	4.8p	1.5p	2.7p	2.4p	1.6p	(31.2)p	4.8p
<b>Diluted Underlying EPS</b>	<b>6.3p</b>	<b>3.5p</b>	<b>(1.7)p</b>	<b>(4.3)p</b>	<b>6.7p</b>	<b>2.6p</b>	<b>4.7p</b>	<b>1.5p</b>	<b>2.7p</b>	<b>2.4p</b>	<b>1.6p</b>	<b>(31.2)p</b>	<b>4.8p</b>
Diluted EPS Reported	(5.3)p	(8.7)p	10.9p	(17.0)p	(14.2)p	(4.4)p	(12.7)p	(23.6)p	3.5p	1.3p	(7.4)p	(77.3)p	1.5p
Dividend per share, reported	6.3p	3.5p	(1.7)p	(4.3)p	6.7p	2.6p	4.7p	1.5p	2.7p	2.4p	1.6p	(31.2)p	4.8p
Diluted BVPS	647.0p	648.3p	669.8p	635.7p	621.2p	623.1p	608.4p	567.4p	577.1p	563.7p	555.8p	474.9p	476.4p
<b>Tangible diluted BVPS</b>	<b>512.5p</b>	<b>513.2p</b>	<b>533.9p</b>	<b>500.9p</b>	<b>487.6p</b>	<b>489.2p</b>	<b>475.9p</b>	<b>446.2p</b>	<b>454.1p</b>	<b>440.2p</b>	<b>433.3p</b>	<b>365.0p</b>	<b>366.5p</b>
<b>OPERATING RATIOS</b>													
Reported NIM	2.0%	1.9%	1.8%	1.8%	1.9%	1.9%	1.9%	1.9%	1.9%	2.0%	2.0%	2.1%	2.2%
<b>Cost-income ratio, adjusted</b>	<b>57.4%</b>	<b>56.5%</b>	<b>73.4%</b>	<b>71.0%</b>	<b>61.6%</b>	<b>65.8%</b>	<b>62.5%</b>	<b>60.9%</b>	<b>65.5%</b>	<b>62.4%</b>	<b>67.1%</b>	<b>82.4%</b>	<b>64.4%</b>
NPL ratio	8.0%	8.3%	8.4%	8.9%	9.0%	9.0%	9.3%	9.1%	9.0%	9.6%	9.4%	9.5%	8.7%
Coverage ratio (Provision / NPL)	46.9%	49.0%	48.5%	48.8%	50.8%	51.3%	50.8%	51.7%	52.4%	51.6%	53.1%	64.0%	64.0%
<b>BALANCE SHEET SUMMARY</b>													
Total Assets (m)	1,413	1,446	1,608	1,507	1,403	1,415	1,377	1,312	1,308	1,216	1,129	1,028	1,011
Net loans and advances to customers	494,148	489,572	485,573	454,112	440,406	434,965	423,155	430,088	432,360	418,792	406,927	390,825	385,319
Customer accounts	518,906	517,525	529,351	502,955	497,510	501,719	506,055	521,279	526,095	526,418	506,941	470,880	472,666
Loan to deposit ratio	95%	95%	92%	90%	89%	87%	84%	83%	82%	80%	80%	83%	82%
Total shareholders funds	69,332	70,000	72,699	70,075	68,672	69,272	67,955	63,386	65,341	63,891	62,376	53,450	53,623
<b>CAPITAL POSITION</b>													
Core tier 1 capital (Basel 2)	49,038	48,001	47,830	46,341	46,802	48,155	48,100	47,320	48,245	48,444	47,525	42,165	42,338
<b>Tier 1 capital (Basel 2)</b>	<b>59,548</b>	<b>58,387</b>	<b>58,336</b>	<b>56,990</b>	<b>57,342</b>	<b>58,459</b>	<b>58,079</b>	<b>57,135</b>	<b>57,459</b>	<b>57,788</b>	<b>56,630</b>	<b>50,626</b>	<b>50,799</b>
Risk weighted assets (Basel 2)	439,700	433,500	423,300	439,000	434,300	434,700	432,900	459,600	445,800	436,000	410,000	385,500	374,858
<b>Basel 2 Core Tier 1 Ratio (%)</b>	<b>11.2%</b>	<b>11.1%</b>	<b>11.3%</b>	<b>10.6%</b>	<b>10.8%</b>	<b>11.1%</b>	<b>11.1%</b>	<b>10.3%</b>	<b>10.8%</b>	<b>11.1%</b>	<b>11.6%</b>	<b>10.9%</b>	<b>11.3%</b>
Basel 2 Tier 1 ratio (%)	13.5%	13.5%	13.8%	13.0%	13.2%	13.4%	13.4%	12.4%	12.9%	13.3%	13.8%	13.1%	13.6%

Source: Company Reports and Citi Research Estimates

Figure 6. Royal Bank of Scotland – Divisional Profit and Loss Account 2010-2017E (£m)

	2010	2011	2012	2013	%chg	2014E	%chg	2015E	%chg	2016E	%chg	2017E	%chg
<b>MARKETS</b>													
Rates	2,312	2,067	2,230	1,314	-41%	935	-29%	795	-15%	676	-15%	669	-1%
Currencies	1,047	1,060	757	920	22%	594	-35%	505	-15%	429	-15%	425	-1%
Asset backed products	1,479	1,254	1,318	940	-29%	823	-12%	659	-20%	527	-20%	522	-1%
Credit markets	1,350	616	862	714	-17%	737	3%	589	-20%	471	-20%	467	-1%
Investor products and equity derivatives	672	0	0	0	n.m.	0	n.m.	0	n.m.	0	n.m.	0	n.m.
<b>Total income continuing businesses</b>	<b>6,860</b>	<b>4,997</b>	<b>5,167</b>	<b>3,888</b>	<b>-25%</b>	<b>3,090</b>	<b>-21%</b>	<b>2,548</b>	<b>-18%</b>	<b>2,104</b>	<b>-17%</b>	<b>2,083</b>	<b>-1%</b>
Inter-divisional revenue share	-883	-767	-691	-611	-12%	-484	-21%	-399	-18%	-330	-17%	-326	-1%
Run-off businesses	256	185	7	45	543%	0	-100%	0	n.m.	0	n.m.	0	n.m.
<b>Total income</b>	<b>6,233</b>	<b>4,415</b>	<b>4,483</b>	<b>3,322</b>	<b>-26%</b>	<b>2,605</b>	<b>-22%</b>	<b>2,149</b>	<b>-18%</b>	<b>1,774</b>	<b>-17%</b>	<b>1,756</b>	<b>-1%</b>
Total Direct Expenses	-2,745	-2,707	-2,175	-1,900	-13%	-1,542	-19%	-1,264	-18%	-1,037	-18%	-985	-5%
Indirect Expenses	-699	-771	-762	-710	-7%	-655	-8%	-537	-18%	-440	-18%	-418	-5%
<b>Operating Profit</b>	<b>2,789</b>	<b>937</b>	<b>1,546</b>	<b>712</b>	<b>-54%</b>	<b>408</b>	<b>-43%</b>	<b>347</b>	<b>-15%</b>	<b>297</b>	<b>-15%</b>	<b>353</b>	<b>19%</b>
Impairment losses	-65	-38	-37	-92	149%	0	-100%	0	n.m.	0	n.m.	0	n.m.
<b>Pretax Contribution</b>	<b>2,724</b>	<b>899</b>	<b>1,509</b>	<b>620</b>	<b>-59%</b>	<b>408</b>	<b>-34%</b>	<b>347</b>	<b>-15%</b>	<b>297</b>	<b>-15%</b>	<b>353</b>	<b>19%</b>
Total third party assets (ex derivs mtm)	396,700	312,600	284,400	212,800	-25%	173,327	-19%	138,662	-20%	110,929	-20%	106,175	-4%
Risk Weighted Assets	146,900	120,300	101,300	64,500	-36%	52,536	-19%	42,029	-20%	33,623	-20%	31,942	-5%
Cost/income	55%	79%	64%	79%		84%		84%		83%		80%	
RoE*	17%	6%	10%	5%		4%		4%		4%		5%	
<b>UK CORP AND COMMERCIAL</b>													
Net Interest Income	3,000	3,092	2,974	2,874	-3%	2,962	3%	3,209	8%	3,047	-5%	3,169	4%
Fees and commissions	1,353	1,375	1,365	1,310	-4%	1,355	3%	1,423	5%	1,352	-5%	1,392	3%
Non-Interest Income	443	396	384	283	-26%	300	6%	315	5%	299	-5%	308	3%
<b>Total Income</b>	<b>4,796</b>	<b>4,863</b>	<b>4,723</b>	<b>4,467</b>	<b>-5%</b>	<b>4,617</b>	<b>3%</b>	<b>4,947</b>	<b>7%</b>	<b>4,698</b>	<b>-5%</b>	<b>4,869</b>	<b>4%</b>
Total Direct Expenses	-1,323	-1,324	-1,304	-1,354	4%	-1,285	-5%	-1,246	-3%	-1,134	-9%	-1,145	1%
Indirect Expenses	-813	-822	-785	-865	10%	-880	2%	-898	2%	-816	-9%	-833	2%
<b>Operating Profit</b>	<b>2,660</b>	<b>2,717</b>	<b>2,634</b>	<b>2,248</b>	<b>-15%</b>	<b>2,452</b>	<b>9%</b>	<b>2,803</b>	<b>14%</b>	<b>2,747</b>	<b>-2%</b>	<b>2,891</b>	<b>5%</b>
Impairment losses	-767	-793	-838	-1,188	42%	-640	-46%	-598	-7%	-508	-15%	-528	4%
<b>Pretax Contribution</b>	<b>1,893</b>	<b>1,924</b>	<b>1,796</b>	<b>1,060</b>	<b>-41%</b>	<b>1,812</b>	<b>71%</b>	<b>2,205</b>	<b>22%</b>	<b>2,240</b>	<b>2%</b>	<b>2,363</b>	<b>6%</b>
Gross Loans & Advances To Customers	113,800	110,700	107,000	102,500	-4%	106,662	4%	99,564	-7%	103,546	4%	107,688	4%
Risk Weighted Assets	84,200	79,300	86,300	86,100	0%	89,596	4%	84,367	-6%	87,742	4%	91,251	4%
Reported NIM	2.51%	3.06%	3.06%	3.07%		3.07%		3.23%		3.28%		3.28%	
Cost income ratio	45%	44%	44%	50%		47%		43%		42%		41%	
Impairment charge / advances (bp)	68	71	77	113		61		55		50		50	
RoE*	12%	12%	15%	8%		13%		17%		16%		17%	
<b>UK RETAIL</b>													
Net Interest Income	4,054	4,302	3,990	3,979	0%	4,200	6%	4,407	5%	4,329	-2%	4,604	6%
Fees and commissions	1,100	1,066	884	919	4%	955	4%	993	4%	983	-1%	1,023	4%
Other non-interest income	237	140	95	39	-59%	40	3%	42	4%	41	-1%	43	4%
<b>Total Income</b>	<b>5,391</b>	<b>5,508</b>	<b>4,969</b>	<b>4,937</b>	<b>-1%</b>	<b>5,195</b>	<b>5%</b>	<b>5,441</b>	<b>5%</b>	<b>5,353</b>	<b>-2%</b>	<b>5,669</b>	<b>6%</b>
Total Direct Expenses	-1,369	-1,290	-1,183	-1,269	7%	-1,160	-9%	-1,102	-5%	-1,001	-9%	-1,011	1%
Indirect Expenses	-1,514	-1,409	-1,366	-1,401	3%	-1,375	-2%	-1,348	-2%	-1,224	-9%	-1,261	3%
<b>Operating Profit</b>	<b>2,508</b>	<b>2,809</b>	<b>2,420</b>	<b>2,267</b>	<b>-6%</b>	<b>2,660</b>	<b>17%</b>	<b>2,830</b>	<b>6%</b>	<b>3,128</b>	<b>11%</b>	<b>3,397</b>	<b>9%</b>
Impairment losses	-1,160	-788	-529	-324	-39%	-316	-2%	-387	22%	-436	13%	-538	23%
<b>Pretax Contribution</b>	<b>1,348</b>	<b>2,021</b>	<b>1,891</b>	<b>1,943</b>	<b>3%</b>	<b>2,344</b>	<b>21%</b>	<b>2,443</b>	<b>4%</b>	<b>2,692</b>	<b>10%</b>	<b>2,859</b>	<b>6%</b>
Gross Loans & Advances To Customers	108,400	110,800	113,600	113,200	0%	117,512	4%	114,006	-3%	118,296	4%	122,751	4%
Risk Weighted Assets	48,800	48,400	45,700	43,900	-4%	45,572	4%	44,292	-3%	46,506	5%	48,832	5%
Reported NIM	3.91%	3.92%	3.58%	3.57%		3.57%		3.86%		3.78%		3.87%	
Cost income ratio	53%	49%	51%	54%		49%		48%		42%		40%	
Impairment charge / advances (bp)	110	72	50	17		28		33		38		45	
RoE*	18%	26%	24%	26%		31%		33%		34%		35%	
<b>UK WEALTH</b>													
Net Interest Income	588	645	720	674	-6%	700	4%	735	5%	772	5%	810	5%
Fees and commissions	376	375	366	355	-3%	360	1%	378	5%	393	4%	409	4%
Other non-interest income	71	84	84	64	-24%	60	-6%	62	4%	65	4%	67	4%
<b>Total Income</b>	<b>1,035</b>	<b>1,104</b>	<b>1,170</b>	<b>1,093</b>	<b>-7%</b>	<b>1,120</b>	<b>2%</b>	<b>1,176</b>	<b>5%</b>	<b>1,230</b>	<b>5%</b>	<b>1,287</b>	<b>5%</b>
Total Direct Expenses	-524	-539	-581	-529	-9%	-500	-5%	-495	-1%	-498	1%	-502	1%
Indirect Expenses	-210	-298	-300	-314	5%	-300	-4%	-303	1%	-306	1%	-309	1%
<b>Operating Profit</b>	<b>301</b>	<b>267</b>	<b>289</b>	<b>250</b>	<b>-13%</b>	<b>320</b>	<b>28%</b>	<b>378</b>	<b>18%</b>	<b>426</b>	<b>13%</b>	<b>476</b>	<b>12%</b>
Impairment losses	-18	-25	-46	-29	-37%	-20	-31%	-18	-10%	-19	5%	-20	5%
<b>Pretax Contribution</b>	<b>283</b>	<b>242</b>	<b>243</b>	<b>221</b>	<b>-9%</b>	<b>300</b>	<b>36%</b>	<b>360</b>	<b>20%</b>	<b>407</b>	<b>13%</b>	<b>456</b>	<b>12%</b>
Gross Loans & Advances To Customers	16,100	16,900	17,100	16,800	-2%	17,604	5%	18,459	5%	19,355	5%	20,295	5%
Risk Weighted Assets	12,500	12,900	12,300	12,000	-2%	12,575	5%	13,185	5%	13,825	5%	14,496	5%
Fees as % of AUM	1.20%	1.19%	1.22%	1.21%		1.19%		1.20%		1.20%		1.20%	
Cost income ratio	71%	76%	75%	77%		71%		68%		65%		63%	
RoE*	19%	19%	13%	12%		16%		18%		19%		20%	

Source: Company Reports and Citi Research Estimates; \*Note: Based on 10% CET1 allocation



Figure 7. Royal Bank of Scotland – Divisional Profit and Loss Account 1Q11-1Q14E (£m)

	1Q11	2Q11	3Q11	4Q11	1Q12	2Q12	3Q12	4Q12	1Q13	2Q13	3Q13	4Q13	1Q14E
<b>MARKETS</b>													
Rates	965	470	118	514	924	507	466	333	340	395	390	189	272
Currencies	241	267	293	259	246	175	173	163	192	257	257	214	173
Asset backed products	617	367	241	29	427	378	374	139	437	174	125	204	350
Credit markets	430	208	-58	36	313	184	186	179	238	146	187	143	214
Investor products and equity derivatives	0	0	0	0	0	0	0	0	0	0	0	0	0
<b>Total income continuing businesses</b>	<b>2,253</b>	<b>1,312</b>	<b>594</b>	<b>838</b>	<b>1,910</b>	<b>1,244</b>	<b>1,199</b>	<b>814</b>	<b>1,207</b>	<b>972</b>	<b>959</b>	<b>750</b>	<b>1,009</b>
Inter-divisional revenue share	-208	-204	-178	-177	-186	-174	-159	-172	-167	-150	-162	-132	-140
Run-off businesses	63	60	31	31	10	-4	2	-1	0	0	37	8	0
<b>Total income</b>	<b>2,108</b>	<b>1,168</b>	<b>447</b>	<b>692</b>	<b>1,734</b>	<b>1,066</b>	<b>1,042</b>	<b>641</b>	<b>1,040</b>	<b>822</b>	<b>834</b>	<b>626</b>	<b>869</b>
Total Direct Expenses	-892	-664	-600	-551	-712	-610	-559	-294	-567	-508	-447	-378	-469
Indirect Expenses	-187	-191	-200	-193	-196	-186	-194	-186	-179	-178	-178	-175	-170
<b>Operating Profit</b>	<b>1,029</b>	<b>313</b>	<b>-353</b>	<b>-52</b>	<b>826</b>	<b>270</b>	<b>289</b>	<b>161</b>	<b>294</b>	<b>136</b>	<b>209</b>	<b>73</b>	<b>230</b>
Impairment losses	0	14	5	-57	-2	-19	6	-22	-16	-43	1	-34	0
<b>Pretax Contribution</b>	<b>1,029</b>	<b>327</b>	<b>-348</b>	<b>-109</b>	<b>824</b>	<b>251</b>	<b>295</b>	<b>139</b>	<b>278</b>	<b>93</b>	<b>210</b>	<b>39</b>	<b>230</b>
Total third party assets (ex derivs mtm)	366,600	362,100	346,400	312,600	299,800	302,000	304,200	284,400	287,900	267,700	248,200	212,800	202,160
Risk Weighted Assets	114,300	106,600	104,000	120,300	115,600	107,900	108,000	101,300	88,500	86,800	73,200	64,500	61,275
Cost/Income	51%	73%	179%	108%	52%	75%	72%	75%	72%	83%	75%	88%	74%
RoE*	26%	8%	-8%	-2%	21%	7%	8%	4%	8%	3%	7%	2%	9%
<b>UK CORP AND COMMERCIAL</b>													
Net Interest Income	811	770	753	758	756	772	729	717	706	715	725	728	733
Fees and commissions	345	336	353	341	336	346	334	349	321	335	328	326	330
Non-Interest Income	106	112	100	78	109	93	75	107	57	92	59	75	75
<b>Total Income</b>	<b>1,262</b>	<b>1,218</b>	<b>1,206</b>	<b>1,177</b>	<b>1,201</b>	<b>1,211</b>	<b>1,138</b>	<b>1,173</b>	<b>1,084</b>	<b>1,142</b>	<b>1,112</b>	<b>1,129</b>	<b>1,138</b>
Total Direct Expenses	-342	-322	-326	-334	-334	-325	-320	-325	-333	-339	-319	-363	-335
Indirect Expenses	-196	-204	-221	-201	-199	-193	-203	-190	-208	-214	-221	-222	-220
<b>Operating Profit</b>	<b>724</b>	<b>692</b>	<b>659</b>	<b>642</b>	<b>668</b>	<b>693</b>	<b>615</b>	<b>658</b>	<b>543</b>	<b>589</b>	<b>572</b>	<b>544</b>	<b>583</b>
Impairment losses	-107	-220	-230	-236	-176	-181	-247	-234	-185	-194	-150	-659	-160
<b>Pretax Contribution</b>	<b>617</b>	<b>472</b>	<b>429</b>	<b>406</b>	<b>492</b>	<b>512</b>	<b>368</b>	<b>424</b>	<b>358</b>	<b>395</b>	<b>422</b>	<b>-115</b>	<b>423</b>
Gross Loans & Advances To Customers	114,800	113,200	112,600	110,700	109,700	110,100	108,300	107,000	106,800	104,600	103,800	102,500	103,525
Risk Weighted Assets	82,300	81,000	78,800	79,300	76,900	79,400	82,100	86,300	87,000	88,100	87,200	86,100	86,961
Reported NIM	3.19%	3.03%	2.98%	3.02%	3.09%	3.17%	2.99%	2.97%	3.01%	3.05%	3.09%	3.13%	3.19%
Cost income ratio	43%	43%	45%	45%	44%	43%	46%	44%	50%	48%	49%	52%	49%
Impairment charge / advances (bp)	37	77	81	85	64	66	90	87	69	73	58	256	62
RoE*	19%	15%	14%	13%	16%	17%	12%	13%	11%	12%	12%	-3%	12%
<b>UK RETAIL</b>													
Net Interest Income	1,086	1,098	1,086	1,032	1,001	988	990	1,011	965	987	1,013	1,014	1,020
Fees and commissions	270	295	259	242	237	214	231	202	212	215	243	249	230
Other non-interest income	34	38	33	35	29	28	21	17	14	10	11	4	10
<b>Total Income</b>	<b>1,390</b>	<b>1,431</b>	<b>1,378</b>	<b>1,309</b>	<b>1,267</b>	<b>1,230</b>	<b>1,242</b>	<b>1,230</b>	<b>1,191</b>	<b>1,212</b>	<b>1,267</b>	<b>1,267</b>	<b>1,260</b>
Total Direct Expenses	-332	-327	-311	-320	-289	-324	-294	-276	-290	-295	-314	-370	-290
Indirect Expenses	-346	-361	-362	-340	-346	-329	-343	-348	-344	-351	-354	-352	-350
<b>Operating Profit</b>	<b>712</b>	<b>743</b>	<b>705</b>	<b>649</b>	<b>632</b>	<b>577</b>	<b>605</b>	<b>606</b>	<b>557</b>	<b>566</b>	<b>599</b>	<b>545</b>	<b>620</b>
Impairment losses	-194	-208	-195	-191	-155	-140	-141	-93	-80	-89	-82	-73	-82
<b>Pretax Contribution</b>	<b>518</b>	<b>535</b>	<b>510</b>	<b>458</b>	<b>477</b>	<b>437</b>	<b>464</b>	<b>513</b>	<b>477</b>	<b>477</b>	<b>517</b>	<b>472</b>	<b>538</b>
Gross Loans & Advances To Customers	110,000	110,400	110,100	110,800	112,500	113,000	112,900	113,600	113,200	112,200	112,700	113,200	114,263
Risk Weighted Assets	50,300	49,667	48,700	48,400	48,200	47,400	47,700	45,700	44,500	44,100	44,800	43,900	44,312
Reported NIM	4.04%	4.00%	3.90%	3.75%	3.61%	3.57%	3.53%	3.60%	3.49%	3.56%	3.62%	3.60%	3.61%
Cost income ratio	49%	48%	49%	50%	50%	53%	51%	51%	53%	53%	53%	57%	51%
Impairment charge / advances (bp)	71	75	71	69	56	50	50	33	28	32	29	26	29
RoE*	25%	26%	25%	23%	24%	23%	24%	27%	26%	26%	28%	26%	29%
<b>UK WEALTH</b>													
Net Interest Income	157	168	152	168	179	178	185	178	169	162	169	174	175
Fees and commissions	97	94	95	89	93	90	94	89	89	91	90	85	90
Other non-interest income	17	21	23	23	18	35	13	18	15	19	12	18	15
<b>Total Income</b>	<b>271</b>	<b>283</b>	<b>270</b>	<b>280</b>	<b>290</b>	<b>303</b>	<b>292</b>	<b>285</b>	<b>273</b>	<b>272</b>	<b>271</b>	<b>277</b>	<b>280</b>
Total Direct Expenses	-126	-144	-147	-122	-159	-157	-146	-119	-132	-137	-132	-128	-130
Indirect Expenses	-72	-77	-76	-73	-78	-73	-75	-74	-80	-77	-78	-79	-75
<b>Operating Profit</b>	<b>73</b>	<b>62</b>	<b>47</b>	<b>85</b>	<b>53</b>	<b>73</b>	<b>71</b>	<b>92</b>	<b>61</b>	<b>58</b>	<b>61</b>	<b>70</b>	<b>75</b>
Impairment losses	-5	-3	-4	-13	-10	-12	-8	-16	-5	-2	-1	-21	-5
<b>Pretax Contribution</b>	<b>68</b>	<b>59</b>	<b>43</b>	<b>72</b>	<b>43</b>	<b>61</b>	<b>63</b>	<b>76</b>	<b>56</b>	<b>56</b>	<b>60</b>	<b>49</b>	<b>70</b>
Gross Loans & Advances To Customers	16,500	16,800	17,000	16,900	16,900	17,000	17,000	17,100	17,200	17,100	16,900	16,800	16,998
Risk Weighted Assets	12,600	12,900	13,000	12,900	12,900	12,300	12,300	12,300	12,500	12,500	12,100	12,000	12,141
Fees as % of AUM	1.13%	1.10%	1.27%	1.15%	1.18%	1.18%	1.23%	1.16%	1.17%	1.17%	1.14%	1.14%	1.20%
Cost income ratio	73%	78%	83%	70%	82%	76%	76%	68%	78%	79%	77%	75%	73%
RoE*	15%	13%	9%	15%	9%	13%	14%	17%	12%	12%	13%	11%	15%

Source: Company Reports and Citi Research Estimates; \*Note: Based on 10% CET1 allocation

Figure 8. Royal Bank of Scotland – Divisional Profit and Loss Account 2010-2017E (£m) (contd)

	2010	2011	2012	2013	%chg	2014E	%chg	2015E	%chg	2016E	%chg	2017E	%chg
<b>INTERNATIONAL BANKING</b>													
Net interest income	1,353	1,199	922	713	-23%	599	-16%	586	-2%	587	0%	598	2%
Non-interest income	1,924	1,356	1,200	1,135	-5%	1,050	-7%	998	-5%	948	-5%	967	2%
<b>Total income</b>	<b>3,277</b>	<b>2,555</b>	<b>2,122</b>	<b>1,848</b>	<b>-13%</b>	<b>1,649</b>	<b>-11%</b>	<b>1,584</b>	<b>-4%</b>	<b>1,535</b>	<b>-3%</b>	<b>1,565</b>	<b>2%</b>
Total direct expenses	-1,145	-938	-744	-701	-6%	-610	-13%	-557	-9%	-509	-9%	-483	-5%
Indirect Expenses	-735	-694	-673	-639	-5%	-620	-3%	-566	-9%	-517	-9%	-491	-5%
<b>Operating Profit</b>	<b>1,397</b>	<b>923</b>	<b>705</b>	<b>508</b>	<b>-28%</b>	<b>419</b>	<b>-17%</b>	<b>461</b>	<b>10%</b>	<b>509</b>	<b>10%</b>	<b>590</b>	<b>16%</b>
Impairment losses	-86	-168	-111	-229	106%	-70	-69%	-48	-32%	-45	-5%	-44	-3%
<b>Pretax Contribution</b>	<b>1,311</b>	<b>755</b>	<b>594</b>	<b>279</b>	<b>-53%</b>	<b>349</b>	<b>25%</b>	<b>413</b>	<b>18%</b>	<b>463</b>	<b>12%</b>	<b>546</b>	<b>18%</b>
Total third party assets	77,900	69,900	53,000	48,500	-8%	43,829	-10%	41,637	-5%	39,556	-5%	39,160	-1%
Risk Weighted Assets	51,700	43,200	51,900	49,000	-6%	44,281	-10%	42,067	-5%	39,963	-5%	39,564	-1%
Reported NIM	1.92%	1.60%	1.64%	1.59%		1.59%		1.68%		1.77%		1.86%	
Cost/income	57%	64%	67%	73%		75%		71%		67%		62%	
Impairment charge / advances (bp)	14	30	27	64		22		15		15		15	
RoE*	15%	8%	9%	4%		5%		7%		8%		9%	
<b>ULSTER BANK</b>													
Net Interest Income	839	736	649	631	-3%	574	-9%	545	-5%	471	-14%	418	-11%
Fees and commissions	156	142	145	141	-3%	134	-5%	120	-10%	108	-10%	97	-10%
Other non-interest income	58	69	51	99	94%	93	-6%	84	-10%	75	-10%	68	-10%
<b>Total Income</b>	<b>1,053</b>	<b>947</b>	<b>845</b>	<b>871</b>	<b>3%</b>	<b>801</b>	<b>-8%</b>	<b>749</b>	<b>-6%</b>	<b>655</b>	<b>-13%</b>	<b>583</b>	<b>-11%</b>
Total Direct Expenses	-311	-292	-263	-302	15%	-280	-7%	-238	-15%	-209	-12%	-188	-10%
Indirect Expenses	-264	-255	-258	-252	-2%	-240	-5%	-204	-15%	-180	-12%	-162	-10%
<b>Operating Profit</b>	<b>478</b>	<b>400</b>	<b>324</b>	<b>317</b>	<b>-2%</b>	<b>281</b>	<b>-11%</b>	<b>307</b>	<b>9%</b>	<b>266</b>	<b>-13%</b>	<b>233</b>	<b>-12%</b>
Impairment losses	-1,161	-1,384	-1,364	-1,774	30%	-510	-71%	-291	-43%	-193	-34%	-123	-36%
<b>Pretax Contribution</b>	<b>-683</b>	<b>-984</b>	<b>-1,040</b>	<b>-1,457</b>	<b>40%</b>	<b>-229</b>	<b>-84%</b>	<b>16</b>	<b>-107%</b>	<b>73</b>	<b>364%</b>	<b>109</b>	<b>51%</b>
Gross Loans To Customers	36,900	34,100	32,600	31,400	-4%	25,648	-18%	20,992	-18%	17,683	-16%	15,234	-14%
Risk Weighted Assets	32,644	36,300	36,100	30,700	-15%	25,076	-18%	20,524	-18%	17,289	-16%	14,894	-14%
Reported NIM (bps)	1.84%	1.77%	1.88%	1.91%		1.91%		2.00%		2.08%		2.17%	
Cost/income	55%	58%	62%	64%		65%		59%		59%		60%	
Impairment charge / advances (bp)	315	406	418	565		199		125		100		75	
RoE*	-21%	-26%	-22%	-32%		-6%		1%		3%		6%	
<b>CORE BANK TOTAL</b>													
Net Interest Income	12,451	11,485	11,071	11,053	0%	11,086	0%	9,239	-17%	8,636	-7%	8,709	1%
Non-interest income	12,261	10,965	10,726	8,735	-19%	8,099	-7%	6,694	-17%	6,183	-8%	6,282	2%
<b>Total Income</b>	<b>25,091</b>	<b>22,450</b>	<b>21,797</b>	<b>19,788</b>	<b>-9%</b>	<b>19,185</b>	<b>-3%</b>	<b>15,933</b>	<b>-17%</b>	<b>14,819</b>	<b>-7%</b>	<b>14,992</b>	<b>1%</b>
Total Expenses	-14,454	-13,570	-12,910	-12,705	-2%	-11,595	-9%	-8,758	-24%	-7,872	-10%	-7,790	-1%
<b>Operating Profit</b>	<b>10,637</b>	<b>8,880</b>	<b>8,887</b>	<b>7,083</b>	<b>-20%</b>	<b>7,590</b>	<b>7%</b>	<b>7,176</b>	<b>-5%</b>	<b>6,947</b>	<b>-3%</b>	<b>7,202</b>	<b>4%</b>
Impairment losses	-3,894	-3,522	-3,056	-3,856	26%	-1,715	-56%	-1,343	-22%	-1,201	-11%	-1,253	4%
<b>Pretax Contribution</b>	<b>6,743</b>	<b>5,358</b>	<b>5,831</b>	<b>3,227</b>	<b>-45%</b>	<b>5,875</b>	<b>82%</b>	<b>5,833</b>	<b>-1%</b>	<b>5,746</b>	<b>-1%</b>	<b>5,949</b>	<b>4%</b>
Cost/income	58%	60%	59%	64%		60%		55%		53%		52%	
Impairment charge / advances (bp)	0.99%	0.92%	0.82%	1.06%		0.49%		0.43%		0.44%		0.46%	
<b>NON-CORE</b>													
Net Interest Income	1,749	828	346	-61	-118%	0	-100%	0	n.m.	0	n.m.	0	n.m.
Fees and commissions	471	54	105	55	-48%	0	-100%	0	n.m.	0	n.m.	0	n.m.
Trading income	-31	-721	-654	-148	-77%	100	-168%	70	-30%	30	-57%	0	-100%
Other operating income	565	813	491	-192	-139%	-575	199%	-225	-61%	-50	-78%	0	-100%
<b>Total Income</b>	<b>2,754</b>	<b>974</b>	<b>288</b>	<b>-346</b>	<b>-220%</b>	<b>-475</b>	<b>37%</b>	<b>-155</b>	<b>-67%</b>	<b>-20</b>	<b>-87%</b>	<b>0</b>	<b>-100%</b>
Total Direct Expenses	-1,756	-963	-686	-407	-41%	-265	-35%	-159	-40%	-79	-50%	-32	-60%
Indirect Expenses	-500	-313	-258	-198	-23%	-135	-32%	-81	-40%	-41	-50%	-16	-60%
<b>Total Expenses</b>	<b>-2,256</b>	<b>-1,276</b>	<b>-944</b>	<b>-605</b>	<b>-36%</b>	<b>-400</b>	<b>-34%</b>	<b>-240</b>	<b>-40%</b>	<b>-120</b>	<b>-50%</b>	<b>-48</b>	<b>-60%</b>
General insurance net income	-35	0	0	0	n.m.	0	n.m.	0	n.m.	0	n.m.	0	n.m.
<b>Operating Profit</b>	<b>463</b>	<b>-302</b>	<b>-656</b>	<b>-951</b>	<b>45%</b>	<b>-875</b>	<b>-8%</b>	<b>-395</b>	<b>-55%</b>	<b>-140</b>	<b>-65%</b>	<b>-48</b>	<b>-66%</b>
Impairment losses	-5,476	-3,919	-2,223	-4,576	106%	-1,178	-74%	-701	-40%	-396	-43%	-92	-77%
<b>Pretax Contribution</b>	<b>-5,013</b>	<b>-4,221</b>	<b>-2,879</b>	<b>-5,527</b>	<b>92%</b>	<b>-2,053</b>	<b>-63%</b>	<b>-1,096</b>	<b>-47%</b>	<b>-536</b>	<b>-51%</b>	<b>-140</b>	<b>-74%</b>

Source: Company Reports and Citi Research Estimates; \*Note: Based on 10% CET1 allocation



Figure 9. Royal Bank of Scotland – Divisional Profit and Loss Account 1Q11-1Q14E (£m) (contd)

	1Q11	2Q11	3Q11	4Q11	1Q12	2Q12	3Q12	4Q12	1Q13	2Q13	3Q13	4Q13	1Q14E
<b>INTERNATIONAL BANKING</b>													
Net interest income	303	301	302	293	260	234	227	201	197	177	166	173	156
Non-interest income	344	364	348	300	282	327	308	283	285	291	288	271	270
<b>Total income</b>	<b>647</b>	<b>665</b>	<b>650</b>	<b>593</b>	<b>542</b>	<b>561</b>	<b>535</b>	<b>484</b>	<b>482</b>	<b>468</b>	<b>454</b>	<b>444</b>	<b>426</b>
Total direct expenses	-257	-240	-229	-212	-237	-202	-182	-123	-172	-170	-178	-181	-160
Indirect Expenses	-170	-172	-179	-173	-173	-165	-166	-169	-161	-157	-165	-156	-155
<b>Operating Profit</b>	<b>220</b>	<b>253</b>	<b>242</b>	<b>208</b>	<b>132</b>	<b>194</b>	<b>187</b>	<b>192</b>	<b>149</b>	<b>141</b>	<b>111</b>	<b>107</b>	<b>111</b>
Impairment losses	6	-104	-14	-56	-35	-27	-12	-37	-55	-99	-28	-47	-20
<b>Pretax Contribution</b>	<b>226</b>	<b>149</b>	<b>228</b>	<b>152</b>	<b>97</b>	<b>167</b>	<b>175</b>	<b>155</b>	<b>94</b>	<b>42</b>	<b>83</b>	<b>60</b>	<b>91</b>
Total third party assets	76,800	79,700	75,500	69,900	63,700	61,400	58,400	53,000	54,400	51,900	53,300	48,500	47,288
Risk Weighted Assets	45,700	46,400	44,100	43,200	41,800	46,000	49,700	51,900	48,900	49,700	48,400	49,000	47,775
Reported NIM	1.83%	1.73%	1.71%	1.64%	1.60%	1.65%	1.70%	1.62%	1.74%	1.62%	1.47%	1.54%	1.52%
Cost/income	66%	62%	63%	65%	76%	65%	65%	60%	69%	70%	76%	76%	74%
Impairment charge / advances (bp)	-4	65	9	39	27	22	10	35	52	99	27	52	23
RoE*	13%	10%	14%	9%	8%	11%	10%	8%	5%	2%	5%	3%	5%
<b>ULSTER BANK</b>													
Net Interest Income	181	182	196	177	165	160	163	161	154	154	154	169	154
Fees and commissions	36	37	41	28	38	35	36	36	34	35	35	37	36
Other non-interest income	15	14	19	21	11	11	14	15	20	53	25	1	25
<b>Total Income</b>	<b>232</b>	<b>233</b>	<b>256</b>	<b>226</b>	<b>214</b>	<b>206</b>	<b>213</b>	<b>212</b>	<b>208</b>	<b>242</b>	<b>214</b>	<b>207</b>	<b>215</b>
Total Direct Expenses	-75	-75	-73	-69	-65	-64	-67	-67	-72	-79	-79	-72	-70
Indirect Expenses	-61	-67	-64	-63	-65	-64	-59	-70	-60	-65	-63	-64	-60
<b>Operating Profit</b>	<b>96</b>	<b>91</b>	<b>119</b>	<b>94</b>	<b>84</b>	<b>78</b>	<b>87</b>	<b>75</b>	<b>76</b>	<b>98</b>	<b>72</b>	<b>71</b>	<b>85</b>
Impairment losses	-461	-269	-327	-327	-394	-323	-329	-318	-240	-263	-204	-1,067	-150
<b>Pretax Contribution</b>	<b>-365</b>	<b>-178</b>	<b>-208</b>	<b>-233</b>	<b>-310</b>	<b>-245</b>	<b>-242</b>	<b>-243</b>	<b>-164</b>	<b>-165</b>	<b>-132</b>	<b>-996</b>	<b>-65</b>
Gross Loans To Customers	37,200	37,400	35,500	34,100	33,900	33,000	32,200	32,600	33,100	32,900	31,900	31,400	29,787
Risk Weighted Assets	31,700	36,300	34,400	36,300	38,400	37,400	35,100	36,100	36,800	33,900	31,800	30,700	29,123
Reported NIM (bps)	1.84%	1.80%	1.96%	1.87%	1.87%	1.82%	1.92%	1.93%	1.85%	1.85%	1.86%	2.10%	1.98%
Cost/income	59%	61%	54%	58%	61%	62%	59%	65%	63%	60%	66%	66%	60%
Impairment charge / advances (bp)	496	288	368	384	465	392	409	390	290	320	256	1,359	201
RoE*	-37%	-17%	-18%	-21%	-26%	-20%	-20%	-21%	-14%	-14%	-12%	-98%	n/a
<b>CORE BANK TOTAL</b>													
Net Interest Income	2,963	2,871	2,811	2,840	2,808	2,821	2,725	2,717	2,700	2,740	2,816	2,797	2,740
Non-interest income	3,644	2,903	2,182	2,236	3,088	2,698	2,783	2,157	2,368	2,434	2,197	1,736	2,250
<b>Total Income</b>	<b>6,607</b>	<b>5,774</b>	<b>4,993</b>	<b>5,076</b>	<b>5,896</b>	<b>5,519</b>	<b>5,508</b>	<b>4,874</b>	<b>5,068</b>	<b>5,174</b>	<b>5,013</b>	<b>4,533</b>	<b>4,990</b>
Total Expenses	-3,646	-3,426	-3,362	-3,136	-3,536	-3,372	-3,261	-2,741	-3,216	-3,243	-3,140	-3,106	-3,018
<b>Operating Profit</b>	<b>2,961</b>	<b>2,348</b>	<b>1,631</b>	<b>1,940</b>	<b>2,360</b>	<b>2,147</b>	<b>2,247</b>	<b>2,133</b>	<b>1,852</b>	<b>1,931</b>	<b>1,873</b>	<b>1,427</b>	<b>1,972</b>
Impairment losses	-872	-853	-854	-943	-825	-728	-752	-751	-600	-719	-589	-1,948	-457
<b>Pretax Contribution</b>	<b>2,089</b>	<b>1,495</b>	<b>777</b>	<b>997</b>	<b>1,535</b>	<b>1,419</b>	<b>1,495</b>	<b>1,382</b>	<b>1,252</b>	<b>1,212</b>	<b>1,284</b>	<b>-521</b>	<b>1,515</b>
Cost/income	55%	59%	67%	62%	60%	61%	59%	56%	63%	63%	63%	69%	60%
<b>NON-CORE</b>													
Net Interest Income	240	264	176	148	115	86	86	59	-28	30	-33	-30	0
Fees and commissions	50	49	-69	24	31	29	17	28	20	18	6	11	0
Trading income	-298	230	-246	-407	-270	-131	-203	-50	45	134	-109	-218	25
Other operating income	307	327	167	12	393	17	150	-69	56	91	17	-356	-144
<b>Total Income</b>	<b>299</b>	<b>870</b>	<b>28</b>	<b>-223</b>	<b>269</b>	<b>1</b>	<b>50</b>	<b>-32</b>	<b>93</b>	<b>273</b>	<b>-119</b>	<b>-593</b>	<b>-119</b>
Total Direct Expenses	-240	-259	-237	-227	-197	-197	-144	-148	-116	-105	-97	-89	-79
Indirect Expenses	-75	-71	-84	-83	-66	-65	-68	-59	-49	-51	-48	-50	-43
<b>Total Expenses</b>	<b>-315</b>	<b>-330</b>	<b>-321</b>	<b>-310</b>	<b>-263</b>	<b>-262</b>	<b>-212</b>	<b>-207</b>	<b>-165</b>	<b>-156</b>	<b>-145</b>	<b>-139</b>	<b>-121</b>
General insurance net income	0	0	0	0	0	0	0	0	0	0	0	0	0
<b>Operating Profit</b>	<b>-16</b>	<b>540</b>	<b>-293</b>	<b>-533</b>	<b>6</b>	<b>-261</b>	<b>-162</b>	<b>-239</b>	<b>-72</b>	<b>117</b>	<b>-264</b>	<b>-732</b>	<b>-240</b>
Impairment losses	-1,075	-1,411	-682	-749	-489	-607	-424	-703	-433	-398	-581	-3,164	-351
<b>Pretax Contribution</b>	<b>-1,091</b>	<b>-871</b>	<b>-975</b>	<b>-1,282</b>	<b>-483</b>	<b>-868</b>	<b>-586</b>	<b>-942</b>	<b>-505</b>	<b>-281</b>	<b>-845</b>	<b>-3,896</b>	<b>-591</b>

Source: Company Reports and Citi Research Estimates; \*Note: Based on 10% CET1 allocation

## Royal Bank of Scotland Group PLC

### Company description

Royal Bank of Scotland (RBS) is a major UK-based, international universal banking group. The group provides banking services and structured financing to medium and large businesses in the UK, where it also offers banking to retail and SME customers, as well as internationally, most notably in the US and Ireland. RBS also sells insurance and investment products and provides private banking.

### Investment strategy

We rate RBS Sell/High Risk. We believe that RBS has made substantial progress in repairing the balance. However progress on profitability has not been as promising. This is now being addressed with RBS re-focusing on Retail & Commercial banking in the UK. However the timeframe over which this can be achieved should not be underestimated – there is a reason the financial targets stretch out to 2020. We see significant execution risks in the medium-term, and believe further tangible book erosion is probable in the short-term.

### Valuation

We set our target price at 270p based on a two-stage dividend discount approach combined with a capital-adjusted warranted-equity valuation to calculate a terminal value. This target price represents 0.8x 2014 TBV per share, a discount to the European banks sector average, which we believe is fair due to RBS's lower RoTE profile in the medium-term.

### Risks

We set a High Risk rating to reflect RBS' exposure to political and regulatory uncertainty. Specific downside risks include risks associated with shrinking the non-core balance sheet and restructuring Ulster Bank and the Markets division. RBS also has potential upside surprise catalysts, that could result in it outperforming our target, such as such as a sharper credit recovery in Ireland than we anticipate, a turnaround in the US, or further margin improvements in the UK following active central bank policy.

## Appendix A-1

### Analyst Certification

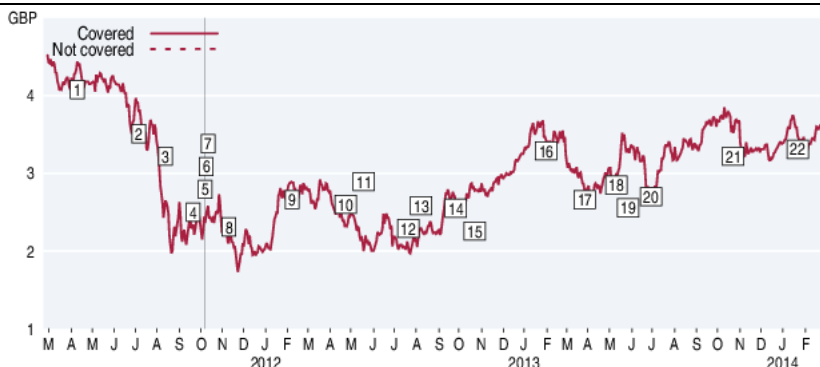
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## IMPORTANT DISCLOSURES

### Royal Bank of Scotland Group PLC (RBS.L)

#### Ratings and Target Price History Fundamental Research

Analyst: Andrew Coombs  
Covered since July 6 2011



	Date	Rating	Target Price	Closing Price
1	11-Apr-11	1M	*6.10	4.44
2	6-Jul-11	1M	*5.00	3.79
3	12-Aug-11	1M	*4.60	2.65
4	21-Sep-11	1M	*4.20	2.34
5	7-Oct-11	Stock rating system changed		
6	8-Oct-11	*1	4.20	2.36
7	12-Oct-11	1	*3.10	2.58
8	10-Nov-11	1	*3.00	2.11

\* Indicates change

	Date	Rating	Target Price	Closing Price
9	8-Feb-12	*2	3.00	2.88
10	24-Apr-12	*2H	*2.80	2.33
11	18-May-12	2H	*2.50	2.00
12	20-Jul-12	2H	*2.35	2.05
13	8-Aug-12	2H	*2.30	2.29
14	26-Sep-12	2H	*2.70	2.55
15	23-Oct-12	2H	*2.85	2.78
16	31-Jan-13	2H	*3.60	3.43

	Date	Rating	Target Price	Closing Price
17	27-Mar-13	2H	*3.00	2.77
18	10-May-13	2H	*2.90	3.00
19	28-May-13	*3H	2.90	3.32
20	28-Jun-13	3H	*2.70	2.74
21	23-Oct-13	3H	*2.75	3.52
22	22-Jan-14	3H	*2.90	3.48

Rating/target price changes above reflect Eastern Standard Time

### Royal Bank of Scotland Group PLC (RBS.L)

#### Ratings and Target Price History Best Ideas Research Relative Call (3 Month)

Analyst: Andrew Coombs  
Covered since July 6 2011



	Date	Rating	Target Price	Closing Price
1	2-Jul-12	*ADD LP	-	2.19

\* Indicates change

	Date	Rating	Target Price	Closing Price
2	22-Jan-14	*REM LP	-	3.48

Rating/target price changes above reflect Eastern Standard Time

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<i>Data current as of 31 Dec 2013</i>	12 Month Rating			Relative Rating		
	Buy	Hold	Sell	Buy	Hold	Sell
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% of companies in each rating category that are investment banking clients	55%	52%	44%	62%	52%	49%

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