Fireside Chat with Andy Halford, Chief Financial Officer, Standard Chartered PLC

(Amended in places to improve accuracy and readability)

Jason Napier:

Good afternoon, and good evening everybody. Thank you for joining us for this fireside chat. I'm Jason Napier. I'm the UK banks analyst here at UBS. It gives us great pleasure to welcome Andy Halford, who is CFO of Standard Chartered, joining us today on a great day for capital markets. Certainly nice to see bank shares up meaningfully on vaccine trial news today. Andy, thank you so much for joining us.

Andy Halford:

A pleasure.

Jason Napier:

So we've seen a lot of evidence of investors taking profits on some of the stay-at-home stock winners. We've seen Peloton and Zoom and so on, falling c15% today. The key question, I guess, that concerns most in the audience is whether we'll see banks as cyclical value trades starting to play a catch-up role in the market. And we'll be getting into that in our conversation today. As a reminder, for those of you on the call, this is a 30 minute Q&A session between Andy and myself. We would be delighted to accommodate your questions, if you were to email them to jason.napier@ubs.com. I will do my very best to fold those into the conversation as we go.

Jason Napier:

Andy, perhaps just to begin with, the market, I think quite rightly, is fairly concerned with what medium term returns may look like. Standard Chartered have been very clear under your management, that double-digit RoTEs are what you expect from the business on a steady state basis. But of course, this year, changes in interest rates have taken their toll. How do you see things in terms of the objectives for returns in the medium term? Is that still a level that you aspire to, and what's going to need to happen to get there?

Andy Halford:

Yes. Our view is that, getting to a double digit number should still be the art of the possible, should still be what we're aiming for. Other banks operating in the region can do it, they do do it, so why should we not be able to do it? If it wasn't for COVID... The sad fact is that we were probably heading quite nicely up into, not quite that range, but not too far away from it. And that aside, we'd be probably having a slightly different discussion today. However, that is life, that is where it is at. I said a couple of weeks ago that financially, probably COVID puts us back a couple of years in terms of getting to that number. We absolutely are focused on getting back to it.

What is going to be necessary for it to happen? I think we will need to see governments getting COVID under control. Obviously, news today on vaccines, is helpful potentially in that regard. I think to have a lessening of the sort of US-China rhetoric will also be helpful to the cause and maybe the resolution last week will be also helpful to that cause. So I think two things have actually moved forwards in quite a positive way, in quite a short space of time. I think we are fortunate in the sense that some of our bigger markets, and more profitable markets, are actually in Northern Asia. For some of us who are based in Europe or maybe the US, it all feels still quite gloomy, but actually in that part of the world, things definitely are feeling much more positive. And our sense is that, that should be a forerunner to what will be happening through other parts of Asia over a period of time.

So at the end of COVID, there roughly will be the same number of people still living on the planet, they will still have that same aspiration to quality of life consumption. We don't see any reason why we shouldn't be seeing overall levels of international trade getting back to where they were before. And bearing in mind, even in the last 12 months, we've had about 5% volume growth even in the COVID era, so there is volume opportunity out there, there is just a bit of reset of the base.

Jason Napier:

Sticking with the sort of issue of the day, if you like, and the potential good news around vaccines and so on, I guess, Q3 results were much stronger than the market expected. And that was predominantly about relative lack of loan losses. Could you perhaps talk a little bit about the work that you do as a firm in terms of trying to scenario plan for what stage migration you might get and so on? Is it just a sort of lull in the credit cycle or is there a potential chance here that we've made really quite good progress in setting aside funds for defaults already?

Andy Halford:

So the first thing I'd say is, the actions we've taken for the last four years or so, in terms of tightening up on credit standards, in terms of reducing the concentration of credit risks that we used to be running, focus upon collateral, focus upon trade insurance, et cetera, I think has stood us in good stead. They were all a little bit invisible, and suddenly when you get a test like this, it actually does make you realize that we've probably come into this in better shape than we had thought, and certainly in better shape than we were four years ago, so I think that is pretty helpful. As I'm sure is the case with most of our competitors, we've had a huge spotlight over the last few months, particularly on those sectors that are obviously more vulnerable, Aviation to name but one. We have gone through every client in all of those sectors by market, with a particular emphasis on the smaller ones in each of those sectors, who may not be quite as robust as some of the others. So I think we've been pretty attentive to where the problem spots could be. We've done that analysis by sector type, we've done it by country, we really have cut it in quite a number of ways. Now at the end of the day, the provisioning under IFRS 9 in the first quarter, the stage one, stage two modeling has a more procyclical sort of approach to it and we built up quite a lot of reserves in that period. We've also put, on one side, about $400 million as a sort of management overlay, particularly thinking about whether there are moratorium periods on re-payments and whether, maybe when people come out of a moratorium period, we have stored up the problem for whether that isn't the case. So I'll tell you, with that amount sort of put on one side on the balance sheet as well, that that would hold us in a reasonably good place going forward.

As we go forwards, I think stage three will become more the issue. It will be the evidential problem areas rather than the theoretical model ones. And if we do find that things like the vaccine are coming through and are starting to be effective, hopefully the duration that companies – and individuals to some extent have got to sort of survive, will be slightly less than might otherwise have been the case. It does seem that governments, generally, are trying to reach out to do things to avoid precipitous insolvency and unemployment. And I think the more that they can sense that the light is at the end of the tunnel, which isn't too far away, I would think the more inclined they will be to continue with that. So fortunately, their propensity to want to do that, to avoid unemployment and social consequences, I think coincides pretty well with what actually the banks would want to happen anyway. That is, fewer of their businesses, their clients, will have problems and hence will minimize the impairments for losses, so that's the sort of way we look at it.

Credit migration, to predict accurately, is difficult. You have to do it by clients, and we've got the list of the ones that we are focused upon. So to follow up, we've actually managed other aspects of the RWAs. So we've absorbed some elements of credit migration of an adverse nature, and still ended up with the RWAs in the broad sort of space that we indicated we thought they'd be earlier in the year.

Jason Napier:

Yes. It was marked, I thought, that your stage three is in early alerts and stage 12, loans were actually down a touch. I mean, to be stable this far, perhaps it's just because we're working from home that the crisis feels as old as it is, but it has been some time in the making and one would have thought that we should be starting to get a reasonable picture of underlying credit strength in those sorts of disclosures.

Andy Halford:

Yes, I think so. Although there's no absolute foresight in terms of, obviously, what happens over the coming months, and I'm sure there will be one or two bumps in the road as that happens. But knowing now a little bit more what governments are doing with airlines, the extent to which they're stepping in and supporting those, that adds a bit more knowledge compared to what we had a few months ago. So passage of time definitely has helped. I think we've got closer to some clients as well, where they have got more challenges, to be able to actually talk to them and actually try to work out jointly, a way forward, rather than just finding out, suddenly one day, that there's a really big problem. So behavior, that's also probably helped, but there's lots of surprising things. The height of capital in the banking sector at the time of peak stress, is nothing like what the stress test would have you believe, but that's a different story.

Jason Napier:

We will definitely come onto that in a moment. Before we do that, can we talk a little bit about the revenue outlook? And we'll do NIM and then financial markets, if that's okay. So NIM, I think, guided to fall a little and then perhaps to go sideways, perhaps even recover. Although, I do note that you're doing quite a lot on the mix of lending. And so just your take really, on where NIM goes in the near term and whether there is a net positive outlook for what you're doing in the mix of business and the spreads that you demand from customers on forward business.

Andy Halford:

Yes. We had the NIM come down quite a lot over the course of this year, most pronounced in the second quarter, which was largely repricing the treasury book, post the interest rate reductions in the US. Then it came down five basis points further, between the second and third quarters. And what we've said is, that we expect it to come down a little bit more over the balance of this year, into the start of next year, but not hugely so. Most of the book has repriced. We've got some assets that are slightly longer tenor, which, obviously, will reprice in their own time. But the majority of the book will have repriced around the end of the year, which is why we're reasonably comfortable making that statement.

Clearly, we have been very focused, particularly upon the liability mix. And we have progressively had a higher proportion of the mix from current accounts and from operating accounts from businesses. That is more cost effective, it is a reasonably sticky source of costs of liability funding as well. So the more we can do of that, the more we will continue to do. We did some legal entity restructuring a couple of years ago, which, progressively over periods of time, is also giving us some benefit. And wherever we can do, we'll obviously look at asset pricing to see whether there is any opportunity on that front. So it's a multifaceted approach, but we hope we're not too far away now from the trough.

Jason Napier:

And then turning to financial markets, clearly, across you and the peer group, you've seen very good market trading conditions. But I think the sense that you shared at Q3, was a year to date run rate with the sort of level that you'd like to hold onto, my sense partially as payback for some of the investment and broadened products that you now make available. Was that right, and how does that square with the expectation that Q4 is going to be slower, just as a seasonal matter?

Andy Halford:

Yes. So our financial markets business, I think maybe up until about three years ago, was lagging other banks a bit. And we knew that we needed to pick up the pace. We made quite a number of changes, managerially. We made quite a number of changes system wise, and in the product range. And I think if you look back now over the last probably eight quarters or so, we've actually had a much stronger engine running in financial markets. So this year has not been a sort of one-off blip, it has actually been a progression. Now that having been said, the first two quarters of the year, for us, for other banks as well, was particularly strong with significant volatility out there, which was very, very helpful. As we move forwards, we are comfortable that the engine is working well. It will be dependent, to some extent, on market volatility.

Every quarter has got its own twists and turns – US elections, whatever, this quarter. But our sense is that there is still a period of uncertainty ahead and therefore volatility is not going to be disappearing anytime soon. We still see things that we can do with penetration of the financial markets products into our client base. We've got different levels of penetration for different parts of the world, and we still see opportunities to actually get some of those normalized. So we're saying, overall, we think the sort of runway we've had this year is something which we should aspire to next year. Q4 is always a little bit slower. Some people will pack up for Christmas or whatever it is, at the end of the period, so we understand that it'll affect next year as well as it will affect this year. So that should normalize as well in that sense.

Jason Napier:

Okay. Wealth has also been doing kind of remarkably well, and I guess it might be useful to draw the distinction between the retail piece, which is the vast majority of those revenues, and what the work you've been doing in the private bank. I wonder whether you could just talk about the sort of base you're building there and the extent to which COVID may have depressed, face-to-face activity. It feels from a statistical perspective, that the retail piece is driven by the level of the Hang Seng, and the volumes of trade there. But I just wonder whether you could split out what you see the drivers of those businesses being, and again, whether that's something you could build on into 2021?

Andy Halford:

Yes. Again, going back a little bit in time, 2015, we recognized that the platform on which we were selling the wealth management products was pretty old and pretty archaic, and that we needed to upgrade it. We've spent the last three, four years in upgrading it onto a modern platform, which is much more customer friendly, it's much more staff friendly. This sort of broader range of products, it is much more useful, so that has put us into a much better position. The first quarter of this year, obviously when we had the huge disturbance to the markets, we saw wealth management activity drop quickly, and again, unsurprisingly. I think when you see a big stock market correction, that is an unsurprising reaction. Then we saw, particularly, maybe in the private bank, to your question, some people who would normally have come in to our offices for advice, particularly in Hong Kong, because of the unrest, et cetera, were reticent to be going and doing that.

But what has been happening in the past, and this has been pretty progressive over the last couple of years, is more clients actually becoming comfortable with interacting digitally. Sometimes purely on systems, sometimes it can be via video conference, but the proportion of our world's activity that is now taking place online, has fundamentally changed over that period of time. What I think is encouraging, and this is not trying to pump it up too much, but now seeing that in the North Asia markets where the recovery from COVID is earlier, that we are now at or around the same level of activity on wealth management as we were going into COVID, I think bodes reasonably well. I think it does suggest that, as other countries, particularly in Southern Asia, do start to work their way out of it, that we should see that confidence coming back and manifesting itself in the numbers. So wealth management's been good, it's been a high single digit growth business for us for a decade now. And with a proper platform and so on, we think as we come out of COVID, it should put us in good stead.

Jason Napier:

Yes. With all of that in mind, I guess you have given very concrete guidance for costs for next year. You've managed to keep costs around the 10 billion mark for years, despite I guess, inflation in your footprint in some areas such as regulation, where no doubt, costs are not going down. To what extent is that going to become too difficult to do, potentially harmful for the sort of growth opportunities and digitalization that you may need to implement? How does the organization feel about the sort of opportunity on gross costs, perhaps thinking about COVID and what that might mean as well?

Andy Halford:

Yes, I think there's a number of dimensions. If you go back over the last four years or so, we probably have eaten about, I don't know, a half a billion dollars a year out of the underlying cost base, in order to be able to cover inflation and to fund the extra investment in IT development work. It looks as if that's just a flat $10 billion, as if nothing really has been going on, it's actually been quite a lot under the surface. I think as we're going forwards, we said for next year – this year and next year – that we aim to keep it below the $10 billion mark. What we really do want to do is to use this to continue to invest in future digital platforms, particularly, and not to cut short on those, but within the business, making sure that other areas, we are constantly working away at. The biggest opportunities still lie in automating parts of the business.

The more that we can have customers who can self-serve and don't require so much human intervention, the easier the businesses is to run. And often, it's not just a cost play, it's a better experience for the customer. And we have less involvement, you have less errors, et cetera. So the journey on costs, I don't think there's any business on the planet that has ever finished the journey, and we certainly are in that space. I think there'll be some other things that come in now, that will be a bit different. So property, clearly we have been running a bank with three quarters of our people based at home, and that does open one's eyes to just how important is an office space going forward. And I think, as with a lot of businesses, people are starting to think more laterally about that. That should take some costs out of the business, albeit, it will be time-phased because it will be more dependent on lease renewals and lease breaks and things like that. So there's still lots of opportunities in front of us.

Jason Napier:

One of the success stories, it appears, in the investment in digital and so on, is Mox in Hong Kong. One of the, I think it's eight licenses that have been awarded and is now up and running. Would you mind just giving us a sense as to what the early returns on that project have been? And also, I think given what we're seeing across the footprint from peer, such as DBS in India and Indonesia, and of course the success that people like ING Direct had 20 years ago, that this is an exportable notion. So I wonder whether you could talk about what you're seeing in Hong Kong and plans for Indonesia and also the parallels with your African initiatives, please.

Andy Halford:

Yes. To your question, I'd frame this in three parts as to what we're doing in the digital space. So Mox is number one. The authorities there are making new virtual bank licenses available. We took the decision that actually, we would build a totally new platform. Use this as an experiment, if you like, to see what was the best customer proposition of banking around the world. Take some component parts of what we already did, take some component parts from outside, and essentially build a platform that could enable it. But more than the platform, to actually see whether we could use this to get into a slightly different age group of customer. We typically service those who are already affluent, who by definition, tend to be a bit older, and actually ask ourselves the question: why should we not try to get to some of those who aspire to be affluent, even if they're not yet affluent? Off the back of that, came using a different brand name, so Mox rather than Standard Chartered, albeit, it's clear Standard Chartered is behind it.

And essentially, to see what happens. Too early to say in terms of returns, because it's literally been up and running for a matter of weeks, but 35,000 accounts set up, some very good ratings on social media. Average account opening time, eight minutes, and I think the record one is something like half that. $300 million dollars of deposits, which to the earlier question of getting good cost of funding, is helpful. So I would say for the first few weeks, very, very pleased at what's happened. And it does, to your point, also have the ability to literally be copied and placed into other countries because it is actually independent of the banking system, so that is one angle.

The second angle is something which we are trialing or will shortly be trialing in Indonesia, which is essentially a platform that we can put between ourselves and an e-commerce player who doesn't have financial services products, but would like to put them into the mix on their website.

And it enables, basically, those customers to come directly onto the website, click on financial services, routed through us. We credit-check them, we decide which ones we are happy taking on board, commission paid to the e-commerce partner – I think that that is potentially of interest in countries that are large on population, where our market share is maybe small, where we don't have a big physical branch presence. And if we pick the partners right, we've now got not one, but two partners coming up, signed up in Indonesia. If we pick partners who have got the type of customer that we think is going to be of the sort of quality that we would like, we see that as being a very effective way to potentially extend the reach of the business.

And then the third one – this is in chronological sense the wrong way round, it was the first one we actually did – was to actually look at low cost, mobile-based banking in Africa, and we have really pushed that into many, many markets very, very quickly there. In fact, we're now at the point where we only allow online applications. You can turn up into a branch, but you'll still be pointed to do it online. And actually, just used it to break one or two myths of the past, that you had to have a branch, you had to have this, you had to have the other.

Generally, an interesting reaction from regulators, who I think at one time had been a bit wary about us reducing the number of branches, but then when we said, "Look, we put this on a mobile phone and then you open it up to huge numbers of people. And if it's easy to sign on, you don't need high levels of literacy", et cetera, et cetera. Actually, in terms of financial inclusion, this is a huge, huge step forwards. So it started with a fairly basic product range, we're gradually adding things to it. So between those three different models, and I'm sure we'll apply them in slightly different mixes in different countries, I think it's quite a different way to attack the market now.

Jason Napier:

And again, it may well be too early to say with much sort of hard fact behind it, but your sense around potential cannibalization of the Hong Kong market, it comes up quite a lot with investors that this might be the beginning of the end of really very good returns, but the point you made, I think around demographic profile of customers, also lands. So I wonder whether there is anything that you've learned so far around, whether the separate branding is helping preserve market position and so on?

Andy Halford:

I think it's just very early days, is the honest answer to it. We obviously know the customers that preregistered with us, and we were pretty happy those were actually from the demographics that we were targeting. So we're not, at this point in time, overly worried by the cannibalization. We are more focused on whether it can actually extend the market that's open and available to us.

Jason Napier:

I guess it'll have to have a wider range of products too, before we will be able to tell exactly how it's competing.

Andy Halford:

Right.

Jason Napier:

Right. Lastly and certainly not least, I think as topics go, capital returns, as you said, I think earlier, it's remarkable that here we are with all UK majors, with more capital than they target through the cycle. You did see some pro cyclicality this year, but you're still well above the top of your range. How are you guiding investors to think about the regulatory test, whether it's likely to be P&L driven, balance sheet driven? And then, what is the thought process around the mix of potential capital returns, if you're given the green light?

Andy Halford:

Yes, so a number of thoughts. We are not natural hoarders of excess capital as a management team. We did have a buyback, and a dividend program in place when we were told to stop everything. So I think there is a track record there to say, we don't want to unnecessarily sit on things. Secondly, obviously we'd have to abide by the rules for regulators, which we did do. They've said that they will pronounce again in the Q4, which we are now halfway through, so somewhere in the next four or five weeks, by inference. So obviously, interesting to see where they will come out on this. For investors, clearly having some level of return would be beneficial. It was really frustrating for a number of them, I know, to not have that return. Although in some senses, I would make this point that, so long as the capital is sitting in the bank, it is just a question of when it comes out. The bigger issue is making sure we don't have leakage of value in the bank to impairments, because there'll just be less to come out at the end of the day.

So a big, big focus still obviously on natural trading performance, to the extent that we are allowed to extract some at the end of the year, which would be good; we haven't yet decided what we'll do by way of dividend or buyback, but we are conscious that with a very low share price, this is true, even more last week than this week, but it's still fairly true today, the buybacks economically do have some interest. Equally, we understand, some shareholders would just like the evidence that we're prepared to get back on the dividend trail. So I think step one is just to see where the regulators come out, then we can see what content, if any, we're allowed to deal with and then we can think about how we do the mix.

Jason Napier:

Andy, thank you so much. That's been really helpful and interesting as always. We're really glad that you joined us. Thank you for your time.

Andy Halford:

Thank you. Thanks, Jason.

Jason Napier:

Thank you to everyone who tuned in.