Bank of Ireland H1 2023 Results Presentation

Monday, 31st July 2023

H1 2023 Performance

Myles O'Grady

Group CEO, Bank of Ireland

Welcome

Good morning, everyone. I hope you are all very well. And you're very welcome to our H1 results presentation.

Strong Strategic Delivery

When we spoke last we set out Bank of Ireland's three-year strategy – centred on stronger relationships; simpler business; and sustainable company.

We're now six months into this strategy.

And today I'm very pleased to announce a strong set of results – demonstrating our progress and delivering for customers; colleagues; shareholders; and society.

Our performance has been supported by three important factors:

- Strategic management actions and business model development;
- A resilient Irish economy; and
- The impact of the interest rate environment.

In the first half of 2023, we delivered a profit before tax of €1bn with all business lines performing strongly.

Net interest income increased by 68% and business income rose 23%.

We tightly managed costs, with like-for-like costs broadly flat.

And our asset quality remained resilient.

We also made a number of structural changes to support our commercial delivery.

In May, we migrated our high net worth customers from Bank of Ireland Private to Davy. This will enhance the service our customers receive, while helping us unlock revenue and value from that acquisition.

And we brought our Corporate and Business Banking operations into one structure, helping us better serve businesses of all sizes and stages of their development.

Over the first six months we've worked hard at delivering a better service to our customers.

And we've made tangible progress on our broader ESG strategy.

All of this contributes to the delivery of our financial targets, with a ROTE of 18.5% in H1 and Cost/Income ratio of 42% translating into capital generation of 180bps, helping our CET1 finish the half at 14.8%.

We expect this to grow in H2 and look forward to a distribution decision at year-end.

We fully appreciate that capital return and its timing is central to our franchise value and investment case for shareholders.

Irish Economy Growing, UK Moderating

Turning now to slide 6, after many years of negative interest rates, the change in the interest rate environment has been a tailwind – one of the components supporting sustainable profitability.

We're also vigilant to the risks associated with higher rates in relation to customer affordability, asset quality and inflation.

And, as this slide shows, on the whole, the economic environment remains supportive. Both Ireland and the UK have essentially full employment.

And, in headline terms, Ireland is set to be the EU's fastest-growing economy for a fourth successive year with inflation moderating.

Our geographical footprint in Ireland and internationally are complementary, with overall asset quality resilient.

Business Line Performance

Slide 7 sets out the performance of our main business lines for the first six months of the year.

As you can see from this slide, in line with our strategy and reflecting market consolidation, we grew our Irish mortgage market share to 41%, with our net lending growing at an annualised rate of 6%.

We continue to maintain pricing discipline, taking a holistic approach to mortgage and deposit customers, while ensuring we secure sustainable economic returns.

We have grown our deposits by €2.5bn year to date, driven by our strong Irish Retail Franchise.

Our Wealth & Insurance business delivered net customer inflows of €1.2bn despite market volatility.

We have also grown our Corporate and Business books in Ireland, albeit credit appetite is relatively muted.

As we guided back in March, we've adopted a cautious stance towards international lending and CRE given the uncertain outlook.

And, in the UK, we successfully continued our 'value over volume' strategy.

Digitalisation Supporting Simpler Business and Stronger Relationships

Digitalisation and simplifying our business is a top priority.

Slide 8 shows what this is delivering:

- Customer satisfaction is up;
- Complaints are down;
- Customers are taking more of our products; and
- We are simplifying our business model.

All of this is core to our strategy, and I'd like to take the opportunity to remind everyone of our recent appointment of Áine McCleary as Chief Customer Officer, a new role to truly embed a 'Customer First' value.

Áine's appointment is in addition to a number of other high-calibre appointments we have made to our Executive Committee this year including Gavin Kelly as CEO of Corporate and Markets and Susan Russell as CEO of Retail Ireland.

ESG Fundamental To Our Sustainable Strategy

Slide 9 sets out the ESG progress we have made in the first half of the year.

We have grown our sustainability-related finance by 18% to €9.7bn.

You've heard me talk before about the importance of practical interventions that make a difference.

We remain Ireland's leading lender of green mortgages.

Today I'm pleased to announce we are increasing our available funding for home building from €1bn to €1.75bn.

And we've also recently announced more than €100m in funding for wind energy and recycling initiatives in Ireland and Scotland.

Given the current backdrop, our focus on Financial Wellbeing has never been more important. Whether that is ensuring the affordability of our products, or our Financial Literacy Programmes which close to half a million students have participated in. And, for colleagues, engagement is ahead of the industry average.

Through progressive hiring policies, we increasingly have a Bank that better reflects the societies we operate in.

With female leaders accounting for 41% of our senior appointments in H1 we have more to do to achieve our gender targets and we are working hard on this.

We also continue to consider more broadly our role in society, and the positive impact our organisation and our colleagues can have.

Creating Value as The National Champion Bank

Before passing over to Mark, I'd like to reiterate what I see as Bank of Ireland's unique position as The National Champion Bank.

We have the opportunity and the capability to serve our customers' diverse financial needs at every stage of their lives.

Through Bank of Ireland, Davy and New Ireland we offer banking, wealth and insurance propositions all from within the Group.

And we operate in an attractive economy with supportive demographics.

Our UK and international businesses are important and complementary.

All of this has allowed us to deliver strongly against our medium-term financial targets, which apply to every year of our strategic plan. And, as Mark will set out, our plan is performing particularly well this year.

As I mentioned at the start, we're now six months into our three-year strategy.

Our strong results show the progress we are making, and our delivery, for customers; colleagues; shareholders; and society.

I'll now pass over to Mark who will take you through the financial performance.

H1 2023 Financials

Mark Spain

Group CFO, Bank of Ireland

Thank you Myles and good morning everyone.

H1 2023 Financial Summary

We delivered a strong financial performance in the first half.

This performance reflects our strategic decisions in recent years and commercial delivery across our business lines, supported by higher interest rates.

Key highlights include:

- Further organic net lending in Ireland; and
- Operating leverage, reflected in a cost income ratio of 42%

Our statutory PBT was €1bn, three times last year's amount, which is reflected in our strong organic capital generation of 180bps.

We have also upgraded our NII guidance for the year reflecting our commercial performance and updated interest rate expectations.

H1 2023 Financial Performance

This slide summarises our key financial metrics. There are two items I want to draw out:

- Firstly, our ROTE of 18.5%, which is our key financial metric, and which all of our capital allocation decisions are based on; and

- Secondly, the 7% year to date growth in our TNAV to 924 cents, reflecting our earnings strength in the period.

NII Guidance for 2023 Upgraded

On Slide 15 we look at our NII in detail.

The growth we are reporting today is driven by:

- Higher liquid asset income, reflecting higher rates and our growing deposit franchise in Ireland; and

- Higher lending income, reflecting rates, our commercial actions and the KBCI transaction

These positive effects were partly offset by higher wholesale funding costs and deposit costs and these will continue to evolve in a higher rate environment.

We continue to maintain our commercial discipline, with loan asset spreads up 27bps from the same period last year.

Looking ahead, we expect H2 NII to be modestly higher than H1, reflecting positive rate impacts and business momentum, partially offset by higher funding costs.

And, as I mentioned earlier, this is a material upgrade on our prior guidance.

Structural Hedge and Net Interest Income Sensitivity

The next slide sets out our NII sensitivity, which has reduced since the start of the year.

As you can see, it also provides some further detail on our structural hedge, where our decisions have protected our NII.

You can see a significant increase in the structural hedge gross income, which is driven by higher swap rates and volumes.

The average gross yield of 134bps is double the H2 2022 level and will continue to pick up as the hedge rolls over.

Loan Book Growth Reflects Acquisitions and Irish Net Lending

Slide 17 shows how we have grown our loan book by more than a tenth since the start of the year.

The single largest driver of this is the closing of the KBCI acquisition in Q1.

But we have also delivered strong organic growth in Ireland, with the book growing by €0.8bn in H1, which is the same level as delivered in 2022 as a whole. Within this, we have delivered a particularly strong performance in mortgages, while maintaining commercial discipline.

In the UK we have seen modest deleveraging, materially lower than last year.

And as Myles mentioned, we have maintained our cautious approach to international and commercial property lending.

Looking ahead, we expect our loan book to grow in H2, driven primarily by Irish mortgages.

Total Business Income 23% Higher

Total business income was up 23% in H1, primarily reflecting a full period contribution from Davy following its June 2022 acquisition and underlying business momentum.

We have restated our Retail Ireland and Corporate and Markets figures to reflect the transfer of Business Banking.

The Wealth & Insurance figures are presented on an IFRS 17 basis, with the comparatives restated.

I spoke about two key drivers of our business income back in March and you see those evidenced here:

- Retail Ireland continuing to grow, reflecting higher current account fees and activity; and
- Wealth & Insurance growing, once the Davy acquisition is adjusted for.

Our expectation for business income in H2 is for the performance to be broadly in line with the H1 outturn.

Operating Expenses In Line With Guidance

Slide 19 covers our operating expenses, and the key message here is that they are performing in line with prior guidance.

On a like-for-like basis, operating expenses are flat year-on-year, with efficiencies and lower pension costs balanced against inflationary pressures and investment.

Our reported operating expenses reflect the impact of acquisitions, an allowance for variable pay and additional investment to drive future efficiencies.

For the full-year, our expectation is for operating expenses to be about €1.85bn.

Impairment Charge of €158m in line with Expectations

The H1 impairment charge is €158m, and reflects a cautious approach to provisioning, notwithstanding the resilience of our customer base.

This caution can be seen in our updated IFRS 9 macro-economic assumptions, where we increased the weightings for downside scenarios by 5 points to 45%, and in the €16m management overlay we have taken to provide a further buffer for affordability risks on mortgage and consumer portfolios.

The charge also reflects a €17m 'Day One' adjustment for the KBCI acquisition.

For the full year, subject to no material change in the economic conditions or outlook, we continue to expect the impairment charge to be in the mid-30s bps.

Diversified Loan Book and Strong Asset Quality

As you can see on slide 21, Bank of Ireland has the benefit of a diversified loan book both by geography and product.

We take a disciplined approach to customer lending across all of our portfolios.

Our loan book is strongly collateralised.

Our mortgage book in Ireland has a weighted average LTV of 53%. Three-fifths of this book has been originated under the macro-prudential mortgage rules.

Our UK mortgage book has a weighted average LTV of 56%.

The Property & Construction portfolio accounts for one tenth of gross loans and we have reduced our exposure during the period. Some 90% of the book relates to Investment Property, with circa 70% of this in Ireland. The weighted average LTV on the entire investment book is 59%.

This slide also highlights the prudent coverage levels across the books – 1.7% at the end of June.

Our NPE ratio is stable in H1, following a very material reduction last year. We will continue to drive this lower through organic and inorganic activity.

Strong Retail Franchise and Liquidity Metrics

Slide 22 illustrates the Group's strong liquidity and funding.

Our deposit volumes have grown by €2.5bn since the start of the year, supported by elevated household savings in Ireland and the strength of our deposit franchise.

We have seen modest migration into term accounts and regular savings products to date, with this expected to increase as we go forwards.

The Group's liquidity metrics continue to be very strong, and our liquid assets are held either at central banks or invested in highly rated bonds.

Net Organic Capital Generation of 180bps

Slide 23 shows the walk in the Fully Loaded CET1 ratio since the start of 2023.

Our closing CET1 ratio of 14.8% is comfortably above our capital target.

A highlight is our strong net organic capital generation of 180bps, 3 times the 50bps delivered in H1 of last year.

The increase in RWAs is driven by mix and KBCI.

We have taken a foreseeable dividend deduction of one third of H1 2023 profit, consistent with our distribution policy.

In terms of the outlook, we expect H2 net organic capital generation to be broadly similar to H1.

As is customary, we will decide on the quantum of ordinary dividend and the level of share buybacks at year-end.

I also want to briefly comment on the EBA stress test results, released after the market close on Friday [28 July].

We were very pleased with our results. They show a significant improvement since the last stress test, the direct result of actions we have taken.

These results underline the strength, resilience and sustainability of our business model.

2023 Guidance Upgraded

Slide 24 recaps on our principal guidance for the Full Year.

All of this leads to our expectation for 2023 ROTE to be similar to H1.

I'll now pass back to Myles for closing remarks.

Concluding Remarks

Myles O'Grady

Group CEO, Bank of Ireland

Thank you, Mark.

Let me conclude by saying that we have a winning strategy because of the trust of our customers, the support of our shareholders, both of which are never taken for granted.

And let me conclude also with a special thanks to my colleagues across the organisation for their remarkable commitment.

We will now open the line for questions. Thank you.

Q&A

Operator: Thank you. [Operator Instructions]. Please stand by while we compile the Q&A roster. We will now go to your first question. One moment, please. And your first question comes from Diarmaid Sheridan from Davy. Please go ahead.

Diarmaid Sheridan (Davy): Hey. Good morning, Myles. Good morning, Mark. Thank you for taking my questions and for the presentation this morning. A couple of questions, if I may, please. Firstly, just around the commentary around organic capital generation, obviously, very strong in the first half of the year and expected to be very strong in the second half, too. So, you know, all things being equal, that that would kind of suggest that Fully Loaded CET1 should be around the 15.5% mark as we look into the end of this year.

So, I guess, you know, based on your greater than 14% CET1 ratio, does that kind of indicate that you could go for higher a payout than you have previously guided?

Secondly, just around your top line performance, which again was very strong in the first half of the year and you've guided a little bit higher into the second half. Just if you could maybe talk through some of the positives and some of the headwinds on particularly on net interest income that you're expecting to see. And I guess more specifically around the deposit book, around the pass-through assumptions and behavioural aspects of migrations from your deposit base, from current accounts and demand accounts into term accounts, what you're seeing there and I guess what you expect to see in 2024?

And finally, maybe if I could just ask you to briefly comment on asset quality trends. I guess within what is still an evolving environment, what are you seeing in terms of customer behaviours? I mean, clearly, you have shown a small increase in Stage 2 and NPE have also ticked up a little in Q2. So, just in terms of what you're seeing there. Thank you.

Myles O'Grady: Diarmaid, good morning and thanks for those questions. I'll take the capital question and I'll also comment on NII, with Mark offering more detail on that, and Mark will take asset quality as well.

Diarmaid, on capital and distributions, so let me start by saying that I would have called this out in the presentation. I fully appreciate that capital return and its timing is central to our franchise value in Bank of Ireland and therefore the investment case for shareholders. Now, in March, as part of our strategy [refresh] I communicated an updated distribution policy, which is a dividend pay-out building to circa 40% by next year. We did 25% last year. And, as you heard from Mark, we're currently accruing to 33% this year. And, of course, the other really important component of that policy is the distribution of surplus capital to be considered annually. This year's performance very much supports that policy with a ROTE of 18.5% compared to our target of c.15%. And therefore we can expect the quantum of cash dividend to be higher. And with capital generation of 180bps in H1 and a similar amount in H2, we know our capital position will be well above our target of holding CET1 greater than 14%, which therefore supports the distribution of surplus capital by way of share buyback. I also would like to say we have an ambition to execute the share buyback more quickly, timed with the announcement of our 2023 annual results. I know Mark and I, we look forward to making those distribution decisions with our board at year-end.

On top line performance, and NII, clearly our net interest income performance, is being enhanced by the current interest rate environment where wholesale rates are higher for longer than previously forecast. And that's one of the factors driving our ROTE performance. But it's worth just unpicking this a little bit. So ECB rates have now increased by 4.25%. Obviously driven by concerns, strong concerns for inflation. Against this backdrop, we've taken a balanced approach to increasing loan rates onto the mortgages and also increasing deposit rates.

And just to offer some context. Our Irish deposit book is broadly the same size as our Irish mortgage book, and therefore it can regard the deposit book as funding the mortgage book. They're fundamentally interrelated. So, with that as a backdrop, and passing on both rates to mortgage and deposit customers, we're very much maintaining a track record of pricing discipline. So far, we've passed on between 1.25% and 1.75% to fixed mortgages, and back to that balance point, we've deployed new deposit product propositions which included the two year term deposit offering 2% interest. And maybe just to comment on customer behaviour because it is relevant to the guidance and to my mind because of the very long period of low and negative rates, customers are slow to move from non-interest bearing to interest bearing accounts.

I expect that to change as customer awareness increases and I very much encourage customers to avail of these products. All of that is captured in our NII guidance for 2023 which Mark has provided and indeed is captured in our 2024 and 2025 ROTE target of 15% and a cost income ratio of below 50%. And before I hand over to Mark, the asset quality overall has proven to be very resilient.

I will pass over to Mark now.

Mark Spain: Thanks, Myles. Morning, Diarmaid. So, just maybe on the NII just maybe on the moving parts there in our H2 guidance. So, really three things. Firstly, business momentum on the loan side and we're seeing that obviously in the first half in Ireland. We expect the loan book at an overall level to grow in the second half of the year. And again, Irish mortgages to be very prominent in that regard. Also some further modest growth on the deposit side and that's really, you know, if you think about those are very much as a result of the strategic decisions we've made and our commercial activity on the ground.

And secondly as a positive factor, average rates will be higher in the second half of the year versus the first half of the year, that's a tailwind. And offsetting that really, higher wholesale funding costs and higher deposit costs and very much reflecting what Myles said there about the anticipated evolution of customer behaviour. All of those factors feed into our guidance for our NII in the second half to be modestly higher than the first half. But that is a material upgrade on our prior guidance and I think it's an upgrade on consensus as well.

Just in relation to 2024, NII clearly we're not giving guidance today in our interim results but maybe just a couple of contextual comments. So, firstly, rates are now expected by the market to be higher and for longer than when we set our three-year targets back in March, even if they have been volatile. And I suppose maybe secondly and just picking up the topic on some of the other results call in terms of peak NII, you know if I was asked that probably back on the 7th of March, I would have had a strong conviction that 2023 would be the peak year for NII in the current cycle. Just given the rates evolution, I'd be less sure about that today.

Just then, maybe turning to asset quality. And again, the overarching message here, as Mark said, is that our customers are exhibiting resilience right across our portfolios. There's no evidence of any material stress. Just to bring it to life, looking at maybe a couple of individual portfolios. So, there's Irish mortgages, almost two-thirds of that book has been originated under the Irish macroprudential rules. The balance of the book, the LTV, is circa 40%.

And CRE, an area of focus, I would say that's performed better than we anticipated in the first half. We've had a lot of proactive engagement with our customers and that engagement has gone well. LTV, there is sub-60%. So, a lot of equity protection from the group's perspective. I'd say notwithstanding that overall resilience, our approach, and its consistency over the past number of periods has been to take a cautious approach in relation to provisioning. We can get into some of the details after in the Q&A. But just to bring it to life, we've increased the weighting to downside scenarios by 5% to 45%, and the downside scenarios constitutes 45% of those overall scenarios.

From an NPE perspective, we are stable in the first half, so 3.6%. And that's after a very significant reduction last year. And if you'll recall, last year, the NPE reduction was second half weighted. We have a slight uptick you mentioned in Q2. That was really due to quite a cautious approach in relation to UK mortgage customers who aren't in arrears. I wouldn't really overread that.

And maybe just briefly then just in the context of asset quality, maybe just to briefly comment on the EBA stress test results, which were released after market close on Friday, we're really quite pleased with those, very significant improvement in our depletion levels versus the 2021 test. That's as a direct result of the actions we have taken to de-risk the balance sheet. Our depletion now is 50 basis points better than the European average and compared to 50 basis points worse in the test two years ago and really, bringing it all together, we'd say that the stress test underlines the sustainability and resilience of the business model.

Diarmaid Sheridan (Davy): Thanks Mark.

Myles O'Grady: Thanks very much, Diarmaid.

Operator: Thank you. We will now go to your next question. And your next question comes from the line of Grace Dargan from Barclays. Please go ahead.

Grace Dargan (Barclays): Hi. Morning. Thank you for taking my questions. Maybe just drilling down a little bit more into NII. Firstly, hopefully a slightly easier one. What are you thinking of as modestly higher into H2? And then thinking a bit more about your guidance and into next year, maybe I could ask kind of what betas have you seen on your deposits in H1? Kind of what are you assuming in the guidance for H2? And what are you thinking about is terminal betas and kind of linked to that as well, kind of how is that deposit mix shift evolution differing between retail and corporates? And then finally, I guess thinking about that, how is that impacting how you're thinking about ROTE into next year and the NII trajectory potentially supporting ROTE some way ahead of that medium-term guidance. So, any thoughts around that would be much appreciated. Thank you.

Myles O'Grady: Grace, good morning and thank you for the questions. I'll comment on the beta component and Mark will take the further details both on net interest income and guidance. And again, back to my comment, I guess, from earlier, because of what's been a very long period of low and negative rates, customers have been slow to move to higher rewarding products. And we do expect that to change, no question, as customer awareness increases. And again, we you know, we've encouraged customers to avail of those products for sure. We're not disclosing specific betas, but you can see in the presentation the evolution of the overall interest income and interest expense that's set out. And what's important, I suppose, is that as we expect those customers to migrate from non-interest-bearing to interest-bearing that will happen. We've captured that in our NII guidance for this year and is also captured clearly in our targets out to 2024 and 2025. Mark, over to you.

Mark Spain: Yeah, Grace, so just maybe on the NII, modestly higher piece. So, I mean, again, the factors are just the same factors as the factors I spoke about in answer to Diarmaid's question on the business momentum. The average rate is higher and then that you know that customer migration which you've spoken to there in terms of the deposit piece, we also have to factor in for example the MRR impact from last Thursday. So, that's just under €40 million annualised cost to us, which comes in from September, so that's built in. And if I bring all those together modestly, for me, it's probably in the low single-digits in H2 versus H1. In terms of ROTE into FY 2024, so again, you know, coming back to what we said earlier, if the rate environment plays out the way the market currently expects from an NII perspective, that's a net positive for us, and, you know, we just need to see how that lands in the second half of the year.

Clearly, if the rate environment is higher, that may be because inflation is higher. And we need to think about whether there are some offsets in other P&L lines. But overall, if the rate environment plays out and I'd say the way the market currently projects, that's a net positive for us going into 2024.

Grace Dargan (Barclays): Thank you.

Myles O'Grady: Thank you, Grace.

Operator: Thank you. We will now go to our next question. And your next question comes from the line of Chris Cant calling from Autonomous. Please go ahead.

Chris Cant (Autonomous): Good morning. Thanks for taking my questions. I just wanted to have a couple of quick follow-ups on NII if I could, and then one around capital return please. So, in terms of NII, it would be really helpful if you could give us a sense of what the 2Q NII run rate is? And or just the sort of figure for 2Q, so we can think about the development in a bit more detail.

And then on the beta, on Grace's question just then, I appreciate, you don't necessarily want to give, too specific figures, but obviously your, your largest domestic peer did give some commentary the other day and talked about less than or a bit less than 30% beta by the end of this year. I'm just wondering if you could speak to that, whether your thinking is at least in that sort of ballpark?

And then on capital return, appreciate the commentary around capital generation for the second half. Obviously, the capital progression is going to be very strong. When I think about the sort of quantum of capital return that consensus is anticipating, we're not going to be bringing the capital ratio down on that basis. So you've, obviously, started to talk about the strength of the performance supporting surplus capital distributions. What sort of quantum should we be thinking about here? Are you actually expecting to now be able to return surplus capital in the sense that the total pay-out ratio, including buybacks, could be over 100%? So, obviously, you are meaningfully ahead of your capital target already. You're talking about generating further additional meaningful capital.

And we've just not crossed that Rubicon in Ireland for some time in terms of actually bringing down capital through surplus capital distributions. So can we expect pay-out ratios to potentially tip north of 100% in order to actually bring the capital ratios down? Thank you.

Myles O'Grady: Hi. Good morning, Chris, and thank you for those questions. I'm going to comment on the capital return and also offer a view on the betas again, and Mark can offer more colour on the NII. So, Chris, the performance of Bank of Ireland this year very much supports our distribution policy. We're very pleased to be in that position, that organic capital generation of 180 basis points, expecting a similar amount over the second half of the year. And the implications of that are, our profitability will be strong and overall capital levels will be strong as well. From a cash dividend perspective, obviously, the P&L is stronger then the quantum of cash dividends will be higher as well, and on the return of surplus capital, most likely by way of a share buyback, I want to – I do want to say we're not assuming it's an automatic sweep down to 14%.

Our target capital is to be above 14%. But we are mindful that the business is generating significant capital, and we've no desire to hoard capital. We look forward to making that decision on both the cash dividend and the return of surplus capital. And, again, just to be helpful also, it's our expectation that we will make that decision on the buyback hopefully sooner to align it with the results presentation for 2023 results.

On the betas again, I mean, I know different institutions have communicated different beta assumptions. The most important message that I can give to you is that we're giving you the building blocks for NII both for this year, and I think as well offering a qualitative view on where NII will be next year. I do expect customer behaviours to change. I expect customers to move from non-interest bearing to interest bearing, and that is very much captured in our guidance.

The other relevance to not just giving you a beta in isolation, it's back to my balance point, how we consider the mortgage book and the deposit book because they are interrelated, and we will most definitely be taking a balanced approach, which is designed to ensure, of course, we pass on rates to mortgage customers but not to push them into unaffordability, and, of course, we seek to reward deposit holders, too. Mark?

Mark Spain: Yes. Thanks, Myles. And Chris, the other piece, obviously, you know, that Myles has talked about and you were very specific about that commercial discipline loan deposit ratio. Our loan deposit ratio is south of 80%. So, that's obviously a factor in all of that as well. I mean, just in the Q2 piece, Q2 would have been a little bit stronger than Q1. Obviously, KBC came on board in early February. So, you know, we've got a sort of a one month differential there and rates a tad higher in Q2 versus Q1. But that is – I mean, the Q2 performance and then the factors that I've spoken about earlier in terms of those tailwinds and some of the puts and takes, those are all factored in in terms of our guidance for the second half of the year.

Chris Cant (Autonomous): Okay. Thank you.

Myles O'Grady: Thanks a lot, Chris.

Operator: Thank you. We will now take your next question. And your next question comes from the line of Borja Ramirez from Citi. Please go ahead.

Borja Ramirez (Citigroup): Hello. Good morning. I have two questions. Firstly is on the commentary on the customer behaviour this is expected to change. From non-interest-bearing to interest-bearing, I would like to ask how – if you could give more details on the timing and also if there's any indications on what could drive migrations so far. Based on industry data, this doesn't seem to be the case at least for – based on industry data.

And then my second question is on the – so, I saw that in the loan loss provisions, there was an impact from the – impact from higher rates on mortgages. I would like to ask if you could please give some details on the mortgage affordability ratio for the customers with floating rate mortgages. These are my two questions. Thank you.

Myles O'Grady: Okay. Borja, thank you very much for that. In relation to the customer behaviour, you're right, there's been and certainly in the Irish franchise there has been minimal movement –

behaviour movement of customers moving from non-interest bearing to interest bearing. And as rates, particularly the context of the products that we've brought out to the marketplace, as an example, a two-year tenure rate of 2%. It's reasonable to presume – to assume that customers will begin to avail of those products.

And again, that's what we would expect and we would encourage customers to do that. And it's – I think it's difficult to be precise as to when that will happen. I think we'll begin to see it over the second half of the year and further into next year as well. And that's why we're – as Mark has provided – the updated guidance for NII and to give, I guess comfort to everybody that we have captured that reality of customer behaviour in our overall NII guidance, and indeed back to that ROTE target of 15%, which is outperforming, as you know, this year at 18.5%. Mark may have more detail on the mortgage question, but what I can say to you is that, for all our product offering, whether that's the fixed products or indeed variable products, we very much take into account affordability. We essentially stress the loan to a higher rate environment.

And as one data point that I think is worth, just calling out, Bank of Ireland has very much promoted a fixed rate mortgage strategy in recent years. Now, the consequence of that, the positive consequence is that 73% of Bank of Ireland fixed mortgages are fixed until 2025 at the earliest, and that offers protection to our customers from the rising interest rate environment and also offers protection to Bank of Ireland as well.

Mark Spain: Yeah, Borja maybe just a couple of other, a couple of other data points. So just on the Irish mortgage book, again, just under two-thirds of that book originated under the macro-prudential rules – and the balance of that book, which is obviously of longer standing, goes back to pre-2015, the average LTV there about 40%.

The other data point that might be helpful for you is that if we go back to 2009, the minimum stress rate for any new mortgage written was 5%. And the entire book today has access to rates which are lower than 5%. So, again, we've got a lot of, let's say, comfort around the quality of that mortgage book.

Operator: Thank you. [Operator Instructions] We will now go to your next question. And the question comes from Seamus Murphy from Carraighill. Please go ahead.

Seamus Murphy (Carraighill): Hi. Good morning, Myles and Mark. Thanks for taking my question. Morning. I suppose we have seen something similar at AIB whereby the customer spread actually hasn't grown significantly since the ECB started to raise rates despite still very obviously low deposit beta. So, I think it's only about 30 basis points for you with close to 100% of NII against that coming from your liquid asset portfolio. And I suppose the question is, it seems quite strange that happened today so when we think about that again, I suppose the question is you know can you give us an indication of the share of your loans that are contractually Euribor linked and if these are 12 month linked, this would seem to be the only rational explanation for slow rise in the spread.

And second then, I suppose, something related to your fixed rate mortgage book, the question is what's the duration of your fixed rate book? You've mentioned 2025 in the prior question so if we do assume a three-year duration and it's not swapped back to floating for the purpose of your hedge, then we should think about NII gains into 2020 – into H2 in 2024 as well. So, in conclusion, that's kind of like surely the customer spreads should rise from here at a more rapid pace that we – than it has to-date on the basis that you have to get some kind of Euribor linking on your loan side. It does seem strange that it hasn't happened to date so some context around that would be appreciated. Thanks.

Myles O'Grady: Sure. Thanks for that. I know Mark will have some detail on that particularly in relation to how the structural hedging works to protect interest income into the future. Let me just offer some comments as well. First of all, the loan spread for Bank of Ireland for the first six months of the year has grown. And again, that speaks to the pricing discipline that Bank of Ireland maintains. We look at the profile of our balance sheet so for our €31 billion of mortgages in Ireland, 68% is fixed; 21% is tracker mortgage, which obviously is aligned to ECB rates, and 10% is variable. And generally, in the Irish franchise, when we look at non-property and property loans, they are typically priced according to wholesale rates plus a margin. So, you could expect those to move in-line with rates, of course, influenced by the structural hedging that we've taken over in the last number of months. Mark?

Mark Spain: Yes. Thanks, Myles. And thanks, Seamus, yeah. So, I mean, exactly, Seamus, as you outline from a customer perspective, you're going to see customer rates rising in those wholesale books. If you take our fixed rate mortgage book, we do swap that back to floating so everything gets more back to floating, then the structural hedge is applied, taking account of our equity and free funds balances. And that's probably the piece that you're missing that ultimately comes back in to the overall NII and gets factored into the customer spread as well. Now, what we've shown is and we've demonstrated that the fixed leg – the fixed – received fixed leg on the structural hedge, that is growing. That's growing a little bit in volume terms. But really, the rate received on the fixed leg is increasing. It's increased quite a bit in the first half relative to last year. And the average rate at 1.34% in H1, that compares to a 7-year – or a sort of 3.5 year swap rate today of about 3%, and we would expect that to increase over time. The structural hedge, ultimately, that enhances our NII resilience and protects us on the upside – or sorry, protects us from the downside as rates go lower, it obviously gives away a little bit on the upside, but its objective is to smooth NII over time. That is all ultimately factored in to our guidance and our targets as we look into 2024 and 2025.

Operator: Thank you. We will now go to your next question. And your question comes from the line of Andrew Stimpson from KBW. Please go ahead.

Andrew Stimpson (KBW): Good morning, everyone. The rate sensitivity to any eventual rate cut has reduced on slide 16. I was just wondering, I mean, are you happy with where that is now or would you be keen to see that rate sensitivity continue to decline from here? And if so, what kind of level are you, you know, happy for that to get to?

And then second question would be, is there any level of rates where you'd start to get more worried on credit quality? I appreciate all the comments that you – where you've underwritten sort of 5% etc. etc. but – and I know it's a sliding scale, but is there any view that you've got of what level of rates is too high? Any thoughts there would be interesting. Thank you.

Myles O'Grady: Great. Thank you very much, Andrew. Let me comment on the rate and affordability and I know Mark will recap on structural hedging in relation to rate sensitivity as well. So, I mean, back to my point from earlier against the backdrop of ECB rates up by 4.25%, we have been quite thoughtful and measured about how much of that we pass on to mortgage customers. Driven, of course, by the reality that ECB rates are increasing because of the concerns for inflation. So, that's the reason why we've passed on 1.25% and 1.75% to fixed mortgage customers.

As part of our overall affordability assessment, we do stress each mortgage. We look at the customer's payment profile, their expenses, what they spend their money on. We stress the mortgage to see how they will perform in a higher rate environment. And again, so far, we're very pleased with the general affordability and behaviour of our customers. I know Mark has called it out earlier, but it is worth reiterating. The macro prudential rules in Ireland have proven to be very successful in the context of the Bank of Ireland three out of five mortgages that have been written under macro prudential rules, and they offer good protection both for customers and indeed for Bank of Ireland as well.

Mark Spain: Yeah. Andrew, just on the NII sensitivity. So, just the sensitivity to 100 basis points drop on rates were €315 million for 100 bps drop on rates. That would compare to €380 million back in December. So, that rate sensitivity has fallen, that's largely as a result of the increase in the structural hedge and that's what the structural hedge is designed to do, is to reduce the NII sensitivity. From here – and sorry, the other key point here is that relative to not having a structural hedge or materially lower structural hedge, we significantly reduced the NII sensitivity and the downside relative to that. So, ultimately, that structural hedge is locking in value from here. The structural hedge, I would say, it's probably modest growth referencing growth in liabilities from here with one-seventh of the hedge rolling over every year.

Andrew Stimpson (KBW): Okay, so, I appreciate that the hedge is what's reducing it, so that might come down a bit as, as deposit betas rise, I guess, is what's in there. But you're not expecting that to come down too much further?

Mark Spain: All these things will depend on the starting point, and again, you know, that €315 million from today, that reflects the starting point of 3.5%. It also reflects the depositor behaviour experience up to this point, which as we've referenced in the call has been pretty muted to date.

Andrew Stimpson (KBW): Okay. Sure. Thank you.

Myles O'Grady: Thank you, Andrew.

Operator: Thank you. [Operator Instructions] We will now take your next question. And the question comes from the line of John Cronin from Goodbody. Please go ahead.

John Cronin (Goodbody): Good morning, both. Thanks for taking my questions. First of all, can I have a go at unpacking the flat half-on-half guidance for business income in the second half? Could you maybe talk through how, how you would expect Wealth & Insurance, Retail Ireland, and Corporate and Markets income to evolve and I guess that the question is, my key question is, is the key reason for flat because you expect to see some downstress in Corporate & Markets related revenue?

And my second question is just in the wake of EBA stress test announcements, and or the results, is there any possibility of a softening of some of your Pillar 2 capital requirements in time on the back of that improved performance relative to the 2021 stress test?

And finally, just to revisit, subsequent to prior question, on the downside NII sensitivity. That €315 million for a minus 100 basis points parallel shift in rates. So does that assume full pass-through of the lower rates to fixed mortgage customers in Ireland? Thanks.

Myles O'Grady: Okay. John, the line was a little bit bad, but we think we've got those questions. In relation to – let me just offer a view on business income and then Mark will want to come back to that as well. Flat in the second half of the year is in the context of H1 being +23%. So we expect a strong performance in business income for 2023, really from a range of factors. Certainly our Wealth & Insurance business is performing quite well actually in the context of a relatively difficult market backdrop. So AUMs are up by 7%, and also net inflows increasing as well significantly.

On the retail side, as a consequence of bringing onboard new customers last year, 240,000 current account customers last year. And indeed this year, customer numbers increasing by 7%, we expect retail fee income to be strong. It was up 5% in the first half of the year.

And on the stress test, I mean, we are very pleased with the outcome of the stress test, particularly in the context that it's representing the management actions that we have specifically taken over the last number of years, very mindful of ensuring our balance sheet is as strong as it can be. And clearly, at this point, it is too early to translate that stress test outcome, as positive as it, into capital requirements. Clearly, we'll have those discussions with the regulators in due course. Mark, go ahead, if you want to add to that.

Mark Spain: And maybe just John a little bit more colour on the business income and I'll come back to the downside NII sensitivity as well. So, as Myles said like a very strong performance the first half of +23% versus H1. And that's really our strategy in action there. And the Ireland fee income is coming through in two lines because we've moved our Business Banking activity from Retail Ireland to Corporate & Markets. So, it's coming through in two lines. The second thing is, which makes things complicated, is that we're now reporting, as required under IFRS 17. But what we see there is that our Wealth & Insurance business had you know, a very strong performance there in the first half. The performance now is more driven by the back book rather than necessarily sales in year which for insurance products now gets factored into the P&L over the life of those products. So, we're pleased with that. The offset and we spoke about before, about the UK where we've got a fee expense there. The fee expense is higher in the half year. That reflects again the business doing well because higher NII release leads to higher partnership fees which come through in this line. So, that's a positive from a business perspective. And then Corporate and Markets, it had had Business Banking growth. But there is lower Corporate Banking fees that reflects a cautious approach to international corporate and property, which we spoke about. And also some cessation of business activity and impacts.

And just in the downside NII just a couple of things there. That sensitivity it is, as you know, it's got a range of simplifying assumptions. So, this assumes instantaneous and parallel path movement in all interest rates. It's a theoretical exercise. And so, there are a few pieces there. The assets and liabilities whose pricing is mechanically linked, they're assumed to pass through, and there are a range of other assumptions which we don't disclose for competitive reasons. But we believe, although it's ultimately a theoretical exercise, that it's hopefully helpful to the market, and helps your thinking about our NII evolution.

John Cronin (Goodbody): Great. Thank you.

Operator: I will now hand the call back for closing remarks.

Myles O'Grady: Thank you very much. And we look forward to meeting many of you and indeed our investors over the coming days. I hope you all have a very good day indeed. Thank you very much.

Mark Spain: Thanks, everyone.

Operator: Thank you. This concludes today's conference call. Thank you for participating. You may now disconnect.