

NatWest Group

Q4 preview – a guide to 2024 and beyond

Reiterate Rating: BUY | PO: 290.00 GBp | Price: 215.50 GBp

A complex picture

With Q4 earnings trends likely negative and immediate capital distributions below peers, guidance will be particularly important for NatWest, but also complex. An uncertain operating environment could make the company more conservative on the outlook and the stock has rallied over 20% from its post Q3 lows, making outperformance around Q4 more challenging. Looking beyond Q4, a 5.6x PE undervalues a mid-teens RoTE and yield, in our view, and we reiterate our Buy.

Lower earnings in Q4

A lower net interest margin and higher costs are likely to result in a 21% QoQ earnings decline (Exhibit 1). Both have been flagged by the company, but the pace of margin decline will be closely watched – we and consensus expect margin erosion halving QoQ. We tweak our estimates.

Looking for guidance

Sharp deposit moves in 2023 and an uncertain rates outlook make net interest margin guidance complex. We estimate 2.81% FY24 (Exhibit 2), with a 3Q24 low. Consensus has moved towards our 2024 estimates (Exhibit 4), since we factored in lower rates at the beginning of the year (see Rates rollercoaster report). After the company highlighted a cost focus at Q3 and with its <50% 2025 cost: income target looking challenging, an update here seems likely. We expect RoTE to dip in 2024E, recovering to the current medium term 14-16% target from 2025E, but consensus is at 12-13% (Exhibit 7). A potential retail offering of NatWest shares is a further complication, we think.

Limited buyback capacity for now

An anticipated Q4 increase in risk weighted assets leaves less capacity than usual for share buybacks. However, we think that delivering one, albeit relatively small at £250m, would be an important signal on commitment to capital distributions. We see NatWest distributing c£3bn capital a year, a mid-teens yield (Exhibit 8).

Estimates (Dec) (GBp)	2021A	2022A	2023E	2024E	2025E
Net Profit (€m)	2,674	3,602	3,995	3,302	3,627
EPS (Adjusted)	23.4	37.8	43.7	38.9	45.5
Dividend / Share	11.3	13.8	16.5	17.0	20.0
Adjusted NAV PS	292	262	277	305	342
ADR EPS (Adjusted - US\$)	0.64	0.93	1.10	0.98	1.15
ADR Dividend / Shares (US\$)	0.31	0.34	0.42	0.43	0.51
Valuation (Dec)					
P/E	9.22	5.70	4.94	5.55	4.74
EPS Change (YoY)	362%	61.6%	15.6%	-11.0%	17.0%
Price / BV	0.60x	0.64x	0.59x	0.54x	0.49x
Price / NAV	0.74x	0.82x	0.78x	0.71x	0.63x
Net Yield	5.24%	6.39%	7.65%	7.88%	9.28%
DPS Change (YoY)	250%	21.8%	19.8%	3.03%	17.6%
Price / GOP	8.45x	3.89x	2.97x	3.21x	2.67x

09 February 2024

Equity

Key Changes

(GBp)	Previous	Current
2024E EPS	38.87	38.86
2025E EPS	45.48	45.47

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Stock Data

Price (Common / ADR)	215.50 GBp / 5.51 USD
Price Objective	290.00 GBp / 7.33 USD
Date Established	27-Oct-2023 / 8-Feb-2024
Investment Opinion	B-1-7 / B-1-7
52-Week Range	168.30 GBp-308.60 GBp
Market Value (mn)	18,882 GBP
Shares Outstanding (mn)	8,762.1 / 4,381.1
Average Daily Value (mn)	36.54 USD
Free Float	65.0%
BofA Ticker / Exchange	RBSPF / LSE
BofA Ticker / Exchange	NWG / NYS
Bloomberg / Reuters	NWG LN / NWGL
ROE (2023E)	12.4%
ESGMeter™	High

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Refer to important disclosures on page 10 to 13. Analyst Certification on page 7. Price Objective Basis/Risk on page 7.

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Timestamp: 09 February 2024 12:00AM EST

iQprofileSM NatWest Group

Key Income Statement Data (Dec)	2021A	2022A	2023E	2024E	2025E
(£ Millions)	Other GAAP	Other GAAP	Other GAAP	Other GAAP	Other GAAP
Net Interest Income	7,614	9,842	11,026	10,242	11,129
Net Fee Income	2,124	2,292	2,264	2,377	2,454
Securities Gains / (Losses)	317	1,133	0	0	0
Other Income	457	(111)	1,312	1,086	986
Total Non-Interest Income	2,898	3,314	3,576	3,464	3,441
Total Operating Income	10,512	13,156	14,602	13,706	14,569
Operating Expenses	(7,758)	(7,687)	(7,956)	(7,997)	(8,136)
Pre-Provision Profit	2,754	5,469	6,645	5,709	6,433
Provisions Expense	1,278	(337)	(661)	(696)	(990)
Operating Profit	4,032	5,132	5,984	5,013	5,443
Non-Operating Items	0	0	0	0	0
Pre-Tax Income	4,032	5,132	5,984	5,013	5,443
Net Income to sh/holders	2,674	3,602	3,995	3,302	3,627
Adjusted Cash Earnings	2,524	3,731	3,995	3,302	3,627

Key Balance Sheet Data

Total Assets	781,992	720,053	706,672	717,479	738,987
Average Interest Earning Assets	504,303	534,524	531,532	510,504	503,711
Risk Weighted Assets	156,971	176,101	184,950	187,328	198,899
Total Gross Customer Loans	362,796	369,774	379,217	386,862	398,784
Total Customer Deposits	479,810	450,318	427,367	423,444	429,797
Tier 1 Capital	32,471	28,867	28,470	28,968	29,650
Tangible Equity	30,689	25,482	24,449	25,270	26,650
Common Shareholders' Equity	37,412	32,598	31,964	32,785	34,165

Key Metrics

Net Interest Margin	1.45%	1.81%	2.12%	2.04%	2.20%
Tier 1 Ratio	20.7%	16.4%	15.4%	15.5%	14.9%
Effective Tax Rate	24.7%	24.8%	29.1%	29.1%	28.8%
Loan / Assets Ratio	45.9%	50.9%	53.1%	53.4%	53.5%
Loan / Deposit Ratio	74.8%	81.4%	87.9%	90.5%	92.0%
Oper Leverage (Inc Growth - Cost Growth)	1.31%	26.1%	7.49%	-6.65%	4.56%
Gearing (Assets / Equity)	20.9x	22.1x	22.1x	21.9x	21.6x
Tangible Equity / Assets	3.92%	3.54%	3.46%	3.52%	3.61%
Tangible Equity / RWAs	19.6%	14.5%	13.2%	13.5%	13.4%

Business Performance

Revenue Growth	0.04%	25.2%	11.0%	-6.14%	6.30%
Operating Expense Growth	-1.27%	-0.92%	3.51%	0.51%	1.74%
Provisions Expense Growth	-141%	-126%	96.3%	5.19%	42.3%
Operating Revenue / Average Assets	0.51%	0.68%	0.84%	0.70%	0.75%
Operating Expenses / Average Assets	-0.98%	-1.02%	-1.12%	-1.12%	-1.12%
Pre-Provision ROA	0.35%	0.73%	0.93%	0.80%	0.88%
ROA	0.34%	0.48%	0.56%	0.46%	0.50%
Pre-Provision ROE	7.27%	15.6%	20.6%	17.6%	19.2%
ROE	7.06%	10.3%	12.4%	10.2%	10.8%
RoTE	8.09%	13.3%	16.0%	13.3%	14.0%
RoRWAs	1.54%	2.24%	2.21%	1.77%	1.88%
Dividend Payout Ratio	48.3%	36.4%	37.8%	43.7%	44.0%
Efficiency Ratio (Cost / Income Ratio)	73.8%	58.4%	54.5%	58.3%	55.8%

Quality of Earnings

Total Non-Interest Inc / Operating Inc	27.6%	25.2%	24.5%	25.3%	23.6%
Market-Related Revenue / Total Revenues	3.02%	8.61%	0%	0%	0%
Provisioning Burden as % of PPP	-46.4%	6.16%	9.95%	12.2%	15.4%
NPLs plus Foreclosed Real Estate / Loans	1.40%	1.39%	1.46%	1.43%	1.39%
Loan Loss Reserves / NPLs	75.8%	67.4%	68.0%	65.0%	65.0%
Loan Loss Reserves / Total Loans	1.06%	0.94%	1.00%	0.93%	0.90%
Provisions Expense / Average Loans	-0.36%	0.09%	0.18%	0.18%	0.25%

Company Sector

Banks-Retail

Company Description

NatWest is primarily a UK-focused retail and commercial banking business. It carries out similar activities in the Republic of Ireland and has a relatively small broader international presence. Investment banking activities have been scaled down substantially and are now primarily aimed at servicing the company's corporate customers.

Investment Rationale

NatWest's focus on growth, clear commitment to cost reduction and strong balance sheet see it well positioned for a UK economic recovery. We see this driving above cost of equity profitability and facilitating attractive capital distributions, not reflected in the current valuation.

Stock Data

Shares / ADR	2.00
Price to Book Value	0.6x

Quarterly Earnings Estimates

	2022	2023
Q1	NA	12.89A
Q2	NA	12.52A
Q3	NA	10.16A
Q4	NA	7.87E

Key data

Exhibit 1: NatWest 4Q23 preview (£m unless stated)

Earnings 21% lower QoQ – less income, more costs. BofAE 5% above consensus, mainly lower provisions

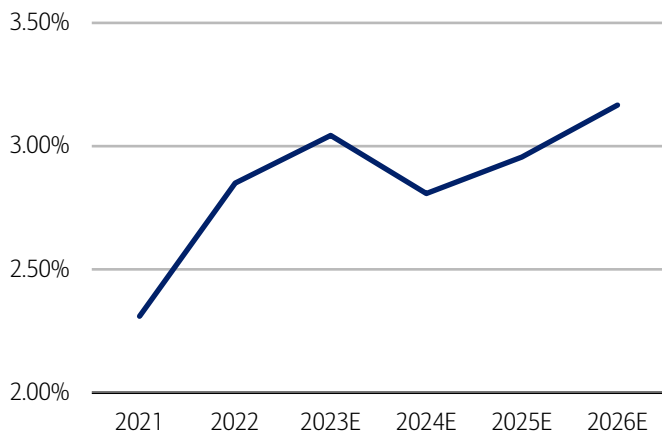
	4Q22	1Q23	2Q23	3Q23	4Q23E					
					BofA	YoY	QoQ	Cons	YoY	QoQ
P&L - NatWest Group										
Net interest income	2,868	2,902	2,824	2,685	2,615	-9%	-3%	2,594	-10%	-3%
Non interest income	840	974	1,027	803	772	-8%	-4%	787	-6%	-2%
Total income	3,708	3,876	3,851	3,488	3,387	-9%	-3%	3,381	-9%	-3%
Other expenses	(2,047)	(1,932)	(1,875)	(1,793)	(2,012)	-2%	12%	(2,017)	-1%	13%
Litigation & conduct costs	(91)	(56)	(52)	(134)	(99)	-	-	(104)	-	-
Operating expenses	(2,138)	(1,988)	(1,927)	(1,927)	(2,111)	-1%	10%	(2,121)	-1%	10%
Gross operating profit	1,570	1,888	1,924	1,561	1,275	-19%	-18%	1,260	-20%	-19%
Impairments	(144)	(70)	(153)	(229)	(209)	45%	-9%	(242)	68%	6%
Profit before tax	1,426	1,818	1,771	1,332	1,066	-25%	-20%	1,018	-29%	-24%
Tax	(46)	(512)	(549)	(378)	(300)	553%	-21%	(288)	526%	-24%
Discontinued operations	(56)	35	(143)	(30)	(12)	-	-	(11)	-	-
Minorities	(62)	(62)	(59)	(58)	(71)	15%	22%	(67)	8%	16%
Attributable profit	1,262	1,279	1,020	866	683	-46%	-21%	652	-48%	-25%
Notable items in income										
	(58)	56	288	(26)	0	-	-	(4)	-	-
Ex notable items, conduct & litigation										
Income ex notable items	3,766	3,820	3,563	3,514	3,387	-10%	-4%	3,385	-10%	-4%
Expenses ex conduct and litigation	(2,047)	(1,932)	(1,875)	(1,793)	(2,012)	-2%	12%	(2,017)	-1%	13%
Impairments	(144)	(70)	(153)	(229)	(209)	45%	-9%	(242)	68%	6%
Profit before tax	1,575	1,818	1,535	1,492	1,165	-26%	-22%	1,125	-29%	-25%
Key metrics - NatWest Group										
Net interest margin (Banking)	3.20%	3.27%	3.13%	2.94%	2.85%	-0.35%	-0.09%	2.83%	-0.37%	-0.11%
Average interest earning assets (Banking), £bn	356	360	362	363	364	2%	0%	364	-	-
Cost: income ratio	55.2%	49.8%	48.7%	51.4%	59.4%	4.2%	8.0%	59.7%	4.5%	8.3%
Cost of risk	0.15%	0.07%	0.16%	0.24%	0.22%	0.06%	-0.02%	0.25%	0.10%	0.01%
CET1 ratio	14.2%	14.4%	13.5%	13.5%	13.3%	-0.9%	-0.2%	13.4%	-0.8%	-0.1%
Risk weighted assets (£bn)	176	178	178	182	185	5%	2%	184	5%	2%
TNAV per share (p)	264	278	262	271	279	6%	3%	281	7%	4%
Ordinary DPS (p)	10.0	0.0	5.5	0.0	11.0	-	-	11.3	-	-
Share buyback (£m)	800	0	1,759	0	250	-	-	120	-	-

Source: BofA Global Research estimates, company reports, company compiled consensus

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Exhibit 2: Margin recovering from 2025E as hedge continues building

Annual banking net interest margin

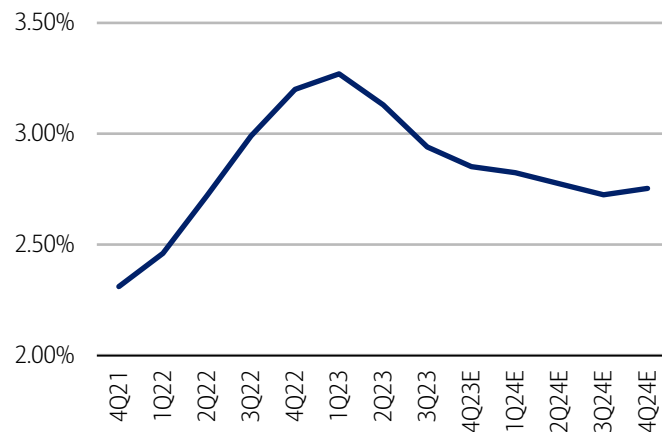


Source: Company data, BofA Global Research estimates

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Exhibit 3: Slowing pace of margin decline, 3Q24E trough

Quarterly banking net interest margin

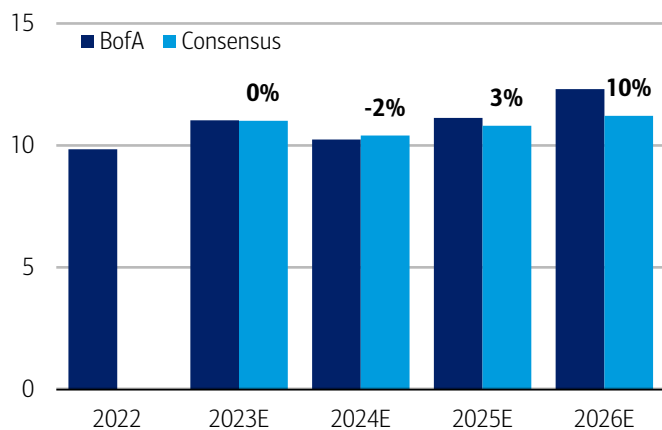


Source: Company data, BofA Global Research estimates

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Exhibit 4: Net interest income, BofAE and consensus (£bn)

We are 2% below 2024E consensus, 10% above by 2026E

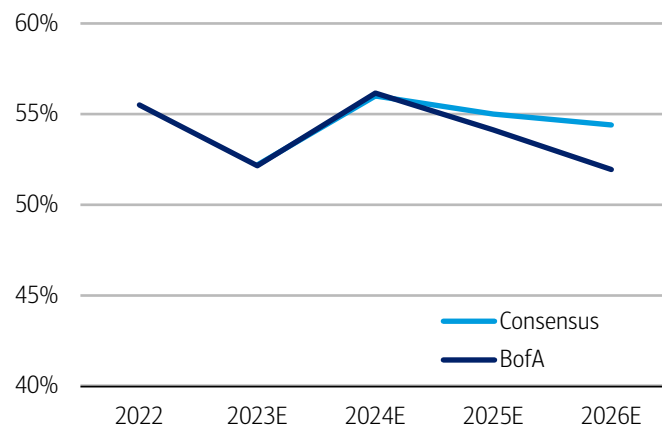


Source: Company data, company consensus, BofA Global research estimates

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Exhibit 5: Cost: income ratio, BofAE and consensus

<50% by 2025 looks hard to achieve

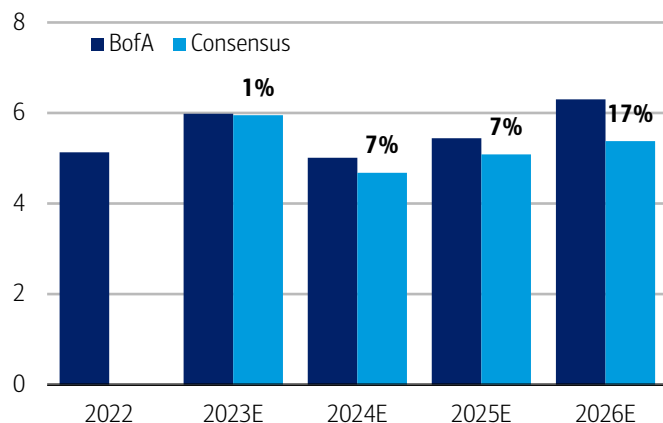


Source: Company data, company consensus, BofA Global research estimates

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Exhibit 6: Profit before tax, BofAE and consensus (£bn)

We are 1-17% above consensus, 2023E-26E

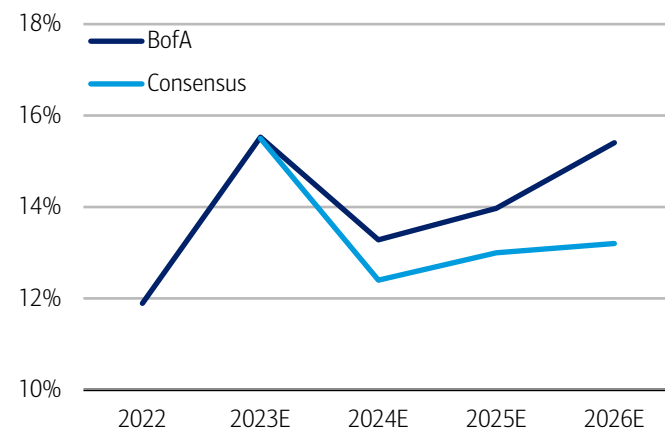


Source: Company data, company consensus, BofA Global research estimates

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Exhibit 7: RoTE, BofAE and consensus (£bn)

Consensus sees RoTE settling at 12-13%, we expect a recovery to 15%

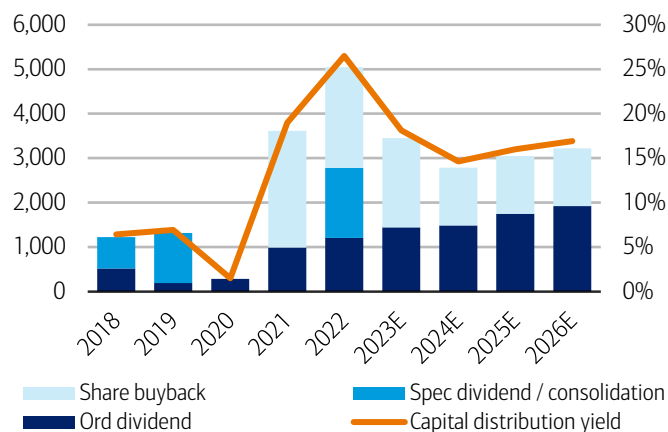


Source: Company data, company consensus, BofA Global research estimates

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Exhibit 8: Mid-teens yield 2023E-26E

Capital distribution (£m)

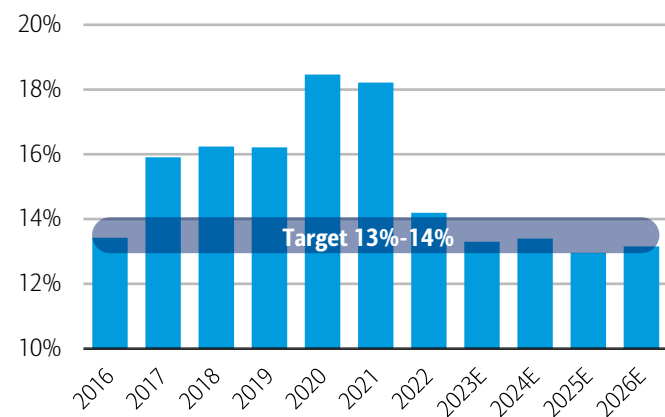


Source: Company data, BofA Global Research estimates

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Exhibit 9: Operating within 13-14% CET1 target

NatWest CET1 ratio



Source: Company data, BofA Global Research estimates

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Exhibit 10: Fundamental valuation

358p Gordon Growth model based valuation

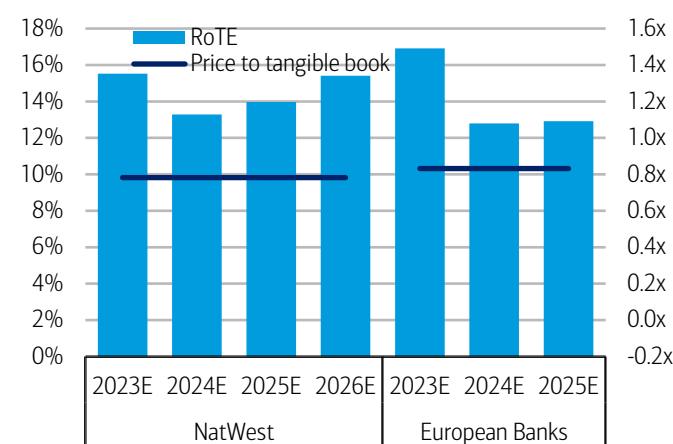
	Value (p)
RoTE 2026E	15.4%
CoE	13.0%
Growth	0%
Book multiple	1.2x
Book multiple discounted to 1 year from now	0.9x
2023E tangible book value	279
Value pre capital distribution	262
Present value of dividend	60
Present value of share buyback	36
Fundamental fair value	358
Price objective	290

Source: BofA Global Research estimates

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Exhibit 11: RoTE and price to tangible book multiple

5% price to book discount for 5% better profitability



Source: Bloomberg, BofA Global Research estimates

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Exhibit 12: European Banks sector relative PE valuation

262p valuation on sector PE

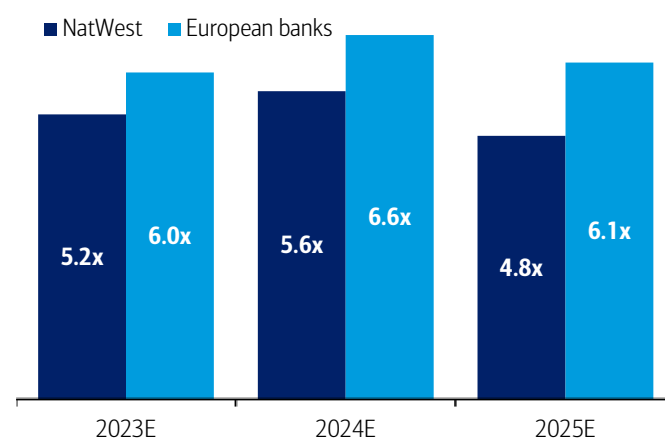
	Value (p)
NatWest 1 year forward EPS	40.0
European Bank sector 1 year forward PE	6.5x
NatWest valued on sector multiple	262

Source: BofA Global Research estimates

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Exhibit 13: PE multiple, NatWest vs European Banks sector

2024E PE 5.6x, 15% below the European Bank sector



Source: Bloomberg, BofA Global Research estimates

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Price objective basis & risk

NatWest Group (RBSPF / NWG)

Our price objective for NatWest is 290p (US\$7.33 per ADR). Our valuation uses a Gordon Growth model based on the outer year of our forecast period, to which we add the present value of expected capital return. We then cross check this against sector PE multiples and our economic scenario analysis. We use 2026E as the base year for our model. With a 13% cost of equity, this suggests a 2026E price to book multiple of 1.2x, reducing to 0.9x when discounted to a year from now at our cost of equity. Applying this to 2023E tangible book value of 279p gives a value of 259p pre capital return. To this we add the present value of the dividends and share buybacks that we forecast through to 2026E.

Downside risks to our price objective are weaker earnings than anticipated from higher impairment losses if the UK economy performs worse than we presently expect, a weaker interest rate outlook, more significant restructuring, tougher regulation and/or increased competition.

Upside risks are a stronger economic recovery, including interest rate and growth prospects, offering revenue upside and reduces credit risk. A more constructive pricing environment would be a further positive.

Analyst Certification

I, Rohith Chandra-Rajan, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

EMEA - Banks Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	Allied Irish Banks	AIBRF	AIBG ID	Alastair Ryan
	Bank of Ireland Group	XBOIF	BIRG ID	Alastair Ryan
	BFF Banking Group	XBBZF	BFF IM	Antonio Reale
	BNP Paribas	BNPQF	BNP FP	Tarik El Mejjad
	BNP Paribas	BNPQY	BNPQY US	Tarik El Mejjad
	CaixaBank	CIXPF	CABK SQ	Antonio Reale
	Credit Agricole	CRARF	ACA FP	Tarik El Mejjad
	Danske Bank	DNSKF	DANSKE DC	Tarik El Mejjad
	Erste Bank	EBKOF	EBS AV	Alastair Ryan
	Erste Bank	EBKDY	EBKDY US	Alastair Ryan
	HSBC	XHSBF	5 HK	Alastair Ryan
	HSBC	HBCYF	HSBA LN	Alastair Ryan
	HSBC -A	HSBC	HSBC US	Alastair Ryan
	Intesa Sanpaolo	IITSF	ISP IM	Antonio Reale
	Intesa Sanpaolo	ISNPY	ISNPY US	Antonio Reale
	KBC Group	KBCSF	KBC BB	Tarik El Mejjad
	KBC Group NV	KBCSY	KBCSY US	Tarik El Mejjad
	NatWest Group	RBSPF	NWG LN	Rohith Chandra-Rajan
	Natwest Group PLC	NWG	NWG US	Rohith Chandra-Rajan
	Nordea	NBNKF	NDA FH	Tarik El Mejjad
	Nordea	XSABF	NDA SS	Tarik El Mejjad
	Nordea Bank Abp	NRDBY	NRDBY US	Tarik El Mejjad
	Santander	SAN	SAN US	Antonio Reale
	Santander	BCDRF	SAN SQ	Antonio Reale
	Societe Generale	SCGLF	GLE FP	Tarik El Mejjad
	Societe Generale	SCGLY	SCGLY US	Tarik El Mejjad
	Unicredit	UNCFF	UCG IM	Antonio Reale
	Unicredit	UNCRY	UNCRY US	Antonio Reale



EMEA - Banks Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
NEUTRAL				
	ABN AMRO	ABMRF	ABN NA	Tarik El Mejjad
	Banco Bilbao Vizcaya Argentaria	BBVA	BBVA US	Antonio Reale
	Banco BPM	BNCZF	BAMI IM	Antonio Reale
	Bankinter	BKIMF	BKT SQ	Antonio Reale
	BBVA	BBVXF	BBVA SQ	Antonio Reale
	Handelsbanken	SVNLF	SHBA SS	Tarik El Mejjad
	ING Groep NV	ING	ING US	Tarik El Mejjad
	ING Groep NV	INGVF	INGA NA	Tarik El Mejjad
	Lloyds Banking Group	LLDTF	LLOY LN	Rohith Chandra-Rajan
	Lloyds Banking Group	LYG	LYG US	Rohith Chandra-Rajan
	Monte dei Paschi	BMDPF	BMPS IM	Antonio Reale
	Raiffeisen Bank International	RAIFF	RBI AV	Alastair Ryan
	StanChart	SCBFF	STAN LN	Alastair Ryan
	StanChart	XCHBF	2888 HK	Alastair Ryan
	Svenska Handelsbanke	SVNLY	SVNLY US	Tarik El Mejjad
	UBS	XUJHF	UBSG SW	Alastair Ryan
	UBS	UBS	UBS US	Alastair Ryan
UNDERPERFORM				
	Banco Sabadell	BNSDF	SAB SQ	Antonio Reale
	Barclays	BCLYF	BARC LN	Rohith Chandra-Rajan
	Barclays	BCS	BCS US	Rohith Chandra-Rajan
	Commerzbank	CRZBF	CBK GY	Rohith Chandra-Rajan
	Deutsche Bank	DB	DB US	Rohith Chandra-Rajan
	Deutsche Bank	XDUSF	DBK GY	Rohith Chandra-Rajan
	DNB	DNBBF	DNB NO	Tarik El Mejjad
	DNB ASA	DNBBY	DNBBY US	Tarik El Mejjad
	Mediobanca	MDIBF	MB IM	Antonio Reale
	Permanent TSB	ILPMF	PTSB ID	Alastair Ryan
	Poste Italiane	PITAF	PST IM	Antonio Reale
	SEB	SVKEF	SEBA SS	Tarik El Mejjad
	Swedbank	SWDBF	SWEDA SS	Tarik El Mejjad
	Swedbank AB	SWDBY	SWDBY US	Tarik El Mejjad
	Virgin Money UK PLC	CBBYF	VMUK LN	Rohith Chandra-Rajan
	Virgin Money UK PLC	CYBBF	VUK AU	Rohith Chandra-Rajan

IQmethodSM Measures Definitions

Business Performance

Return On Capital Employed

Return On Equity

Operating Margin

Earnings Growth

Free Cash Flow

Numerator

NOPAT = (EBIT + Interest Income) × (1 – Tax Rate) + Goodwill Amortization

Net Income

Operating Profit

Expected 5 Year CAGR From Latest Actual

Cash Flow From Operations – Total Capex

Denominator

Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill

Amortization

Shareholders' Equity

Sales

N/A

N/A

Quality of Earnings

Cash Realization Ratio

Asset Replacement Ratio

Tax Rate

Net Debt-To-Equity Ratio

Interest Cover

Numerator

Cash Flow From Operations

Capex

Tax Charge

Net Debt = Total Debt – Cash & Equivalents

EBIT

Denominator

Net Income

Depreciation

Pre-Tax Income

Total Equity

Interest Expense

Valuation Toolkit

Price / Earnings Ratio

Price / Book Value

Dividend Yield

Free Cash Flow Yield

Enterprise Value / Sales

EV / EBITDA

Numerator

Current Share Price

Current Share Price

Annualised Declared Cash Dividend

Cash Flow From Operations – Total Capex

EV = Current Share Price × Current Shares + Minority Equity + Net Debt +

Other LT Liabilities

Enterprise Value

Denominator

Diluted Earnings Per Share (Basis As Specified)

Shareholders' Equity / Current Basic Shares

Current Share Price

Market Cap = Current Share Price × Current Basic Shares

Sales

Basic EBIT + Depreciation + Amortization

Valuation Toolkit

Numerator

Denominator

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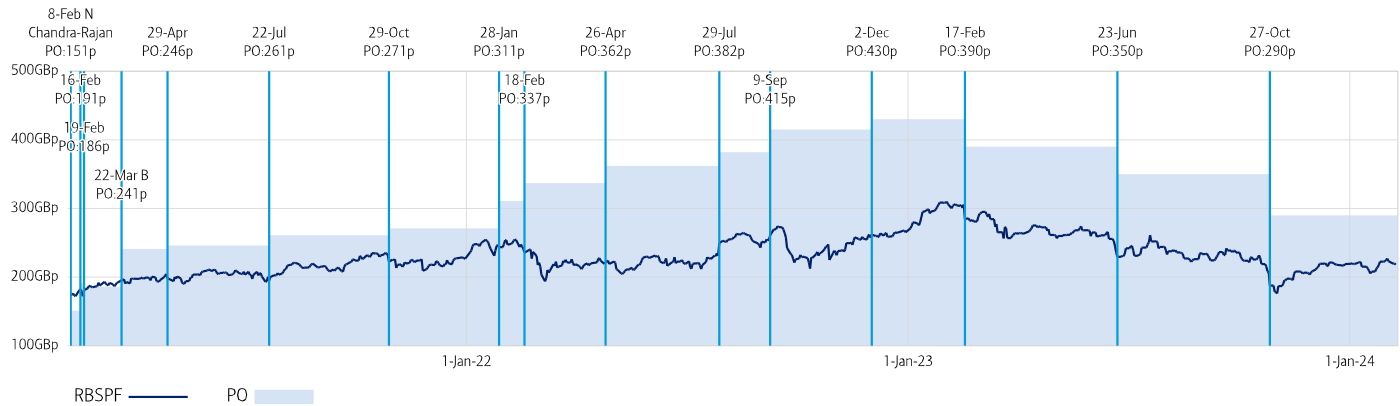
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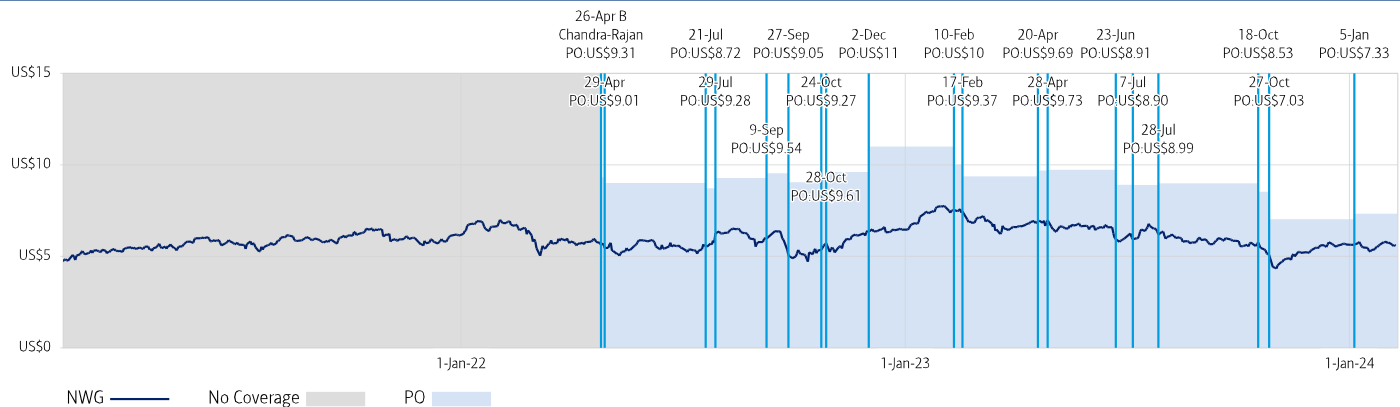
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NatWest Group (RBSPF) Price Chart



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Natwest Group PLC (NWG) Price Chart



The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

Equity Investment Rating Distribution: Banks Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	100	49.75%	Buy	84	84.00%
Hold	54	26.87%	Hold	41	75.93%
Sell	47	23.38%	Sell	35	74.47%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

^{R1} Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster ^{R2}
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Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

^{R2}Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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