CYBG pays the price for not knowing its share of £50bn PPI bill

Uncertainty over how many claims may be upheld sent shares down

Matthew Vincent FT – 6 September 2019

Payouts to bank customers who were mis-sold payment protection insurance have been a feature of the UK economy since 2011, when the first major claims were made. So how is it that CYBG, owner of the Clydesdale, Yorkshire and Virgin Money brands, still cannot accurately model the cost? Its latest estimate of an additional £300m-£450m charge, based on somewhere between 5 and 12 per cent of claims being upheld, contrasts with the apparent precision of economic analyses.

In 2013, when PPI payouts had reached £18bn, against today's almost £50bn, the BBC confidently calculated the stimulus as "1 per cent of GDP". One year and another £4bn later, research by VoucherCodesPro showed 88 per cent of recipients had recycled the money into holidays, cars and household goods, with only 12 per cent adding to their savings. CYBG's uncertainty over how much its customers will receive, let alone what they might do with it, sent its shares down 20 per cent on Thursday.

CYBG also admitted it will be costly finding out. An eightfold increase in customer information requests in August, to 340,000, ahead of the claims deadline, will lift processing costs by £100m, which suggests £300 per request. An extra 42,000 complaints will add another £100m, which is £2,300 per complaint. But as CYBG noted, "the key sensitivity in relation to information requests is the conversion rate into an upheld complaint and it is not yet possible to accurately determine . . . this variable until the group has processed more of the outstanding requests." So it could be 5 per cent or 12 per cent, and it won't know until it knows.

That leaves CYBG's shareholders not knowing what its full-year loss will be, and having to assume analysts are right to say that its core tier one capital ratio will now fall below a target of 13 per cent, and its forecast dividend will fall from 6p a share to 3p, or zero. How could they all have missed a PPI charge equivalent to a fifth of the bank's market value? Two reasons suggest themselves. First, CYBG's smaller scale exacerbates a modelling error made by all UK banks.

Royal Bank of Scotland was barely more precise in estimating a further £600m-£900m PPI charge, but its vagueness is more easily absorbed into a larger cost base. As JPMorgan Cazenove analysts said: "CYBG is more impacted due to lower scale and hence higher cost of processing claims". Second, CYBG's lesser experience makes it more cautious. Lloyds — the most claimed-against bank — has found that the later the PPI enquiry, the less valid it tends to be: its conversion rate has fallen from 13 to 10 per cent.

As Citigroup analysts suggested: "It may be the case that this late surge in information requests is primarily a 'fishing expedition' prior to the final deadline . . . so uphold rates could potentially be far lower." CYBG shares — now 20 per cent cheaper and trading on an earnings multiple 10 per cent below rivals' — might yet prove an equally speculative punt.