Sherborne Investors / Barclays PLC Update

Dear -----

Since we saw you we have increased our position slightly and Sherborne Investors now has an interest of approximately 5.51% in Barclays, spread across the funds that we manage, including, of course, SIGC. Recently, we obtained the official share register from the company and, based on analysis of this detailed data, it appears that we now hold the second largest interest in Barclays. The composition of our holdings has also changed somewhat as we have increased the portion held in derivatives as a way to hedge against declines in Barclays' share price while retaining a majority of the potential increases.

In round numbers we hold, at present, approximately 440 million shares outright, which we purchased for total consideration of slightly less than £900 million in cash, as well as the equivalent of approximately 500 million additional shares through derivatives with maturities stretching out to 2021. As discussed with you, our funds also retain a substantial amount of cash to purchase, at our discretion, our share of any rights offering that Barclays may be required to make or to increase our holdings if this risk begins to abate.

Our recent meeting with the Chairman, Senior Independent Director, and the executive directors of Barclays was pleasant and polite, illustrating that it is possible for people to differ in a spirit of goodwill. In the course of extensive correspondence and several meetings with Barclays we have raised many of the points we have discussed with you, including:

1) **Valuation:** Market multiples of book value for investment banks, like Barclays' Corporate and Investment Bank ("CIB") tend to be lower, globally, than for consumer orientated banks. This raises the threshold return that shareholders require from capital invested in investment banking businesses to a level that the CIB, in its current form, is unlikely to meet or be able to maintain so that it will continue to be a long-term depressant on Barclays' valuation.

2) **Capital Allocation:** The diversion of resources from Barclays' consumer businesses that, in the last 12 months, earned an 18% return to fund an investment banking business that earned at most 7% is, inevitably, destructive of shareholder value and could only be justified by the prospect of a sustainable future level of return that the current CIB business cannot realistically achieve.

3) **Strategic Weaknesses:** The CIB has legacy strategic weaknesses in customer and product mix that fundamentally limit the yield on assets it can achieve, resulting in uncompetitive returns on capital. The current strategy of adding more and more leverage to generate revenue from low-yielding assets does not address these underlying issues.

4) **Capital Structure:** Barclays PLC, the entity that issues shares to the public, is no longer a "bank," but has become a financial holding company that owns interests in ring-fenced subsidiary banks. As a result its risk and liquidity profile is profoundly different than it was in the past and ought to be managed more prudently.

   Four years ago Barclays PLC had relatively immaterial borrowings, but it has now borrowed £47 billion to fund regulatory capital requirements of the CIB. These borrowings are a prior claim on the assets and cash flow of the holding company which, self-evidently, increases the risk to

shareholders of dividend volatility or material capital losses. As a result, Moody's has lowered Barclays PLC's credit rating to Baa3, which is only one step above "junk" and is the lowest of any UK or US banking peer.

5) **Shareholder Base:** Many institutions that would typically have significant shareholdings in Barclays do not, because it has lower equity capital and higher leverage ratios than any UK peer but, despite this added risk, still is expected to generate the lowest consensus returns. The CIB has been described to us as a "black box with too much leverage" and this deters many long-term investors from acquiring shares even at an exceptionally large discount to tangible book value.

In response to certain of these points, Barclays has told us that the improvement in its most recent reported 9 month group returns demonstrates that its strategy is working. However, it is widely recognised that more than 100% of the reported improvement in Core profit in this period resulted from approximately £900 million of net non-recurring items of income, without which Core attributable profit would actually have declined from the prior year.

Less well reported is the fact we pointed out to you that, although Q3 CIB revenues declined from the prior year and pre-tax profits fell by approximately £70 million, what appears to have been a fortunately timed income tax benefit transformed this decline into a reported increase in CIB's attributable profit.

As we also discussed with you, it appears that the CIB's Markets segment revenue increase and market share gain in Q3, which the company has highlighted, resulted from deploying substantially greater assets to "buy" revenue at prices that competitors did not feel compelled to match, rather than from any change in Barclays' long-term strategic competitiveness.

With respect to the capital structure and financial position of the holding company, Barclays told us that they have heard similar concerns from other shareholders, but that the board disagrees and considers the parent company credit rating to be strong, pointing, *inter alia*, to the various stress tests that Barclays has passed. However, this overlooks the fact that it is quite possible to pass a stress test, but still devastate shareholders by virtue of the structure and magnitude of the holding company borrowings that Barclays continues to incur.

It seems clear to us that, in order for the board to protect the long-term interests of Barclays PLC's shareholders, it will be required to adopt more conservative capital, leverage, and liquidity levels than strictly required by the regulators. The most expedient way of meeting this objective is through a judicious reduction in the CIB's assets, which should, we believe, be accomplished before market conditions, now relatively benign, deteriorate. The capital that is released should be retained to make Barclays' capital strength undoubted and to protect shareholders over a full cycle.

Barclays has attractive consumer businesses that unquestionably merit additional attention and resources. The same is true of segments of the CIB. However, we believe that the CIB must become a realistically viable business that can contribute positive shareholder value to Barclays, but without the credit support and subsidies from other parts of the company on which it currently depends. Importantly, the resulting business should no longer threaten the overall stability of the group.

In an interesting exchange about holding company leverage, Barclays argued that the more conservative financial policy we have suggested would lower its returns from levels that are already uncompetitive

and that shareholders, therefore, have no choice other than to continue to accept the added level of risk. This captures, rather succinctly, the dilemma that is presented by the strategic weaknesses noted above. In our view, the better course would be to re-evaluate the strategy of the CIB and balance the business so that excessive leverage is no longer the default option.

We have listened to and considered all of the problems, potentially prohibitive costs, product interdependency, *et cetera*, that make it too hard for Barclays to make any changes. As we discussed with you, there are common sense approaches to dealing with all of these business issues to produce a positive outcome for all stakeholders, and we would be happy to work with the board to develop them.

In this regard, we made a written proposal to the board in September to appoint me as a non-executive director, on the basis that it would add relevant experience and broaden the board's range of perspectives. We felt that this would allow us to participate with the other Barclays directors, in a low-key way, to address the concerns that we have raised, as well as any others that might present themselves in the future. After our meeting, we were told that the directors would look forward to continued engagement with us but that board representation would not be "needed". At the same time, Barclays proposed a meeting following the announcement of their annual results, and we have confirmed an appointment with the CEO at our offices in New York on the 12th of March.

We have undertaken a long process of consistent engagement, deliberately allowing ample time and opportunity for Barclays to respond to our concerns and to demonstrate that the strategy that it has pursued since 2015 will produce appropriate returns at a reasonable risk. After considering the situation carefully we do not have confidence that continued engagement with the company, strictly as an outsider, will produce any more measurable results in the future than it has to date. It seems increasingly likely that, for any progress to be made on our concerns, we will be required to seek a shareholder vote to make changes in the composition of the board. Were we to do so, the most pragmatic approach, in view of the calendar, appears to be for us to present resolutions to be voted on at the Annual General Meeting, but if circumstances were to change we could requisition a separate General Meeting instead.

We continue to believe that it is possible to increase Barclays' shareholder value in line with our customary return objective, and Stephen and I will be coming to see you in the New Year to update you.

In the meantime, both of us wish you the very best for the season and the New Year.

Kind regards,
Ed