annual report and accounts

Lloyds TSB Group plc

2002

Lloyds TSB Group

consumer credit up 17% to £14.9 billion

Profit before tax

Contents

By main businesses

	2002 £ million	2001* £ million
UK Retail Banking and Mortgages	**1,172**	1,205
Insurance and Investments	**1,231**	1,421
Wholesale Markets	**626**	852
International Banking	**379**	357
Central group items	**96**	185
Profit before tax, excluding changes in economic assumptions and investment variance	**3,504**	4,020
Changes in economic assumptions	**55**	–
Investment variance	**(952)**	(859)
Profit before tax	**2,607**	3,161

** Restated to reflect the implementation of UITF33, 'Obligations in capital instruments', FRS17, 'Retirement benefits', FRS19, 'Deferred tax' and detailed guidance from the Association of British Insurers for best practice in the preparation of results using the achieved profits method of accounting. 2001 figures have been restated to incorporate efficiency programme related restructuring costs within business units, and the reclassification of emerging markets debt earnings from International Banking to Central group items.*

Our governing objective is to maximise shareholder value over time

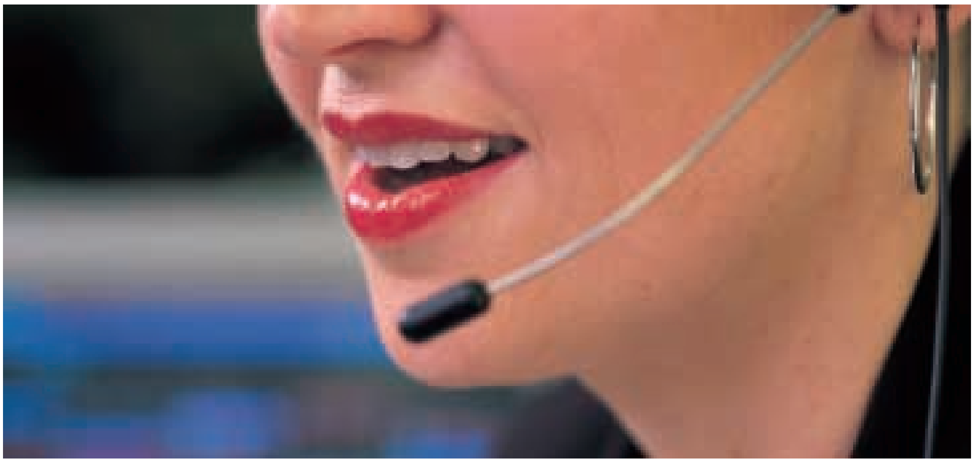
To meet our governing objective we aim:

- To be a leader in our chosen markets
- To be the first choice for our 16 million customers
- To reduce day-to-day operating costs through increased effectiveness

Presentation of results

During 2002 the Group implemented a number of changes in accounting policies following the issue of new accounting standards and guidelines: Urgent Issues Task Force Abstract 33 – 'Obligations in capital instruments', FRS 17 – 'Retirement benefits', FRS 19 – 'Deferred tax', and detailed guidance from the Association of British Insurers (ABI) for best practice in the preparation of results using the achieved profits method of accounting. In accordance with the requirements of accounting standards, the Group has restated comparative figures to reflect these changes.

In order to provide a clearer representation of the underlying performance, the results of the Group's life and pensions business include investment earnings calculated using longer-term investment rates of return and annual management charges based on unsmoothed fund values. The difference between the normalised investment earnings and the actual return ('the investment variance') together with the impact of changes in the economic assumptions used in the embedded value calculation have been separately analysed and a reconciliation to the Group's profit before tax is given on this page.



Market leadership in personal finance

During 2002, the Group increased its market share in both personal loans and credit card lending. Personal loan balances increased by 15 per cent to £8.6 billion, while more than 700,000 new credit cards were issued, leading to a growth of 27 per cent in credit card balances outstanding to £4.9 billion.

2002 highlights

Results

Total income
decreased by £11 million to £8,878 million.

Operating expenses
increased by 3 per cent to £4,915 million.

Trading surplus
decreased by 4 per cent to £3,963 million.

Profit before tax
decreased by £554 million to £2,607 million.

Profit attributable to shareholders
decreased by 20 per cent to £1,781 million.

Earnings per share
decreased by 21 per cent to 32.0p.

Economic profit
decreased by 27 per cent to £821 million.

Post-tax return on average shareholders' equity
16.7 per cent.

Total capital ratio
9.6 per cent, tier 1 capital ratio 7.8 per cent.

Final dividend
of 23.5p per share, making a total of 34.2p for the year, an increase of 1.5 per cent.

Excluding changes in economic assumptions and investment variance:

Profit before tax
decreased by £516 million, or 13 per cent, to £3,504 million.

Post-tax return on average shareholders' equity
was 23.0 per cent.

Achievements in 2002 include

Total income
adjusted for investment variance, acquisitions and other specified items (see page 31), increased by 2 per cent to £9,484 million.

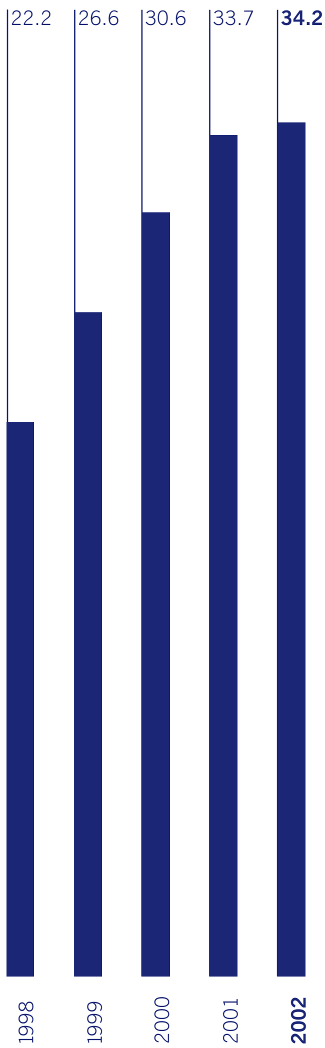
Operating expenses
excluding the impact of acquisitions and the netting of operating lease depreciation (see page 31), were flat at £4,580 million.

Customer lending
grew by 9 per cent to £134.5 billion and customer deposits increased by 7 per cent to £116.3 billion.

Significant repositioning
of UK Retail Banking to support customer franchise development and growth.

Improved market share
in many key product areas, including personal lending, credit cards, life, pensions and long-term savings and, in the fourth quarter of 2002, mortgages.

Dividends per share (pence)



customer deposit balances up 7% to £116.3 billion

Chairman's statement

Maarten van den Bergh

The turmoil surrounding the operating, regulatory and stockmarket environment in which we operate has been unprecedented in recent times.

Whilst these issues have had a direct effect on the Group's results for 2002, and are likely to continue to have an impact until some stability returns to global stockmarkets, they do not impact our long-term strategic goals, the fundamental strength of the Group or the way in which we run our business. In the UK, from where the Group derives the vast majority of its earnings, the slowdown in economic growth has partly been alleviated by the continued strength of the housing market and high levels of consumer spending. We expect levels of growth in the housing market and consumer spending to fall during 2003 although overall economic growth for the year is expected to be slightly higher than the 1.7 per cent growth experienced in 2002.

Our strategic aims

The Group remains totally committed to maximising shareholder value over time and our business units continue to be focused on the Group's three strategic aims: to be a leader in our chosen markets, to be first choice for our customers and to drive down day-to-day operational costs to enable us to further invest in our business franchise. This is a strategy that is being well implemented and delivered, and ensures that the Group continues to seek the optimum balance between short-term profit growth and investment in the future of the business, to create sustainable long-term value for all our stakeholders.

Our results

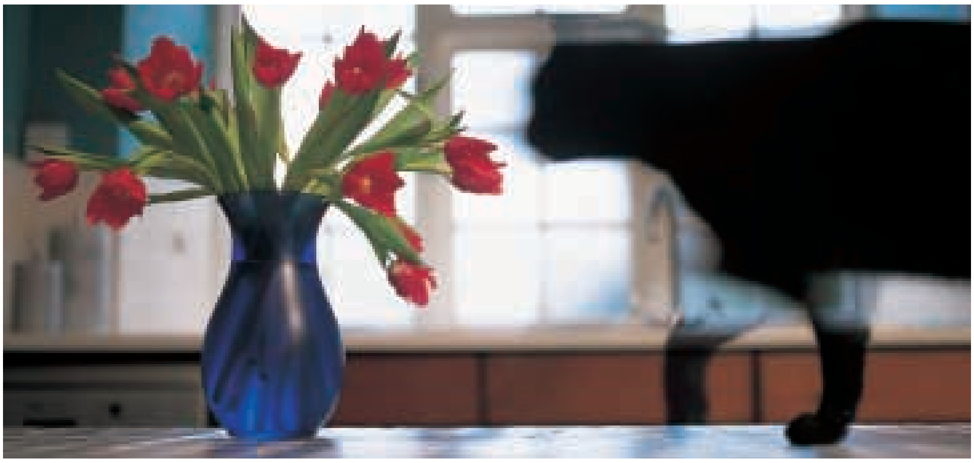
Notwithstanding the slowdown in the UK and all major global economies, Lloyds TSB continues to trade satisfactorily, with strong market share performances in many of its key product areas, and good growth in customer lending and deposits. During the year the Group also achieved its target of an average 2.5 products per customer, whilst maintaining its strict control on operational expenses with costs in 2002, excluding acquisitions and growth in operating lease depreciation, held flat, in part as a result of the significant investment in efficiency programmes made over the last three years. Profit before tax for the year, however, fell by 18 per cent to £2,607 million, partly as a result of a significant increase in provisions for bad and doubtful debts but also as a result of a number of special items including additional provisions for redress to past purchasers of certain pension and endowment products and a higher negative investment variance of £952 million in our insurance businesses, reflecting the weakness of equity markets.

The high level of government interference in all areas of our business has continued throughout 2002 and into 2003. The annual cost of responding to this government intervention is substantial and in 2003 the cost of implementing the findings of the Competition Commission's 'Report into the supply of banking services to small and medium-sized enterprises' is alone likely to be in the region of £150 million.

This industry is already immensely competitive. If the Government wishes to foster greater competition within financial services it should recognise that the level of returns available must be acceptable to both existing and new competitors.

The Government's interventions include the removal of dividend tax credits – increasing corporate pension contributions – the cost of the Universal Bank and the automation of benefits, as well as more specific price controls in both the banking and pensions businesses.

If interference continues, there is a danger that one of the UK's great success stories – the financial services industry – will be less able to compete on the world financial scene where the really strong players will dominate in the future.



Market leadership in home insurance

With over 9 million policies in force, Lloyds TSB Insurance is one of the largest distributors of personal lines general insurance in the UK, with market leadership in the distribution of home and creditor insurance.

Dividend

The Group continues to generate strong cashflows from its banking businesses and, excluding investment variance, the profit attributable to shareholders in 2002 was £2,496 million. The Board has decided to maintain the final dividend at 23.5p, to make a total for the year of 34.2p, an increase of 1.5 per cent. The Board is mindful of the level of dividend cover and, consequently, profit growth may not necessarily result in increases in dividend. The Board recognises the importance attached by shareholders to the Group's dividend.

Our people

In all of my dealings with staff throughout the Group it never ceases to amaze me how professional and motivated the entire staff of the Group continues to be, in the face of very difficult circumstances. Lloyds TSB's continuing success is underpinned by the significant contribution made by its entire staff and the Group's people strategy will continue to be shaped around harnessing this superb commitment, creating a workplace where staff understand their roles and contribution, and continue to feel proud to work for Lloyds TSB. I know the management and staff remain as committed as ever to the future development of the Group and delivery of value to its shareholders.

Board changes

After more than 40 years in the banking industry and over 12 years of outstanding service and leadership to TSB and the Lloyds TSB Group, Peter Ellwood will retire on 31 May 2003. His tremendous contribution to the Group has included bringing together Lloyds Bank and TSB in a most effective combination. Our highest regards and warmest wishes go with him. I am delighted that Peter will be succeeded by Eric Daniels, who has exceptional financial services experience throughout the world, and who has already made a significant impact on the quality and positioning of our retail business. Peter Ayliffe will succeed Eric Daniels as Group Executive Director, UK Retail Banking, and join the Board on 1 June 2003. We shall also bid farewell to Kent Atkinson who retires, with our best wishes, at the annual general meeting after more than 38 years with the Group. He was succeeded as Group Finance Director by Philip Hampton, who joined the Board on 1 June 2002.

Alan Moore, Deputy Chairman, will also be leaving the Board at the annual general meeting after 23 years of valuable service, including 14 as a member of the Board, and will be replaced by David Pritchard, who will retire as an executive director. Steve Targett will join the Board on 10 March 2003, and succeed David as Group Executive Director, Wholesale and International Banking, following the annual general meeting.

Other non-executive directors leaving the Board at the annual general meeting are Clive Butler, who has served since 1993, and Sheila Forbes, who joined the Board in 1994.

All the departing directors leave with our warm thanks for their contribution to the Group over many years.

Our future

The business environment in which we operate is characterised by increasing levels of competition, volatile equity markets and increasing government intervention in, and regulation of, the financial services industry. Against this backdrop, Lloyds TSB will continue to focus on its long standing principles of prudent and sustainable revenue growth from the creation of value for customers, tight management of its cost base and strong credit risk management. With a clear focus on these core strengths, and supported by a dedicated and resourceful team of people, Lloyds TSB is well positioned for future growth and the challenges ahead.

Maarten van den Bergh
Chairman
13 February 2003

current account balances

up 12% to £27.9 billion

Group chief executive's review

Peter Ellwood CBE

The trading environment of 2002 has been a substantial challenge for both the financial services industry and, within it, Lloyds TSB. In order to prosper in such a challenging environment it remains essential that the Lloyds TSB Group has in place a clearly defined strategy. To this end we remain committed to maximising shareholder value over time through leveraging world class leadership and management of our people to achieve our three strategic aims. We have made progress in a number of areas.

The year has been characterised by some encouraging features but also by a number of issues which have adversely affected the profit and loss account. The encouraging side of the story is the growth in market share in personal loans, credit cards, general insurance, and life and pensions, and the fact that we sold more products to more people than we have ever done before, with a record net increase in products of 1.6 million compared with 1.3 million last year. Our improved cross-selling ratio of 2.5 products per customer remains industry leading. Customer lending increased by 9 per cent and customer deposits increased by 7 per cent. Our efficiency programme delivered benefits in 2002 in line with our forecasts resulting in a significant improvement in our underlying efficiency. Excluding the impact of acquisitions and operating lease depreciation, operating costs were flat in comparison with 2001, and there was a reduction in our headcount of over 4,000. At the same time we have continued to invest heavily in improving our service to customers.

All these factors augur well for future sustainable growth. However, we have also had to absorb a number of significant hits to our profit and loss account. During the year we have experienced a reduction in profit of £952 million as a result of the adverse investment variance following the 24 per cent fall in the FT All Share Index during 2002. We have increased the Group's general provision by £50 million in respect of our business in Argentina and significantly increased our provisions in respect of certain US corporate customers as a result of their accounting and other irregularities. In addition, we have absorbed provisions totalling £205 million for redress to past purchasers of pensions and Abbey Life endowment and long-term savings products, much of which relates to policies written in the late 1980s and early 1990s. The Group has also experienced a reduction of £59 million in unit trust and asset management fees, largely as a result of stockmarket falls, a cost of £57 million to reflect the implementation of revised mortality assumptions in the Group's life businesses, and a £142 million reduction in income as a result of lower other finance income, following the adoption of Financial Reporting Standard 17. The overall impact of these issues meant that the Group's statutory pre-tax profits fell to £2,607 million from £3,161 million in 2001, and earnings per share fell by 21 per cent to 32.0p. Our post-tax return on equity was 16.7 per cent. Excluding changes in economic assumptions and investment variance, our post-tax return on equity was 23.0 per cent.

Within our businesses, the performance of retail banking is now benefiting from the substantial investments we have made to reposition the business for profitable growth. Product sales were at an all time high during 2002 and the Group continues to grow its current account customer franchise in the light of intense competition. Scottish Widows, in line with the rest of the life assurance industry, has experienced difficult trading conditions as a result of the considerable fall in equity markets. However, we believe the long-term growth prospects for this sector of the market, and for Scottish Widows in particular, remain

Market leadership in motor finance

In 2002, Lloyds TSB strengthened its leading position in the motor finance market, growing its business by 17 per cent. Lloyds TSB is also the leading contract hire and fleet management company in the UK, now managing a fleet of some 150,000 vehicles.

good. The long-term winners will be those with extensive customer franchises and distribution reach, augmented by economies of scale and strong brand power.

We have these in abundance. Our market leading general insurance business has continued to prosper and delivered very strong profitable growth, with pre-tax profits increasing by 16 per cent, compared with 2001.

In our wholesale markets and international banking businesses good growth has continued to be achieved in a number of our specialist businesses, although this growth has been offset by a significant increase in the level of corporate bad and doubtful debt provisions. Whilst overall credit quality continues to be robust, the Group does have a cautious outlook on a number of corporate sectors and exposures which has led to these higher levels of corporate provisioning. The economic situation in Argentina continues to be difficult and the outlook is likely to remain uncertain at least until after the new Argentine government takes office during 2003. During 2002 the Group increased its general provision for its exposure to Argentina by £50 million and the Group's total exposure to Argentina at the end of the year had been reduced to £190 million, net of provisions and charges, compared to £610 million a year ago.

Against the volatile background, it is essential that we are not swayed from the successful implementation of our vision and strategic aims.

As a Group we have a unifying vision whereby our first strategic aim is to be first choice for our customers because we understand and meet their needs more effectively than any of our competitors. It is a vision of a business where we truly create value for our customers; where our customers trust us enough to give us the privilege of looking after more of their business. It is a vision of a business where our staff understand the Group's strategy, understand what we are seeking to do, agree with it and know that what they do is vital to our future success. Our second strategic aim of being a leader in our chosen markets also links in to the customer. Market leaders earn higher returns and generate greater value, some of which can be passed on to the customer. Our third strategic aim of driving down day-to-day operational costs allows the Group to create headroom to invest for the future. Throughout the Group these three themes underpin the development of our businesses and in the last twelve months considerable progress has been made to meet these strategic aims and our world class aspirations.

First choice for our customers

The Group's strategy of maximising shareholder value over time can only be sustainably achieved by putting our customers at the heart of everything we do. Lloyds TSB's multi-channel banking infrastructure, including internet and telephony services, means that the Group can provide its customers with significant options in terms of both convenience and choice. The knowledge and expertise of our staff ensures that the Group provides comprehensive financial solutions to meet the needs of all of our customers. But the environment in which we work is changing rapidly as customer needs are evolving and as customers continue to seek greater value in terms of the benefits they receive from their products and services. Customers expect excellent customer service and error free operation of their banking arrangements. Those organisations that can develop a reputation for providing excellent customer service will retain existing customers and attract new ones. Over the last twelve months Lloyds TSB has made considerable progress in addressing customer service issues, and these improvements in customer service during 2002 have been a significant contributory factor to strong recruitment of new customers during the year and the improvement in the Group's cross selling rates.

A leader in our chosen markets

The Group continues to strengthen its market position in many of its key product

mortgage balances up 10% to £62.5 billion

areas despite high levels of competition throughout our business. In retail banking we continue to grow our customer franchise and during 2002 saw income growth of 5 per cent from our retail banking business. Our personal loan and credit card portfolios grew by 15 per cent and by 27 per cent respectively, again showing significant improvements in our market share. In Scottish Widows the second half of the year showed a good improvement in market share notwithstanding the very difficult stockmarket environment. In our general insurance business the Group further enhanced its UK market leadership position in the distribution of home and creditor insurance to deliver growth in premium and commission income of 19 per cent. Within asset finance, the Group has acquired First National Vehicle Holdings, Abbey National Vehicle Finance and the Dutton-Forshaw Group. These acquisitions have further enhanced the Group's leading position in UK motor finance. So, in most areas of our business, the Group continues to maintain and develop market leading positions to enable high levels of returns to be sustained, or improved.

Driving down our day-to-day costs

The Group is already amongst the leaders in cost efficiency. However, in a relatively low growth, low inflation and low interest rate macro-economic environment, cost control remains critically important. Augmented by our efficiency programmes the Group's control and focus on costs has meant that in 2002 costs, excluding the impact of acquisitions and operating lease depreciation, were held flat. Overall Group staff numbers decreased by 4,191 to 79,537 during 2002, after adjusting for an increase of 2,328 from acquisitions during the year. The Group will, of course, continue its significant programme of investment in improved efficiency, to support business growth.

On a personal note, we announced in December last year that I will retire as Group Chief Executive on 31 May 2003, shortly after my 60th birthday. I have thoroughly enjoyed my time at Lloyds TSB and it has been a great privilege to lead this organisation as Chief Executive for the last six years. I am delighted to hand over the mantle to Eric Daniels, who shares my passion for this organisation, and my drive to create value for our customers and shareholders by providing excellent products and superior service. He will be supported by a fantastic team of over 79,000 people across the Group to whom my heartfelt thanks go for their help and support over the years.

Lloyds TSB is an extremely successful organisation with strong returns on shareholders' equity and a first class efficiency ratio. However, the Group does operate in a world of greater competitive ferocity, greater regulation and a tough global economic environment, exacerbated by concerns over geo-political stability. The Group has continued to strive constantly to refresh existing and new revenue streams, build upon its financial and intellectual capital and optimally manage risk and cost. These are not easy times but we have three businesses, UK Retail Banking and Mortgages, Insurance and Investments, and Wholesale Markets and International Banking, all of which have considerable scope for sustainable profitable growth and which can build on the track record in income growth which the Group has seen over the last six years, with costs growing at a considerably slower pace. For any successful business to maintain and improve on such an excellent track record it is important to go forward with realism, confidence and excitement about the future. This, we do.

Peter Ellwood CBE
Group Chief Executive
13 February 2003

The leading corporate donor in the UK

Since 1996, the Lloyds TSB Foundations have received over £200 million to distribute to local charities.

Our work in the community

Lloyds TSB is committed to making a positive impact on local communities. As one of the UK's leading financial services organisations we recognise the need to play our part in tackling some of the social issues that confront the communities in which our business is based.

Our community programme was valued at £40 million in 2002 which makes us the UK's largest corporate giver. The majority of our support is channelled through the independent Lloyds TSB Foundations which receive one per cent of the Group's pre-tax profits, averaged over three years, instead of the dividend on their shareholdings. This year they will receive £33 million to distribute to grassroots causes which help to improve the quality of life for disabled and disadvantaged people.

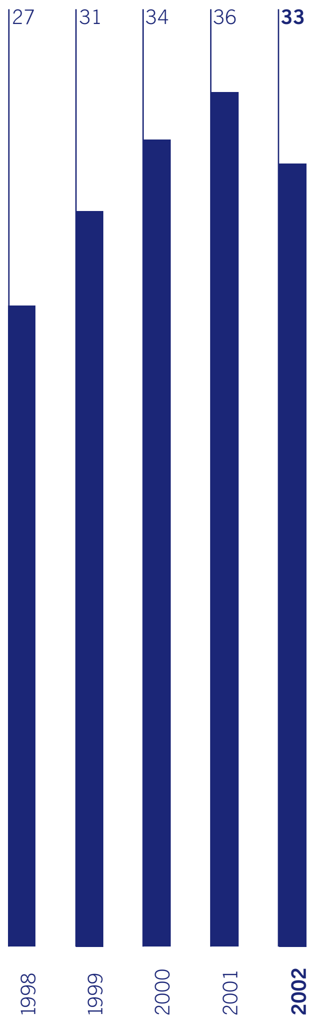
The Foundations also run a 'Matched Giving Scheme' for Lloyds TSB Group staff which matches money raised and time given to registered charities. In 2003 the Foundations have set aside £1.25 million to encourage staff to support local groups. We support national charities through our Charity of the Year campaign. In 2002 staff raised some £685,000 for the Royal National Institute for Deaf People to fund its Information and Tinnitus Helpline for one year. This year we aim to raise £750,000 for Help the Hospices, to support both adult and children's hospices across the country.

As well as providing charitable support, we also focus our resources on education and economic and social regeneration. Our Quality in Education programme promotes the use of a self-assessment and improvement tool which helps schools to drive their own efforts to raise standards. In 2002, the programme received a Business in the Community Impact Endorsement Mark in recognition of the results we have achieved. By working through local education authorities, professional teacher associations and in partnership with the Department for Education and Skills and the Cabinet Office, the programme has been introduced to over 4,000 schools so far.

Business has an important role to play in neighbourhood renewal which is why we work with community based organisations to foster economic and social regeneration. Our programme focuses on creating access to finance in disadvantaged communities, providing backing for small business and encouraging entrepreneurship among young people.

One of our main projects this year has been the development of the Wessex Reinvestment Trust (WRT) which will deliver loan services to develop enterprise and facilitate access to affordable housing and workspace. This is the first entirely rural community finance initiative which seeks to provide a springboard for rural regeneration in Devon, Dorset and Somerset.

Distribution to the Lloyds TSB Foundations (£m)



The businesses of Lloyds TSB

Lloyds TSB is one of the leading UK-based financial services groups, whose businesses provide a comprehensive range of banking and financial services in the UK and overseas. At the end of 2002 total group assets were £253 billion and there were over 79,000 employees. Market capitalisation was £24.8 billion.

The main businesses and activities of the Group during 2002 are described below:

UK Retail Banking and Mortgages

UK Retail Banking and Mortgages provides a full range of banking and financial services to some 15 million customers. With more than 2,200 branches of Lloyds TSB Bank, Lloyds TSB Scotland and Cheltenham & Gloucester (C&G), the Group provides comprehensive geographic coverage in England, Scotland and Wales.

• *Current accounts, savings and investment accounts, and consumer lending.* The retail branches of Lloyds TSB Bank offer a broad range of branded products and C&G provides retail investments through its branch network and a postal investment centre.

• *Card Services* provides a range of card-based products and services, including credit and debit cards and card transaction processing services for retailers. The Group is a member of both the VISA and MasterCard payment systems and is the third largest credit card issuer in the UK.

• *Cash machines.* The Group has one of the largest cash machine networks of any leading banking group in the UK and personal customers of Lloyds TSB Bank are able to withdraw cash, check balances and obtain mini statements through 4,210 *cashpoint** machines at branches and external locations around the country. In addition, they have access to a further 37,000 cash machines via LINK in the UK and to cash machines worldwide through the VISA and MasterCard networks.

• *Telephone Banking.* Telephone Banking continues to grow and the Group provides one of the largest telephony services in Europe. At the end of 2002 3.2 million customers had registered to use the services of PhoneBank and the automated voice response service PhoneBank Express.

* *cashpoint* is a registered trade mark of Lloyds TSB Bank plc

• *Internet Banking.* Internet Banking provides online banking facilities for personal and business customers and enables them to conduct their financial affairs without using the branch network. Over 1.9 million customers have registered to use the Group's internet banking services.

• *Business Banking.* Small businesses are served by dedicated business managers based in some 450 locations throughout the UK. Customers have access to a wide range of tailored business services ranging from traditional banking products through factoring, insurance and investments to non-financial solutions to their business problems such as Debtor Management service providing legal support to help customers recover debts and Prospect Finder providing customers with a tailored list of potential customers for their business. Lloyds TSB is one of the leading banks for new business start-ups with around one in five opening accounts with the Group.

• *UK Wealth Management.* Private Banking provides a range of tailor-made wealth management services and products to individuals from 40 offices throughout the UK. In addition to asset management, these include tax and estate planning, executor and trustee services, deposit taking and lending, insurance, and personal equity plan and ISA products. At the end of 2002, client funds under management totalled some £10 billion.

Lloyds TSB Stockbrokers undertakes retail stockbroking through its Sharedeal Direct telephone service.

• *Cheltenham & Gloucester* is the Group's specialist residential mortgage provider, selling its mortgages through branches of C&G and Lloyds TSB Bank in England and Wales, as well as through the telephone, internet and postal service, C&G TeleDirect. The Group is the third largest residential market lender in the UK, with a market share of 9.3 per cent, loans outstanding at the end of 2002 of £62.5 billion and over 980,000 borrowers.

Insurance and Investments

• *Scottish Widows* is the Group's specialist provider of life assurance, pensions and investment products, which are distributed through the Lloyds TSB branch network, through independent financial advisors and directly to the consumer via the telephone, internet, and face-to-face.

The businesses of Lloyds TSB

• *General insurance.* Lloyds TSB General Insurance provides general insurance and broking services through the retail branches of Lloyds TSB Bank and C&G, and through a direct telephone operation and the internet. The business is the market leader in the distribution of household insurance in the UK.

• *Scottish Widows Investment Partnership* manages funds for the Group's retail life, pensions and investment products. Clients also include corporate pension schemes, local authorities and other institutions in the UK and overseas. At the end of 2002 funds under management totalled some £70 billion.

Wholesale Markets

The Group's relationships with major UK and multinational companies, banks and financial institutions, and medium-sized UK businesses, together with its activities in financial markets, are managed through dedicated offices in the UK and a number of locations overseas, including New York.

• *Treasury* is a leading participant in the Sterling money market. It is active in currency money markets, foreign exchange markets and also in certain derivatives markets to meet the needs of customers, and as part of the Group's trading activities, including liquidity management.

• *Corporate* provides a wide range of banking and related services, including electronic banking, large value lease finance, share registration, venture capital, correspondent banking and capital markets services to major UK and multinational companies, financial institutions and, through a network of dedicated offices, to medium-sized businesses in the UK.

• *Asset Finance* through the Lloyds TSB Commercial Finance, Alex Lawrie and autolease brands is a market leader in invoice discounting, factoring and contract hire. The Black Horse branded point of sale finance operation has leading positions in the motor, motorbike and caravan markets. Specialist personal lending, store credit, small/medium ticket leasing and the recently acquired Dutton-Forshaw motor dealership complete this group of businesses.

International Banking

• *The Americas.* The Group has operated in The Americas for over 130 years and has offices in Brazil, Argentina, Colombia and 6 other countries. In addition there are private banking and investment operations in the United States.

• *New Zealand.* The National Bank of New Zealand is the country's second largest bank and provides a full range of banking services through some 160 outlets.

• *Europe.* The Group has private banking operations for wealthy individuals outside their country of residence. The business is conducted through Switzerland and through four other countries overseas. There are additional corporate and private banking operations in Belgium, Netherlands, France and Spain.

• *Offshore Banking* comprises all the Group's offices in the Channel Islands and Isle of Man providing a full range of retail banking, private banking, trust and financial services to overseas residents and islanders, together with deposit services offshore for UK residents.

• *Middle East and Asia.* There are banking operations in Hong Kong, Singapore, Tokyo, Malaysia and Dubai.

Financial review

Accounting policies and presentation

Accounting policies are set out on pages 64 to 67. During 2002 the Group has made a number of changes in accounting policy to implement the requirements of new accounting standards and guidelines. Comparative figures have been restated. The effect of these changes in policy on the results for the year and the comparative period is set out below.

Urgent Issues Task Force Abstract 33 (UITF 33)

UITF 33 was issued in February 2002 and is effective for accounting periods ending on or after 23 March 2002. Following its implementation the Group has reclassified €750 million (£482 million) of Perpetual Capital Securities as undated loan capital and the related cost is included within interest expense. Previously these securities were included within minority interests in the balance sheet and the cost was treated as a minority interest deduction.

Financial Reporting Standard 19 (FRS 19) – Deferred Tax

FRS 19 was issued in December 2000 and is effective for accounting periods ending on or after 23 January 2002. Following its implementation, the Group makes full provision for deferred tax assets and liabilities arising from timing differences between the recognition of gains and losses in the financial statements and their recognition in a tax computation. Previously provision was only made where it was considered that there was a reasonable probability that a liability or asset would crystallise in the foreseeable future. An adjustment has been made increasing shareholders' equity at 31 December 2001 by £40 million to reflect the revised policy.

Financial Reporting Standard 17 (FRS 17) – Retirement Benefits

FRS 17 replaces SSAP 24 and UITF 6 as the accounting standard dealing with post-retirement benefits. The Group has decided to implement the requirements of FRS 17 in 2002 to coincide with the triennial full actuarial valuations of the Group's pension schemes and because of the significant impact that implementation has on the Group's reported results.

The new standard requires the Group to include the assets of its defined benefit schemes on its balance sheet together with the related liability to make benefit payments. The profit and loss account includes a charge in respect of the cost of accruing benefits for active employees, any benefit improvements and the cost of severances borne by the schemes; the expected return on the schemes' assets is included as other finance income less a charge in respect of the unwinding of the discount applied to the schemes' liabilities. Under SSAP 24 the profit and loss account included a charge in respect of the cost of accruing benefits for active employees offset by a credit representing the amortisation of the surplus in the Group's defined benefit schemes; a pension prepayment was included in the Group's balance sheet together with a provision in respect of post-retirement healthcare obligations. An adjustment has been made reducing shareholders' equity at 31 December 2001 by £236 million to reflect the revised policy.

The amounts included in the Group's profit and loss account in 2002 are reflected in other finance income and administrative expenses, and are summarised below.

Other finance income	2002 £m	2001 £m
Expected return on scheme assets	**817**	844
Interest cost of scheme liabilities	**(652)**	(537)
Other finance income	**165**	307

Administrative expenses	2002 £m	2001 £m
Defined contribution schemes	**25**	18
Defined benefit schemes	**293**	329
Pension costs	**318**	347

At 31 December 2002 a net pension deficit of £2,077 million was included in the Group's balance sheet, based upon actuarial valuations carried out at that date. This reflects a fall in the value of the schemes' assets caused by the significant reduction in equity market values. The valuations were prepared in accordance with the requirements of the accounting standard which seek to place a market value on the schemes' assets and liabilities at a point in time. As a result, these valuations are not indicative of the long-term funding position of the schemes which is assessed in the light of triennial formal actuarial valuations of the schemes. The last formal actuarial valuation of the Group's principal schemes was performed at 30 June 2002 and, whilst these valuations have yet to be finalised, they disclosed that the schemes remained satisfactorily funded although it is probable that it will be necessary to recommence employer's cash contributions shortly. These cash contributions, which are likely to be in the order of £150 million in 2003 and £300 million in 2004, do not affect the Group's profit and loss account as normal pension costs are already, under FRS 17, included within the Group's operating expenses.

Financial review

Accounting policies and presentation (continued)

Investment variance

In December 2001, the Association of British Insurers (ABI) published detailed guidance for the preparation of figures using the achieved profits method of accounting which are published as supplementary financial information accompanying the accounts of most listed insurance companies. The ABI guidance recommends the use of unsmoothed fund values to calculate the value of in-force business. To improve the comparability of the results of the Group's insurance operations with the supplementary financial information published by listed insurers the Group has changed the basis of its embedded value calculations to use unsmoothed fund values; previously the effect of investment fluctuations had been amortised in the profit and loss account over a two year period. An adjustment has been made reducing shareholders' equity at 31 December 2001 by £208 million to reflect the revised policy.

The following tables show the impact of the changes in accounting policies:

2002	**UITF 33 £m**	**FRS 19 £m**	**FRS 17 £m**	**Investment variance £m**	**Total adjustment £m**
Net interest income	**(31)**	**–**	**–**	**–**	**(31)**
Other finance income	**–**	**–**	**165**	**–**	**165**
Other income	**–**	**–**	**–**	**(104)**	**(104)**
Total income	**(31)**	**–**	**165**	**(104)**	**30**
Operating expenses	**–**	**–**	**323**	**–**	**323**
Trading surplus	**(31)**	**–**	**(158)**	**(104)**	**(293)**
Provisions/claims	**–**	**–**	**–**	**–**	**–**
Joint ventures	**–**	**–**	**–**	**–**	**–**
Profit before tax	**(31)**	**–**	**(158)**	**(104)**	**(293)**
Tax	**–**	**(29)**	**(47)**	**(31)**	**(107)**
Profit after tax	**(31)**	**29**	**(111)**	**(73)**	**(186)**
Minority interests	**(31)**	**–**	**–**	**–**	**(31)**
Attributable profit	**–**	**29**	**(111)**	**(73)**	**(155)**

2001	Original results £m	UITF 33 £m	FRS 19 £m	FRS 17 £m	Investment variance £m	Restated results £m
Net interest income	4,944	(22)	–	–	–	4,922
Other finance income	–	–	–	307	–	307
Other income	3,882	–	–	–	(222)	3,660
Total income	8,826	(22)	–	307	(222)	8,889
Operating expenses	4,324	–	–	452	–	4,776
Trading surplus	4,502	(22)	–	(145)	(222)	4,113
Provisions/claims	981	–	–	–	–	981
Joint ventures	(10)	–	–	–	–	(10)
Profit on sale of businesses	39	–	–	–	–	39
Profit before tax	3,550	(22)	–	(145)	(222)	3,161
Tax	971	–	14	(43)	(67)	875
Profit after tax	2,579	(22)	(14)	(102)	(155)	2,286
Minority interests	79	(22)	–	–	–	57
Attributable profit	2,500	–	(14)	(102)	(155)	2,229

Consequential adjustments have been made to the balance sheet to reflect these changes in accounting policy.

Forward looking statements

This document contains forward looking statements with respect to the business, strategy and plans of the Lloyds TSB Group, its current goals and expectations relating to its future financial condition and performance. By their nature, forward looking statements involve risk and uncertainty because they relate to events and depend on circumstances that will occur in the future. Lloyds TSB Group's actual future results may differ materially from the results expressed or implied in these forward looking statements as a result of a variety of factors, including UK domestic and global economic and business conditions, risks concerning borrower credit quality, market related risks such as interest rate risk and exchange rate

Financial review

Forward looking statements (continued)

risk in its banking business and equity risk in its insurance businesses, changing demographic trends, unexpected changes to regulation or regulatory actions, changes in customer preferences, competition and other factors. Please refer to the latest Annual Report on Form 20-F of Lloyds TSB Group filed with the US Securities and Exchange Commission for a discussion of such factors.

Summary of group results

In 2002 the Group's profit before tax decreased by £554 million to £2,607 million from £3,161 million in 2001. Total income decreased by £11 million whilst operating expenses increased by £139 million, or 3 per cent. Excluding changes in economic assumptions, investment variance, endowment and pension related provisions, investment returns on the Group's pension scheme assets, the netting of operating lease depreciation and the impact of acquisitions, total income increased by 2 per cent whilst total costs, excluding the impact of acquisitions and operating lease depreciation, were held flat (see page 31). Customer lending and deposits continue to grow well with further growth in market share being achieved in a number of our core markets. Customer lending grew by 9 per cent to £134.5 billion and customer deposits increased by 7 per cent to £116.3 billion. The Group net interest margin was 3.20 per cent, compared with 3.40 per cent in 2001. This reduction was more than compensated for by increased volumes, resulting in an increase of 5 per cent in net interest income.

Profit attributable to shareholders was 20 per cent lower at £1,781 million and earnings per share decreased by 21 per cent to 32.0p. Shareholders' equity decreased by £2,384 million to £7,972 million following a reduction of £2,331 million in the value of the Group's pension schemes, largely caused by the significant reduction in equity market values. These pension scheme related movements are ignored for regulatory capital purposes and, excluding these market movements, shareholders' equity decreased by £53 million. The post-tax return on average shareholders' equity was 16.7 per cent, compared to 18.1 per cent in 2001. Excluding changes in economic assumptions and investment variance, post-tax return on average shareholders' equity was 23.0 per cent. Economic profit decreased by 27 per cent to £821 million. The post-tax return on average assets was 0.93 per cent, and the post-tax return on average risk-weighted assets was 1.61 per cent.

Pre-tax profit from UK Retail Banking and Mortgages decreased by £33 million to £1,172 million, compared to £1,205 million in 2001. Excluding the impact of a reduction of £57 million in profits from the sale and leaseback of premises and the non-recurrence of certain provision releases in 2001, profit before tax increased by £96 million, or 9 per cent. There was strong growth in personal loans, up 15 per cent, and in credit card lending, up 27 per cent. Current account and savings and investment account balances, within Retail Banking, increased by 10 per cent. Overall, retail banking product sales were 6 per cent higher than in 2001. Costs remained tightly controlled and asset quality generally remains satisfactory, notwithstanding the general slowdown in economic activity within the UK. Provisions for bad and doubtful debts increased by £148 million to £563 million, as a result of volume related asset growth in the personal loan and credit card portfolios and a lower level of recoveries and releases than in 2001. Overall the arrears position was stable. An improved arrears position in personal lending was offset by a slight deterioration in the credit card portfolio.

In the Mortgages business, gross new lending increased by 36 per cent to a record £19.0 billion, compared with £14.0 billion a year ago. Net new lending was £5.9 billion, compared with £3.9 billion in 2001, resulting in a market share of net new lending of 7.5 per cent. The Group's current mortgage pipeline is at record levels and its market share of net new lending in the second half of 2002, at 8.8 per cent, was considerably better than in the first half of the year. Net new lending in the second half of 2002 was £3.9 billion compared with £2.0 billion in the first half of the year. The Group's market share of net new lending in the fourth quarter of 2002 was 10.0 per cent.

Profit before tax, excluding changes in economic assumptions and investment variance, from Insurance and Investments decreased by £190 million, or 13 per cent, to £1,231 million, partly as a result of a £135 million increase in provisions for redress to past purchasers of endowment and pension products to £205 million, and a reduction of £55 million in benefits from experience variances and assumption changes, largely reflecting the implementation of revised actuarial mortality assumptions. Overall weighted sales in the Group's life, pensions and unit trust businesses were £767.6 million compared to £754.7 million last year, an increase of 2 per cent. This increase in weighted sales reflected a 7 per cent increase in weighted sales from life and pensions, partly offset by a 13 per cent reduction in weighted sales from unit trusts, largely caused by the continuing stockmarket volatility which has significantly reduced customer demand for equity-based ISA products. In the second half of 2002, weighted sales of £394.9 million were 10 per cent higher than the £358.9 million in the second half of 2001, and 6 per cent higher than the £372.7 million in the first half of 2002. Weighted sales from independent financial advisors rose by 25 per cent. There was further strong profit growth from the Group's general insurance operations. A 19 per cent growth in the combined premium income from underwriting and commissions from insurance broking led to an increase in profit before tax of £103 million, or 16 per cent, to £754 million.

Wholesale Markets pre-tax profit decreased by £226 million, or 27 per cent, to £626 million, partly as a result of a substantial increase in provisions for bad and doubtful debts. Growth in customer lending, increased operating lease assets and the impact of acquisitions in the asset finance business resulted in a £174 million, or 9 per cent, increase in total income. Operating expenses increased by £202 million, again largely as a result of the asset finance acquisitions and higher operating lease depreciation. The provisions charge for bad and doubtful debts increased by £156 million. In 2002, provisions against Group loans and advances to certain large US corporate customers, caused by accounting and operational irregularities, totalled some £100 million. There was also an increase in provisions within the corporate lending portfolio, reflecting weak equity markets and the slowdown in economic activity in the UK. In the less favourable economic and trading environment, all the individual businesses continued to perform well.

Financial review

Summary of group results (continued)

International Banking pre-tax profit was £22 million, or 6 per cent, higher at £379 million compared with 2001. Profits from New Zealand increased by 32 per cent to £218 million as a result of good growth in all core businesses. Our consumer finance business in Brazil, Losango Consumer Finance, performed well, notwithstanding difficult local economic circumstances, and increased pre-tax profits on a local currency basis by 14 per cent. After the impact of adverse exchange rate movements, which were partly hedged, Losango made a pre-tax profit of £40 million, compared with £43 million in 2001.

The total Group charge for bad and doubtful debts was 38 per cent higher at £1,029 million, compared with £747 million in 2001. In UK Retail Banking the provisions charge increased by £125 million, or 28 per cent, to £564 million, largely as a result of volume related asset growth in the personal loan and credit card portfolios which grew by 15 per cent and 27 per cent respectively. In Wholesale Markets the provisions charge increased by £156 million to £311 million, reflecting the higher provisions against certain large US customers and an increase in the provisions charge from the corporate lending portfolio, reflecting weak equity markets and the slowdown in economic activity in the UK.

International Banking provisions decreased to £162 million from £183 million, as a result of lower specific provisions in Losango, our consumer finance business in Brazil, largely reflecting exchange rate movements. The Group's charge for bad and doubtful debts, expressed as a percentage of average lending, was 0.77 per cent compared to 0.62 per cent in 2001. At the end of the year provisions for bad and doubtful debts for the Group totalled £1,767 million, representing over 120 per cent of non-performing loans (2001: 120 per cent), and the level of non-performing loans increased to £1,414 million, compared with £1,222 million in December 2001, largely reflecting higher levels of non-performing lending in the corporate portfolio, and general portfolio growth throughout the Group. Importantly, non-performing lending as a percentage of total lending was unchanged at 1.0 per cent. The Group's customer lending portfolio continues to be heavily infuenced by our high quality, relatively low risk, mortgage business and, as a result, the Group remains well positioned to withstand a continued economic slowdown.

Since the October presidential election in Brazil the economic situation has somewhat stabilised. The Group reduced its total exposure to Brazil, net of provisions, to £1.9 billion during 2002, from £3.3 billion at the end of 2001, largely from not replacing maturing Government bonds. Economic activity in Brazil has remained reasonably robust and we believe this relative strength in the local economy, in conjunction with the significant International Monetary Fund support package which the newly elected president and incoming government have indicated they will support, should alleviate current concerns about the Brazilian economy. The economic situation in Argentina continues to be difficult and the outlook is likely to remain uncertain at least until after the new Argentine government takes office during 2003. In 2002 the Group increased its general provision relating to its exposure to Argentina by £50 million and the Group's total exposure to Argentina at the end of the year was some £190 million, net of provisions and charges, compared with £610 million at the end of 2001. The Group has now provided for some 50 per cent of its total exposure to Argentina.

In common with a number of companies in the life assurance industry, the Group has been carrying out a review of the past sales of certain endowment based and long-term savings products. As a result the Group has made a provision of £165 million to cover its liability for redress to policyholders in respect of past sales made, primarily in the late 1980s and early 1990s, by the Abbey Life salesforce prior to its disposal by the Group in February 2000. The adequacy of the provision for redress to past purchasers of pension policies has been reviewed as lower stockmarket levels have increased the expected remaining cost of redress. The Group has made a final provision for this purpose of £40 million. The Group is also carrying out, in conjunction with the regulator, an investigation into the appropriateness of sales of a stockmarket related investment product, the Extra Income & Growth Plan. This investigation is expected to be completed during 2003, when the Group will be in a position to estimate the financial effect.

The total capital ratio was 9.6 per cent and the tier 1 capital ratio was 7.8 per cent. Balance sheet assets increased by £17 billion, or 7 per cent, to £253 billion from £236 billion at the end of 2001. Loans and advances to customers increased by £11.5 billion, or 9 per cent. Risk-weighted assets increased by 13 per cent to £122 billion, from £108 billion at the end of 2001. At the end of December 2002, the Scottish Widows free asset ratio was an estimated 10.0 per cent, compared to 11.5 per cent at the end of 2001.

Scottish Widows' investment policy for the with-profit fund is determined, in conjunction with the views of the fund's investment advisors, taking into account the long-term commitments of the fund. From time to time investment policy necessitates the use of derivatives and other hedging instruments, and at the end of 2002 such instruments were held to provide some protection against the short-term volatility in the UK equity markets. The Group keeps its investment policy under review. The equity backing ratio for traditional with-profits policies at 31 December 2002 was 53 per cent (equities 40 per cent; property 13 per cent). Scottish Widows remains sufficiently well capitalised to be able to sustain further stockmarket falls without an injection of capital. During 2002 the Group has not needed to inject additional capital from outside the Group's insurance businesses into Scottish Widows. Scottish Widows is, however, well positioned to participate in a rapidly changing market and to support business growth, as well as maintaining prudent financial management. The Group may inject some capital into Scottish Widows if the level of the FTSE 100 index falls to, and remains at, approximately 3,000. At this FTSE 100 level the capital injection is unlikely to exceed £300 million. To optimise the financial management of the Group's life businesses Lloyds TSB Life was transferred into the ownership of Scottish Widows in December 2002.

Profit before tax by main businesses

Segmental analysis

Year ended 31 December 2002	UK Retail Banking and Mortgages £m	Insurance and Investments £m	Wholesale Markets £m	International Banking £m	Central group items £m	Total £m
Net interest income	3,340	74	1,158	745	(146)	5,171
Other finance income	–	–	–	–	165	165
Other operating income	1,076	1,876	975	374	138	4,439
Total income	4,416	1,950	2,133	1,119	157	9,775
Operating expenses	2,670	490	1,139	578	38	4,915
Trading surplus	1,746	1,460	994	541	119	4,860
General insurance claims	–	229	–	–	–	229
Bad debt provisions	563	–	311	162	(7)	1,029
Amounts written off fixed asset investments	–	–	57	–	30	87
Income from joint ventures	(11)	–	–	–	–	(11)
Profit before tax*	1,172	1,231	626	379	96	3,504
Changes in economic assumptions	–	55	–	–	–	55
Investment variance	–	(952)	–	–	–	(952)
Profit before tax	1,172	334	626	379	96	2,607

Year ended 31 December 2001	UK Retail Banking and Mortgages £m	Insurance and Investments £m	Wholesale Markets £m	International Banking £m	Central group items £m	Total £m
Net interest income	3,102	80	1,096	749	(105)	4,922
Other finance income	–	–	–	–	307	307
Other operating income	1,135	2,006	863	345	170	4,519
Total income	4,237	2,086	1,959	1,094	372	9,748
Operating expenses	2,607	491	937	586	155	4,776
Trading surplus	1,630	1,595	1,022	508	217	4,972
General insurance claims	–	174	–	–	–	174
Bad debt provisions	415	–	155	183	(6)	747
Amounts written off fixed asset investments	–	–	15	7	38	60
Income from joint ventures	(10)	–	–	–	–	(10)
Profit on sale of businesses	–	–	–	39	–	39
Profit before tax*	1,205	1,421	852	357	185	4,020
Investment variance	–	(859)	–	–	–	(859)
Profit before tax	1,205	562	852	357	185	3,161

**excluding investment variance and changes in economic assumptions*

Year end assets by main businesses	2002 £m	2001 £m
UK Retail Banking	23,279	21,124
Mortgages	62,589	56,858
UK Retail Banking and Mortgages	85,868	77,982
Insurance and Investments*	9,161	9,270
Wholesale Markets	89,066	79,370
International Banking	21,779	21,407
Central group items	1,544	1,375
Total assets*	207,418	189,404

**excluding long-term assurance assets attributable to policyholders*

Financial review

UK Retail Banking and Mortgages

(covering the Group's UK retail businesses, providing banking and financial services to personal and small business customers; mortgages; private banking and stockbroking)

	2002 £m	2001 £m
Net interest income	**3,340**	3,102
Other income	**1,076**	1,135
Total income	**4,416**	4,237
Operating expenses	**2,670**	2,607
Trading surplus	**1,746**	1,630
Provisions for bad and doubtful debts	**563**	415
Income from joint ventures	**(11)**	(10)
Profit before tax	**1,172**	1,205
Efficiency ratio	**60.5%**	61.5%
Total assets (year-end)	**£85.9bn**	£78.0bn
Total risk-weighted assets (year-end)	**£54.2bn**	£48.3bn

Profit before tax from UK Retail Banking and Mortgages decreased by £33 million to £1,172 million, compared with £1,205 million in 2001. Strong growth in the Group's consumer lending portfolios and a focus on cost control were offset by the impact of a number of special items. These included a reduction of £57 million in profits from the sale and leaseback of premises and, in the mortgage, personal lending and credit card portfolios, the non-recurrence of provision releases totalling £72 million in 2001. Excluding these items pre-tax profits increased by 9 per cent.

Total income increased by £179 million, or 4 per cent, to £4,416 million. Excluding the 2001 profits from the sale and leaseback of premises, total income grew by 6 per cent. Net interest income increased by £238 million, or 8 per cent, to £3,340 million. Personal loans and credit card lending increased by 15 per cent and 27 per cent respectively and, within Retail Banking, balances on current accounts and savings and investment accounts grew by 10 per cent. Mortgage balances outstanding increased by 10 per cent to £62.5 billion.

Other income decreased by £59 million to £1,076 million. There was an improvement in income earned from credit and debit cards, and increased income from added value current accounts, but this was offset by a higher level of fees and commissions payable and a reduction of £57 million in profits from the sale and leaseback of premises, as the Group's strategy of converting much of its branch portfolio from freehold tenure to leasehold is almost complete.

Operating expenses increased by £63 million, or 2 per cent, to £2,670 million during 2002, compared to £2,607 million in 2001. Staff numbers decreased by 3,329 to 47,895. The trading surplus increased by £116 million, or 7 per cent, to £1,746 million. Bad debt provisions increased by £148 million to £563 million, as a result of volume related asset growth in the personal loan and credit card portfolios and a lower level of recoveries and releases than in 2001. Excluding the impact of the non-recurrence of provision releases totalling £72 million in 2001, the provisions charge as a percentage of average lending for personal loans and overdrafts decreased to 3.73 per cent, from 3.88 per cent in 2001, and the charge in the credit card portfolio decreased to 3.52 per cent, from 3.60 per cent in 2001. Overall the arrears position remained stable.

Provisions for bad and doubtful debts by product	2002 %	2001 %
Charge as a percentage of average lending*		
Personal loans/overdrafts	**3.73**	3.88
Credit cards	**3.52**	3.60
Business Banking	**1.22**	1.05
Mortgages	**0.00**	0.01

* *excluding the impact of the non-recurrence of provision releases totalling £72 million in 2001*

UK Retail Banking has the responsibility for managing the core relationship with our current account customers and, therefore, acts as the principal gateway for the cross-sale of our full range of bancassurance products and services. As such it contributes significantly to the profitability of other businesses. There were good market share gains, particularly in customer deposits, credit cards and personal lending, and greater unit cost efficiencies, offset by the higher level of provisions for bad and doubtful debts. The Group is now starting to see the benefit of recent investments made in the strategic repositioning of the retail bank, which is well positioned to capture the benefits of future customer franchise development and growth.

Financial review

UK Retail Banking and Mortgages (continued)

We continue to offer a comprehensive multichannel distribution service to our customers. In addition to our network of over 2,000 branches, *lloydstsb.com*, our internet banking system, continues to grow and remains one of the most visited financial websites in Europe. Over 450,000 product sales were achieved via the internet in 2002, more than four times the number achieved in 2001. Our telephone banking operation, comprising PhoneBank and PhoneBank Express, is one of the largest in the UK with over 3 million registered customers. Our telephone banking contact centres handled some 46 million calls in 2002, making extensive use of interactive voice recognition technology to improve efficiency and service.

The retail bank continued to develop its strategy of building deeper customer relationships, particularly with our higher value customers, which has resulted in good growth in customer lending and deposit balances. Our relationship offers will be extended further in 2003 with the launch of the Premier Service, which has been successfully piloted in 2002, and the extension of our existing Personal Choice programme. Results from both of these programmes have already shown improved business flows and enhanced customer loyalty as we seek to meet a greater share of our customers' financial needs, supported by the application of our advanced customer relationship management tools.

The recent launch of the Group's new, market leading, credit interest current account reflects the Group's continuing commitment to invest in developing its retail banking franchise by attracting new high quality customers, and rewarding both new and existing customers for using lower cost distribution channels.

Business Banking continued to grow its customer franchise with customer deposits growing by 8 per cent to £9,412 million from £8,715 million in December 2001, and customer lending by 1 per cent to £5,487 million from £5,435 million in December 2001. Following the launch of the Group's unique segmentation strategy for the Business Banking market in 2001, roll-out to all existing customers is complete with customers now migrated to their choice of relationship offer. Underpinning these offers, and central to ensuring that our customers continue to grow their businesses successfully, is RouteMap, a suite of diagnostic tools to help and support customers. Use of *success4business.com*, our small business portal, also continues to grow.

In March 2002, the Competition Commission's report, following its investigation into the supply of banking services to small and medium size enterprises (SMEs), was published by the Government. The Group has implemented the remedies suggested by the Competition Commission and, as a result, it is likely that the annualised impact on profit before tax will be a reduction of some £150 million, based on the Group's forecast level of interest rates.

Mortgages	2002	2001
Gross new mortgage lending	**£19.0bn**	£14.0bn
Market share of gross new mortgage lending	**8.7%**	8.7%
Net new mortgage lending	**£5.9bn**	£3.9bn
Market share of net new mortgage lending	**7.5%**	7.2%
Mortgages outstanding (year-end)	**£62.5bn**	£56.6bn
Market share of mortgages outstanding	**9.3%**	9.5%

Gross new lending increased by 36 per cent to a record £19.0 billion, compared with £14.0 billion a year ago. Net new lending increased to £5.9 billion resulting in a market share of net new lending of 7.5 per cent. Mortgage balances outstanding increased by 10 per cent to £62.5 billion.

Mortgages remain a key recruitment vehicle in support of the Group's cross-sell targets and, during 2002, the Group's key objective in the mortgage business has been to achieve an appropriate balance between growth in market share and profitability. Gross new mortgage lending of £19.0 billion in the year was a record for the Group, and the Group's market share of net new lending in the second half of 2002, at 8.8 per cent, was considerably better than in the first half of the year. Net new lending in the second half of 2002 was £3.9 billion, compared with £2.0 billion in the first half of the year. The Group's market share of net new lending in the fourth quarter of 2002 was 10.0 per cent.

The Group continues to be one of the most efficient mortgage providers in the UK. C&G continues to benefit from mortgage sales distribution through the Lloyds TSB branch network, the IFA market and from the strength of the C&G brand. In addition C&G TeleDirect, its internet and telephone operation, continued to perform strongly. Business levels sourced from intermediaries remain strong and, for the eighth consecutive year, C&G received a 5-star award from the Association of Independent Financial Advisors, an achievement unequalled by any UK financial services provider.

A slightly improved arrears position and the beneficial effect of house price increases have meant that bad debt provisions remained at low levels. New provisions were offset by releases and recoveries resulting in a £1 million net provisions release for the year, compared with a net release of £24 million in 2001 which resulted from a release of £32 million of the Group's mortgage general provision. The quality of our mortgage lending continues to be satisfactory. The average indexed loan-to-value ratio on the C&G mortgage portfolio was 46 per cent and the average loan-to-value ratio for C&G mortgage business written during 2002 was 67 per cent. C&G has a policy of not exceeding a 95 per cent loan-to-value ratio on new lending.

Financial review

Insurance and Investments

(the life, pensions and unit trust businesses of Scottish Widows and Abbey Life; general insurance underwriting and broking; and Scottish Widows Investment Partnership)

	2002 £m	2001 £m
Net interest income	**74**	80
Other income	**1,876**	2,006
Total income	**1,950**	2,086
Operating expenses	**490**	491
Trading surplus	**1,460**	1,595
General insurance claims	**229**	174
Profit before tax*	**1,231**	1,421
Changes in economic assumptions	**55**	–
Investment variance	**(952)**	(859)

**excluding changes in economic assumptions and investment variance*

	2002 £m	2001 £m
Life, pensions and unit trusts		
– Scottish Widows	**573**	585
– Abbey Life	**(98)**	175
	475	760
General insurance	**754**	651
Operating profit from Insurance	**1,229**	1,411
Scottish Widows Investment Partnership	**2**	10
Profit before tax*	**1,231**	1,421

**excluding changes in economic assumptions and investment variance*

Profit before tax from Insurance and Investments, excluding changes in economic assumptions and investment variance, decreased by £190 million, or 13 per cent, to £1,231 million, from £1,421 million in 2001. On the same basis, profit before tax from our life, pensions and unit trust businesses decreased by £285 million, or 38 per cent, to £475 million, partly as a result of a £135 million increase in provisions for redress to past purchasers of endowment and pension products, but also following a reduction of £55 million in benefits from experience variances and actuarial assumption changes. The market for medium and long-term investments continued to be adversely affected by the continued volatility in global stockmarkets. Total sales from the Group's life, pensions and unit trust businesses were £4,456.3 million, compared with £4,423.5 million in 2001, an increase of 1 per cent. Overall weighted sales were £767.6 million compared to £754.7 million last year, an increase of 2 per cent. This increase in weighted sales reflected a 7 per cent increase in weighted sales from life and pensions, partly offset by a 13 per cent reduction in weighted sales from unit trusts and equity-based ISAs, largely caused by the continuing volatility in global stockmarkets throughout 2002. In the second half of 2002, weighted sales of £394.9 million were 10 per cent higher than the £358.9 million in the second half of 2001, and 6 per cent higher than the £372.7 million in the first half of 2002.

The Group's market share of the life, pensions and unit trusts market to September 2002 was 5.3 per cent, with a market share in the third quarter of 2002 of 5.9 per cent. By distribution channel, weighted sales from independent financial advisors rose by 25 per cent as a result of strong life and pensions sales. This compares with an increase of 11 per cent in the first half of the year, compared with the first half of 2001. Our share of the IFA market to September 2002 was 4.5 per cent, a significant improvement on the 3.8 per cent market share in 2001. In the branch network weighted sales were 7 per cent lower, as a result of the substantial reduction in sales of unit trusts, in comparison to a 10 per cent reduction in the first half of the year, compared with the first half of 2001. Scottish Widows remains the leading equity-based ISA provider in the UK as confirmed by the Investment Management Association (IMA) and the Group remains well placed in this sector of the market.

A major programme to convert our unit trust range of some 80 funds into a range of Open Ended Investment Companies (OEICs) has now been completed and the resulting simpler range of mutual funds means that the Group is well positioned to take advantage of the likely changes in the market place, in particular the proposals outlined in the recently published Sandler report.

Financial review

Insurance and Investments (continued)

	2002 £m	2001 £m
Total new business premium income		
Regular premiums:		
Life		
– mortgage related	**35.0**	24.7
– non-mortgage related	**32.7**	19.9
Pensions	**212.7**	232.8
Health	**5.9**	4.6
Total regular premiums	**286.3**	282.0
Single premiums:		
Life	**1,531.8**	1,684.2
Annuities	**497.0**	338.6
Pensions	**1,060.2**	718.2
Total single premiums	**3,089.0**	2,741.0
External unit trust sales:		
Regular payments	**71.5**	65.0
Single amounts	**1,009.5**	1,335.5
Total external unit trust sales	**1,081.0**	1,400.5
Weighted sales (regular + 1/10 single)		
Life and pensions	**595.2**	556.1
Unit trusts	**172.4**	198.6
Life, pensions and unit trusts	**767.6**	754.7
Weighted sales by distribution channel:		
Branch network	**350.6**	376.2
Independent financial advisors	**348.5**	279.8
Direct	**68.5**	98.7
Life, pensions and unit trusts	**767.6**	754.7
	£bn	£bn
Group funds under management		
Scottish Widows Investment Partnership	**70**	78
UK Wealth Management	**10**	11
International	**18**	20
	98	109

Profit before tax from general insurance operations, excluding investment variance, rose by £103 million, or 16 per cent, to a record £754 million, mainly as a result of continued strong revenue growth from creditor and home insurance. With over 9 million general insurance policies in force, we estimate that the Group has market leadership positions in the distribution of home and creditor insurance.

The principal focus of Scottish Widows Investment Partnership (SWIP) is the delivery of consistently superior investment performance. Pre-tax profits from SWIP for the year were £2 million compared with £10 million in 2001, the reduction in profitability being driven primarily by lower stockmarket levels and significant investment in new infrastructure to support future business growth. At the end of the year SWIP had £70 billion of funds under management, out of Groupwide funds under management totalling £98 billion. Overall fund management performance in 2002 showed a significant improvement. SWIP's largest UK equity fund, the UK Growth Fund, has achieved a top quartile performance within its sector over six and twelve months. This improvement in performance is also reflected in each of SWIP's mainstream, actively managed, UK equity funds which have all achieved top quartile performance, over a twelve month period, within their sector. In addition, SWIP now has a total of 14 funds rated A and above by Standard and Poor's. A number of new products have been launched during the year, most notably the SWIP Global Liquidity Fund, one of the largest sterling Institutional Money Market Funds, and the UK Balanced Property Trust, an innovative closed-end commercial property fund.

Financial review

Insurance and Investments (continued)

The Financial Services Authority has announced the abolition of the polarisation regime and the Group has been positioning itself to achieve competitive advantage in the new depolarised world. The Lloyds TSB Group has extensive interests in both the manufacture and distribution of long-term savings products. With Scottish Widows continuing to be the best recognised brand in the medium to long-term savings market and the actions already taken to improve choice by offering a range of externally managed funds alongside those offered by Scottish Widows Investment Partnership, the Group remains well placed to prosper in a depolarised world. In particular, Scottish Widows' unique multi-manager partnership with Frank Russell has been well received both in the IFA market and by our own customers.

Life, pensions and unit trusts	**2002 £m**	2001 £m
New business income	**398**	358
Existing business		
– expected return	**273**	307
– experience variances	**(1)**	37
– assumption changes and other items	**78**	95
– pension provisions	**(40)**	(70)
– Abbey Life endowment provision	**(165)**	–
	145	369
Investment earnings	**214**	247
Life and pensions distribution costs	**(283)**	(255)
	474	719
Unit trusts	**90**	141
Unit trust distribution costs	**(89)**	(100)
	1	41
Profit before tax*	**475**	760
New business margin (life and pensions)	**19.3%**	18.5%

* *excluding changes in economic assumptions and investment variance*

New business income increased by 11 per cent supported by a 7 per cent growth in weighted sales from life and pensions products, and an improved performance in the more profitable life products. The life and pensions new business margin, defined as new business income less distribution costs divided by weighted sales, increased to 19.3 per cent, from 18.5 per cent in 2001. The improvement largely arose from an improved product mix, particularly higher margin protection and regular premium life products. The new business margin improved in all distribution channels.

Profit before tax from existing business fell by 61 per cent to £145 million, reflecting the £135 million increase in provisions for redress to past purchasers of endowment and pension products, and a reduction of £55 million in benefits from experience variances and actuarial assumption changes, largely reflecting the implementation of revised actuarial mortality assumptions. The expected return from existing business, which reflects the unwinding of the long-term discount rate applied to the expected cash flows from the Group's portfolio of in-force business, decreased by £34 million, or 11 per cent, to £273 million. This reduction reflects the lower value of in-force business at the beginning of the year, caused by the effect of lower stockmarkets on annual management charges.

The Group has, along with other companies in the life assurance industry, been reviewing the past sales of certain endowment based and long-term savings products. As a result the Group has made a provision of £165 million to cover its liability for redress to policyholders in respect of past sales made, primarily in the late 1980s and early 1990s, by the Abbey Life salesforce prior to its disposal by the Group in February 2000. The adequacy of the provision for redress to past purchasers of pension policies has been reviewed as lower stockmarket levels have increased the expected remaining cost of redress. The Group has made a final provision for this purpose of £40 million. The Group is also carrying out, in conjunction with the regulator, an investigation into the appropriateness of sales of a stockmarket related investment product, the Extra Income & Growth Plan. This investigation is expected to be completed during 2003, when the Group will be in a position to estimate the financial effect.

Financial review

Insurance and Investments (continued)

General Insurance	2002 £m	2001 £m
Premium income from underwriting:		
Creditor	**107**	110
Home	**350**	281
Health	**44**	45
Re-insurance premiums	**(15)**	(8)
	486	428
Commissions from insurance broking:		
Creditor	**426**	323
Home	**44**	41
Health	**17**	22
Other	**160**	142
	647	528
Profit before tax*	**754**	651

**excluding investment variance*

Profit before tax, excluding investment variance, from our general insurance operations, comprising both underwriting and broking activities, rose by £103 million, or 16 per cent, to £754 million.

Total income increased to a record £1.1 billion. Premium income from underwriting increased by £58 million, or 14 per cent, largely as a result of higher home insurance income which increased by 25 per cent. Commissions from insurance broking increased by £119 million, or 23 per cent, largely as a result of higher levels of creditor insurance.

New business sales of 2.8 million products were 6 per cent higher than last year with home, creditor and motor business all growing strongly, particularly through direct channels (direct mail, telephone, affinity and internet) where sales grew by 11 per cent. Overall income from creditor insurance increased by 23 per cent, reflecting higher personal sector loan and credit card volumes and an improved personal lending penetration rate. Home insurance income increased by 22 per cent, with sales volumes increasing by 7 per cent to 1.2 million policies.

Claims were £55 million, or 32 per cent, higher at £229 million than in 2001. The overall claims ratio of 46 per cent was higher than in 2001 (40 per cent) largely as a result of increased property claims which reflected a 26 per cent growth in the home underwritten portfolio, and higher weather and flood related insurance claims.

As a leading distributor of general insurance products, Lloyds TSB now has over 9 million policies in force and we estimate that the Group is a UK market leader in the distribution of home and creditor insurance.

Financial review

Wholesale Markets

(banking, treasury, large value lease finance, long-term agricultural finance, share registration, venture capital, and other related services for major UK and multinational companies, banks and financial institutions, and medium-sized UK businesses; and Lloyds TSB Asset Finance)

	2002 £m	2001 £m
Net interest income	**1,158**	1,096
Other income	**975**	863
Total income	**2,133**	1,959
Operating expenses	**1,139**	937
Trading surplus	**994**	1,022
Provisions for bad and doubtful debts	**311**	155
Amounts written off fixed asset investments	**57**	15
Profit before tax	**626**	852
Efficiency ratio	**53.4%**	47.8%
Total assets (period-end)	**£89.1bn**	£79.4bn
Total risk-weighted assets (period-end)	**£52.9bn**	£45.4bn

Wholesale Markets pre-tax profit decreased by £226 million, or 27 per cent, to £626 million. The acquisitions during the year of First National Vehicle Holdings, Abbey National Vehicle Finance and the Dutton-Forshaw Group had a significant impact on the figures within Wholesale Markets. In 2002 these acquisitions contributed £101 million of income, and £102 million of operating expenses, including goodwill amortisation of £3 million, resulting in a loss before tax of £1 million. The acquisitions are expected to achieve substantial synergies in 2003 and beyond.

Net interest income increased by £62 million resulting primarily from asset growth. Other income increased by £112 million, as an increase in operating lease rentals of £111 million, largely as a result of the asset finance acquisitions, and a higher level of insurance commission and corporate banking fees, were offset by a reduction in the realisations of venture capital gains, after record gains in 2001. Operating expenses increased by £202 million of which £102 million reflected the asset finance acquisitions, and a further £33 million reflected an increase in operating lease depreciation.

The charge for provisions for bad and doubtful debts in Wholesale Markets increased by £156 million. The charge relating to the Group's corporate lending portfolio increased by £145 million largely as a result of provisions against the Group's loans and advances to certain large US corporate customers, which totalled some £100 million, and an increase in the provisions charge against the corporate lending portfolio, reflecting weak equity markets and the slowdown in economic activity in the UK. Amounts written off fixed asset investments increased by £42 million, as a result of a £21 million write-down relating to operating irregularities on one specific securitisation issue, and portfolio growth related write-downs in the Lloyds TSB Development Capital investment portfolio.

Assets grew by 12 per cent to £89 billion, an increase of £10 billion. Of this increase, some £5 billion resulted from a growth in debt securities, reflecting an increase in the Group's portfolio of asset backed securities, most of which were triple A rated, and £2.6 billion from an increase in customer lending. The Group's policy to grow its asset backed securities portfolio is conservative, only targeting high quality tranches of asset backed securities issues, concentrating on mainstream asset classes such as mortgages, credit cards, student loans and retail car loans. The portfolio allows the Group to provide a securitised asset funding service for its corporate clients and to participate in structured deals with a limited number of global financial institutions. The high level of recent growth in the portfolio largely reflects the development of the Group's capability in this market and, having now achieved a meaningful presence in the market, it is not intended that recent rates of portfolio growth will continue into 2003 and beyond.

Our Treasury operations had another good year, however, primarily as a result of less favourable trading conditions, pre-tax profits decreased by 16 per cent to £196 million, compared with a record £233 million in 2001. The Group's risk-based activity in the derivatives markets continues to remain largely focused on straight cash based products in support of our customers' transactions.

Lloyds TSB Leasing maintained its position as the largest 'big ticket' leasing company in the UK and continued to develop its position as an established provider of operating leases within its chosen market sectors. Pre-tax profits were £60 million compared to £67 million in 2001. At the end of the year, Lloyds TSB Registrars' registration market share of FTSE 100 companies was 57 per cent, and its market leadership in employee share administration services continued to strengthen, having achieved market leadership in the new Share Incentive Plan market. Lower transactional activity, however, led to a reduction in pre-tax profit to £48 million, from £54 million in 2001.

Financial review

Wholesale Markets (continued)

Lloyds TSB Development Capital achieved record levels of venture capital investment, however, in a difficult market for disposals, realisations of venture capital gains were £35 million lower than in 2001. During the year, Lloyds TSB Development Capital was named Private Equity House of the Year for 2001.

Pre-tax profits in Lloyds TSB Asset Finance, which incorporates the Group's asset finance and receivables finance businesses, were £86 million, compared with £87 million in 2001. Lloyds TSB Commercial Finance and Alex Lawrie Factors continued to expand their customer base, including a new venture in Germany through an agreement with Bertelsmann Finanz. In April 2002 Lloyds TSB Asset Finance acquired First National Vehicle Holdings and Abbey National Vehicle Finance, both previously wholly owned subsidiaries of Abbey National plc, for a provisional cash consideration of £47 million. The premium on acquisition was £86 million. The businesses have been combined with Lloyds TSB autolease to create the leader in the UK contract hire and fleet management markets. In December 2002, the Group also acquired the Dutton-Forshaw Group, one of the leading motor dealer groups in the UK with 38 franchised dealerships representing 14 manufacturers, for a cash consideration of £49 million. Our CarSelect and Cars4Staff initiatives continue to expand rapidly through a range of channels, supplying new and used cars to Group staff, customers, and employees of our corporate customers. Over 5,000 cars were supplied during 2002.

Financial review

International Banking

(banking and financial services overseas in three main areas: The Americas, New Zealand, and Europe and Offshore Banking)

	2002 £m	2001 £m
Net interest income	**745**	749
Other income	**374**	345
Total income	**1,119**	1,094
Operating expenses	**578**	586
Trading surplus	**541**	508
Provisions for bad and doubtful debts	**162**	183
Amounts written off fixed asset investments	**–**	7
	379	318
Profit on sale of Lloyds TSB Asset Management S.A.	**–**	39
Profit before tax	**379**	357
Efficiency ratio	**51.7%**	53.6%
Total assets (year-end)	**£21.8bn**	£21.4bn
Total risk-weighted assets (year-end)	**£14.3bn**	£13.2bn

International Banking pre-tax profit was £22 million, or 6 per cent, higher at £379 million compared with 2001, despite a profit in 2001 of £39 million from the sale of the Group's Brazilian fund management business.

Net interest income decreased by £4 million to £745 million as volume growth in New Zealand and Brazil was offset by the impact of adverse exchange rate movements. Other income increased by £29 million, or 8 per cent, to £374 million, as a result of profits on the sale and leaseback of premises totalling £32 million. Operating expenses reduced by £8 million as increased local currency costs in New Zealand, which supported higher business volumes, and in Argentina, were more than offset by favourable exchange rate movements. Provisions for bad and doubtful debts were £21 million lower, as a result of lower specific provisions in Losango, our consumer finance business in Brazil, largely reflecting exchange rate movements.

Pre-tax profits from The National Bank of New Zealand increased by 32 per cent to £218 million as a result of asset growth across all business sectors, growth in the number of personal customers and higher levels of retail deposits and residential mortgages. Our consumer finance business in Brazil, Losango Consumer Finance, performed well, notwithstanding difficult local economic circumstances, and increased pre-tax profits on a local currency basis by 14 per cent. After the impact of adverse exchange rate movements, which were partly hedged, Losango made a pre-tax profit of £40 million, compared with £43 million in 2001.

The Group's offshore banking operations increased their pre-tax profit by £3 million to £123 million. In Europe Private Banking, pre-tax profits were £24 million, compared to £20 million in 2001.

Since the October presidential election in Brazil the economic situation has somewhat stabilised. The Group reduced its total exposure to Brazil, net of provisions, to £1.9 billion during 2002 (December 2001: £3.3 billion), largely from not replacing maturing Government bonds. Economic activity in Brazil has remained reasonably robust, and we believe this relative strength in the local economy, in conjunction with the significant International Monetary Fund support package which the newly elected president and incoming government have indicated they will support, should alleviate current concerns about the Brazilian economy. The economic situation in Argentina continues to be difficult and the outlook is likely to remain uncertain at least until after the new Argentine government takes office during 2003. In 2002 the Group increased its general provision relating to its exposure to Argentina by £50 million. The Group's total exposure to Argentina at the end of the year was reduced to some £190 million net of provisions and charges, compared to £610 million at the end of 2001. The Group has now provided for some 50 per cent of its total exposure to Argentina.

In October 2001, the Group sold its Brazilian fund management and private banking business, including its subsidiary Lloyds TSB Asset Management S.A., to Banco Itaú S.A., resulting in a profit on sale of £39 million.

Financial review

Central group items

(earnings on surplus capital and the emerging markets debt investment portfolio, central costs and other unallocated items)

	2002 £m	2001 £m
Accrual for payment to Lloyds TSB Foundations	**(33)**	(36)
Other finance income	**165**	307
Pension scheme benefit augmentations	**–**	(82)
Earnings on surplus capital and the emerging markets debt investment portfolio	**2**	63
Abbey National offer costs	**–**	(16)
Central costs and other unallocated items	**(38)**	(51)
	96	185

The four independent Lloyds TSB Foundations support registered charities throughout the UK that enable people, particularly disabled and disadvantaged people, to play a fuller role in society. The Foundations receive 1 per cent of the Group's pre-tax profit, averaged over three years, instead of the dividend on their shareholdings. In 2003 they will receive £33 million (2002: £36 million) to distribute to charities, making them in aggregate the largest independent grant giving body in the UK.

Other finance income represents income from the expected return on the Group's pension fund assets less the charge for unwinding the discount on the pension fund liabilities. The significant reduction in income in 2002 reflects the combined impact of a reduction in the expected return on lower pension scheme assets as a result of the continuing weakness in global equity markets, and increased pension fund liabilities caused by the expected greater lifespan of pension scheme members.

Earnings on surplus capital and the emerging markets debt investment portfolio largely reflect earnings on capital held at the Group centre, less the funding cost of Scottish Widows, and profits from the Group's investment portfolio of, largely, emerging markets debt securities. During the year the Group accelerated its disposal programme for these investments as a result of concerns over credit and liquidity risks, particularly in Latin America. Given the higher level of disposals the Group has decided to mark the portfolio to market in 2002 and in future reporting periods. This change had no profit impact in 2002. The Group does not expect to achieve similar levels of emerging markets debt portfolio contributions, which in 2002 totalled £103 million, in 2003 and beyond.

Net interest income

	2002	2001
Group:		
Net interest income £m	**5,171**	4,922
Average interest-earning assets £m	**161,818**	144,945
Gross yield on interest-earning assets %	**6.52**	7.84
Interest spread %	**2.94**	3.00
Net interest margin %	**3.20**	3.40
Domestic:		
Net interest income £m	**4,425**	4,202
Average interest-earning assets £m	**134,902**	121,244
Gross yield on interest-earning assets %	**6.10**	7.38
Interest spread %	**3.08**	3.11
Net interest margin %	**3.28**	3.47
International:		
Net interest income £m	**746**	720
Average interest-earning assets £m	**26,916**	23,701
Gross yield on interest-earning assets %	**8.63**	10.19
Interest spread %	**2.12**	2.43
Net interest margin %	**2.77**	3.04

Notes:
a) Gross yield is the rate of interest earned on average interest-earning assets.
b) Interest spread is the difference between the rate of interest earned on average interest-earning assets and the rate of interest paid on average interest-bearing liabilities.
c) Net interest margin is net interest income as a percentage of average interest-earning assets.
d) The analysis of net interest income by domestic and international operations shown above is based on the location of the office recording the transaction, except for lending by the international business booked in London.

Net interest income (continued)

Group net interest income increased by £249 million, or 5 per cent, to £5,171 million, despite a reduction of £290 million caused by a 20 basis point reduction in the net interest margin. Average interest-earning assets increased by 12 per cent to £162 billion. The 20 basis points decrease in the overall net interest margin, to 3.20 per cent, reflected a lower contribution from interest-free liabilities, caused by the lower average interest rates, the continuing shift in the mix of average interest-earning assets towards high quality, but finer margin, corporate and wholesale lending, and the impact of adverse exchange rate movements on our higher margin Latin American businesses, which led to a 27 basis point reduction in the international net interest margin. The interest spread reduced by 6 basis points.

Domestic net interest income increased by £223 million, or 5 per cent, to £4,425 million, notwithstanding a reduction of £226 million caused by a 19 basis point reduction in the net interest margin. This represents 86 per cent of total group net interest income. Average interest-earning assets increased by £13.7 billion, or 11 per cent to £134.9 billion. Average personal lending and mortgage balances grew by £6.7 billion and wholesale balances increased by £7.2 billion. The net interest margin decreased by 19 basis points reflecting a reduction in the contribution of interest-free liabilities and the continuing shift in the mix of average interest-earning assets towards high quality, but finer margin, corporate and wholesale lending. In UK Retail Banking and Mortgages there was a 4 basis point decrease in the net interest margin as continued gradual erosion of the mortgage margin was partly offset by a shift in the mix of retail business growth towards personal lending and credit cards. In Wholesale Markets there was an 18 basis point reduction caused by further growth in finer margin corporate lending. The interest spread reduced by only 3 basis points.

Net interest income from international operations increased by £26 million, or 4 per cent, to £746 million. This represents 14 per cent of total group net interest income. Strong volume growth, particularly in New Zealand, was offset by the adverse effect of exchange rate movements. Average interest-earning assets on a local currency basis increased by 16 per cent but again this was partly offset by the adverse effect of exchange rate movements. The net interest margin reduced by 27 basis points as a result of lower margins in our Latin American businesses. In particular, the effect of adverse exchange rate movements had a significant impact on the contribution to the interest margin from our higher margin businesses in Brazil.

Other income

	2002 £m	2001 £m
Fees and commissions receivable:		
UK current account fees	**579**	573
Other UK fees and commissions	**1,163**	1,220
Insurance broking	**647**	528
Card services	**414**	332
International fees and commissions	**250**	269
	3,053	2,922
Fees and commissions payable	**(645)**	(602)
Dealing profits (before expenses):		
Foreign exchange trading income	**173**	158
Securities and other gains	**15**	75
	188	233
Income from long-term assurance business	**(303)**	(29)
General insurance premium income	**486**	428
Other operating income	**763**	708
Total other income	**3,542**	3,660

Other income decreased by £118 million, or 3 per cent, to £3,542 million, partly as a result of a £38 million reduction in income from the combined effect of changes in economic assumptions and the higher negative investment variance.

Fees and commissions receivable increased by 4 per cent to £3,053 million, largely reflecting strong growth in income from insurance broking and card services. Other UK fees and commissions decreased by £57 million, or 5 per cent, from £1,220 million to £1,163 million as a result of a £59 million reduction in unit trust and asset management fees, which reflected the impact of the continued fall in the level of stockmarkets during 2002. There was also a £20 million increase in fees from large corporate and factoring activity reflecting increased transaction volumes.

Other income (continued)

Insurance broking commission income increased by £119 million, compared with 2001, with continued strong growth in creditor insurance products. Income from credit and debit card services increased by £82 million, mainly as a result of higher merchant service charges and fees. UK current account fee income rose by £6 million, reversing the downward trend experienced in recent years; a £37 million increase in fee income from added value current accounts more than offset a reduction in service charges and unauthorised borrowing and other fees.

Fees and commissions payable increased by £43 million against last year as a result of higher reciprocity fees and an increase in package costs relating to a number of products.

Dealing profits decreased by £45 million compared with 2001 as a result of a reduction of £60 million in gains from securities trading. Income from long-term assurance business decreased by £274 million however, excluding changes in economic assumptions, investment variance and the impact of a £135 million increase in provisions for redress to past purchasers of endowment and pension products, it was £115 million lower, partly reflecting a reduction of £55 million in benefits from experience variances and actuarial assumption changes.

Other operating income increased by £55 million to £763 million. Increases of £25 million in earnings on the sale and restructuring of emerging markets debt investments and £111 million in operating lease rentals, largely as a result of the acquisition of First National Vehicle Holdings and Abbey National Vehicle Finance, were partly offset by a £35 million reduction in the realisation of venture capital gains by Lloyds TSB Development Capital and a reduction of £25 million in profits on the sale and leaseback of premises.

Operating expenses

	2002 £m	2001 £m
Administrative expenses		
Staff:		
Salaries and profit sharing	**1,758**	1,776
National insurance	**134**	140
Pensions	**318**	347
Restructuring	**105**	69
Other staff costs	**202**	221
	2,517	2,553
Premises and equipment:		
Rent and rates	**280**	261
Hire of equipment	**18**	18
Repairs and maintenance	**131**	115
Other	**114**	123
	543	517
Other expenses:		
Communications and external data processing	**446**	483
Advertising and promotion	**147**	154
Professional fees	**113**	110
Other	**448**	409
	1,154	1,156
Administrative expenses	**4,214**	4,226
Depreciation	**642**	511
Amortisation of goodwill	**59**	39
Total operating expenses	**4,915**	4,776
Efficiency ratio	**55.4%**	53.7%
Efficiency ratio, excluding changes in economic assumptions and investment variance	**50.3%**	49.0%

Total operating expenses increased by £139 million, or 3 per cent, compared with 2001. Excluding the impact of acquisitions and operating lease depreciation, operating expenses were flat.

Administrative expenses decreased by £12 million to £4,214 million. Staff costs fell by £36 million to £2,517 million and other expenses decreased by £2 million to £1,154 million. Depreciation rose by £131 million, reflecting an increase of £95 million in operating lease depreciation. Goodwill amortisation was £20 million higher. The efficiency ratio, excluding changes in economic assumptions and investment variance, was 50.3 per cent, compared to 49.0 per cent in 2001.

Financial review

Efficiency programme

In February 2000 the Group announced the commencement of a substantial medium-term efficiency programme to improve the Group's overall efficiency, to maintain our continuing focus on operating costs and to support increasing levels of investment in the Group's businesses. The efficiency programme has been a major contributing factor to the net reduction in Group staff numbers of 4,191, after adjusting for an additional 2,328 staff following a number of acquisitions, against the targeted net reduction in staff numbers of 3,000 by the end of 2002.

The Group remains committed to strict cost control and, largely as a result of the continuing efficiency initiatives, we expect that the Group's operating expenses in 2003, excluding the impact of acquisitions and operating lease depreciation, will grow by no more than the rate of inflation. This focus on cost control will be continued notwithstanding further significant investment throughout the business in 2003, to support increased business volumes, further improvements in productivity, and increases in investment in mandatory projects. These include projects such as the Universal Banking Service, anti-money laundering financial crimes programmes, and preparation for the forthcoming introduction of the Basel 2 capital accord.

Number of employees (full-time equivalent)

Staff numbers decreased by 1,863 to 79,537 during the year, notwithstanding an increase of 2,328 from acquisitions made during the year. Excluding the impact of acquisitions, staff numbers decreased by 4,191. This is significantly in excess of the targeted net reduction of 3,000 staff.

Within UK Retail Banking staff numbers decreased by 3,513 as increases from planned improvements to customer service and a substantial increase in our branch sales activities have been more than offset by reductions of staff numbers in back office operations as part of the Group's efficiency programme. In Wholesale Markets staff numbers increased by 2,151 as a result of the asset finance acquisitions, but reduced by 114 on an underlying basis. In International Banking staff numbers decreased by 466.

	31 December 2002	31 December 2001
UK Retail Banking*	**44,184**	47,697
Mortgages	**3,711**	3,527
Insurance and Investments	**6,170**	6,316
Wholesale Markets	**11,385**	9,234
International Banking	**11,788**	12,254
Other	**2,299**	2,372
Total number of employees (full-time equivalent)	**79,537**	81,400

* *although the costs of distributing mortgages and insurance through the Lloyds TSB network are allocated to the mortgage and insurance businesses, the number of employees involved in these activities in the network is included under UK Retail Banking*

Financial review

Charge for bad and doubtful debts

	2002 £m	2001 £m
UK Retail Banking	**564**	439
Mortgages	**(1)**	(24)
Wholesale Markets	**311**	155
International Banking	**162**	183
Central group items	**(7)**	(6)
Total charge	**1,029**	747
Specific provisions	**965**	736
General provisions	**64**	11
Total charge	**1,029**	747
	%	%
Charge as % of average lending:		
Domestic	**0.70**	0.54
International	**1.28**	1.10
Total charge	**0.77**	0.62

The total charge for bad and doubtful debts increased to £1,029 million from £747 million. In UK Retail Banking the provisions charge increased by £125 million, from £439 million in 2001, to £564 million, as a result of volume related asset growth in the personal loan and credit card portfolios and a lower level of recoveries and releases. In Wholesale Markets the provisions charge increased by £156 million to £311 million from £155 million in 2001. Provisions against the Group's exposure to certain large US corporate customers totalled some £100 million, and there was also an increase in the provision charge from the corporate lending portfolio, reflecting weak equity markets and the slowdown in economic activity in the UK. In International Banking provisions decreased by £21 million as a result of lower specific provisions in Losango, largely reflecting exchange rate movements. There was also an increase of £64 million in the Group's overall general provision reflecting a £50 million general provision charge relating to the Group's exposure to Argentina, and a more cautious outlook following the slowdown in economic growth in the UK.

Non-performing loans increased to £1,414 million compared with £1,222 million in December 2001, largely reflecting higher levels of non-performing lending in the Group's corporate portfolio and general portfolio growth throughout the Group. In UK Retail Banking and Mortgages the overall arrears position remained stable. An improved position in personal lending and mortgages was offset by a slight deterioration in the credit card portfolio, largely reflecting the slowdown in economic growth in the UK. Non-performing lending represented 1.0 per cent of total lending, compared with 1.0 per cent in December 2001. Our lending portfolio remains heavily influenced by our high quality, relatively low risk, mortgage business and, as a result, we remain relatively well positioned to withstand any continued economic slowdown.

Total provisions for bad and doubtful debts

Closing provisions as % of lending (excluding unapplied interest)	31 December 2002 £m	31 December 2002 %	31 December 2001 £m	31 December 2001 %
Specific:				
– Domestic	**1,016**	**(0.8)**	848	(0.8)
– International	**318**	**(1.7)**	251	(1.5)
	1,334	**(1.0)**	1,099	(0.9)
General	**433**	**(0.3)**	369	(0.3)
	1,767	**(1.3)**	1,468	(1.2)

At the end of December 2002 provisions for bad and doubtful debts totalled £1,767 million. This represented 1.3 per cent of total lending (December 2001: 1.2 per cent). Non-performing lending increased to £1,414 million from £1,222 million in December 2001, largely reflecting higher levels of non-performing lending in the Group's corporate portfolio, and general portfolio growth throughout the Group. At the end of the year, total provisions represented over 120 per cent of non-performing loans (December 2001: 120 per cent).

Capital ratios

	31 December 2002 £m	31 December 2001 £m
Capital: tier 1	**9,490**	8,408
: tier 2	**8,846**	7,831
	18,336	16,239
Supervisory deductions	**(6,588)**	(6,752)
Total capital	**11,748**	9,487
	£bn	£bn
Risk-weighted assets:		
UK Retail Banking	**22.7**	19.6
Mortgages	**31.5**	28.7
UK Retail Banking and Mortgages	**54.2**	48.3
Insurance and Investments	**0.2**	0.2
Wholesale Markets	**52.9**	45.4
International Banking	**14.3**	13.2
Central group items	**0.8**	0.8
Total risk-weighted assets	**122.4**	107.9
Risk asset ratios: total capital	**9.6%**	8.8%
: tier 1	**7.8%**	7.8%
Post-tax return on average risk-weighted assets	**1.61%**	2.26%

Notes:
a) Tier 1 capital comprises mainly shareholders' funds, tier 1 capital instruments and minority interests.
b) Tier 2 capital comprises loan capital and the general provision for bad and doubtful debts.
c) Supervisory deductions comprise mainly the investment in the insurance businesses.

At the end of December 2002 the risk asset ratios were 9.6 per cent for total capital and 7.8 per cent for tier 1 capital.

During 2002, total capital for regulatory purposes increased by £2,261 million to £11,748 million. Tier 1 capital increased by £1,082 million, mainly from the issue of new tier 1 capital instruments. The total amount of embedded value earnings contained within the Group's tier 1 capital is now some £2.2 billion. Tier 2 capital increased by £1,015 million and supervisory deductions decreased by £164 million, as a result of a decrease in the Group's embedded value to £6,228 million, from £6,366 million in December 2001.

Risk-weighted assets increased by 13 per cent to £122.4 billion and the post-tax return on average risk-weighted assets decreased to 1.61 per cent.

Tax

The effective rate of tax was 29.3 per cent (2001: 27.7 per cent). The lower effective rate of tax, compared with the standard tax rate of 30 per cent, is largely due to tax relief on payments to the QUEST to satisfy Save As You Earn options, non taxable gains on disposals of properties sheltered by capital losses, and tier 1 capital interest payments, partly offset by a higher effective rate of tax in the Group's life and pensions businesses in 2002 (see note 8b, page 70).

Free asset ratio

The free asset ratio is a common measure of financial strength in the UK for long-term insurance businesses. It is the ratio of assets less liabilities (including actuarial reserves but before the required regulatory minimum solvency margin) expressed as a percentage of the liabilities. It is derived from annual insurance returns which are due to be completed in March 2003, and have yet to be finalised. However, based on current expectations, at 31 December 2002 the free asset ratio for Scottish Widows plc was an estimated 10.0 per cent, compared with 11.5 per cent at 31 December 2001. This free asset ratio included some £400 million allowance for future profits (December 2001: nil). After adjusting for the inclusion of the required regulatory minimum solvency margin within liabilities, the Scottish Widows plc ratio was an estimated 5.5 per cent at 31 December 2002, compared with 6.6 per cent at 31 December 2001.

Financial review

Economic profit

In pursuit of our aim to maximise shareholder value, we use a system of value based management as a framework to identify and measure value in order to help us make better business decisions. Accounting profit is of limited use as a measure of value creation and performance as it ignores the cost of the equity capital that has to be invested to generate the profit. We choose economic profit as a measure of performance because it captures both growth in investment and return. Economic profit represents the difference between the earnings on the equity invested in a business and the cost of the equity. Our calculation of economic profit uses average equity for the year and is based on a cost of equity of 9 per cent (2001: 9 per cent).

Economic profit instils a rigorous financial discipline in determining investment decisions throughout the Group. It enables us to evaluate alternative strategies objectively, with a clear understanding of the value created by each strategy, and then to select the strategy which creates the greatest value.

	2002 £m	2001 £m
Average shareholders' equity	**10,672**	12,338
Profit attributable to shareholders	**1,781**	2,229
Less: notional charge	**(960)**	(1,110)
Economic profit	**821**	1,119

The notional charge has been calculated by multiplying average shareholders' equity by the cost of equity.

Investment variance

In accordance with generally accepted accounting practice in the UK, it is the Group's accounting policy to carry the investments comprising the reserves held by its life companies at market value. The reserves held to support the with-profits business of Scottish Widows are substantial and changes in market values will result in significant volatility in the Group's embedded value earnings, which is beyond the control of management. Consequently, in order to provide a clearer representation of the underlying performance, the results of the life and pensions business are separately analysed to include investment earnings calculated using longer-term investment rates of return, and annual management charges based on unsmoothed fund values. This investment variance represents the difference between the actual investment return in the year on investments backing shareholder funds and the expected return based upon the economic assumptions made at the beginning of the year, and the effect of these fluctuations on the value of in-force business. The effects of other changes in economic circumstances beyond the control of management are also reflected in the investment variance.

The longer-term rates of return for the period are consistent with those used by the Group in the calculation of the embedded value at the beginning of the period, which were 8 per cent for equities and 5.25 per cent for gilts. Following changes in economic assumptions made at the end of 2002 the longer-term rates of return for 2003 have been revised to 7.10 per cent for equities and 4.50 per cent for gilts.

Lloyds TSB General Insurance also holds investments to support its underwriting business; these are carried at market value and gains and losses included within dealing profits. Consistent with the approach adopted for the life and pensions business, an operating profit for the general insurance business is calculated including investment earnings normalised using the same long-term rates of return.

During 2002 the FTSE All-Share index fell by 24 per cent and this created an adverse investment variance totalling £952 million. This adverse variance should not represent a permanent impairment to the value of the Group's reserves which fluctuate as stockmarket values fluctuate.

Financial review

Income and expenses reconciliations

To facilitate comparison of results, certain key financial information and commentaries have been considered excluding changes in economic assumptions, investment variance, pension and endowment provisions, the impact of investment returns of the Group's pension scheme assets, operating lease depreciation, and the impact of acquisitions. Reconciliations are detailed below.

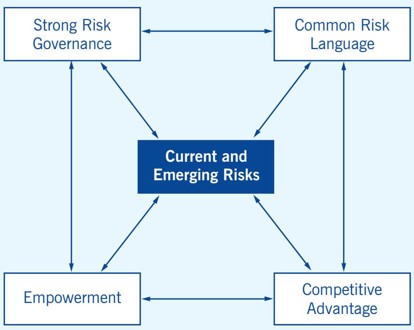
	2002 £m	2001 £m
Income, excluding changes in economic assumptions, investment variance, pension and endowment provisions, the impact of investment returns on the Group's pension scheme assets, operating lease depreciation and the impact of acquisitions	**9,484**	9,314
Changes in economic assumptions	**55**	–
Investment variance	**(952)**	(859)
Pension and endowment provisions	**(205)**	(70)
Other finance income	**165**	307
Netting of operating lease depreciation	**230**	197
Acquisitions	**101**	–
Total income	**8,878**	8,889

	2002 £m	2001 £m
Expenses, excluding operating lease depreciation and the impact of acquisitions	**4,580**	4,579
Netting of operating lease depreciation	**230**	197
Acquisitions	**105**	–
Total operating expenses	**4,915**	4,776

Enterprise-wide risk management

Lloyds TSB has adopted an enterprise-wide framework for the identification, assessment and management of risk, designed to meet its customers' needs and maximise shareholder value by aligning risk management with the corporate strategy; assessing the impact of emerging risks from new technologies or markets; and developing risk tolerances and mitigating strategies.

Enterprise-wide risk management (EWRM) is founded on four principal concepts: strong risk governance; empowerment; competitive advantage and common risk language.



Strong risk governance

The risk governance structure is designed to create a risk-aware culture in which the nature and size of risks are well understood, and business decisions strike a balance between risk and reward which is consistent with the Group's risk appetite, whilst maximising shareholder value. The governance structure is based on the following elements:

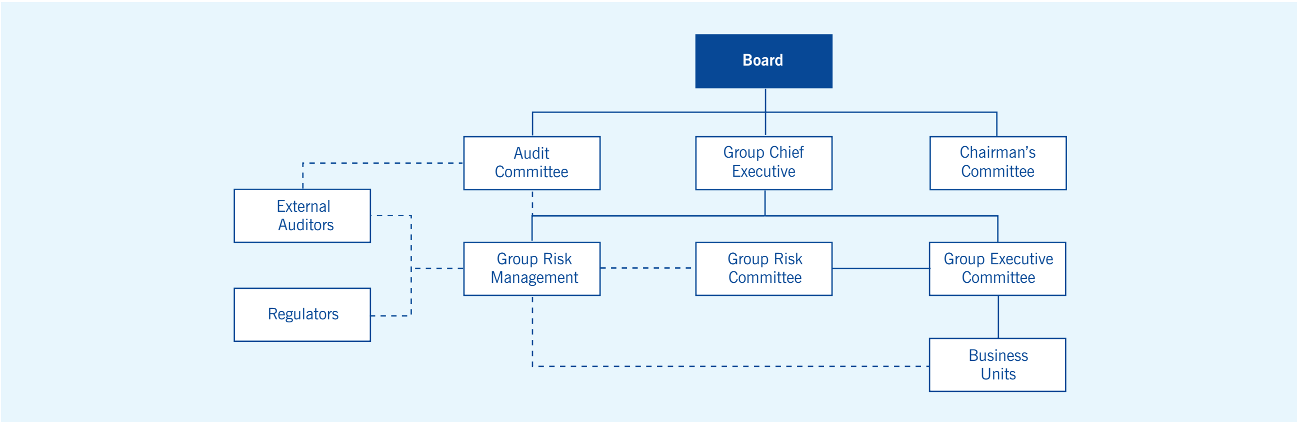
The Board is responsible for determining the long-term strategy of the business, the markets in which the Group will operate and the level of risk acceptable to the Group in each area of its business. As explained on page 55, it is assisted in this by the Chairman's Committee and the Audit Committee.

The Group Executive Committee is responsible to the Group Chief Executive for the development and implementation of strategy, operational plans, policies and budgets. It monitors operating and financial performance, assesses and controls risk, and prioritises and allocates resources.

The Group Risk Committee is responsible to the Group Executive Committee for protecting shareholder value through assessment and control of the high level risks assumed by the Group; approving the Group's high level policies; ensuring that the necessary culture, practices and systems are in place to enable the Group to meet its internal and external obligations; and reviewing the allocation and deployment of capital at risk, taking into account the Group's risk appetite.

The Director of Group Risk Management is responsible for the implementation of risk policy and the provision of independent assurance to the Audit Committee and Board, who receive regular reports on risk issues prepared by Group Risk Management. The Director of Group Risk Management reports to the Group Chief Executive and has access to the Chairman and members of senior management; he is also a member of the Group Risk Committee.

These relationships are illustrated in the following diagram:



Empowerment

The directors of the Group's business units have primary responsibility for measuring, monitoring and controlling risks within their areas of accountability. They are empowered to establish control frameworks for their businesses that are consistent with the Group's high level policies and within parameters set by Group Risk Management.

Competitive advantage

The EWRM model strengthens the Group's ability to identify and assess risks; aggregate risks and define the corporate risk appetite; develop solutions for reducing or transferring risk, where appropriate; and exploit risks to gain competitive advantage, thereby increasing shareholder value.

Common risk language

The Group has adopted a risk language in which all risks are classified by one or more of the following 11 Risk Drivers:

The Group's high level policy and reporting to the Group Risk Committee, Audit Committee and Board have been aligned to the Risk Drivers. Roll-out of the risk language to the business has commenced and will be completed during 2003, ensuring a consistent approach to classifying and describing risks.

1 Governance, people and organisation

Definition

The risk of loss from poor corporate governance at Group and business unit level, sub-optimal organisational structuring, or failure to recruit, manage and retain appropriate skilled staff to achieve business objectives.

Group Policy Manual

The Group's policy for managing Governance, People and Organisation risk is set out in the Group Policy Manual, which is approved by the Group Risk Committee. The salient elements of the policy are summarised below.

Governance and Organisation

The Group's governance and organisation policy is to:

– Organise itself into three principal business units (UK Retail Banking and Mortgages, Wholesale and International Banking, and Insurance and Investments) with a centralised IT and operational support function (Group IT and Operations). These units are run in a manner consistent with strategic direction from the Board, tight financial and operating controls and the prudent management of risk.
– Develop and maintain a strong risk management and control culture across all businesses.
– Follow industry best practice on corporate governance, and conduct business with integrity, due skill, care and diligence.

Management of Risks

The Group sets high standards for the conduct of its business and values its reputation. Responsibility for establishing an effective organisational structure is vested in Group and business unit management. Sound internal risk management practices are promoted through business unit directors who are responsible for identifying, measuring, monitoring and controlling the risks within their specific areas of accountability.

The Group seeks to identify and classify risks in a timely manner. The likelihood of risks crystallising and the significance of the consequent impact on the business, the Group and its customers are evaluated. The Group's business control environment ensures effective and efficient operational management; reliability, integrity and consistency of financial and other reporting; and compliance with governing laws and regulations. Business unit directors ensure that material risks are reported to the relevant Group Executive Director and to Group Risk Management.

Information and Communication

The Board and senior management at both Group and business unit level receive relevant, reliable and timely management information in line with business objectives to ensure that activities are appropriately controlled, key risks are identified and monitored, decisions are implemented and regulatory obligations are met.

1 Governance, people and organisation (continued)

Audit Responsibilities and Rights

Group Audit independently reviews adherence to the policies and processes that make up the control environment, disseminating best practices throughout the Group in the course of its monitoring and corrective action activities. The Group Audit Director meets regularly with the Group Chief Executive and periodically with the Audit Committee.

People

The Group's approach to people management is to employ skilled, committed staff, working as a team for the benefit of customers and shareholders, who are given the opportunity to fulfil their potential; employ the highest ethical standards of behaviour and best practice management principles; and recruit on the basis of ability and competence.

Standards of Behaviour

The Group seeks to ensure that its employees act with integrity and seek to deliver high levels of customer service. It promotes a working environment free from discrimination, harassment, bullying or victimisation of any kind. Employees are encouraged and expected to alert management to suspected misconduct, fraud or other serious malpractice.

Performance and Reward Management

The Group seeks to:

- Ensure that all employees understand their role, the purpose of the role and where it fits into the wider team and organisational context.
- Manage and measure employees' performance and contribution to collective goals.
- Recognise the contribution of individuals in the context of the pay market and the performance of the business in which they work, and reward appropriately.

Training and Development

The Group believes that:

- Long term success depends on the quality and skills of its staff.
- It has a joint responsibility with employees for their personal and career development to improve current performance and to enhance future prospects.

2 Strategy risk

Definition

The risk arising from the adoption of the Group's agreed strategy and its implementation at corporate or business unit level.

Processes

The Group's governing objective is to maximise value for its shareholders by:

- Being first choice for its customers.
- Being a leader in its chosen markets.
- Driving down day-to-day costs to facilitate investment.

The risks arising from the adoption of the Group's strategy at corporate and business unit level are managed by a number of processes.

A common approach is applied across the Group to assess the creation of shareholder value. This is measured by Economic Profit (the profit attributable to shareholders, less a notional charge for the equity invested in the business). The focus on Economic Profit allows the Group to compare the returns being made on capital employed in each business.

The use of risk-based economic capital and regulatory capital is closely monitored at business unit and Group level. The Group's equity attribution model covers credit, market, insurance, business and operational risks.

A rigorous annual strategic planning process is conducted at Group and business unit level and includes a quantitative and qualitative assessment of the risks in the Group plan.

The Group's strategy and those of its constituent business units are reviewed and approved by the Board. Regular reports are provided to the Group Executive Committee and the Board on the progress of the Group's key strategies and plans.

2 Strategy risk (continued)

Revenue and capital investment decisions require additional formal assessment and approval. Formal risk assessment is conducted as part of the financial approval process.

Company mergers and acquisitions require specific approval by the Board. In addition to the standard due diligence conducted during a merger or acquisition, Group Risk Management conducts an independent risk assessment of the target company and its proposed integration into the Group.

3 Credit risk

Definition

The risk of loss arising from counterparty default subsequent to the provision of credit facilities (both on- and off-balance sheet).

Measurement

The Group has dedicated standards, policies and procedures to control and monitor credit and related risks. Examples of the way in which such risks are measured include:

Group Rating System – all business units are required to operate an authorised rating system that complies with the Group's standard methodology. The Group uses a 'Master Scale' rating structure with ratings corresponding to a range of probability of future default.

Portfolio Analysis – in conjunction with Group Risk Management, Group businesses identify and define portfolios of credit and related risk exposures and the key benchmarks, behaviours and characteristics by which those portfolios are managed in terms of credit risk exposure. This entails the production and analysis of regular portfolio monitoring reports for review by Group Risk Management.

To further enhance the ability to measure and predict future risk, the Group continues to develop new policies and risk management systems.

Limits

A number of tools, including Group-level credit policy where appropriate, are used to control the Group's exposure to undue levels of credit risk:

Counterparty Limits – exposure to individual counterparties, groups of counterparties or customer risk segments is controlled through a tiered hierarchy of delegated sanctioning authorities. Approval requirements for each decision are based on the transaction amount, the customer's aggregate facilities, credit risk ratings and the nature and term of the risk. Regular reports on significant credit exposures are provided to the Group Executive Committee and Board.

Bank Exposures – an in-house proprietary rating system is used to approve bank facilities, which are sanctioned on a Group-wide basis.

Cross-border Exposures – country limits are authorised and managed by a dedicated unit, using an in-house rating system, which takes into account economic and political factors.

Concentration Risk – formulation of concentration limits on certain industries and sectors. Group Risk Management sets Sector Caps that reflect risk appetite, and monitors exposures to prevent excessive concentration of risk.

Credit Risk Arising from the Use of Derivatives – note 46 on page 87 shows the total notional principal amount of interest rate, exchange rate and equity contracts outstanding at 31 December 2002. The notional principal amount does not, however, represent the Group's real exposure to credit risk, which is limited to the current cost of replacing contracts with a positive value to the Group, should the counterparty default. This replacement cost is also shown in note 46. To reduce credit risk the Group uses a variety of credit enhancement techniques such as netting and collateralisation, where security is provided against the exposure.

Credit Derivatives – these are a method of transferring credit risk from one counterparty to another and of managing exposure to selected counterparties. Credit derivatives include credit swaps, credit spread options and credit linked notes. Lloyds TSB has limited exposure to such instruments.

3 Credit risk (continued)

Processes

The processes by which Group Risk Management discharges its responsibilities in respect of credit risk include the following:

– Formulation of high-level credit policies designed to ensure a balanced and managed approach to the identification and mitigation of credit risk.
– Provision of lending guidelines. These define the responsibilities for lending officers and provide a disciplined and focused benchmark for credit decisions.
– Establishment and maintenance of the Group's Large Exposure and Provisioning policies, in accordance with regulatory reporting requirements.
– Monitoring of scorecards. The Group utilises statistically-based decisioning techniques (primarily credit scoring and performance scoring) for its principal consumer lending portfolios. Group Risk Management reviews and monitors new and material changes to scorecards.
– Maintenance of a facilities database. Group Risk Management operates a centralised database of large corporate, sovereign and bank facilities designed to ensure a consistent aggregation policy is maintained throughout the Group.
– Monitoring and controlling residual value risk exposure. The Group's appetite for such exposure is communicated to the business by a series of time referenced Sector Caps, ensuring an acceptable distribution of future risk.
– Communication and provision of general guidance on all credit-related risk issues, including regulatory changes and environmental risk policy, to promote consistent and best practice throughout the Group.

Day-to-day credit management and asset quality within each business unit is the primary responsibility of the relevant business unit director. Such responsibility is fulfilled by:

– Each business unit having in place established credit processes which are consistent with the corresponding Group policies.
– Authority to delegate lending authorities within business units resting with officers holding divisional delegated lending authority. All material authorities are advised to Group Risk Management.
– Specialist units established within Group businesses to provide, for example: intensive management and control; security perfection, maintenance and retention; expertise in documentation for lending and associated products; sector-specific expertise; and legal services applicable to the particular market place and product range offered by the business unit.

4 Market risk

Definition

The risk of loss arising from unexpected changes in financial prices, including interest rates, exchange rates, bond, equity and commodity prices.

The Group's banking activities expose it to the risk of adverse movements in interest rates or exchange rates, with little or no exposure to equity or commodity risk. The Group's insurance activities also expose it to market risk (see 'Insurance Risk' below).

Measurement

Measurement Techniques – a variety of techniques are used to quantify the market risk arising from the Group's banking and trading activities. These reflect the nature of the business activity, and include simple interest rate gapping, open exchange positions, sensitivity analysis and Value at Risk (VaR). Stress testing and scenario analysis are also used in certain portfolios, and at Group level, to simulate extreme conditions to supplement these core measures.

Trading Portfolios – market risk within the Group's trading portfolios is calculated using various parameters to calculate the VaR on a given trading portfolio of positions, thus avoiding undue reliance on a single measure. Based on the commonly-quoted 95 per cent confidence level, assuming positions are held overnight and using observation periods with greater emphasis given to more recent data, during 2002 the VaR on the Group's global trading averaged £1.26 million (2001: £1.17 million) with a maximum of £2.07 million (2001: £1.62 million) and a minimum of £0.93 million (2001: £0.78 million). The figure at 31 December 2002 was £1.02 million (2001: £1.62 million).

Non-trading Portfolios – interest rate risk within the Group's non-trading exposure is summarised in the form of an interest rate repricing table, as set out on page 89. Items are allocated to time bands by reference to the earlier of the next contractual interest rate repricing date and the maturity date. However, the table does not take into account the effect of interest rate options used by the Group to hedge its exposure.

Structural Foreign Exchange Risk – this arises from the Group's investments in its overseas operations. The structural position is managed after having regard to the currency composition of the Group's risk-weighted assets, the objective being to limit the effect of exchange rate movements on the risk asset ratio. The Group's structural position at 31 December 2002 is set out on page 90 in note 46d. The position implies that a hypothetical increase of 10 per cent in the value of sterling against all other currencies would lead to a £191 million reduction in reserves. There would be no material impact upon the Group's risk asset ratio.

4 Market risk (continued)

Limits

Market Risk Limits – limits to control market risk in respect of trading positions, UK wholesale banking and overseas centres are set by Group Risk Management up to a total authorised by the Board. A combination of position and sensitivity limits is used, depending on the nature of the business activity.

Retail Portfolios – limits to control interest rate risk within the Group's UK retail portfolios are set out in the policy for Group Balance Sheet Management (GBSM), which is established by the Group Asset and Liability Committee (ALCO) and ratified by the Board. The policy is to optimise the stability of future net interest income, and this is achieved by entering into hedging transactions using interest rate swaps and other financial instruments. Both short and long-term interest rate parameters are applied to management of the balance sheet. Overseas operations are managed within limits authorised by Group Risk Management, in addition to which some centres have adopted benchmark profiles for investment of interest rate insensitive liabilities as approved by Group Risk Management.

Processes

Wholesale Banking – market risk in the wholesale banking books is managed in the UK by Lloyds TSB Treasury, and internationally by an authorised local treasury operation in each overseas centre. The levels of exposure within these books are controlled and monitored within approved limits, both locally and also centrally by Group Risk Management. Active management of the book is necessary to meet customer requirements and changing market circumstances.

Trading Activities – trading is restricted to a number of specialist centres, authorised by Group Risk Management, the most important centre being the Group's principal Treasury department in London. The level of exposure is strictly controlled and monitored within approved limits locally and centrally by Group Risk Management. Most of the Group's trading activity is undertaken to meet the requirements of customers for foreign exchange and interest rate products. However, some interest rate and exchange rate positions are taken out using derivatives (forward foreign exchange contracts, interest rate swaps and forward rate agreements) and on-balance sheet instruments (mainly debt securities), with the objective of earning a profit from favourable movements in market rates. Accordingly, these transactions are reflected in the accounts at their fair value and gains and losses shown in the profit and loss account as dealing profits.

Retail Portfolios and Capital Funds – market risk in the Group's retail portfolios, including mortgages, and in the Group's capital funds arises from the different repricing characteristics of the Group's banking assets and liabilities and is managed by GBSM, reporting to the ALCO. The simulation models used by GBSM include assumptions about the relationships between customer behaviour and the level of interest rates; the anticipated level of future business is also taken into account. The accuracy of these assumptions will impact the efficiency of hedging transactions. The assumptions are regularly updated and the projected exposure is actively managed in accordance with the policy.

Derivatives – these are used to meet customers' financial needs; as part of the Group's trading activities; and to reduce the Group's own exposure to fluctuations in interest and exchange rates. The principal derivatives used by the Group are interest rate contracts (including interest rate swaps, forward rate agreements and options) and exchange rate contracts (including forward foreign exchange contracts, currency swaps and options). Particular attention is paid to the liquidity of the markets and products in which the Group trades to ensure that there are no undue concentrations of activity and risk.

5 Insurance risk

Definition

The risk of loss arising from the sensitivity of profits to movements in claims experience and expectation; movements in the market value of invested assets which are not matched by similar movements in the value of insurance liabilities; the presence of options and guarantees in insurance products; and changes in the legal, regulatory and fiscal environment.

Measurement

Financial risks are measured through deterministic studies of the impact of different insurance and investment market scenarios on the future free assets of the business.

Processes

Insurance risks are both retained and reinsured with external underwriters. The retained risk level is carefully controlled and monitored, with close attention being paid to the analysis of underwriting experience, product design, policy wordings, adequacy of reserves, solvency management and regulatory requirements.

5 Insurance risk (continued)

General insurance exposure to accumulations of risk and possible catastrophes is mitigated by reinsurance arrangements which are broadly spread over different reinsurers. Detailed modeling, including that of the Probable Maximum Loss under various catastrophe scenarios, supports the choice of reinsurance arrangements. Appropriate reinsurance arrangements also apply within the life and pensions businesses.

Investment strategy is determined by the term and nature of the underwriting liabilities, and asset/liability matching positions are actively monitored. Investment strategy for surplus assets held in excess of liabilities takes account of the regulatory and internal business requirements for capital to be held to support the business now and in the future.

Equity derivatives are used by the Group to match equivalent liabilities arising from some of its retail products. Derivatives may also be used for efficient portfolio management purposes in client funds where such activity is in accordance with Group approved policy and the customer mandate.

With-profits life and pensions business involves guaranteed benefits that create a contingent market risk to the Group. Accordingly, in extreme investment market conditions the surplus assets in the life and pensions business could be called upon to support with-profits benefits. Options and guarantees are only incorporated in new insurance products after careful consideration of the risk management issues that they present. This occurs under the New Product Approval process (see ‘Product and Service Risk’ below).

6 Operational risk

Definition

The risk of loss resulting from inadequate or failed internal processes, people and systems, or from external events. For internal purposes, reputational impact is also included.

Processes

Business units have primary responsibility for identifying and managing their operational risks. They employ internal control techniques to reduce their likelihood or impact to tolerable levels within the Group’s risk appetite. Where appropriate, risk is mitigated by way of insurance.

Group Risk Management’s responsibilities in relation to operational risk include:

- Defining high-level operational risk policies to ensure a comprehensive and consistent approach to the identification and management of operational risk.
- Implementation of a Group-wide standard methodology to ensure consistency in the identification, assessment and management of operational risk.
- Communication and provision of general guidance on operational risk related issues, including regulatory changes and developments in the measurement and management of operational risk, to promote best practice throughout the Group.
- Continuous review and improvement of all aspects of operational risk management to reflect developments in industry best practice and regulatory requirements, e.g. the New Basel Accord.
- Approval from a risk perspective of all new products launched throughout the Group, to ensure their risks are understood by the business and managed appropriately (see ‘Product and Service Risk’ below).
- Identification of risk through formal risk reviews, covering specific risks, activities, business sectors or products, and ensuring that prompt and pre-emptive action is taken to address any actual or perceived risks that may emerge, whether specific to the Group or to the industry generally.

7 Product and service risk

Definition

The risk of loss arising from the inherent characteristics, management or distribution of products or services, or from failure to meet or exceed customer expectations and competitor offerings.

Processes

For the Group to achieve its strategic aims of leadership in chosen markets and being first choice for customers, product life cycles must be effectively managed and new products developed to meet customer needs.

Business units are responsible for maintaining a range of products which meets the needs of customers and the business strategy; managing and controlling product risks; and compliance with applicable regulations.

7 Product and service risk (continued)

Product Planning and Development – business units have formal processes for reviewing the range of their product portfolios and subjecting all product development to rigorous assessment. They are also responsible for ensuring compliance with all relevant regulatory and legislative requirements.

Product Pricing – business units have pricing objectives consistent with Group strategy.

Product Promotion, Distribution and Sales – business units have a defined channel distribution strategy for products, consistent with the Group's distribution strategy. Business units launching new products are responsible for ensuring that proposed sales activity within delivery channels is compliant with regulatory requirements.

All advertising and marketing material complies with the Group's governing policy on Business Conduct. Any statement of fact is substantiated through documentary evidence; any comparison is presented in a fair and balanced way; and any reference to past performance clearly states the basis of measurement.

Business units are required, prior to the publication of any sales material, to seek confirmation that it complies with the regulatory and legal requirements of the jurisdiction in which the product is offered and marketed. Terms and conditions (to include mandates, agreements and other documentation) are approved by legal advisers and reviewed periodically.

New Product Approval – the Group defines a New Product as a new or amended product that introduces a significantly different risk profile at Group or business unit level. In line with defined policy, business units provide Group Risk Management with details of New Products at an early stage of product or service development to ensure compliance with the Group's risk appetite and strategy.

Where appropriate, technical advice/approval is sought from specialist functions, e.g. Tax, Legal and Compliance. Only products carrying the approval of Group Risk Management and the business units involved in their manufacture/delivery are offered to customers.

Product Performance – business units establish and monitor performance standards for all marketed products across a range of indicators, e.g. sales volumes, customer service, risk profile. Significant deviations from these standards are investigated and appropriate action taken.

8 Financial risk

Definition

The risk of financial failure arising from lack of capital or liquidity, poor management or poor quality/volatile earnings.

Measurement

The international standard for measuring capital adequacy is the risk asset ratio, which relates to on- and off-balance sheet exposures weighted according to broad categories of risk. The Group's capital ratios, calculated in line with the requirements of the Financial Services Authority (FSA), are set out in detail within this report.

Liquidity Policy – a Group Liquidity Policy is in place which requires a common methodology for measuring liquidity across the Group. The methodology derives a liquidity ratio calculated by taking the sum of liquid assets, five-day wholesale inflows and back-up lines, and then dividing this by the sum of five-day wholesale outflows and a percentage of retail maturities and contingent claims drawable over the next five days.

Accounting Policies – the Group seeks to use appropriate accounting policies, consistently applied and supported by reasonable and prudent judgements and estimates.

Limits

The Group and its regulated subsidiary banks have been allocated an Individual Capital Ratio by the FSA, and the Board has agreed a formal buffer to be maintained in addition to the Individual Capital Ratio. Actual or prospective breaches of the formal buffer must be notified to the FSA, together with proposed remedial action; no such notifications have been made during 2002. Informally, a further buffer is maintained. In addition, the Board has agreed a maximum limit for the proportion of debt instruments in the capital base. Risk-weighted assets are monitored by business unit, while capital is controlled centrally.

The Liquidity Policy requires all authorised local treasury operations to maintain a liquidity ratio of over 100 per cent, in addition to ensuring compliance with local regulatory requirements.

8 Financial risk (continued)

Processes

Capital ratios are a key factor in the Group's budgeting and planning processes, and updates of expected ratios are prepared regularly during the year. Capital raised takes account of expected growth and currency of risk assets, and also allows for the sensitivity of the Group's capital to movements in equity markets.

Each reporting entity within the Group has a finance function which is responsible for the production of financial, management and regulatory information. It is the responsibility of Group Finance to produce consolidated information for use internally and to meet external regulatory and statutory reporting requirements. In conjunction with directives laid down by Group Finance, business units or reporting entities:

– Have formal month-end and quarter-end procedures in place for preparation of management and financial accounts respectively.
– Review and formally approve management accounts at a determined level of detail, ensuring consistency with financial accounts.
– Prepare forecasts and detailed annual budgets that are subject to formal review and approval.
– Implement measures to monitor performance at local level to identify significant fluctuations or unusual activity.

It is the responsibility of local line management to ensure that the Liquidity Policy is met, and the sources and maturities of assets and liabilities are continually managed and appropriately diversified to avoid any undue concentration as market conditions evolve. Compliance is monitored by regular liquidity returns to Group Risk Management.

9 Customer treatment risk

Definition

The risk of financial loss or reputational damage arising from inappropriate or poor customer treatment.

Measurement

Service improvements are monitored by customer satisfaction surveys. The results of the research are fed into the Group's CARE Index, which measures ongoing performance against five principal objectives: customer understanding; accessibility; responsibility; expertise; and overall service quality improvement.

Processes

Trends across all the CARE Index categories are monitored and fed into a programme of continuous customer service improvement. Lloyds TSB also provides its staff with clear FSA-compliant guidelines and processes for dealing with customer complaints.

10 Legal and regulatory risk

Definition

The risk of financial loss or reputational damage arising from failing to comply with the laws, regulations or codes applicable to the financial services industry.

Processes

The Group's business is regulated overall by the FSA, and additionally by local regulators in offshore and overseas jurisdictions.

Each Group business has a nominated individual with 'Compliance Oversight' responsibility under FSA rules. The role of such individuals is to ensure that management have in place within the business a control structure which creates awareness of the rules and regulations to which the Group is subject, and to monitor and report on adherence to these rules and regulations.

Group Compliance – all compliance personnel also have a reporting line to Group Compliance, which sets compliance standards across the Group and provides independent reporting and assessment to the Board and business unit directors.

Financial Crime – Group Compliance includes a dedicated unit, led by the Group Financial Crime Director, which is responsible for ensuring that the Group has effective processes in place to identify and report on suspicious transactions and customers in support of the world-wide fight against financial crime.

The Group Compliance Director has access to the Chairman, Group Chief Executive and members of senior management.

11 Change management risk

Definition

The risk of financial loss or reputational damage arising from programmes or projects failing to deliver to requirements, budget or timescale, or failing to implement change effectively.

Processes

To deliver the Group's strategic aims, change must be managed in an effective, risk-aware and appropriately controlled manner throughout the organisation. The Group's Change Management Standards provide consistency of approach across the Group's project portfolio. In particular, the following control processes are in place:

– The Group's approach to change management is regularly benchmarked against other organisations around the world.
– A specialist Group Project Services function provides a pool of experienced, professional project managers to be deployed on major projects across the Group.
– An Investment Committee oversees the Group's investment in projects, and is constituted as a sub-committee of the Group Executive Committee.
– Changes that significantly impact customers or staff are managed as part of an overall Group Change Plan managed by the Change Implementation Review Committee (CIRC). The CIRC ensures that the aggregate impact of the implementation of change on customers, staff and systems is understood, managed and controlled.
– A six-monthly update on the Group's Aggregate Change Plan is provided to the Board.

Corporate social responsibility

Lloyds TSB adopts a responsible attitude to Social, Environmental and Ethical (SEE) issues, and publishes a separate annual information pack on its role in the community, its code of business conduct and its environmental performance: 'the community and our business' (see page 93 for details).

The Group has a dedicated Environmental Risk unit which is responsible for the development of environmental policies and procedures, and provides practical advice and guidance on environmental issues to business units. Significant progress has been made in developing the Group's environmental management system, and this is detailed in the environmental report forming part of 'the community and our business'.

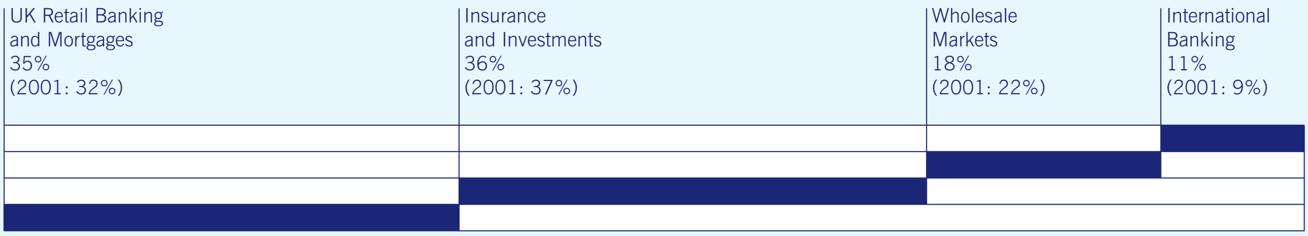
During the year, the Group has reviewed its SEE performance and is of the opinion that it already complies with the majority of the guidelines published by the Association of British Insurers in 2001. The Group continues to develop its policies and procedures and will monitor its performance more rigorously in 2003.

Five year
financial summary

	2002 £ million	2001 £ million	2000 £ million	1999 £ million	1998 £ million
Profit and loss account					
Net interest income	**5,171**	4,922	4,587	4,783	4,398
Other finance income	**165**	307	424	268	252
Other operating income	**3,542**	3,660	3,765	3,267	2,792
Total income	**8,878**	8,889	8,776	8,318	7,442
Operating expenses	**(4,915)**	(4,776)	(4,279)	(3,884)	(3,876)
Trading surplus	**3,963**	4,113	4,497	4,434	3,566
General insurance claims	**(229)**	(174)	(142)	(169)	(146)
Provisions	**(1,116)**	(807)	(573)	(622)	(570)
Income from joint ventures	**(11)**	(10)	3	12	14
Profit (loss) on sale and closure of businesses	**–**	39	–	(126)	84
Profit on ordinary activities before tax	**2,607**	3,161	3,785	3,529	2,948
Profit on ordinary activities after tax	**1,843**	2,286	2,703	2,445	2,086
Profit for the year attributable to shareholders	**1,781**	2,229	2,654	2,439	2,073
Economic profit	**821**	1,119	1,524	1,522	1,189

Note
Figures for 2001 and earlier years have been restated to reflect the implementation of UITF33, 'Obligations in capital instruments', FRS 17, 'Retirement benefits', FRS 19, 'Deferred tax' and detailed guidance from the Association of British Insurers for best practice in the preparation of results using the achieved profits method of accounting.

Quality
of earnings



Excluding central group items, changes in economic assumptions and investment variance

Five year financial summary

	2002 £ million	2001 £ million	2000 £ million	1999 £ million	1998 £ million
Balance sheet and capital ratios					
Loans and advances to banks and customers	**152,003**	138,159	129,722	119,196	113,706
Investments	**29,565**	24,489	14,861	15,125	13,324
Other assets	**25,850**	26,756	25,004	18,851	19,445
	207,418	189,404	169,587	153,172	146,475
Long-term assurance assets attributable to policyholders	**45,340**	46,389	51,085	26,542	23,692
Total assets	**252,758**	235,793	220,672	179,714	170,167
Deposits by banks and customers and debt securities in issue	**172,032**	157,846	136,623	123,668	119,389
Other liabilities	**16,515**	12,548	13,001	11,218	13,690
Subordinated liabilities (loan capital)	**10,168**	8,108	7,510	6,493	4,021
Minority interests (equity and non-equity)	**731**	546	552	33	42
Shareholders' funds (equity)	**7,972**	10,356	11,901	11,760	9,333
	207,418	189,404	169,587	153,172	146,475
Long-term assurance liabilities to policyholders	**45,340**	46,389	51,085	26,542	23,692
Total liabilities	**252,758**	235,793	220,672	179,714	170,167
Risk asset ratio : total capital	**9.6%**	8.8%	8.7%	14.9%	11.2%
: tier 1 capital	**7.8%**	7.8%	8.0%	9.9%	8.6%
Share information					
Earnings per share	**32.0p**	40.3p	48.4p	44.8p	38.4p
Dividends per share (net)	**34.2p**	33.7p	30.6p	26.6p	22.2p
Dividend cover (times)	**0.9**	1.2	1.6	1.7	1.7
Market price (year-end)	**446p**	746p	708p	774p	855p
Net assets per share	**141p**	184p	213p	212p	170p
Number of shareholders (thousands)	**973**	981	1,026	1,024	1,028
Average shares in issue (millions)	**5,570**	5,533	5,487	5,445	5,400
Performance measures					
Post-tax return on average shareholders' equity	**16.7%**	18.1%	21.1%	23.9%	23.5%
Post-tax return on average assets*	**0.93%**	1.28%	1.68%	1.63%	1.48%
Post-tax return on average risk-weighted assets*	**1.61%**	2.26%	3.07%	2.94%	2.62%
Efficiency ratio	**55.4%**	53.7%	48.8%	46.7%	52.1%

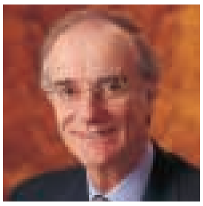
*Assets exclude long-term assurance assets attributable to policyholders.

Note
Figures for 2001 and earlier years have been restated to reflect the implementation of UITF33, 'Obligations in capital instruments', FRS 17, 'Retirement benefits', FRS 19, 'Deferred tax' and detailed guidance from the Association of British Insurers for best practice in the preparation of results using the achieved profits method of accounting.

The board

Non-executive directors

Maarten A van den Bergh◆
Chairman
Joined the Group in 2000 as deputy chairman and was appointed chairman in 2001. Joined the Royal Dutch/Shell Group of companies in 1968 and after a number of senior and general management appointments in that group, became group managing director in 1992. Appointed president of Royal Dutch Petroleum Company and vice chairman of the committee of managing directors of the Royal Dutch/Shell Group in 1998 and continued in these roles until 2000. A non-executive director of Royal Dutch Petroleum Company, BT Group and British Airways. Aged 60.

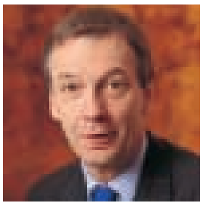


M Kent Atkinson
(leaving on 16 April 2003)
Joined Bank of London & South America in 1964, which became a Lloyds Bank subsidiary in 1971, and held a number of senior and general management appointments, including positions in Latin America and the Middle East, before being appointed to the board in 1997 as group finance director. Became a non-executive director of the group in June 2002. A non-executive director of Coca-Cola HBC SA, Marconi and Marconi Corporation. Aged 57.

Sheila M Forbes CBE✠†
(leaving on 16 April 2003)
A director of TSB Group since 1994. Chairs the board of governors of Thames Valley University and is a civil service commissioner. Head of personnel for Unigate from 1980 to 1988 and personnel director for Storehouse from 1988 to 1992. Director of human resources at Reed Elsevier (UK) from 1992 to 1996. A non-executive director of OCS Group. Aged 56.

DeAnne S Julius CBE✠†
Joined the board in 2001. Held a number of senior appointments in the UK and USA with the World Bank, Royal Dutch/Shell Group and British Airways, before membership of the Bank of England Monetary Policy Committee from 1997 to 2001. Chaired HM Treasury's banking services consumer codes review group. A non-executive director of the Bank of England, BP, Serco Group and Roche Holdings SA. Aged 53.

Alan E Moore CBE*§
Deputy Chairman
(leaving on 16 April 2003)
Joined Lloyds Bank International in 1980. Held a number of senior and general management appointments in that company and in Lloyds Bank before becoming a director of Lloyds Bank in 1989 and deputy chief executive and treasurer in 1994. Following the merger with TSB Group in 1995, became deputy group chief executive of Lloyds TSB Group and then deputy chairman in 1998. Joined Glyn Mills & Co in 1953, holding senior appointments there until his secondment, as director general, to the Bahrain Monetary Agency from 1974 to 1979. Aged 66.

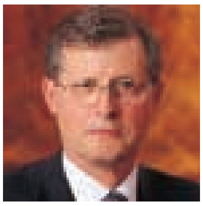


Ewan Brown CBE FRSE✠**
Chairman of Lloyds TSB Scotland
A director since 1999. A non-executive director of Lloyds TSB Scotland since 1997. Executive director of Noble Grossart since 1971. Chairman of Transport Initiatives Edinburgh. A non-executive director of John Wood Group and Stagecoach Holdings. Aged 60.

Gavin J N Gemmell CBE✠*
Chairman of Scottish Widows
Joined the board in 2002. A non-executive director of Scottish Widows since 1984. Retired as senior partner of Baillie Gifford in 2001, after 37 years with that firm. A non-executive director of Archangel Informal Investment. Chairman of the court of Heriot-Watt University. Aged 61.

Sir Tom McKillop✠*†
(▲ from 16 April 2003)
A director since 1999. Joined ICI in 1969 and held a number of senior and general management appointments before the demerger in 1993, when Zeneca was created. Chief executive of Zeneca Pharmaceuticals from 1994 to 1999 and chief executive of AstraZeneca from 1999. Pro-chancellor of Leicester University. Aged 59.

A Clive Butler‡§▲
(leaving on 16 April 2003)
A director of TSB Group since 1993. Joined Unilever in 1970 and following a number of senior and general management appointments was appointed an executive director of Unilever in 1992. Aged 56.



Christopher S Gibson-Smith✠†
A director since 1999. Chairman of National Air Traffic Services. Managing director of BP from 1997 to 2001, having held senior and general management appointments in the UK, USA, Canada and Europe, since joining that company in 1970. A non-executive director of The British Land Company. Aged 57.

The Earl of Selborne KBE FRS✠§
A director since 1995, having been a director of Lloyds Bank since 1994. Managing director of The Blackmoor Estate, his family business. Chancellor of Southampton University since 1996. President of the Royal Geographical Society from 1997 to 2000. Aged 62.

* Member of the audit committee
** Chairman of the audit committee
† Member of the remuneration committee
‡ Chairman of the remuneration committee
§ Member of the nomination committee
◆ Chairman of the nomination committee
✠ Independent director
▲ Senior independent director

Executive directors

Peter B Ellwood CBE
Group Chief Executive
(until 31 May 2003)
Joined TSB Bank in 1989 as chief executive, retail banking. Appointed a director of TSB Group in 1990 and became group chief executive in 1992. Following the merger with Lloyds Bank in 1995, became deputy group chief executive of Lloyds TSB Group and then group chief executive in 1997. Joined Barclays Bank in 1961 and held a number of senior and general management appointments, including chief executive of Barclaycard from 1985 to 1989. Chairman of the Work Foundation. Former chairman of Visa International. Aged 59.

J Eric Daniels
Group Executive Director, UK Retail Banking
(Group Chief Executive from 1 June 2003)
Joined the board in 2001. Served with Citibank from 1975 and held a number of senior and general management appointments in the USA, South America and Europe before becoming chief operating officer of Citibank Consumer Bank in 1998. Following the Citibank/Travelers merger in 1998, he was chairman and chief executive officer of Travelers Life and Annuity until 2000. Chairman and chief executive officer of Zona Financiera from 2000 to 2001. Aged 51.

Archie G Kane
Group Executive Director, IT and Operations
Joined TSB Commercial Holdings in 1986 and held a number of senior and general management appointments in the Group before being appointed to the board in 2000. After some 10 years in the accountancy profession, joined General Telephone & Electronics Corporation in 1980, serving as finance director in the UK from 1983 to 1985. Chairman of the council of the Association for Payment Clearing Services. Aged 50.

Steve C Targett
(Group Executive Director, Wholesale and International Banking from 16 April 2003)
Joins the board on 10 March 2003. Served with National Australia Bank from 1997, where he held a number of senior and general management appointments in Australia and the UK before becoming chief executive officer, Europe, in 2002. Previously held a number of senior and general management appointments in Cargill, a commodity trading group, from 1980 to 1988, State Bank of South Australia from 1988 to 1991 and ANZ Bank from 1991 to 1997. His early career, between 1972 and 1980, was spent with National Australia Bank. Aged 47.

Michael E Fairey
Deputy Group Chief Executive
Joined TSB Group in 1991 and held a number of senior and general management appointments before being appointed to the board in 1997 and deputy group chief executive in 1998. Joined Barclays Bank in 1967 and held a number of senior and general management appointments, including managing director of Barclays Direct Lending Services from 1990 to 1991. Aged 54.

Philip R Hampton
Group Finance Director
Joined the board in 2002. Previously, finance director of BT Group from 2000 to 2002, BG Group from 1996 to 2000 and British Steel from 1990 to 1996. Before that, he worked for Coopers & Lybrand from 1975 to 1980 and Lazard Brothers from 1981 to 1990. A non-executive director of RMC Group. Aged 49.

David P Pritchard
Group Executive Director, Wholesale and International Banking
(Deputy Chairman from 16 April 2003)
Joined TSB Group in 1995 as group treasurer. Seconded to the Securities and Investments Board as head of supervision & standards, markets & exchanges, from 1996 to 1998. Appointed to the board in 1998. Held senior and general management appointments with Citicorp from 1978 to 1986 and Royal Bank of Canada from 1986 to 1995. A non-executive director of The London Clearing House. Aged 58.

Michael D Ross CBE
Deputy Group Chief Executive
Joined the board in 2000. Joined Scottish Widows in 1964 and following a number of senior and general management appointments became group chief executive of that company in 1991. Chairman of the Association of British Insurers. Aged 56.

Company Secretary
Alastair J Michie FCIS FCIBS

Directors' report

Results and dividends

The consolidated profit and loss account on page 58 shows a profit attributable to shareholders for the year ended 31 December 2002 of £1,781 million.

An interim dividend of 10.7p per ordinary share was paid on 9 October 2002 and a final dividend of 23.5p per ordinary share will be paid on 7 May 2003. These dividends will absorb £1,908 million.

Principal activities

The company is a holding company and its subsidiaries provide a wide range of banking and financial services through branches and offices in the UK and overseas.

Business review and future developments

A review of the business and an indication of future developments are given on pages 2 to 41.

Authority to purchase shares

The authority for the company to purchase, in the market, up to 564 million of its shares, representing some 10 per cent of the issued ordinary share capital, expires at the annual general meeting. It was not used during the year and shareholders will be asked to give a similar authority at the annual general meeting. Details are contained in the accompanying notice of meeting.

Directors

Biographical details of directors are shown on pages 44 and 45. Particulars of their emoluments and interests in shares in the company are given on pages 48 to 54.

Mr Urquhart left the board at the annual general meeting in 2002. Mr Atkinson, Mr Butler, Miss Forbes and Mr Moore will leave the board at the annual general meeting in 2003.

Mr Gemmell became a director on 17 April 2002 and was elected at the annual general meeting on that day.

Mr Hampton joined the board on 1 June 2002 and Mr Targett will join the board on 10 March 2003. Under the articles of association they offer themselves for election at the annual general meeting.

Mr Kane and Mr Ross retire by rotation at the annual general meeting and offer themselves for re-election.

No director had a material interest at any time during the year in any contract of significance with the company or its subsidiaries.

Employees

The group is committed to employment policies which follow best practice, based on equal opportunities for all employees irrespective of sex, race, national origin, religion, colour, disability, sexual orientation, age or marital status.

In the UK, the group supports Opportunity Now and Race for Opportunity; campaigns to improve opportunities for women and ethnic minorities in the work place. The group is a member of the Employers' Forum on Disability in support of employment of people with disabilities. This recognises the need for ensuring fair employment practices in recruitment and selection, and the retention, training and career development of disabled staff.

Employees are kept closely involved in major changes affecting them through such measures as team meetings, briefings, internal communications and opinion surveys. There are well established procedures, including regular meetings with recognised unions, to ensure that the views of employees are taken into account in reaching decisions.

Schemes offering share options or the acquisition of shares are available for most staff, to encourage their financial involvement in the group.

Donations

The profit and loss account includes a charge for charitable donations totalling £33,403,000 (2001: £36,747,000), including £33,336,667 (2001: £36,376,667) under deeds of covenant to the four Lloyds TSB Foundations, which will be paid during 2003. No donations were made to political parties.

Policy and practice on payment of creditors

The company follows 'The Better Payment Practice Code' published by the Department of Trade and Industry regarding the making of payments to suppliers. Details of how to obtain a copy of the code and other related information is shown on page 93.

The company's policy is to agree terms of payment with suppliers and these normally provide for settlement within 30 days after the date of the invoice, except where other arrangements have been negotiated. It is the policy of the company to abide by the agreed terms of payment, provided the supplier performs according to the terms of the contract.

As the company owed no amounts to trade creditors at 31 December 2002, the number of days required to be shown in this report, to comply with the provisions of the Companies Act 1985, is nil. The equivalent figure for the Lloyds TSB Group in the UK is 27. This bears the same proportion to the number of days in the year as the aggregate of the amounts owed to trade creditors at 31 December 2002 bears to the aggregate of the amounts invoiced by suppliers during the year.

Auditors

Following the transfer of substantially all of the business of the UK firm of PricewaterhouseCoopers, the company's auditors, to a limited liability partnership on 1 January 2003, PricewaterhouseCoopers resigned and the directors appointed the new firm, PricewaterhouseCoopers LLP. Resolutions concerning the re-appointment of the auditors and authorising the directors to set their remuneration will be proposed at the annual general meeting.

On behalf of the board

A J Michie
Secretary

13 February 2003

Directors' remuneration

The remuneration committee

The remuneration committee, comprising Mr Butler (chairman), Miss Forbes, Dr Gibson-Smith, Dr Julius and Sir Tom McKillop, makes recommendations to the board on the framework of executive directors' remuneration and its cost, and determines, on the board's behalf, specific remuneration packages for each of the chairman, the deputy chairman and the executive directors. Additionally, all the non-executive directors receive the minutes of remuneration committee meetings and have the opportunity to comment and have their views taken into account before the committee's decisions are implemented.

Each year, with the help of external management consultants, the total remuneration package of the directors is reviewed, and in 2002 The Hay Group Management Limited were commissioned by the remuneration committee to conduct the review. The consultants have also provided services, such as salary survey information and job evaluation, to other parts of the Group.

Mr van den Bergh, Mr Ellwood, Mr Fairey, Mr Mitchinson, Director of Group Human Resources, and Mr Wilson, Compensation and Benefits Director, assisted the committee in their deliberations but did not participate in any decision relating to their own remuneration.

Directors' remuneration policy

The Group aims to ensure that the executive directors' remuneration arrangements, in line with the Group's overall practice on pay and benefits, are competitive and designed to attract, retain and motivate executive directors of the highest calibre, who are expected to perform to the highest standards. Account is taken of information, from internal and independent sources, on the remuneration for comparable positions in a wide range of FTSE 100 companies. The strategy for executive directors' pay is for basic salaries to reflect the relevant market median; for benefits such as a company car, medical insurance and pension to reflect market practice; and for total direct compensation (basic salary, annual incentives and the value of long-term incentives) to be at the upper quartile of the market place, provided that performance justifies the amount. This strategy is consistent with the Group's belief that performance should determine a significant proportion of the total remuneration package for executive directors. There are no plans to change the strategy.

The fees of the non-executive directors are agreed by the board within a total amount determined by the shareholders. They are designed to recognise the significant responsibilities of directors and to attract individuals with the necessary experience and ability to make an important contribution to the Group's affairs. The fees, which are neither performance related nor pensionable, are comparable with those paid by other companies.

Reward package

The current package for executive directors comprises the following elements:

Basic salary

The aim is to ensure that salaries are competitively set in relation to similar jobs in a wide range of FTSE 100 companies.

Current salaries for the chairman, deputy chairman and executive directors, following the most recent salary review in December 2002 are:

Mr Daniels	£450,000
Mr Ellwood	£700,000
Mr Fairey	£498,000
Mr Hampton	£483,000
Mr Kane	£397,500
Mr Moore	£215,250
Mr Pritchard	£409,500
Mr Ross	£443,000
Mr van den Bergh	£422,500

Annual incentive

The annual incentive scheme is designed to reflect specific goals linked to the performance of the business.

In 2002, the group chief executive had a maximum incentive opportunity equal to 100 per cent of his salary as did Mr Daniels, whose bonus opportunity and payment for 2002 were agreed as part of his recruitment package. Each of the other executive directors could earn an incentive equal to 75 per cent of their salary. The awards were based on group performance and the attainment of predetermined targets relating to total income, profit before tax and economic profit. Each will receive an award equal to 4.7 per cent of salary based on achievement against the income target, which was met in part. No bonus has been earned for the other targets.

In 2003, all the executive directors will have a maximum incentive opportunity equal to 100 per cent of their salaries. Awards will be based on group performance, with predetermined targets relating to profit before tax and economic profit. 75 per cent of the award will be payable on achievement of profit before tax and economic profit relating to the Group's stretching budget for 2003 and the remuneration committee has set a higher target for the maximum award. The threshold performance levels, below which no bonus will be payable, have also been set by the remuneration committee at higher figures than those achieved in 2002.

Directors' remuneration

The remuneration committee reviewed the attainment of targets in 2002 and agreed the incentive payments, and the auditors confirmed the calculations. These payments are not pensionable.

Long-term rewards

Executive share option schemes

The Group is committed to the governing objective of maximising shareholder value over time. The board believes that the executive share option schemes for senior executives, approved by the shareholders at the annual general meeting in 1997 and amended at the annual general meeting in 2001, provide an effective method of giving executives an incentive to achieve that objective.

Performance conditions are set when the grant of options is made and the options cannot normally be exercised unless the conditions have been met. To meet the performance conditions, the company's ranking, based on total shareholder return (calculated by reference to both dividends and growth in share price) over the relevant (three year) period, within the comparator group, must be at least ninth. Hoare Govett independently provides the information on total shareholder return and the company's ranking and the auditors are also involved before the remuneration committee confirms whether the conditions have been met.

In 2002, options were granted to executive directors and senior executives within the scheme limits. These limits relate to the number of shares under option and the price payable on exercise. The maximum limit for the grant of options to an executive director in any one year is equal to one and a half times annual basic salary multiplied by a performance multiplier of 3.5 (although in exceptional circumstances, for example on the recruitment of a new executive, that could be increased to four times annual basic salary multiplied by 3.5).

The full grant of options for executive directors will only become exercisable if the company is ranked first within the comparator group.

The following table illustrates the percentage of the grant which would be exercisable depending on the ranking within the comparator group.

At the end of 2002 Lloyds TSB Group was ranked:

6th after two years of the performance period for options granted in 2001; and

11th after one year of the performance period for options granted in 2002.

Any awards made to executive directors in 2003 will be subject to the same scheme limits and performance conditions as outlined above.

Ranking position within comparator group	% of option which may be exercised
1	100
2	86
3	71
4	57
5	43
6	29
7	23
8	17
9	14
10 or below	Nil – options not exercisable

The current constituents of the comparator group are:

Abbey National	ABN Amro	Alliance and Leicester
Aviva	Barclays	Citigroup
Fortis	HBOS	HSBC Holdings
ING	Legal and General	National Australia Bank
Prudential	Royal Bank of Scotland	Royal & Sun Alliance
Standard Chartered		

In addition, share options have been granted in previous years in accordance with the relevant scheme rules and market practice at that time. The table on page 53 includes options granted under these previous schemes.

Options granted	Performance conditions
Prior to March 1996	None
March 1996-August 1999	That the company's ranking based on shareholder return (calculated by reference to both dividends and growth in share price) over the relevant period should be in the top fifty companies of the FTSE 100 and that there must have been growth in earnings per share which is equal to the aggregate percentage change in the Retail Price Index plus two percentage points for each complete year of the relevant period.
March 2000-March 2001	As for March 1996 – August 1999 except that there must have been growth in the earnings per share equal to the change in the Retail Price Index plus three percentage points for each complete year of the relevant period.

The remuneration committee chose the relevant performance condition, where applicable, because it was felt to be challenging, aligned to shareholder interests and appropriate at the time.

At the annual general meeting in April 2003, shareholders will be asked to approve an amendment to the rules of the executive share option schemes. Under the existing rules, a share option may not be granted to any person who, at the date of grant, is within 2 years of retirement. It is proposed to amend the rules of the schemes to allow share options to be granted to executives up to six months before retirement.

Directors' remuneration

Since the introduction of the new performance condition in 2001, the exercise of options after retirement would still require the condition to be satisfied over the original performance period. Also, if the optionholder retired within 3 years of the date of grant, the number of shares which could be acquired on exercise would be reduced according to the length of time the optionholder was employed between the date of grant and the date of retirement.

Other share plans

The executive directors, the chairman and the deputy chairman may participate in the Group's 'sharesave' scheme and 'shareplan' on the same basis as other employees.

Pensions

Executive directors are entitled to pensions based on salary and length of service with the Group, with a maximum pension of two thirds of final salary.

Service agreements

The general group policy is for executive directors to have service agreements with notice periods of no greater than one year, to reflect current corporate governance best practice. Executive directors are required to give the Group six months' notice if they wish to leave. The Association of British Insurers and the National Association of Pension Funds published a joint statement of best practice on executive contracts and severance in December 2002 and, during 2003, the remuneration committee will consider what changes would be desirable in respect of service agreements.

Mr Fairey, Mr Kane and Mr Hampton each has a service agreement which the company may terminate by giving one year's notice. Mr Ross's service agreement, entered into in connection with the arrangements for the transfer of the business of Scottish Widows to the Group in March 2000, provided for two years' notice for the first two years, but since March 2002 the notice period has decreased by one month for each month of service, to one year's notice. From March 2003, therefore, Mr Ross's agreement may be terminated on one year's notice.

Mr Daniels' service agreement provides for two years' notice for the first eighteen months (from November 2001): after that, the notice period reduces to one year. His contract also provides that if, within eighteen months of the commencement of his employment, there were to be a change of circumstances of the company (as defined in the agreement) so that there was, in his reasonable judgement, a materially adverse effect on his prospects or a material diminution in his status, he would be entitled to serve notice terminating his employment and appropriate compensation would be payable to him.

None of the other directors has a service agreement with a notice period of one year or more.

The remuneration committee has considered the provisions of the UK listing authority's corporate governance code and the recent ABI/NAPF joint statement mentioned above, relating to compensation in the event of early termination of directors' service agreements and a departing director's duty to mitigate his or her loss. The Group will have regard to that duty on a case by case basis when assessing the appropriate level of compensation which may be payable. It is the Group's policy that where compensation on early termination is due, in appropriate circumstances it should be paid on a phased basis.

Non-executive directors do not have service agreements and, in accordance with the articles of association, their appointment may be terminated at any time without compensation.

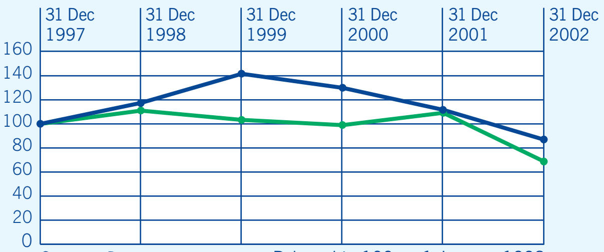
External appointments

Lloyds TSB recognises that executive directors may be invited to become non-executive directors of other companies and that such appointments can broaden their knowledge and experience, to the benefit of the Group. Fees are normally retained by the individual director, as the post entails personal responsibility on their part. Directors are generally allowed to accept one such appointment.

Performance graph

As required by recent legislation regarding the directors' remuneration report, this graph illustrates the performance of Lloyds TSB Group plc measured by total shareholder return (share price growth plus dividends paid) against a 'broad equity market index' over the past five years. As Lloyds TSB Group plc has been a constituent of the FTSE 100 index throughout this five-year period, that index is considered to be the most appropriate benchmark.

Comparative total shareholder return



Source: Datastream Rebased to 100 on 1 January 1998

Lloyds TSB Group plc — FTSE 100 index

Directors' remuneration

Directors' emoluments

	Salaries/fees £000	Other benefits £000	Performance-related payments £000	Shareplan £000	2002 Total £000	2001 £000
Current directors who served during 2002:						
M K Atkinson (service agreement dated 2 February 1999)	**174**	**370**	**18**	**5**	**567**	588
Ewan Brown	**60**				**60**	59
A C Butler	**40**				**40**	40
J E Daniels (service agreement dated 19 October 2001)	**450**	**349**	**450**	**14**	**1,263**	192
P B Ellwood (service agreement dated 19 June 1989)	**660**	**22**	**31**	**20**	**733**	1,001
M E Fairey (service agreement dated 28 August 1991)	**470**	**137**	**22**	**14**	**643**	791
S M Forbes	**38**				**38**	38
G J N Gemmell	**68**				**68**	–
C S Gibson-Smith	**38**				**38**	38
P R Hampton (service agreement dated 30 May 2002)	**268**	**9**	**13**	**8**	**298**	–
D S Julius	**38**				**38**	9
A G Kane (service agreement dated 9 February 2000)	**375**	**14**	**18**	**11**	**418**	548
Sir Tom McKillop	**45**				**45**	45
A E Moore	**210**	**11**		**6**	**227**	229
D P Pritchard (service agreement dated 13 February 1998)	**390**	**17**	**18**	**12**	**437**	588
M D Ross (service agreement dated 7 March 2000)	**430**	**15**	**20**	**13**	**478**	650
Lord Selborne	**33**				**33**	43
M A van den Bergh	**400**	**15**			**415**	406
Former director who served during 2002:						
L M Urquhart	**25**				**25**	93
Former directors who served during 2001						391
	4,212	**959**	**590**	**103**	**5,864**	5,749

'Other benefits' include the use of a car, private medical insurance, life insurance cover and payments to a former executive director on termination of his service contract (see below). Allowances for relocation, housing and legal advice arising from Mr Daniels' service agreement, and an additional payment in respect of the contribution to the separate fund relating to Mr Fairey's pension, are also included. The separate fund, which was mentioned in previous annual reports, was established to cover pension obligations of those who joined the Group after 1 June 1989 and who are subject to the Inland Revenue earnings cap relating to pensions, introduced by the Finance Act 1989.

£348,637 included in 'other benefits' for Mr Atkinson represents the amount to which he was contractually entitled when his employment was terminated on 31 May 2002. This included 12 months' salary from which he elected to pay £318,637 to purchase additional pension from Lloyds TSB Group Pension Scheme No. 1. As part of his termination package, he is also entitled to a bonus reflecting what he would have received during his notice period. He became entitled to a pension of £273,514 immediately when his employment terminated, which took into account the additional 12 months' service for the notice period. He also continues to receive beneficial rights to medical insurance and use of a car for 12 months after departure. His outstanding share options are exercisable either up to 12 months after departure or, for those options granted after August 2001, at the later appropriate time providing the performance condition has been met.

Performance-related payments

These payments relate solely to cash bonuses earned in 2002 under the annual incentive scheme. They do not include any amounts relating to the former medium-term incentive plan, approved by shareholders in 2000, which ended in 2002 without any payments being made, as the relevant performance targets were not met.

Shareplan

Amounts shown are those receivable by directors in respect of the Group's 'shareplan'. Under the scheme, employees received an award equal to 3 per cent of salary in 2002. A maximum of £3,000 is receivable in shares for those eligible, with any balance paid in cash.

Directors' remuneration

Directors' pensions

The executive directors are all members of one of the defined benefit schemes provided by the Lloyds TSB Group. Those directors who joined the Group after 1 June 1989 have pensions provided on salary in excess of the earnings cap either through membership of a Funded Unapproved Retirement Benefits Scheme ('FURBS') or by an unfunded pension promise.

Retirement pensions accrue at rates of between 1/60 and 1/30 of basic salary.

With the exception of Mr Pritchard, directors have a normal retirement age of 60. Mr Pritchard's retirement date is 16 April 2003. In the event of death in service, a lump sum of 4 times salary is payable plus a spouse's pension of 2/3 of the member's prospective pension. On death in retirement, a spouse's pension of 2/3 of the member's pension is payable. The schemes are non-contributory.

Mr Pritchard has a deferred cash entitlement of £71,310 from his membership of the defined contribution section of the Group's FURBS.

	Accrued pension at 31 December 2002 (a)	Accrued pension at 31 December 2001 (b)	Transfer value at 31 December 2002 (c)	Transfer value at 31 December 2001 (d)	Change in transfer value (c) - (d)	Additional pension earned to 31 December 2002 (e)	Transfer value of the increase (f)
M K Atkinson	**273,514**	**227,274**	**4,632,189**	**3,455,667**	**1,176,522**	**42,376**	**717,673**
J E Daniels	**31,250**	**23,750**	**346,555**	**312,504**	**34,051**	**7,096**	**78,693**
P B Ellwood	**393,875**	**336,441**	**7,093,775**	**5,943,051**	**1,150,724**	**51,715**	**931,398**
M E Fairey	**155,805**	**127,183**	**2,075,301**	**1,862,642**	**212,659**	**26,460**	**352,443**
P R Hampton	**5,963**	**–**	**58,631**	**–**	**58,631**	**5,963**	**58,631**
A G Kane	**144,353**	**118,599**	**1,514,190**	**1,503,489**	**10,701**	**23,737**	**248,989**
D P Pritchard	**38,974**	**30,582**	**656,073**	**518,412**	**137,661**	**7,872**	**132,514**
M D Ross	**274,125**	**245,229**	**4,395,896**	**3,564,387**	**831,509**	**24,727**	**392,853**
In addition, the following unfunded benefits have accrued for Mr van den Bergh instead of a salary increase in 2002:							
M A van den Bergh	**3,378**	**–**	**36,160**	**–**	**36,160**	**3,378**	**36,160**

The disclosures in columns (a) to (d) are as required by the Companies Act 1985 Schedule 7A.

Columns (a) and (b) represent the deferred pension to which the directors would have been entitled had they left the Group on 31 December 2002 and 2001, respectively (ignoring the two-year requirement to qualify for a deferred pension).

Column (c) is the transfer value of the deferred pension in column (a) calculated as at 31 December 2002 based on factors supplied by the actuary of the relevant Group pension scheme in accordance with actuarial guidance note GN11.

Column (d) is the equivalent transfer value, but calculated as at 31 December 2001 on the assumption that the director left service at that date. Mr Hampton joined the Group on 1 June 2002 and previous years' figures are not shown.

Column (e) is the increase in pension built up during the year, recognising (i) the accrual rate for the additional service based on the pensionable salary in force at the year end, and (ii) where appropriate the effect of pay changes in 'real' (inflation adjusted) terms on the pension already earned at the start of the year.

Column (f) is the capital value of the pension in column (e).

The disclosures in columns (e) and (f) are as required by the UK listing authority's listing rules. The requirements of the listing rules differ from those of the Companies Act. The listing rules require the additional pension earned over the year to be calculated as the difference between the pension accrued at the end of the financial year and the pension accrued at the start of the financial year less the increase in the pension earned over the year solely due to inflation. The change in the transfer value required by the Companies Act will also be significantly influenced by the assumptions underlying the calculation at the beginning and the end of the financial year and market conditions.

Members of the Group's pension schemes have the option to pay additional voluntary contributions: neither the contributions nor the resulting benefits are included in the above table.

Directors' interests

The directors' interests, all beneficial, in shares in Lloyds TSB Group were:

Shares	At 31 December 2002	At 1 January 2002 (or date of appointment if later)		At 31 December 2002	At 1 January 2002 (or date of appointment if later)
M K Atkinson	**93,394**	124,815	P R Hampton	**6,021**	–
Ewan Brown	**3,548**	3,402	D S Julius	**2,000**	2,000
A C Butler	**2,000**	2,000	A G Kane	**81,248**	80,120
J E Daniels	**1,029**	1,000	Sir Tom McKillop	**1,000**	1,000
P B Ellwood	**183,999**	178,751	A E Moore	**1,108,475**	1,107,396
M E Fairey	**75,425**	74,158	D P Pritchard	**4,446**	3,367
S M Forbes	**2,000**	2,000	M D Ross	**2,500**	2,500
G J N Gemmell	**50,000**	30,000	Lord Selborne	**3,372**	3,372
C S Gibson-Smith	**3,151**	3,151	M A van den Bergh	**5,079**	4,000

Directors' remuneration

Directors' interests (continued)

Options to acquire shares:		At 1 January 2002 (or date of appointment if later)	Granted during the year	Exercised/ lapsed during the year	At 31 December 2002	Weighted average exercise price at 31 December 2002	Exercise price of share options granted, exercised or lapsed	Market price at date of exercise	Amount of gain on exercise*** 2002 £000	2001 £000
M K Atkinson	Exercisable	147,600			97,600	259p				
	Not exercisable	253,155			–	–				
	Exercisable*	–			92,000	670p				
	Not exercisable*	92,000			232,122	676p				
			275,349				715p		–	577
				916†			442p			
				1,245†			591p			
				91,817†			733p			
				252,404†			715p			
J E Daniels	Exercisable	–			–	–				
	Not exercisable	907,780			–	–				
	Exercisable*	–			–	–				
	Not exercisable*	–			1,238,597	700p				
			330,419				715p			
			398				474p			
P B Ellwood**	Exercisable	321,340			211,340	280p				
	Not exercisable	276,725			–	–				
	Exercisable*	–			190,000	657p				
	Not exercisable*	165,000			357,579	663p				
				4,146			416p	632.5p	9	–
M E Fairey	Exercisable	54,000			–	–				
	Not exercisable	288,329			–	–				
	Exercisable*	–			102,809	675p				
	Not exercisable*	105,809			691,230	701p				
			345,104				715p			
			797				474p		–	882
P R Hampton	Exercisable	–			–	–				
	Not exercisable	–			–	–				
	Exercisable*	–			–	–				
	Not exercisable*	–			326,351	740p				
			326,351				740p			
A G Kane**	Exercisable	171,547			131,547	252p				
	Not exercisable	233,721			4,157	442p				
	Exercisable*	–			90,000	716p				
	Not exercisable*	77,000			531,913	701p				
			275,349				715p			
D P Pritchard	Exercisable	–			–	–				
	Not exercisable	250,096			4,687	416p				
	Exercisable*	–			50,000	860p				
	Not exercisable*	90,000			571,772	700p				
			286,363				715p			
M D Ross	Exercisable	–			–	–				
	Not exercisable	440,549			–	–				
	Exercisable*	–			–	–				
	Not exercisable*	–			756,283	657p				
			315,734				715p			
Gain made by Dennis Holt, who left the board on 31 August 2001									–	53
Gain made by A E Moore, who no longer holds share options									–	281
									9	1,793
Share retention plan										
J E Daniels	Not exercisable	216,763			216,763	(see page 54)				

Directors' remuneration

Directors' interests (continued)

Options may be exercised between 2003 and 2012.

Options were not exercisable because they had not been held for the period required by the relevant scheme or the performance conditions had not been met.

* Market price of shares is below the share option exercise price.

** These directors will receive additional Lloyds TSB Group shares on exercising share options held on 28 December 1995. These shares will compensate them for the special dividend of 68.3p per share which was paid to former TSB Group shareholders in 1996 following the merger with Lloyds Bank, but which was not paid to optionholders.

*** This is the difference between the market price of the shares on the day on which the share option was exercised and the price paid for the shares, and includes the value of shares issued to compensate directors for the special dividend mentioned above.

† These share options lapsed following termination of Mr Atkinson's service contract.

The market price for a share in the Company at 1 January 2002 and 31 December 2002 was 746p and 446p respectively. The range of prices between 1 January 2002 and 31 December 2002 was 427.5p to 817p.

None of the other directors at 31 December 2002 had options to acquire shares in the Company or its subsidiaries.

Share retention plan

Mr Daniels is the only participant in the share retention plan, which was adopted in 2001 as part of the remuneration package considered necessary to attract him from the USA to the UK. An option was granted to him under the plan on 2 November 2001 to acquire 216,763 ordinary shares in the Company (with a value of £1.5 million at the date of grant) for a total price of £1.

The option is designed to encourage him to remain with the Company and, accordingly, is not subject to any performance condition but will normally become exercisable only if he remains an employee, and has not given notice of resignation, on 31 December 2004. However, the option will become exercisable if before that date Mr Daniels becomes entitled to terminate his service agreement by way of breach (including circumstances treated as breach) or if, following a reconstruction or takeover of the Company, the remuneration committee so decides.

The option will lapse if before 31 December 2004 Mr Daniels dies, or ceases to be an employee or resigns, except in the circumstances described in the preceding paragraph. Otherwise, the option will become exercisable between 1 January 2005 and 30 June 2005.

The benefits conferred by the option are not pensionable and the option is not transferable.

Scottish Widows loan capital

At the end of the year, Mr Ross had an interest in £28,394 of Scottish Widows Group Limited floating rate unsecured loan notes 2008 (2001: £43,194).

Non-beneficial interests

Directors had non-beneficial interests as follows:

1. Mr Daniels, Mr Ellwood, Mr Fairey, Mr Hampton, Mr Kane, Mr Moore, Mr Pritchard, Mr Ross and Mr van den Bergh together with some 80,000 other employees, were potential beneficiaries in the 1,721,503 and 1,684,041 shares held at the end of the year by the Lloyds TSB qualifying employee share ownership trust and the Lloyds TSB Group employee share ownership trust, respectively. 2,417,245 and 1,952,179 shares, respectively, were held by these trusts at the beginning of the year. These holdings were 1,487,696 and 1,677,280, respectively, on 13 February 2003.
2. At the beginning and end of the year, Mr Ellwood also had a non-beneficial interest in 7,000 shares held in another trust.

None of those who were directors at the end of the year had any other interest in the capital of the Company or its subsidiaries and there were no changes in their beneficial interests between 31 December 2002 and 13 February 2003.

The register of directors' interests, which is open to inspection, contains full particulars of directors' shareholdings and options to acquire shares in the Company.

On behalf of the board

A J Michie
Secretary

13 February 2003

Corporate governance

The UK listing authority's rules require companies to make statements on corporate governance in their annual reports. The following comments are, therefore, included to comply with these rules.

Corporate governance principles

The board considers that good governance is central to achieving the Group's governing objective of maximising shareholder value. That has been uppermost in directors' minds when applying the governance principles contained in the code annexed to the UK listing authority's listing rules.

The following remarks demonstrate how the board has applied these principles.

The information on pages 44 and 45 shows that the Company is led and controlled by a board comprising executive and non-executive directors with wide experience. The appointment of directors is considered by the board and, following the provisions in the articles of association, they must retire by rotation, and may stand for re-election by the shareholders, at least every three years.

The board meets nine times a year and a programme is prepared and agreed each year, which ensures that the directors are able regularly to review corporate strategy and the operations and results of the business units in the Group and to discharge their other duties. The roles of the chairman, the group chief executive and the board and its governance arrangements are reviewed annually.

The board has a chairman's committee, comprising the chairman, the deputy chairman, the group chief executive and his deputy. The chairman's committee meets to discuss current issues and strategy, examine and test proposals and prepare for board meetings. It also has specific powers delegated to it by the board from time to time.

The board has audit, nomination and remuneration committees which comply with the provisions of the code.

Information about directors' remuneration is given in the directors' remuneration report on pages 48 to 54 and details of how the board reviews financial and operational controls and risk management generally are shown on page 56 and in the financial review on pages 10 to 41.

The chairman, the group chief executive and the group finance director have meetings with representatives of institutional shareholders and all shareholders are encouraged to participate in the Company's annual general meeting.

Compliance with the code

The directors believe that the Company complies with the provisions of the code and that it has complied throughout the year with the provisions where the requirements are of a continuing nature.

Directors' responsibilities

The directors are required by the Companies Act 1985 to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company and the Group as at the end of the year and of the profit or loss for the year. Following discussions with the auditors, the directors consider that in preparing the financial statements on pages 58 to 92, the Company has used appropriate accounting policies, consistently applied and supported by reasonable and prudent judgements and estimates, and that all accounting standards which they consider applicable have been followed.

The directors have responsibility for ensuring that the Company keeps accounting records which disclose with reasonable accuracy the financial position of the Company and which enable them to ensure that the financial statements comply with the Companies Act 1985. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

Going concern

The directors are satisfied that the Company and the Group have adequate resources to continue to operate for the foreseeable future and are financially sound. For this reason, they continue to adopt the going concern basis in preparing the accounts.

Internal control

The board of directors is responsible for the Group's system of internal control, which is designed to ensure effective and efficient operations, internal control, including financial reporting, and compliance with laws and regulations. It should be noted, however, that such a system is designed to manage, rather than eliminate, the risk of failure to achieve business objectives. In establishing and reviewing the system of internal control the directors have regard to the materiality of relevant risks, the likelihood of a loss being incurred and the costs of control. It follows, therefore, that the system of internal control can only provide reasonable but not absolute assurance against the risk of material loss.

The directors and senior management of the Group are committed to maintaining a control-conscious culture across all areas of operation. This is communicated to all employees by way of procedures manuals and regular management briefings. Key business risks are identified, and these are controlled by means of procedures such as physical controls, credit, trading and other authorisation limits and segregation of duties. There are well established budgeting and forecasting procedures in place and reports are presented regularly to the board detailing the results of each principal business unit, variances against budget and prior year, and other performance data. Internal controls contain procedures which assist the board in identifying new and emerging risks.

The effectiveness of the internal control system is reviewed regularly by the board and the audit committee, which also receives reports of reviews undertaken around the Group by the Group's risk management function, including Group Audit and Group Compliance. The audit committee receives reports from the Company's auditors, PricewaterhouseCoopers LLP, (which include details of significant internal control matters that they have identified) and has a discussion with the auditors at least once a year without executives present, to ensure that there are no unresolved issues of concern.

The audit committee reviews the objectivity and independence of the auditors and monitors any non-audit work undertaken by them. Steps have also been taken to ensure that the auditors do not perform any management consultancy work for the Group. However, in certain circumstances, PricewaterhouseCoopers LLP undertake work which is not specifically related to the statutory or regulatory audits, but only where there is clear evidence that their experience with the Group would be key and valuable and in these cases any significant engagement is subject to approval by the audit committee.

Independent auditors' report

To the members of Lloyds TSB Group plc

We have audited the financial statements which comprise the consolidated profit and loss account, the consolidated balance sheet, the Company balance sheet, the consolidated cash flow statement, the statement of total recognised gains and losses and the related notes which have been prepared under the accounting policies set out on pages 64 to 67. We have also audited the disclosures required by Part 3 of Schedule 7A to the Companies Act 1985 contained in the directors' remuneration report under the headings reward package, directors' emoluments, directors' pensions and directors' interests ('the auditable part').

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the annual report and the financial statements in accordance with applicable United Kingdom law and accounting standards are set out in the statement of directors' responsibilities on page 55. The directors are also responsible for preparing the directors' remuneration report.

Our responsibility is to audit the financial statements and the auditable part of the directors' remuneration report in accordance with relevant legal and regulatory requirements and United Kingdom Auditing Standards issued by the Auditing Practices Board. Our report, including the opinion, has been prepared for and only for the Company's members as a body in accordance with Section 235 of the United Kingdom Companies Act 1985 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or in to whose hands it may come save where expressly agreed by our prior consent in writing.

We report to you our opinion, as to whether the financial statements give a true and fair view and are properly prepared in accordance with the United Kingdom Companies Act 1985. We also report to you if, in our opinion, the directors' report is not consistent with the financial statements, if the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and transactions is not disclosed.

We read the other information contained in the annual report and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. The other information comprises only the directors' report, the chairman's statement, the group chief executive's review, the financial review, the remainder of the directors' remuneration report and the corporate governance statement.

We review whether the corporate governance statement on pages 55 and 56 reflects the Company's compliance with the seven provisions of the Combined Code specified for our review by the Listing Rules of the Financial Services Authority, and we report if it does not. We are not required to consider whether the board's statements on internal control cover all risks and controls, or to form an opinion on the effectiveness of the Company's or Group's corporate governance procedures or its risk and control procedures.

Basis of audit opinion

We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements and the auditable part of the directors' remuneration report. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Company's and the Group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements and the auditable part of the directors' remuneration report are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In our opinion:

• the financial statements give a true and fair view of the state of affairs of the Company and the Group as at 31 December 2002 and of the profit and cash flows of the Group for the year then ended;

• the financial statements have been properly prepared in accordance with the Companies Act 1985; and

• those parts of the directors' remuneration report required by Part 3 of Schedule 7A to the Companies Act 1985 have been properly prepared in accordance with the Companies Act 1985.

PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors
Southampton

13 February 2003

Consolidated
profit and loss account

for the year ended 31 December 2002

	Note	**2002 £ million**	2001* £ million
Interest receivable:			
Interest receivable and similar income arising from debt securities		**567**	530
Other interest receivable and similar income		**9,982**	10,834
Interest payable		**5,378**	6,442
Net interest income		**5,171**	4,922
Other finance income	44	**165**	307
Other income			
Fees and commissions receivable		**3,053**	2,922
Fees and commissions payable		**(645)**	(602)
Dealing profits (before expenses)	3	**188**	233
Income from long-term assurance business	30	**(303)**	(29)
General insurance premium income		**486**	428
Other operating income		**763**	708
		3,542	3,660
Total income		**8,878**	8,889
Operating expenses			
Administrative expenses	4	**4,214**	4,226
Depreciation	24	**642**	511
Amortisation of goodwill	23	**59**	39
Depreciation and amortisation		**701**	550
Total operating expenses		**4,915**	4,776
Trading surplus		**3,963**	4,113
General insurance claims		**229**	174
Provisions for bad and doubtful debts	15		
Specific		**965**	736
General		**64**	11
		1,029	747
Amounts written off fixed asset investments	5	**87**	60
Operating profit		**2,618**	3,132
Income from joint ventures	20	**(11)**	(10)
Profit on sale of businesses	6	**–**	39
Profit on ordinary activities before tax	7	**2,607**	3,161
Tax on profit on ordinary activities	8	**764**	875
Profit on ordinary activities after tax		**1,843**	2,286
Minority interests: equity		**19**	17
: non-equity	40	**43**	40
Profit for the year attributable to shareholders	9	**1,781**	2,229
Dividends	10	**1,908**	1,872
(Loss) profit for the year	42	**(127)**	357
Earnings per share	11	**32.0p**	40.3p
Diluted earnings per share	11	**31.8p**	39.9p

** restated (see note 1)*

Consolidated balance sheet

at 31 December 2002

	Note	**2002 £ million**	2001* £ million
Assets			
Cash and balances at central banks		**1,140**	1,240
Items in course of collection from banks		**1,757**	1,664
Treasury bills and other eligible bills	12	**2,409**	4,412
Loans and advances to banks	13	**17,529**	15,224
Loans and advances to customers		**134,498**	123,059
Non-returnable finance		**(24)**	(124)
	14	**134,474**	122,935
Debt securities	17	**29,314**	24,225
Equity shares	18	**206**	225
Interests in joint ventures:	20		
– share of gross assets		**336**	281
– share of gross liabilities		**(291)**	(242)
		45	39
Intangible fixed assets	23	**2,634**	2,566
Tangible fixed assets	24	**4,096**	3,365
Own shares	27	**18**	23
Other assets	28	**5,263**	4,468
Prepayments and accrued income	29	**2,305**	2,296
Post-retirement benefit asset	44	**–**	356
Long-term assurance business attributable to the shareholder	30	**6,228**	6,366
		207,418	189,404
Long-term assurance assets attributable to policyholders	30	**45,340**	46,389
Total assets		**252,758**	235,793

** restated (see note 1)*

The directors approved the accounts on 13 February 2003.

M A van den Bergh
Chairman

P B Ellwood CBE
Group Chief Executive

P R Hampton
Group Finance Director

Consolidated balance sheet

	Note	2002 £ million	2001* £ million
Liabilities			
Deposits by banks	32	**25,443**	24,310
Customer accounts	33	**116,334**	109,116
Items in course of transmission to banks		**775**	534
Debt securities in issue	34	**30,255**	24,420
Other liabilities	35	**8,289**	6,673
Accruals and deferred income	36	**3,696**	3,563
Post-retirement benefit liability	44	**2,077**	75
Provisions for liabilities and charges:			
Deferred tax	37	**1,317**	1,411
Other provisions for liabilities and charges	38	**361**	292
Subordinated liabilities:			
Undated loan capital	39	**5,496**	4,102
Dated loan capital	39	**4,672**	4,006
Minority interests:			
Equity		**37**	37
Non-equity	40	**694**	509
		731	546
Called-up share capital	41	**1,416**	1,411
Share premium account	42	**1,093**	959
Merger reserve	42	**343**	343
Profit and loss account	42	**5,120**	7,643
Shareholders' funds (equity)		**7,972**	10,356
		207,418	189,404
Long-term assurance liabilities to policyholders	30	**45,340**	46,389
Total liabilities		**252,758**	235,793
Memorandum items	45		
Contingent liabilities:			
Acceptances and endorsements		**1,879**	2,243
Guarantees and assets pledged as collateral security		**5,927**	3,789
Other contingent liabilities		**2,540**	1,931
		10,346	7,963
Commitments		**64,504**	53,342

** restated (see note 1)*

Company balance sheet

at 31 December 2002

	Note	2002 £ million	2001 £ million
Fixed assets			
Investments:			
Shares in group undertakings	21	**9,091**	11,960
Loans to group undertakings	21	**1,723**	759
Own shares	27	**18**	23
		10,832	12,742
Current assets			
Debtors falling due within one year:			
Amounts owed by group undertakings		**1,375**	1,369
Other debtors		**89**	47
Tax recoverable		**11**	29
Cash balances with group undertakings		**250**	114
		1,725	1,559
Current liabilities			
Amounts falling due within one year:			
Amounts owed to group undertakings		**1,801**	1,760
Other creditors		**103**	62
Dividend payable		**1,311**	1,306
Loan capital	39	**14**	–
		3,229	3,128
Net current liabilities		**(1,504)**	(1,569)
Total assets less current liabilities		**9,328**	11,173
Creditors			
Amounts falling due after more than one year:			
Loan capital	39	**1,356**	413
Net assets		**7,972**	10,760
Capital and reserves			
Called-up share capital	41	**1,416**	1,411
Share premium account	42	**1,093**	959
Revaluation reserve	42	**3,025**	5,894
Profit and loss account	42	**2,438**	2,496
Shareholders' funds (equity)		**7,972**	10,760

The directors approved the accounts on 13 February 2003.

M A van den Bergh
Chairman

P B Ellwood CBE
Group Chief Executive

P R Hampton
Group Finance Director

Other statements

Statement of total recognised gains and losses

for the year ended 31 December 2002

	2002 £ million	2001* £ million
Profit attributable to shareholders	**1,781**	2,229
Currency translation differences on foreign currency net investments	**(3)**	(86)
Actuarial losses recognised in post-retirement benefit schemes (note 44)	**(3,299)**	(2,873)
Deferred tax thereon (note 44)	**968**	863
	(2,331)	(2,010)
Total recognised gains and losses relating to the year	**(553)**	133
Prior year adjustment at 1 January 2002 in respect of current year changes in accounting policy (note 1)	**(404)**	–
Prior year adjustment in respect of the adoption of FRS 18	**–**	248
Total gains and losses recognised during the year	**(957)**	381

** restated (see note 1)*

Historical cost profits and losses

for the year ended 31 December 2002

There was no material difference between the results as reported and the results that would have been reported on an unmodified historical cost basis. Accordingly, no note of historical cost profits and losses has been included.

Reconciliation of movements in shareholders' funds

for the year ended 31 December 2002

	2002 £ million	2001* £ million
Profit attributable to shareholders	**1,781**	2,229
Dividends	**(1,908)**	(1,872)
(Loss) profit for the year	**(127)**	357
Currency translation differences on foreign currency net investments	**(3)**	(86)
Actuarial losses recognised in post-retirement benefit schemes	**(2,331)**	(2,010)
Issue of shares	**77**	194
Net decrease in shareholders' funds	**(2,384)**	(1,545)
Shareholders' funds at beginning of year	**10,356**	10,024
Prior year adjustment at 1 January 2001 (note 1)	**–**	1,877
Shareholders' funds at end of year	**7,972**	10,356

** restated (see note 1)*

Consolidated cash flow statement

for the year ended 31 December 2002

	2002 £ million	2001* £ million
Net cash inflow from operating activities (note 48a)	**5,394**	9,927
Dividends received from associated undertakings	**2**	2
Returns on investments and servicing of finance:		
Dividends paid to equity minority interests	**(18)**	(17)
Payments made to non-equity minority interests	**(43)**	(40)
Interest paid on subordinated liabilities (loan capital)	**(463)**	(514)
Interest element of finance lease rental payments	**–**	(1)
Net cash outflow from returns on investments and servicing of finance	**(524)**	(572)
Taxation:		
UK corporation tax	**(758)**	(682)
Overseas tax	**(193)**	(147)
Total taxation	**(951)**	(829)
Capital expenditure and financial investment:		
Additions to fixed asset investments	**(46,830)**	(47,049)
Disposals of fixed asset investments	**45,507**	40,530
Additions to tangible fixed assets	**(1,315)**	(1,157)
Disposals of tangible fixed assets	**359**	285
Capital injections to life fund	**(140)**	(100)
Net cash outflow from capital expenditure and financial investment	**(2,419)**	(7,491)
Acquisitions and disposals:		
Additions to interests in joint ventures	**(21)**	(44)
Acquisition of group undertakings (note 48e)	**(117)**	(180)
Disposal of group undertakings and businesses (note 48g)	**–**	40
Net cash outflow from acquisitions and disposals	**(138)**	(184)
Equity dividends paid	**(1,903)**	(1,738)
Net cash outflow before financing	**(539)**	(885)
Financing:		
Issue of subordinated liabilities (loan capital)	**2,120**	742
Issue of ordinary share capital net of £62 million (2001: £185 million) charge in respect of the QUEST (note 27)	**77**	194
Repayments of subordinated liabilities (loan capital)	**(55)**	(131)
Minority investment in subsidiaries	**167**	–
Capital element of finance lease rental payments	**(4)**	(20)
Net cash inflow from financing	**2,305**	785
Increase (decrease) in cash (note 48c)	**1,766**	(100)

** restated (see note 1)*

Notes to the accounts

1 Accounting policies

Accounting policies are unchanged from 2001, except that:

(i) The Group has implemented the requirements of the Urgent Issues Task Force's Abstract 33 'Obligations in capital instruments'. Following its implementation the Group has reclassified €750 million of Perpetual Capital Securities as undated loan capital and the related cost is included within interest expense. Previously these securities were included within minority interests in the balance sheet and the cost was treated as a minority interest deduction. The effect of this change on the profit and loss account for the year ended 31 December 2002 has been to increase interest payable and reduce non-equity minority interests by £31 million (2001: £22 million); there has been no effect on attributable profit. The effect on the Group's balance sheet at 31 December 2002 has been to increase undated loan capital and reduce non-equity minority interests by £482 million (2001: £451 million).

(ii) The Group has implemented the requirements of Financial Reporting Standard 19 ('FRS 19') 'Deferred Tax'. Following its implementation, the Group makes full provision for deferred tax assets and liabilities arising from timing differences between the recognition of gains and losses in the financial statements and their recognition in a tax computation. Previously provision was only made where it was considered that there was a reasonable probability that a liability or asset would crystallise in the foreseeable future. A prior year adjustment has been made increasing shareholders' funds by £54 million to reflect the revised policy. The effect of this change on the profit and loss account for the year ended 31 December 2002 has been to reduce the tax charge by £29 million (2001: increase the tax charge by £14 million). The effect on the Group's balance sheet at 31 December 2002 has been to reduce the deferred tax liability and increase shareholders' funds by £69 million (2001: £40 million).

(iii) The Group has adopted fully the accounting requirements of Financial Reporting Standard 17 ('FRS 17') 'Retirement Benefits'. FRS 17 replaces Statement of Standard Accounting Practice 24 and the Urgent Issues Task Force's Abstract 6 as the accounting standard dealing with post-retirement benefits. The Group has decided to implement the requirements of FRS 17 in 2002 to coincide with the triennial full actuarial valuations of the Group's pension schemes and because of the significant impact that implementation has on the Group's reported results.

FRS 17 requires the assets of post-retirement defined benefit schemes to be included on the balance sheet together with the related liability to make benefit payments. The profit and loss account includes a charge in respect of the cost of accruing benefits for active employees, benefit improvements and the cost of severances borne by the schemes; the expected return on the schemes' assets is included within other finance income net of a charge in respect of the unwinding of the discount applied to the schemes' liabilities. It also includes a charge in respect of post-retirement healthcare obligations. Under Statement of Standard Accounting Practice 24 the profit and loss account included a charge in respect of the cost of accruing benefits for active employees offset by a credit representing the amortisation of the surplus in the Group's defined benefit pension schemes; a pension prepayment was included in the Group's balance sheet, together with a provision in respect of post-retirement healthcare obligations. A prior year adjustment has been made increasing shareholders' funds by £1,876 million to reflect the revised policy.

The effect of this change on the profit and loss account for the year ended 31 December 2002 has been to introduce other finance income of £165 million (2001: £307 million), and to increase administrative expenses by £323 million (2001: £452 million). Profit before tax has been reduced by £158 million (2001: £145 million). The effect on the Group's balance sheet at 31 December 2002 has been to reflect a net post-retirement benefit liability of £2,077 million (2001: a net post-retirement benefit asset of £356 million and a post-retirement benefit liability of £75 million), to reduce prepayments and accrued income by £928 million (2001: £894 million), to reduce the deferred tax liability by £251 million (2001: £268 million), to reduce other provisions for liabilities and charges by £76 million (2001: £109 million) and to reduce shareholders' funds by £2,678 million (2001: £236 million).

(iv) In December 2001, the Association of British Insurers (ABI) published detailed guidance for the preparation of figures using the achieved profits method of accounting which are published as supplementary financial information accompanying the accounts of most listed insurance companies. The ABI guidance recommends the use of unsmoothed fund values to calculate the value of in-force business. To improve the comparability of the results of the Group's insurance operations with the supplementary financial information published by listed insurers the Group has changed the basis of its embedded value calculations to use unsmoothed fund values; previously the effect of investment fluctuations had been amortised to the profit and loss account over a two year period. A prior year adjustment has been made reducing shareholders' funds by £53 million, to reflect the revised policy.

The effect of this change on the profit and loss account for the year ended 31 December 2002 has been to reduce income from long-term assurance business before tax by £104 million (2001: £222 million). The effect on the Group's balance sheet at 31 December 2002 has been to reduce the value of the long-term assurance business attributable to the shareholder by £281 million (2001: £208 million) and to reduce shareholders' funds by the same amount.

Comparative figures for 2001 have been restated in respect of all of the above changes.

The prior year adjustments in respect of these changes can be summarised as follows:

	Adjustment to shareholders' funds at 1 January 2001 £m	Impact on attributable profit for year ended 31 December 2001 £m	Actuarial losses recognised in post-retirement benefit schemes for year ended 31 December 2001 £m	Adjustment to shareholders' funds at 31 December 2001 £m
FRS 19 Deferred tax (ii)	54	(14)	–	40
FRS 17 Retirement benefits (iii)	1,876	(102)	(2,010)	(236)
ABI guidance (iv)	(53)	(155)	–	(208)
Total	1,877	(271)	(2,010)	(404)

a Accounting convention

The consolidated accounts are prepared under the historical cost convention as modified by the revaluation of debt securities and equity shares held for dealing purposes (see g) and assets held in the long-term assurance business (see o), in compliance with Section 255A, Schedule 9 and other requirements of the Companies Act 1985 except as described below (see c), in accordance with applicable accounting standards, pronouncements of the Urgent Issues Task Force and with the Statements of Recommended Practice issued by the British Bankers' Association and the Finance & Leasing Association. The Group's methodology for calculating embedded value follows the guidance published by the Association of British Insurers for the preparation of figures using the achieved profits method of accounting except that tangible assets attributable to the shareholder are valued at market value. The guidance would require those assets backing capital requirements to be discounted to reflect the cost of encumbered capital, but such a treatment would be inconsistent with the treatment of capital supporting the Group's banking operations. If this treatment had been followed income from long-term assurance business before tax in 2002 would have been slightly improved. Conversely, embedded value would have been some 8 per cent lower given the size of the shareholder capital required to be retained within Scottish Widows under the terms of the demutualisation.

The accounts of the Company are prepared under the historical cost convention as modified by the revaluation of shares in group undertakings (see h), in compliance with Section 226, Schedule 4 and other requirements of the Companies Act 1985 and in accordance with applicable accounting standards and pronouncements of the Urgent Issues Task Force.

1 Accounting policies (continued)

a Accounting convention (continued)

The Group continues to take advantage of the dispensation in the Urgent Issues Task Force's Abstract 17 'Employee Share Schemes' not to apply that Abstract to the Group's Inland Revenue approved SAYE schemes.

b Basis of consolidation

Assets, liabilities and results of group undertakings and joint ventures are included in the consolidated accounts on the basis of accounts made up to 31 December. Entities that do not meet the legal definition of a subsidiary but which give rise to benefits that are in substance no different to those that would arise from subsidiaries are also included in the consolidated accounts. In order to reflect the different nature of the shareholder's and policyholders' interests in the long-term assurance business, the value of long-term assurance business attributable to the shareholder and the assets and liabilities attributable to policyholders are classified under separate headings in the consolidated balance sheet. Details of transactions entered into by the Group which are not eliminated on consolidation are given in note 43.

c Goodwill

Goodwill arising on acquisitions of or by group undertakings is capitalised. For acquisitions prior to 1 January 1998, goodwill was taken direct to reserves in the year of acquisition. As permitted by the transitional arrangements of Financial Reporting Standard 10, this goodwill was not reinstated when the Group adopted the standard in 1998.

The useful economic life of the goodwill arising on each acquisition is determined at the time of the acquisition. The directors consider that it is appropriate to assign an indefinite life to the goodwill which arose on the acquisition of Scottish Widows during 2000 in view of the strength of the Scottish Widows brand, developed through over 185 years of trading, and the position of the business as one of the leading providers of life, pensions, unit trust and fund management products. Both of these attributes are deemed to have indefinite durability, which has been determined based on the following factors: the nature of the business; the typical lifespans of the products; the extent to which the acquisition overcomes market entry barriers; and the expected future impact of competition on the business.

The Scottish Widows goodwill is not being amortised through the profit and loss account; however, it is subjected to annual impairment reviews in accordance with Financial Reporting Standard 11. Impairment of the goodwill is evaluated by comparing the present value of the expected future cash flows, excluding financing and tax, (the 'value-in-use') to the carrying value of the underlying net assets and goodwill. If the net assets and goodwill were to exceed the value-in-use, an impairment would be deemed to have occurred and the resulting write-down in the goodwill would be charged to the profit and loss account immediately.

Paragraph 28 of Schedule 9 to the Companies Act 1985 requires that all goodwill carried on the balance sheet should be amortised. In the case of the goodwill arising on the acquisition of Scottish Widows, the directors consider that it is appropriate to depart from this requirement in order to comply with the over-riding requirement for the accounts to show a true and fair view. If this goodwill was amortised over a period of 20 years, profit before tax for the year ended 31 December 2002 would be £93 million lower (2001: £94 million lower), with a corresponding reduction in reserves of £265 million (2001: £172 million); intangible assets on the balance sheet would also be £265 million lower (2001: £172 million lower).

Goodwill arising on all other acquisitions after 1 January 1998 is amortised on a straight line basis over its estimated useful economic life, which does not exceed 20 years.

At the date of the disposal of group or associated undertakings, any unamortised goodwill, or goodwill taken directly to reserves prior to 1 January 1998, is included in the Group's share of the net assets of the undertaking in the calculation of the profit or loss on disposal.

d Income recognition

Interest income is recognised in the profit and loss account as it accrues, with the exception of interest on non-performing lending which is taken to income either when it is received or when there ceases to be any significant doubt about its ultimate receipt (see e).

Fees and commissions receivable from customers to reimburse the Group for costs incurred are taken to income when due. Fees and commissions relating to the ongoing provision of a service or risk borne for a customer are taken to income in proportion to the service provided or risk borne in each accounting period. Fees and commissions charged in lieu of interest are taken to income on a level yield basis over the period of the loan. Other fees and commissions receivable are accounted for as they fall due.

e Provisions for bad and doubtful debts and non-performing lending

Provisions for bad and doubtful debts

It is the Group's policy to make provisions for bad and doubtful debts, by way of a charge to the profit and loss account, to reflect the losses inherent in the loan portfolio at the balance sheet date. There are two types of provision, specific and general, and these are discussed further below.

Specific provisions

Specific provisions relate to identified risk advances and are raised when the Group considers that recovery of the whole of the outstanding balance is in serious doubt. The amount of the provision is equivalent to the amount necessary to reduce the carrying value of the advance to its expected ultimate net realisable value.

For the Group's portfolios of smaller balance homogeneous loans, such as the residential mortgage, personal lending and credit card portfolios, specific provisions are calculated using a formulae driven approach. These formulae take into account factors such as the length of time that payments from the customer are overdue, the value of any collateral held and the level of past and expected losses, in order to derive an appropriate provision.

For the Group's other lending portfolios, specific provisions are calculated on a case-by-case basis. In establishing an appropriate provision, factors such as the financial condition of the customer, the nature and value of any collateral held and the costs associated with obtaining repayment and realisation of the collateral are taken into consideration.

General provisions

General provisions are raised to cover latent bad and doubtful debts which are present in any portfolio of advances but have not been specifically identified. The Group holds general provisions against each of its principal lending portfolios, which are calculated after having regard to a number of factors; in particular, the level of watchlist or potential problem debt, the observed propensity for such debt to deteriorate and become impaired and prior period loss rates. The level of general provision held is reviewed on a regular basis to ensure that it remains appropriate in the context of the perceived risk inherent in the related portfolio and the prevailing economic climate.

Non-performing lending

An advance becomes non-performing when interest ceases to be credited to the profit and loss account. There are two types of non-performing lending which are discussed further below.

Accruing loans on which interest is being placed in suspense

Where the customer continues to operate the account, but where there is doubt about the payment of interest, interest continues to be charged to the customer's account, but it is not applied to income. Interest is placed on a suspense account and only taken to income if there ceases to be significant doubt about its being paid.

Loans accounted for on a non-accrual basis

In those cases where the operation of the customer's account has ceased and it has been transferred to a specialist recovery department, the

1 Accounting policies (continued)

e Provisions for bad and doubtful debts and non-performing lending (continued)

advance is written down to its estimated realisable value and interest is no longer charged to the customer's account as its recovery is considered unlikely. Interest is only taken to income if it is received.

f Mortgage incentives

Payments made under cash gift and discount mortgage schemes, which are recoverable from the customer in the event of early redemption, are amortised as an adjustment to net interest income over the early redemption charge period. Payments cease to be deferred and are charged to the profit and loss account in the event that the related loan is redeemed or becomes impaired.

g Debt securities and equity shares

Debt securities, apart from those held for dealing purposes, are stated at cost as adjusted for the amortisation of any premiums and discounts arising on acquisition, which are amortised from purchase to maturity in equal annual instalments, less amounts written off for any permanent diminution in their value. Equity shares, apart from those held for dealing purposes, are stated at cost less amounts written off for any permanent diminution in their value.

Debt securities and equity shares held for dealing purposes are included at market value. In rare circumstances where securities are transferred from dealing portfolios to investment portfolios or vice versa, the transfer is effected at an amount based on the market value at the date of transfer. Any resulting profit or loss is reflected in the profit and loss account.

h Shares in group undertakings

Shares in group undertakings are stated in the balance sheet of the Company at its share of net assets, with the exception of the life assurance group undertakings which are stated on the basis described in o. Attributable goodwill is included, where this has not been written-off directly to reserves.

i Tangible fixed assets

Tangible fixed assets are included at cost less depreciation.

Land is not depreciated. Leasehold premises with unexpired lease terms of 50 years or less are depreciated by equal annual instalments over the remaining period of the lease. Freehold and long leasehold buildings are depreciated over 50 years. The costs of adapting premises for the use of the Group are separately identified and depreciated over 10 years, or over the term of the lease if less; such costs are included within premises in the balance sheet total of tangible fixed assets.

Equipment is depreciated by equal annual instalments over the estimated useful lives of the assets, which for fixtures and furnishings are 10-20 years and for computer hardware, operating software and application software and the related development costs relating to separable new systems, motor vehicles and other equipment are 3-8 years.

Premises and equipment held for letting to customers under operating leases are depreciated over the life of the lease to give a constant rate of return on the net investment, taking into account anticipated residual values. Anticipated residual values are reviewed regularly and any impairments identified are charged to the profit and loss account.

j Vacant leasehold property

When a leasehold property ceases to be used in the business or a commitment is entered into which would cause this to occur, provision is made to the extent that the recoverable amount of the interest in the property is expected to be insufficient to cover future obligations relating to the lease.

k Leasing and instalment credit transactions

Assets leased to customers are classified as finance leases if the lease agreements transfer substantially all of the risks and rewards of ownership to the lessee; all other leases are classified as operating leases.

Income from both finance and operating leases is credited to the profit and loss account in proportion to the net cash invested so as to give a constant rate of return over each period after taking account of tax. Income from instalment credit transactions is credited to the profit and loss account using the sum of the digits method.

In those cases where the Group is the lessee, operating lease costs are charged to the profit and loss account in equal annual instalments over the life of the lease.

l Deferred tax

Full provision is made for deferred tax liabilities arising from timing differences between the recognition of gains and losses in the financial statements and their recognition in a tax computation. Deferred tax assets are recognised to the extent that it is regarded as more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted, or where they can be offset against deferred tax liabilities. Deferred tax is measured at the average tax rates that are expected to apply in the periods in which the timing differences are expected to reverse, based on tax rates and laws that have been enacted or substantively enacted by the balance sheet date.

m Pensions and other post-retirement benefits

The Group operates a number of defined benefit pension and post-retirement healthcare schemes, and a number of employees are members of defined contribution pension schemes.

Full actuarial valuations of the Group's main defined benefit schemes are carried out every three years with interim reviews in the intervening years; these valuations are updated to 31 December each year by qualified independent actuaries. For the purposes of these annual updates, scheme assets are included at market value and scheme liabilities are measured on an actuarial basis using the projected unit method; these liabilities are discounted at the current rate of return on a high quality corporate bond of equivalent currency and term. The post-retirement benefit surplus or deficit is included on the Group's balance sheet, net of the related amount of deferred tax. Surpluses are only included to the extent that they are recoverable through reduced contributions in the future or through refunds from the schemes. The current service cost and any past service costs are included in the profit and loss account within operating expenses and the expected return on the schemes' assets, net of the impact of the unwinding of the discount on scheme liabilities, is included within other finance income. Actuarial gains and losses, including differences between the expected and actual return on scheme assets, are recognised, net of the related deferred tax, in the statement of total recognised gains and losses.

The costs of the Group's defined contribution pension schemes are charged to the profit and loss account in the period in which they fall due.

n Foreign currency translation

Assets, liabilities and results in foreign currencies are expressed in sterling at the rates of exchange ruling on the dates of the respective balance sheets. Exchange adjustments on the translation of opening net assets held overseas are taken direct to reserves. All other exchange profits or losses, which arise from normal trading activities, are included in the profit and loss account.

o Long-term assurance business

A number of the Group's subsidiary undertakings are engaged in writing long-term assurance business, including the provision of life assurance, pensions, annuities and permanent health insurance contracts. In common with other life assurance companies in the UK, these companies are structured into one or more long-term business funds, depending upon the nature of the products being written, and a shareholder's fund. All premiums received, investment returns, claims and expenses, and changes in liabilities to policyholders are accounted for within the related long-term business fund. Any surplus, which is determined annually by the Appointed Actuary after taking account of these items, may either be distributed between the shareholder and the policyholders according to a predetermined formula or retained within the long-term business fund. The shareholder will also levy investment management and administration charges upon the long-term business fund.

1 Accounting policies (continued)

o Long-term assurance business (continued)

The Group accounts for its interest in long-term assurance business using the embedded value basis of accounting, in common with other UK banks with insurance subsidiaries. The value of the shareholder's interest in the long-term assurance business ('the embedded value') included in the Group's balance sheet is an actuarially determined estimate of the economic value of the Group's life assurance subsidiaries, excluding any value which may be attributed to future new business. The embedded value is comprised of the net tangible assets of the life assurance subsidiaries, including any surplus retained within the long-term business funds, which could be transferred to shareholder, and the present value of the in-force business. The value of the in-force business is calculated by projecting the future surpluses and other net cash flows attributable to the shareholder arising from business written by the balance sheet date, using appropriate economic and actuarial assumptions, and discounting the result at a rate which reflects the shareholder's overall risk premium attributable to this business.

Changes in the embedded value, which are determined on a post-tax basis, are included in the profit and loss account. For the purpose of presentation, the change in this value is grossed up at the underlying rate of corporation tax.

The assets held within the long-term business funds are legally owned by the life assurance companies, however the shareholder will only benefit from ownership of these assets to the extent that surpluses are declared or from other cash flows attributable to the shareholder. Reflecting the different nature of these assets, they are classified separately on the Group's balance sheet as 'Long-term assurance assets attributable to policyholders', with a corresponding liability to the policyholders also shown. Investments held within the long-term business funds are included on the following basis: equity shares, debt securities and unit trusts held for unit linked funds are valued in accordance with policy conditions at market prices; other equity shares and debt securities are valued at middle market price and other unit trusts at bid price; investment properties are included at valuation by independent valuers at existing use value at the balance sheet date, and mortgages and loans are at cost less amounts written off.

p General insurance business

The Group both underwrites and acts as intermediary in the sale of general insurance products. Underwriting premiums are included, net of refunds, in the period in which insurance cover is provided to the customer; premiums received relating to future periods are deferred and only credited to the profit and loss account when earned. Where the Group acts as intermediary, commission income is included in the profit and loss account at the time that the underwriter accepts the risk of providing insurance cover to the customer. Where appropriate, provision is made for the effect of future policy terminations based upon past experience.

The underwriting business makes provision for the estimated cost of claims notified but not settled and claims incurred but not reported at the balance sheet date. The provision for the cost of claims notified but not settled is based upon a best estimate of the cost of settling the outstanding claims after taking into account all known facts. In those cases where there is insufficient information to determine the required provision, statistical techniques are used which take into account the cost of claims that have recently been settled and make assumptions about the future development of the outstanding cases. Similar statistical techniques are used to determine the provision for claims incurred but not reported at the balance sheet date. Claims equalisation provisions are calculated in accordance with the relevant legislative requirements.

q Derivatives

Derivatives are used in the Group's trading activities to meet the financial needs of customers, for proprietary purposes and to manage risk in the Group's trading portfolios. Such instruments include exchange rate forwards and futures, currency swaps and options together with interest rate swaps, forward rate agreements, interest rate options and futures. These derivatives are carried at fair value and all changes in fair value are reported within dealing profits in the profit and loss account. Fair values are normally determined by reference to quoted market prices; internal models are used to determine fair value in instances where no market price is available. The unrealised gains and losses on trading derivatives are included within other assets and other liabilities respectively. These items are reported gross except in instances where the Group has entered into legally binding netting agreements, where the Group has a right to insist on net settlement that would survive the insolvency of the counterparty; in these cases the positive and negative fair values of trading derivatives with the relevant counterparties are offset within the balance sheet totals.

Derivatives used in the Group's non-trading activities are taken out to reduce exposures to fluctuations in interest and exchange rates and include exchange rate forwards and futures, currency swaps together with interest rate swaps, forward rate agreements and options. These derivatives are accounted for in the same way as the underlying items which they are hedging. Interest receipts and payments on hedging interest derivatives are included in the profit and loss account so as to match the interest payable or receivable on the hedged item.

A derivative will only be classified as a hedge in circumstances where there was evidence of the intention to hedge at the outset of the transaction and the derivative substantially matches or eliminates the risk associated with the exposure being hedged.

Where a hedge transaction is superseded, ceases to be effective or is terminated early the derivative is measured at fair value. Any profit or loss arising is then amortised to the profit and loss account over the remaining life of the item which it was originally hedging. When the underlying asset, liability or position that was being hedged is terminated, the hedging derivative is measured at fair value and any profit or loss arising is recognised immediately.

2 Segmental analysis

	Profit on ordinary activities before tax 2002 £m	2001* £m
Class of business:		
UK Retail Banking and Mortgages	**1,172**	1,205
Insurance and Investments		
Operating profit	**1,231**	1,421
Changes in economic assumptions	**55**	–
Investment variance	**(952)**	(859)
	334	562
Wholesale Markets and International Banking	**1,005**	1,209
Central group items	**96**	185
	2,607	3,161

Operating profit from Insurance and Investments is further analysed as follows:

	2002 £m	2001* £m
Life and pensions	**474**	719
Unit trusts	**1**	41
General insurance	**754**	651
Asset management	**2**	10
	1,231	1,421

The operating profit for the life and pensions business shown above reconciles to the income from long-term assurance business shown in the profit and loss account as follows:

	2002 £m	2001* £m
Life and pensions segmental profit	**474**	719
Changes in economic assumptions	**55**	–
Investment variance relating to the life and pensions business	**(892)**	(813)
Other items	**60**	65
Income from long-term assurance business	**(303)**	(29)

Geographical area:**	Domestic 2002 £m	International 2002 £m	Total 2002 £m
Interest receivable	**8,226**	**2,323**	**10,549**
Other finance income	**165**	**–**	**165**
Fees and commissions receivable	**2,773**	**280**	**3,053**
Dealing profits (before expenses)	**125**	**63**	**188**
Income from long-term assurance business	**(314)**	**11**	**(303)**
General insurance premium income	**486**	**–**	**486**
Other operating income	**552**	**211**	**763**
Total gross income	**12,013**	**2,888**	**14,901**
Profit on ordinary activities before tax	**2,111**	**496**	**2,607**

	Domestic 2001* £m	International 2001 £m	Total 2001* £m
Interest receivable	8,950	2,414	11,364
Other finance income	307	–	307
Fees and commissions receivable	2,636	286	2,922
Dealing profits (before expenses)	138	95	233
Income from long-term assurance business	(41)	12	(29)
General insurance premium income	428	–	428
Other operating income	538	170	708
Total gross income	12,956	2,977	15,933
Profit on ordinary activities before tax	2,595	566	3,161

	Net assets† 2002 £m	Net assets† 2001* £m	Assets‡ 2002 £m	Assets‡ 2001* £m
Class of business:				
UK Retail Banking and Mortgages	**2,541**	2,437	**85,868**	77,982
Insurance and Investments	**6,936**	6,811	**9,161**	9,270
Wholesale Markets and International Banking	**4,925**	4,405	**110,845**	100,777
Central group items	**(6,393)**	(3,260)	**1,544**	1,375
	8,009	10,393	**207,418**	189,404
Geographical area:**				
Domestic	**6,634**	9,319	**177,702**	160,796
International	**1,375**	1,074	**29,716**	28,608
	8,009	10,393	**207,418**	189,404

*2001 figures have been restated to take account of the changes in accounting policy explained in note 1 and the reclassification of emerging markets debt earnings from Wholesale Markets and International Banking to Central group items.

**The geographical distribution of gross income sources, profit on ordinary activities before tax and assets by domestic and international operations is based on the location of the office recording the transaction, except for lending by the international business booked in London.

†Net assets represent shareholders' funds plus equity minority interests. Disclosure of information on net assets is an accounting standard requirement (SSAP25); it is not appropriate to relate it directly to the segmental profits above because the business is not managed by the allocation of net assets to business units.

‡Assets exclude long-term assurance assets attributable to policyholders.

As the business of the Group is mainly that of banking and insurance, no segmental analysis of turnover is given.

3 Dealing profits (before expenses)

	2002 £m	2001 £m
Foreign exchange trading income	**173**	158
Securities and other gains	**15**	75
	188	233

Dealing profits include the profits and losses arising both on the purchase and sale of trading instruments and from the year-end revaluation to market value, together with the interest income earned from these instruments and the related funding cost.

Notes to the accounts

4 Administrative expenses

	2002 £m	2001* £m
Salaries and profit sharing	**2,065**	2,066
Social security costs	**134**	140
Other pension costs (note 44)	**318**	347
Staff costs	**2,517**	2,553
Other administrative expenses	**1,697**	1,673
	4,214	4,226

*restated (see note 1)

The average number of persons on a headcount basis employed by the Group during the year was as follows:

	2002	2001
UK	**71,134**	71,184
Overseas	**11,491**	11,768
	82,625	82,952

The above staff numbers exclude 5,870 (2001: 5,450) staff employed in the long-term assurance business. Costs of £209 million (2001: £168 million) in relation to those staff are reflected in the valuation of the long-term assurance business.

Details of directors' emoluments, pensions and interests are given on pages 51 to 54.

During the year the auditors earned the following fees:

	2002 £m	2001 £m
Statutory audit	**4.8**	4.0
Other audit fees including regulatory reporting	**2.6**	5.5
Due diligence	**0.8**	5.7
Internal control reviews	**0.3**	0.2
Other	**0.2**	0.5
Audit related fees	**1.3**	6.4
Audit and audit related fees	**8.7**	15.9
Tax fees	**0.7**	0.4
Management consultancy fees	**0.1**	3.5
Other fees	**1.0**	1.3
Total fees	**10.5**	21.1

The auditors' remuneration for the holding company was £50,000 (2001: £50,000).

It is the Group's policy to employ the auditors on assignments additional to their statutory audit duties, where their expertise and experience with the Group are important, principally relating to tax advice and due diligence reporting on acquisitions and disposals. Following a change in policy earlier this year, the auditors are no longer permitted to perform management consultancy work on behalf of the Group.

5 Amounts written off fixed asset investments

	2002 £m	2001 £m
Debt securities	**84**	58
Equity shares	**3**	2
	87	60

6 Profit before tax on sale of businesses

On 3 October 2001 the Group announced the sale of its Brazilian fund management and private banking business, including its subsidiary, Lloyds TSB Asset Management S.A. This resulted in a profit on sale of £39 million (tax: £11 million).

7 Profit on ordinary activities before tax

Profit on ordinary activities before tax is stated after taking account of:

	2002 £m	2001* £m
Income from:		
Aggregate amounts receivable, including capital repayments, in respect of assets leased to customers and banks under:		
Finance leases and hire purchase contracts	**3,290**	3,250
Operating leases	**440**	329
Profit less losses on disposal of investment securities	**160**	160
Charges:		
Rental of premises	**220**	203
Hire of equipment	**18**	18
Interest on subordinated liabilities (loan capital)	**537**	515

*restated (see note 1)

8 Tax on profit on ordinary activities

a Analysis of charge for the year

	2002 £m	2001* £m
UK corporation tax		
Current tax on profits for the year	**784**	769
Adjustments in respect of prior years	**12**	(14)
	796	755
Double taxation relief	**(129)**	(87)
	667	668
Foreign tax		
Current tax on profits for the year	**216**	179
Adjustments in respect of prior years	**(15)**	(17)
	201	162
Current tax charge	**868**	830
Deferred tax	**(106)**	44
Associated undertakings and joint ventures	**2**	1
	764	875

*restated (see note 1)

The charge for tax on the profit for the year is based on a UK corporation tax rate of 30 per cent (2001: 30 per cent).

In addition to the tax charge in the profit and loss account detailed above, £968 million (2001: £863 million) of deferred tax has been credited to the statement of total recognised gains and losses in respect of actuarial losses recognised in post-retirement benefit schemes (note 44).

Notes to the accounts

8 Tax on profit on ordinary activities (continued)

b Factors affecting the tax charge for the year

A reconciliation of the charge that would result from applying the standard UK corporation tax rate to profit before tax to the current tax charge and total tax charge for the year is given below:

	2002 £m	2001 £m
Profit on ordinary activities before tax	**2,607**	3,161
Tax charge thereon at UK corporation tax rate of 30%	**782**	948
Factors affecting charge:		
Goodwill amortisation	**9**	8
Overseas tax rate differences	**24**	12
Non-allowable and non-taxable items	**(28)**	8
Gains exempted or covered by capital losses	**(23)**	(39)
Tax deductible coupons on non-equity minority interests	**(12)**	(12)
Payments to employee trust	**(20)**	(60)
Capital allowances in excess of depreciation	**7**	(48)
Other timing differences	**99**	4
Life companies rate differences	**44**	21
Other items	**(14)**	(12)
Current tax charge	**868**	830
Deferred tax		
– capital allowances in excess of depreciation	**(7)**	48
– other timing differences	**(99)**	(4)
Associated undertakings and joint ventures	**2**	1
Tax on profit on ordinary activities	**764**	875
Effective rate	**29.3%**	27.7%

c Factors that may affect the future tax charge

The current tax charge includes a credit of £46 million (2001: charge of £11 million) in respect of notional tax on the shareholder's interest in the movement in value of the long-term assurance business. Since this derives from the use of a combination of tax rates it can give rise to a higher or lower charge compared to an expected 30 per cent rate, depending upon the reported investment returns.

Following Government changes recently announced in respect of employee benefit trusts the future benefit to the tax charge from this source will be less.

In December 2002 the Inland Revenue announced its intention to introduce legislation which may affect the tax treatment of certain transfers from Scottish Widows plc's long term business fund to its shareholder's fund. The precise impact of these proposals is yet to be determined, however it is possible that these transfers will be subject to a higher tax charge than was previously anticipated.

Factors that may affect the future deferred tax charge are dealt with in Note 37.

9 Profit for the financial year attributable to shareholders

The profit attributable to shareholders includes a profit of £1,912 million (2001: £1,893 million) dealt with in the accounts of the parent company, for which no profit and loss account is shown as permitted by Section 230 of the Companies Act 1985.

10 Ordinary dividends

	2002 pence per share	2001 pence per share	2002 £m	2001 £m
Interim: paid	**10.7**	10.2	**597**	566
Final: proposed	**23.5**	23.5	**1,311**	1,306
	34.2	33.7	**1,908**	1,872

11 Earnings per share

	2002	2001*
Profit attributable to shareholders†	**£1,781m**	£2,229m
Weighted average number of ordinary shares in issue during the year††	**5,570m**	5,533m
Dilutive effect of options outstanding	**27m**	50m
Diluted weighted average number of ordinary shares in issue during the year	**5,597m**	5,583m
Earnings per share	**32.0p**	40.3p
Diluted earnings per share	**31.8p**	39.9p

*restated (see note 1)

†No adjustment was made to profit attributable to shareholders in calculating diluted earnings per share.

††The weighted average number of shares for the year has been calculated after deducting 5 million (2001: 15 million) ordinary shares held by Lloyds TSB Group Holdings (Jersey) Limited and the trustees of the TSB Group Employee Trust, the Lloyds TSB Group Employee Share Ownership Trust and the Lloyds TSB Qualifying Employee Share Ownership Trust, on which dividends have been waived (note 27).

12 Treasury bills and other eligible bills

	2002 Balance sheet £m	2002 Valuation £m	2001 Balance sheet £m	2001 Valuation £m
Investment securities:				
Treasury bills and similar securities	**257**	**258**	748	748
Other eligible bills	**1,622**	**1,620**	2,034	2,032
	1,879	**1,878**	2,782	2,780
Other securities:				
Treasury bills and similar securities	**530**		1,630	
	2,409		4,412	
Geographical analysis by issuer:				
United Kingdom	**1,726**		2,620	
Latin America	**567**		1,412	
Other	**116**		380	
	2,409		4,412	
Included above:				
Unamortised discounts net of premiums on investment securities	**5**		6	

Notes to the accounts

12 Treasury bills and other eligible bills (continued)

Movements in investment securities comprise:	Cost £m	Premiums and discounts £m	Total £m
At 1 January 2002	**2,777**	**5**	**2,782**
Exchange and other adjustments	**(3)**	**–**	**(3)**
Additions	**30,402**	**–**	**30,402**
Bills sold or matured	**(31,301)**	**(76)**	**(31,377)**
Amortisation of premiums and discounts	**–**	**75**	**75**
At 31 December 2002	**1,875**	**4**	**1,879**

Investment securities are those intended for use on a continuing basis in the activities of the Group and not for dealing purposes.

The difference between the cost of other securities and market value, where the market value is higher than the cost, is not disclosed as its determination is not practicable.

It is expected that tax of £1 million (2001: £1 million) would be recoverable if the investment securities were sold at their year end valuation.

13 Loans and advances to banks

	2002 £m	2001 £m
Lending to banks	**2,212**	1,616
Deposits placed with banks	**15,318**	13,610
Total loans and advances to banks	**17,530**	15,226
Provisions for bad and doubtful debts	**(1)**	(2)
	17,529	15,224
Repayable on demand	**4,313**	2,443
Other loans and advances by residual maturity repayable:		
3 months or less	**8,512**	8,995
1 year or less but over 3 months	**2,624**	2,698
5 years or less but over 1 year	**1,700**	708
Over 5 years	**381**	382
Provisions for bad and doubtful debts	**(1)**	(2)
	17,529	15,224

14 Loans and advances to customers

	2002 £m	2001 £m
Lending to customers	**123,007**	111,541
Hire purchase debtors	**5,990**	5,345
Equipment leased to customers	**7,300**	7,585
Total loans and advances to customers	**136,297**	124,471
Provisions for bad and doubtful debts	**(1,766)**	(1,466)
Interest held in suspense	**(57)**	(70)
	134,474	122,935
Loans and advances by residual maturity repayable:		
3 months or less	**23,989**	21,393
1 year or less but over 3 months	**10,357**	8,867
5 years or less but over 1 year	**30,637**	27,910
Over 5 years	**71,314**	66,301
Provisions for bad and doubtful debts	**(1,766)**	(1,466)
Interest held in suspense	**(57)**	(70)
	134,474	122,935
Of which repayable on demand or at short notice	**11,852**	10,116

The cost of assets acquired during the year for letting to customers under finance leases and hire purchase contracts amounted to £3,752 million (2001: £3,166 million).

Securitisations

Certain instalment credit receivables have been securitised and are subject to non-returnable financing arrangements. In accordance with Financial Reporting Standard 5, these items have been shown under the linked presentation method.

The Group's subsidiary, Black Horse Limited (formerly Chartered Trust plc), entered into transactions whereby it disposed of its interest in portfolios of motor vehicle and caravan instalment credit agreements for a total of £980 million to Cardiff Automobile Receivables Securitisation (UK) No 4 plc (CARS 4). CARS Trustee (UK) No 4 Limited is responsible for the collection and onward payment of all amounts falling due under the terms of the receivables sold to CARS 4. Principal receipts up to 10 December 2000 were used to purchase further receivables; subsequent to this date they are being used to redeem floating rate notes. Income receipts are applied in the following order of priority: interest due on the floating rate notes; credit manager fees; payments under swaps; amounts due to third parties; dividends; and residual income to Black Horse Limited. Black Horse Limited has been appointed by CARS Trustee (UK) No 4 Limited as credit manager and receives a fee for fulfilling this function. It has no liability to the noteholders or any creditor of CARS 4 or CARS Trustee (UK) No 4 Limited other than through failure to meet its obligations as credit manager or for breach of warranties given. Black Horse Limited has no interest in the share capital of CARS 4 or CARS Trustee (UK) No 4 Limited.

Black Horse Limited and CARS 4 have also entered into interest rate swaps in respect of this transaction, the interest rates payable and receivable under these swaps are set by reference to market rates of interest on an arm's length basis.

At 31 December 2002 CARS 4 held £24 million (2001: £124 million) of receivables, matched by non-returnable finance of the same amount.

15 Provisions for bad and doubtful debts and non-performing lending

	2002 Specific £m	2002 General £m	2001 Specific £m	2001 General £m
At 1 January	**1,099**	**369**	1,069	357
Exchange and other adjustments	**(55)**	**(3)**	(15)	1
Adjustments on acquisition	**–**	**3**	–	–
Advances written off	**(878)**	**–**	(885)	–
Recoveries of advances written off in previous years	**203**	**–**	194	–
Charge to profit and loss account:				
New and additional provisions	**1,544**	**64**	1,310	64
Releases and recoveries	**(579)**	**–**	(574)	(53)
	965	**64**	736	11
At 31 December	**1,334**	**433**	1,099	369
	1,767		1,468	

	2002	2001
In respect of:		
Loans and advances to banks	**1**	2
Loans and advances to customers	**1,766**	1,466
	1,767	1,468

Notes to the accounts

15 Provisions for bad and doubtful debts and non-performing lending (continued)

	2002 £m	2001 £m
Non-performing lending comprises:		
Accruing loans on which interest is being placed in suspense	**752**	843
Loans accounted for on a non-accrual basis	**662**	379
	1,414	1,222
Provisions	**(992)**	(829)
Interest held in suspense	**(57)**	(70)
	365	323

16 Concentrations of exposure

	2002 £m	2001 £m
Loans and advances to customers:		
Domestic:		
Agriculture, forestry and fishing	**2,076**	2,074
Manufacturing	**3,373**	3,321
Construction	**1,482**	1,309
Transport, distribution and hotels	**4,696**	4,440
Property companies	**4,008**	2,907
Financial, business and other services	**8,352**	8,736
Personal: mortgages	**62,467**	56,578
: other	**14,931**	12,784
Lease financing	**7,285**	7,552
Hire purchase	**5,990**	5,345
Other	**3,397**	2,992
Total domestic	**118,057**	108,038
International:		
Latin America	**1,591**	2,347
New Zealand	**10,447**	8,435
Rest of the world	**6,202**	5,651
Total international	**18,240**	16,433
	136,297	124,471
Provisions for bad and doubtful debts*	**(1,766)**	(1,466)
Interest held in suspense*	**(57)**	(70)
	134,474	122,935

*Figures exclude provisions and interest held in suspense relating to loans and advances to banks.

The classification of lending as domestic or international is based on the location of the office recording the transaction, except for certain lending of the international business booked in London.

17 Debt securities

	2002 Balance sheet £m	2002 Valuation £m	2001 Balance sheet £m	2001 Valuation £m
Investment securities:				
Government securities	**2,140**	**2,141**	2,781	2,976
Other public sector securities	**1**	**1**	–	–
Bank and building society certificates of deposit	**3,147**	**3,148**	4,670	4,677
Corporate debt securities	**1,495**	**1,496**	613	616
Mortgage backed securities	**893**	**892**	521	527
Other asset backed securities	**2,817**	**2,820**	1,193	1,198
Other debt securities	**1,369**	**1,367**	1,211	1,209
	11,862	**11,865**	10,989	11,203
Other securities:				
Government securities	**6,035**	**6,035**	4,103	4,103
Other public sector securities	**112**	**112**	151	151
Bank and building society certificates of deposit	**340**	**340**	234	234
Corporate debt securities	**7,842**	**7,842**	7,102	7,102
Mortgage backed securities	**1,838**	**1,838**	1,054	1,054
Other asset backed securities	**1,191**	**1,191**	592	592
Other debt securities	**94**	**94**	–	–
	29,314	**29,317**	24,225	24,439
Due within 1 year	**6,412**		6,745	
Due 1 year and over	**22,902**		17,480	
	29,314		24,225	
Geographical analysis by issuer:				
United Kingdom	**5,569**		5,947	
Other European	**13,254**		9,920	
North America and Caribbean	**6,077**		4,708	
Latin America	**1,231**		1,290	
Asia Pacific	**2,763**		1,921	
Other	**420**		439	
	29,314		24,225	
Unamortised discounts net of premiums on investment securities	**337**		622	
Investment securities:				
Listed	**6,102**	**6,101**	5,544	5,751
Unlisted	**5,760**	**5,764**	5,445	5,452
	11,862	**11,865**	10,989	11,203
Other securities:				
Listed	**16,034**	**16,034**	12,139	12,139
Unlisted	**1,418**	**1,418**	1,097	1,097
	17,452	**17,452**	13,236	13,236

Notes to **the accounts**

17 Debt securities (continued)

Movements in investment securities comprise:

	Cost £m	Premiums and discounts £m	Provisions £m	Total £m
At 1 January 2002	**10,553**	**519**	**83**	**10,989**
Exchange and other adjustments	**(479)**	**(28)**	**(4)**	**(503)**
Additions	**16,418**	**–**	**–**	**16,418**
Transfers to other securities	**(694)**	**(451)**	**(63)**	**(1,082)**
Securities sold or matured	**(13,913)**	**(61)**	**(11)**	**(13,963)**
Charge for the year	**–**	**–**	**84**	**(84)**
Amortisation of premiums and discounts	**–**	**87**	**–**	**87**
At 31 December 2002	**11,885**	**66**	**89**	**11,862**

Investment securities are those intended for use on a continuing basis in the activities of the Group and not for dealing purposes. Transfers to other securities mainly relates to the reclassification of the Group's portfolio of emerging market securities, following the decision to accelerate the disposal programme for these investments.

The difference between the cost of other securities and market value, where the market value is higher than the cost, is not disclosed as its determination is not practicable.

It is expected that tax of £4 million (2001: £60 million) would be payable if the investment securities were sold at their year end valuation.

18 Equity shares

	2002 Balance sheet £m	**2002 Valuation £m**	2001 Balance sheet £m	2001 Valuation £m
Investment securities:				
Listed	**5**	**5**	4	14
Unlisted	**33**	**62**	34	52
	38	**67**	38	66
Other securities:				
Listed	**168**		187	
	206		225	

Movements in investment securities comprise:

	Cost £m	Provisions £m	Total £m
At 1 January 2002	**50**	**12**	**38**
Additions	**10**	**–**	**10**
Disposals	**(9)**	**(2)**	**(7)**
Charge for the year	**–**	**3**	**(3)**
At 31 December 2002	**51**	**13**	**38**

Investment securities are those intended for use on a continuing basis in the activities of the Group and not for dealing purposes.

The difference between the cost of other securities and market value, where the market value is higher than the cost, is not disclosed as its determination is not practicable.

If investment securities were sold at their year end valuation no tax is expected to be payable as any such gains would be covered by available capital losses.

19 Assets transferred under sale and repurchase transactions

Included in the Group's balance sheet are assets subject to sale and repurchase agreements as follows:

	2002 £m	2001 £m
Treasury bills and other eligible bills	**588**	1,036
Debt securities	**5,651**	4,498
	6,239	5,534

These investments have been sold to third parties but, since the Group is committed to reacquire them at a future date and at a predetermined price, they are shown in the balance sheet.

20 Interests in joint ventures

	£m
At 1 January 2002	**39**
Additions	**21**
Share of losses	**(15)**
At 31 December 2002	**45**

The Group's principal investments are in two joint ventures:

	Group interest	Nature of business
iPSL	19.5% of issued ordinary share capital	Cheque processing
Goldfish Holdings Limited	25.0% of issued ordinary share capital	Financial services

During 2002 the Group contributed a further £21 million of capital to Goldfish Holdings Limited.

In the year ended 31 December 2002 £31 million (2001: £27 million) of fees payable to iPSL have been included in the Group's administrative expenses and £6 million (2001: £6 million) of charges to iPSL have been included in the Group's income. The Group has also prepaid £6 million (2001: £8 million) of fees in respect of 2003 and this amount is included in prepayments and accrued income.

In the year ended 31 December 2002 £25 million (2001: £1 million) of interest receivable from Goldfish Bank Limited and £12 million (2001: £22 million) of charges to Goldfish Bank Limited in respect of administrative costs have been included in the Group's income. At 31 December 2002 Goldfish Bank Limited owed £430 million (2001: £611 million) to the Group, which is included in loans and advances to banks. In addition, at 31 December 2002, the Group had made facilities available for Goldfish Bank Limited to borrow a further £420 million (2001: £239 million); these facilities are included in undrawn commitments (note 45).

Included in the gross assets disclosed on the balance sheet is an investment of £8 million (2001: £5 million) in associated undertakings.

Notes to the accounts

21 Interests in group undertakings

	Company Shares £m	Company Loans £m
At 1 January 2002	**11,960**	**759**
Amounts advanced	**–**	**964**
Revaluation	**(2,869)**	**–**
At 31 December 2002	**9,091**	**1,723**

	2002 £m	2001 £m
Shares in banks	**9,093**	11,960
Shares in other group undertakings	**(2)**	–
Total – all unlisted	**9,091**	11,960

On an historical cost basis, shares in group undertakings would have been included at cost of £6,066 million (2001: £6,066 million). No deferred tax provision has been made against the liability which could arise if group undertakings were disposed of at their balance sheet carrying value because of surplus capital losses and the exemptions for disposals of substantial shareholding investments.

The principal group undertakings, all of which have prepared accounts to 31 December and whose results are included in the consolidated accounts of Lloyds TSB Group plc, are:

	Country of registration/ incorporation	Percentage of equity share capital and voting rights held	Nature of business
Lloyds TSB Bank plc	England	100%	Banking and financial services
Cheltenham & Gloucester plc	England	†100%	Mortgage lending and retail investments
Lloyds TSB Commercial Finance Limited	England	†100%	Credit factoring
Lloyds TSB Leasing Limited	England	†100%	Financial leasing
Lloyds TSB Private Banking Limited	England	†100%	Private banking
The Agricultural Mortgage Corporation PLC	England	†100%	Long-term agricultural finance
The National Bank of New Zealand Limited	New Zealand	†100%	Banking and financial services
Lloyds TSB Bank (Jersey) Limited	Jersey	†100%	Banking and financial services
Lloyds TSB Scotland plc	Scotland	†100%	Banking and financial services
Lloyds TSB General Insurance Limited	England	†100%	General insurance
Scottish Widows Investment Partnership Group Limited	England	†100%	Investment management
Abbey Life Assurance Company Limited	England	†100%	Life assurance
Lloyds TSB Insurance Services Limited	England	†100%	Insurance broking
Lloyds TSB Life Assurance Company Limited	England	†100%	Life assurance and other financial services
Lloyds TSB Asset Finance Division Limited	England	†100%	Consumer credit, leasing and related services
Black Horse Limited	England	†100%	Consumer credit, leasing and related services
Scottish Widows plc	Scotland	†100%	Life assurance
Scottish Widows Annuities Limited	Scotland	†100%	Life assurance

†Indirect interest.

The country of registration/incorporation is also the principal area of operation for each of the above group undertakings except as follows:

Lloyds TSB Bank plc operates principally in the UK but also through branches in Argentina, Belgium, Brazil, Dubai, Ecuador, Gibraltar, Guatemala, Hong Kong, Honduras, Japan, Luxembourg, Malaysia, Monaco, Netherlands, Panama, Paraguay, Singapore, Spain, Switzerland, Uruguay, the USA and a representative office in Iran. The National Bank of New Zealand Limited also operates through representative offices in the UK and Hong Kong.

22 Quasi-subsidiaries

The Group has interests in a number of entities which, although they do not meet the legal definition of a subsidiary, give rise to benefits that are in substance no different from those that would arise if those entities were subsidiaries. As a consequence, these entities are consolidated in the same way as if they were subsidiaries.

The primary financial statements of these entities can be summarised as follows:

	Equipment leasing vehicles **2002 £m**	Equipment leasing vehicles 2001 £m	Structured finance vehicles **2002 £m**	Structured finance vehicles 2001 £m
Profit and loss account				
Interest receivable	**–**	–	**12**	–
Interest payable	**(55)**	(41)	**(4)**	–
Other operating income	**80**	58	**–**	–
Total income	**25**	17	**8**	–
Operating expenses	**(24)**	(8)	**–**	–
Profit on ordinary activities before taxation	**1**	9	**8**	–
Tax on profit on ordinary activities	**5**	(6)	**–**	–
Retained profit	**6**	3	**8**	–
Balance sheet				
Assets				
Loans and advances to customers	**–**	–	**329**	–
Tangible fixed assets	**1,307**	911	**–**	–
Other assets and prepayments	**25**	45	**4**	–
Total assets	**1,332**	956	**333**	–
Liabilities				
Deposits by banks	**1,245**	923	**–**	–
Debt securities in issue	**–**	–	**73**	–
Other liabilities and accruals	**77**	29	**2**	–
Shareholders' funds	**10**	4	**258**	–
Total liabilities	**1,332**	956	**333**	–
Cash flow statement				
Net cash inflow (outflow) from operating activities	**422**	391	**(250)**	–

Notes to the accounts

23 Intangible fixed assets

	Cost £m	Amortisation £m	Net book value £m
Goodwill			
At 1 January 2002	**2,640**	**74**	**2,566**
Exchange and other adjustments	**28**	**4**	**24**
Acquisitions (note 47)	**103**	**–**	**103**
Charge for the year	**–**	**59**	**(59)**
At 31 December 2002	**2,771**	**137**	**2,634**

24 Tangible fixed assets

	Premises £m	Equipment £m	Operating lease assets £m
Cost:			
At 1 January 2002	**1,074**	**2,270**	**1,771**
Exchange and other adjustments	**(1)**	**(7)**	**(3)**
Adjustments on acquisition	**31**	**2**	**351**
Additions	**174**	**260**	**881**
Disposals	**(82)**	**(210)**	**(428)**
At 31 December 2002	**1,196**	**2,315**	**2,572**
Depreciation:			
At 1 January 2002	**334**	**1,278**	**138**
Exchange and other adjustments	**(2)**	**1**	**–**
Charge for the year	**64**	**286**	**292**
Disposals	**(19)**	**(170)**	**(215)**
At 31 December 2002	**377**	**1,395**	**215**
Balance sheet amount at 31 December 2002	**819**	**920**	**2,357**
		4,096	
Balance sheet amount at 31 December 2001	740	992	1,633
		3,365	

	2002 £m	2001 £m
Balance sheet amount of premises comprises:		
Freeholds	**414**	436
Leaseholds 50 years and over unexpired	**132**	36
Leaseholds less than 50 years unexpired	**273**	268
	819	740
Land and buildings occupied for own activities	**749**	664

The Group's residual value exposure in respect of operating lease assets, all of which are expected to be disposed of at the end of the lease terms, was as follows:

	2002 £m	2001 £m
Residual value expected to be recovered in:		
1 year or less	**272**	156
2 years or less but over 1 year	**173**	119
5 years or less but over 2 years	**542**	388
Over 5 years	**617**	482
Total exposure	**1,604**	1,145

25 Lease commitments

Annual commitments under non-cancellable operating leases were:

	2002 Premises £m	2002 Equipment £m	2001 Premises £m	2001 Equipment £m
Leases on which the commitment is due to expire in:				
1 year or less	**10**	**2**	7	5
5 years or less but over 1 year	**29**	**1**	33	3
Over 5 years	**188**	**–**	181	–
	227	**3**	221	8

Obligations under finance leases were:

	2002 Equipment £m	2001 Equipment £m
Amounts payable in 1 year or less	**1**	3

26 Capital commitments

Capital expenditure contracted but not provided for at 31 December 2002 amounted to £117 million (2001: £137 million), of which £107 million (2001: £125 million) relates to assets to be leased to customers under operating leases.

27 Own shares

Lloyds TSB Group plc sponsors the Lloyds TSB Group Employee Share Ownership Trust, a discretionary trust for the benefit of employees and former employees of the Lloyds TSB Group. The Company has lent £21 million to the trustees, interest free, to enable them to purchase Lloyds TSB Group plc ordinary shares, which are used to satisfy options granted by the Company or to meet commitments arising under other employee share schemes. Under the terms of the trust, the trustees have waived all but a nominal dividend on the shares they hold. The cost of providing these shares is charged to the profit and loss account on a systematic basis over the period that the employees are expected to benefit. At 31 December 2002, 2 million shares were held by the trustees with a book value of £13 million and a market value of £7 million. (2001: 2 million shares with a book value of £15 million and a market value of £15 million).

The Group has also established the Lloyds TSB Qualifying Employee Share Ownership Trust ('the QUEST') for the purpose of providing shares on the exercise of options under certain of the Group's Save As You Earn (SAYE) share option schemes. During 2002, Lloyds TSB Group plc contributed £66 million to the QUEST, and the trustees subscribed for 18 million shares in the Company for a consideration of £136 million. During 2001, Lloyds TSB Group plc contributed £200 million and the trustees subscribed for 47 million shares for a consideration of £316 million. At 31 December 2002, 2 million shares were held by the QUEST with a book value of £5 million (2001: 2 million shares with a book value of £8 million) reflecting the exercise price of the options the shares are expected to be used to satisfy. Under the terms of the QUEST's trust deed, the trustees have waived all but a nominal dividend on the shares they hold. The difference between the amount contributed by the Company and the movement in the book value of the shares and cash held by the QUEST has been charged to profit and loss account reserves.

27 Own shares (continued)

In addition, a further 0.4 million ordinary shares were held by Lloyds TSB Group Holdings (Jersey) Limited at 31 December 2002 (2001: 0.5 million shares). These shares, on which the dividend entitlement has been waived, were gifted to the Group some years ago at nil cost and are used to satisfy outstanding options or to meet commitments arising under other employee share schemes.

28 Other assets

	2002 £m	2001 £m
Balances arising from derivatives used for trading purposes (note 46a)	**3,428**	2,090
Balances arising from derivatives used for hedging purposes	**778**	931
Settlement balances	**76**	570
Other assets	**981**	877
	5,263	4,468

29 Prepayments and accrued income

	2002 £m	2001* £m
Interest receivable	**931**	843
Deferred expenditure incurred under cash gift and discount mortgage schemes	**201**	256
Other debtors and prepayments	**1,173**	1,197
	2,305	2,296

*restated (see note 1)

30 Long-term assurance business

a Methodology

For the purposes of the Group's consolidated accounts, the value of the shareholder's interest in the long-term assurance business is calculated on an embedded value basis. The embedded value is comprised of the net tangible assets of the life assurance subsidiaries, including any surplus retained in the long-term business funds, which could be transferred to shareholders, and the present value of the in-force business. The value of the in-force business is calculated by projecting future surpluses and other net cash flows attributable to the shareholder arising from business written by the balance sheet date and discounting the result at a rate which reflects the shareholder's overall risk premium attributable to this business.

Surpluses arise following annual actuarial valuations of the long-term business funds, which are carried out in accordance with the statutory requirements designed to ensure and demonstrate the solvency of the funds. Future surpluses will depend upon experience in a number of areas such as investment returns, lapse rates, mortality and administrative expenses. Surpluses can be projected by making realistic assumptions about future experience, having regard to both actual experience and forecast long-term economic trends. Other net cash flows principally comprise annual management charges and other fees levied upon the policyholders by the life assurance subsidiaries.

Changes in the embedded value, which are determined on a post-tax basis, are included in the profit and loss account and described as income from long-term assurance business. For the purpose of presentation the change in this value is grossed up at the underlying rate of corporation tax.

b Analysis of embedded value

The embedded value included in the consolidated balance sheet comprises:

	2002 £m	2001* £m
Net tangible assets of life companies including surplus	**3,324**	3,628
Value of other shareholder's interests in the long-term assurance business	**2,904**	2,738
	6,228	6,366

Movements in the embedded value balance have been as follows:

	2002 £m	2001* £m
At 1 January – as previously reported	**6,366**	6,549
Prior year adjustment (note 1)	**–**	(53)
At 1 January – restated	**6,366**	6,496
Exchange and other adjustments	**(14)**	(35)
Loss after tax	**(257)**	(40)
Capital injection	**140**	100
Dividends	**(7)**	(155)
At 31 December	**6,228**	6,366

*restated (see note 1)

c Analysis of income from long-term assurance business

Income from long-term assurance business included in the profit and loss account can be divided into those items comprising the operating profit of the business and other items. Included within operating profit are the following items:

New business contribution: this represents the value recognised at the end of the year from new business written during the year after taking into account the cost of establishing technical provisions and reserves.

Contribution from existing business: this comprises the following elements:

- The expected return arising from the unwinding of the discount applied to the expected cash flows at the beginning of the year;
- Experience variances caused by the differences between the actual experience during the year and the expected experience;
- The effects of changes in assumptions, other than economic assumptions, and other items;
- Pension provisions (see d); and
- Endowment provision (see e).

Investment earnings: this represents the expected investment return on both the net tangible assets and the value of the shareholder's interest in the long-term business account, based upon the economic assumptions made at the beginning of the year.

Distribution costs: this represents the actual costs of acquiring new business during the year and includes commissions paid to independent financial advisors and other direct sales costs.

Operating profit is adjusted by the following items to arrive at income from long-term assurance business:

Investment variance: this represents (a) the difference between the actual investment return in the year on investments backing shareholder funds and the expected return based upon the economic assumptions made at the beginning of the year; (b) the effect of these fluctuations on the value of in-force business; and (c) other effects of changes in extraneous economic circumstances beyond the control of management.

30 Long-term assurance business (continued)

c Analysis of income from long-term assurance business (continued)

Changes in economic assumptions: this represents the effect of changes in the economic assumptions referred to in g.

Income from long-term assurance business is set out below:

	2002 £m	2001* £m
New business contribution	**413**	374
Contribution from existing business		
– expected return	**312**	348
– experience variances	**(1)**	37
– changes in assumptions and other items	**78**	95
– pension provisions (see d)	**(40)**	(70)
– endowment provision (see e)	**(165)**	–
Investment earnings	**214**	247
Distribution costs	**(277)**	(247)
Operating profit	**534**	784
Investment variance	**(892)**	(813)
Changes in economic assumptions (see g)	**55**	–
Income from long-term assurance business before tax	**(303)**	(29)
Attributed tax	**46**	(11)
Income from long-term assurance business after tax	**(257)**	(40)

*restated (see note 1)

d Pension provisions

During the early 1990s, there was increasing concern that many customers had been given poor advice when they were advised to set up their own personal pension plan and that they would, in fact, have been in a better position if they had remained in, or joined, employer sponsored pension schemes. The regulator of the pension industry (now the responsibility of the Financial Services Authority) carried out an industry wide investigation into the conduct of business involving the transfer of pensions. The conclusion of this investigation was that a large number of customers had been poorly advised, by insurance companies and intermediaries across the industry. As a result of this investigation the regulator established an action plan for the pensions industry to follow in reviewing all cases of possible misselling and determining the necessary compensation. As the review of pension cases in the Group has progressed, provisions have been established for the estimated cost of compensation.

Movements in the provision over the last two years have been as follows:

	2002 £m	2001 £m
At 1 January	**203**	352
Accrual of interest on the provision	**17**	20
Charge for the year	**40**	70
Compensation paid	**(223)**	(238)
Guarantees*	**–**	(1)
At 31 December	**37**	203

*In some cases, rather than pay cash compensation directly into the customer's personal pension plan, the Group has guaranteed to 'top-up' the customer's pension income, on retirement, to the level that they would have received under the relevant occupational scheme.

A review of the adequacy of the provision was carried out as at 31 December 2001. Lower stock market levels had had a significant impact on total redress costs as the cost of restitution into company pension schemes rose as personal pension fund values reduced. As a result of this and the fact that there was greater certainty as to the number and size of compensation claims to be paid, an additional provision of £70 million was made in the Group's results for the year ended 31 December 2001.

The adequacy of the provision has again been reviewed at 31 December 2002, in the light of final experience as to the amount of compensation to be paid. Lower stockmarket levels have increased the final cost of redress and a further provision of £40 million has been made in the year ended 31 December 2002.

e Endowment provision

In common with a number of companies in the life assurance industry, Abbey Life Assurance Company Limited ('Abbey Life'), one of the Group's life assurance subsidiaries, has been carrying out a review of the past sales of certain endowment based and long-term savings products made, primarily in the late 1980s and early 1990s, by the Abbey Life sales force prior to its disposal by the Group in February 2000. The Group has assessed the likely implications for redress to policyholders and as a result a provision of £165 million has been raised.

f Guaranteed annuity options

After an extensive review of its existing practices, carried out in the light of the judgement of the House of Lords in the guaranteed annuities case *Equitable Life vs Hyman*, it was announced that Scottish Widows was revising the way it calculates benefits for guaranteed annuity policies with effect from 1 February 2002. As a result of this change, the terminal bonuses for guaranteed annuity option policies were increased.

Under the terms of the transfer of the Scottish Widows business, a separate memorandum account was created within the With Profits Fund called the Additional Account. This Account had a value at 31 December 2002 of approximately £1.5 billion (2001: £1.7 billion) and is available to meet any additional costs of providing guaranteed benefits on transferred policies, including guaranteed annuity option policies. The assets allocated to the Additional Account include certain hedge assets, to provide protection to the With Profits Fund against the consequences of a future fall in interest rates.

The eventual costs of providing the enhanced benefits is dependent upon a number of factors, including in particular:

- The proportion of policyholders with a guaranteed annuity option policy who choose to exercise their options;
- The effect of future interest rate and mortality trends on the cost of annuities; and
- The future investment performance of the With Profits Funds.

Having considered a range of possible outcomes, the Group currently expects that the most likely outcome is that the balance in the Additional Account available for this purpose will be sufficient to meet the cost of the enhanced benefits payable to the guaranteed annuity option policyholders, as well as other contingencies. The cost of enhanced benefits, currently estimated to be approximately £1.1 billion (2001: £1.4 billion) on a net present value basis, will be paid out over many years as policies mature. In the event that the amount in the Additional Account proves, over time, to be insufficient, the shortfall will be met by the Group. At this time, no provision is considered necessary for such risk.

g Assumptions

Following the publication, in December 2001, of the Association of British Insurers' detailed guidance for the preparation of figures using the achieved profits method of accounting the Group has reviewed the way in which economic assumptions are set for the purposes of the embedded value calculations. The guidance requires that the assumptions should be reviewed at each reporting date. In order to comply with this guidance, and achieve greater comparability with other major insurers, the Group has adopted this approach.

30 Long-term assurance business (continued)

g Assumptions (continued)

The principal economic assumptions have been revised at 31 December 2002 as follows:

	2002 %	2001 %
Risk-adjusted discount rate (net of tax)	**7.35**	8.50
Return on equities (gross of tax)	**7.10**	8.00
Return on fixed interest securities (gross of tax)	**4.50**	5.25
Expenses inflation	**3.30**	3.00

The revised assumptions have resulted in a net credit to the profit and loss account of £55 million.

Other assumptions used to derive the embedded value are as follows:

- Assumed rates of mortality and morbidity are taken from published tables adjusted for demographic differences. Assumptions in respect of lapse rates reflect the recent actual experience of the companies concerned.
- Current tax legislation and rates have been assumed to continue unaltered, except where future changes have been announced. The UK corporation tax rate used for grossing up was 30 per cent (2001: 30 per cent). The normalised investment earnings have been grossed up at a composite longer term tax rate of 17 per cent (2001: 17 per cent).
- The value of the in-force business does not allow for future premiums under recurring single premium business or non-contractual increments, which are included in new business when the premium is received. Department of Social Security rebates have been treated as recurring single premiums.
- Future bonus rates on with-profits business are set at levels which would fully utilise the assets supporting the with-profits business. The proportion of profits derived from with-profits business allocated to the shareholder has been assumed to continue at the current rate of one-ninth of the cost of the bonus.

h Sensitivities

The table below shows the effect on both the embedded value at 31 December 2002 and the new business contribution for the year then ended of theoretical changes in the main economic assumptions.

	Embedded value £m	New business contribution £m
As published	**6,228**	**413**
Effect of a 1% increase in the discount rate	**(152)**	**(27)**
Effect of a 1% reduction in the discount rate	**166**	**32**
Effect of a 1% reduction in the return on equities	**(70)**	**(12)**

i Balance sheet

The long-term assurance assets attributable to policyholders comprise:

	2002 £m	2001* £m
Investments	**47,151**	47,910
Premises and equipment	**45**	16
Other assets	**1,468**	2,091
	48,664	50,017
Net tangible assets of life companies including surplus	**(3,324)**	(3,628)
	45,340	46,389

Investments shown above comprise:

	2002 £m	2001* £m
Fixed interest securities	**14,779**	12,642
Stocks, shares and unit trusts	**24,143**	27,018
Investment properties	**3,623**	3,722
Other properties	**121**	121
Mortgages and loans	**53**	102
Deposits	**4,432**	4,305
	47,151	47,910

	2002 £m	2001* £m
The liabilities to policyholders comprise:		
Technical provisions:		
Long-term business provision (net of reinsurance)	**23,217**	24,129
Claims outstanding (net of reinsurance)	**225**	211
Technical provisions for linked liabilities	**20,996**	21,098
Fund for future appropriations	**12**	75
Other liabilities	**890**	876
	45,340	46,389

*restated (see note 1)

j Disclosures on a modified statutory solvency basis

The individual statutory accounts of the Group's life assurance subsidiaries are prepared under the modified statutory solvency basis, in the same way as the statutory accounts of listed insurance groups in the UK. The principal difference between the modified statutory solvency basis and the embedded value basis used for the preparation of the Group's accounts is that accounts prepared under the modified statutory solvency basis do not reflect the value of in-force business.

Under the modified statutory solvency basis, the results of the Group's long-term life and pensions businesses were as follows:

	2002 £m	2001 £m
Premiums	**5,524**	4,854
Investment income	**1,942**	1,832
Other income	**33**	93
	7,499	6,779
Claims	**(5,031)**	(4,957)
Change in technical provisions	**3,877**	2,759
Expenses	**(720)**	(625)
Realised losses on investments	**(1,790)**	(1,031)
Unrealised losses on investments	**(4,445)**	(4,423)
Other charges	**(3)**	(8)
Tax attributable to long-term business	**200**	280
Transfer from the fund for future appropriations	**63**	1,365
Balance on the technical account – long-term business	**(350)**	139
Tax credit attributable to balance on the technical account – long-term business	**(190)**	(103)
Income in shareholder fund	**35**	38
Expenses in shareholder fund	**(1)**	–
(Loss) profit on ordinary activities before tax	**(506)**	74
Tax on (loss) profit on ordinary activities	**179**	94
(Loss) profit for the financial year	**(327)**	168

30 Long-term assurance business (continued)

j Disclosures on a modified statutory solvency basis (continued)

Income from long-term assurance business after tax reconciles to the loss calculated on a modified statutory solvency basis as follows:

	2002 £m	2001 £m
Income from long-term assurance business attributable to the shareholder after tax	**(257)**	(40)
(Increase) decrease in value-in-force	**(166)**	111
	(423)	71
Other differences:		
– movement in deferred acquisition costs	**45**	(79)
– tax adjustment	**55**	150
– other	**(4)**	26
(Loss) profit for the financial year – modified statutory solvency basis	**(327)**	168

A summarised balance sheet on a modified statutory solvency basis was as follows:

	2002 £m	2001 £m
Assets		
Investments	**26,555**	27,204
Assets held to cover linked liabilities	**20,996**	21,098
Other assets	**1,718**	2,210
Total assets	**49,269**	50,512
Liabilities		
Shareholder's funds	**3,929**	4,123
Fund for future appropriations	**12**	75
Long-term business provision†	**23,217**	24,129
Technical provision for linked liabilities†	**20,996**	21,098
Other creditors	**1,115**	1,087
Total liabilities	**49,269**	50,512

†Net of reinsurers' share of technical provisions

The value of long-term business attributable to the shareholder on an embedded value basis reconciles to the net assets of the Group's life and pensions subsidiaries calculated on a modified statutory solvency basis as follows:

	2002 £m	2001 £m
Long-term assurance business attributable to the shareholder – embedded value basis	**6,228**	6,366
Value of in-force business	**(2,904)**	(2,738)
	3,324	3,628
Other differences:		
– deferred acquisition costs	**430**	385
– tax adjustment	**205**	150
– other adjustments	**(30)**	(40)
Net tangible assets of life operations – modified statutory solvency basis	**3,929**	4,123

31 Assets and liabilities denominated in foreign currencies

	2002 £m	2001* £m
Assets: denominated in sterling	**142,661**	132,812
: denominated in other currencies	**64,757**	56,592
	207,418	189,404
Liabilities: denominated in sterling	**142,641**	132,915
: denominated in other currencies	**64,777**	56,489
	207,418	189,404

*restated (see note 1)

Assets and liabilities exclude long-term assurance assets attributable to policyholders and liabilities to policyholders.

32 Deposits by banks

	2002 £m	2001 £m
Repayable on demand	**8,500**	6,634
Other deposits by banks with agreed maturity dates or periods of notice by residual maturity repayable:		
3 months or less	**14,692**	14,227
1 year or less but over 3 months	**1,634**	2,529
5 years or less but over 1 year	**487**	751
Over 5 years	**130**	169
	25,443	24,310

33 Customer accounts

	2002 £m	2001 £m
Repayable on demand	**87,918**	80,635
Other customer accounts with agreed maturity dates or periods of notice by residual maturity repayable:		
3 months or less	**19,047**	19,902
1 year or less but over 3 months	**3,099**	2,889
5 years or less but over 1 year	**4,140**	3,369
Over 5 years	**2,130**	2,321
	116,334	109,116

34 Debt securities in issue

	2002 £m	2001 £m
Bonds and medium-term notes by residual maturity repayable:		
1 year or less	**437**	589
2 years or less but over 1 year	**443**	178
5 years or less but over 2 years	**746**	405
Over 5 years	**1,659**	928
	3,285	2,100
Other debt securities by residual maturity repayable:		
3 months or less	**19,525**	17,070
1 year or less but over 3 months	**7,174**	4,931
5 years or less but over 1 year	**30**	104
Over 5 years	**241**	215
	26,970	22,320
	30,255	24,420

35 Other liabilities

	2002 £m	2001 £m
Balances arising from derivatives used for trading purposes (note 46a)	**4,462**	2,288
Balances arising from derivatives used for hedging purposes	**611**	475
Current tax	**528**	598
Dividends	**1,311**	1,306
Settlement balances	**49**	542
Other liabilities	**1,328**	1,464
	8,289	6,673

36 Accruals and deferred income

	2002 £m	2001 £m
Interest payable	**1,385**	1,310
Other creditors and accruals	**2,311**	2,253
	3,696	3,563

37 Deferred tax

	2002 £m	2001* £m
Short-term timing differences	**(353)**	(271)
Accelerated depreciation allowances	**1,670**	1,682
	1,317	1,411

	£m
At 1 January 2002 – as previously reported	**1,719**
Prior year adjustment (note 1)	**(308)**
At 1 January 2002 – restated	**1,411**
Exchange and other adjustments	**25**
Adjustments on acquisition	**(13)**
Tax provided	**(106)**
At 31 December 2002	**1,317**

*restated (see note 1)

Deferred tax is recognised in respect of the retained earnings of overseas subsidiaries and associates only to the extent that, at the balance sheet date, dividends have been accrued as receivable or a binding agreement to distribute past earnings in future has been entered into. Deferred tax balances have not been discounted.

The deferred tax balance at 31 December 2002 does not include any amounts in respect of the Group's post-retirement benefit liability which is shown on the balance sheet after deduction of a deferred tax asset of £854 million (2001: a net post-retirement benefit asset of £281 million after deduction of a deferred tax liability of £152 million) (note 44).

38 Other provisions for liabilities and charges

	Pension obligations £m	Insurance provisions £m	Post-retirement healthcare £m	Vacant leasehold property and other £m	Total £m
At 1 January 2002 – as previously reported	**34**	**204**	**75**	**88**	**401**
Prior year adjustment (note 1)	**(34)**	**–**	**(75)**	**–**	**(109)**
At 1 January 2002 – restated	**–**	**204**	**–**	**88**	**292**
Exchange and other adjustments	**–**	**(2)**	**–**	**–**	**(2)**
Provisions applied	**–**	**(210)**	**–**	**(40)**	**(250)**
Charge for the year	**–**	**233**	**–**	**88**	**321**
At 31 December 2002	**–**	**225**	**–**	**136**	**361**

Insurance provisions
The Group's general insurance subsidiary maintains provisions for outstanding claims which represent the ultimate cost of settling all claims arising from events which have occurred up to the balance sheet date and these include provisions for the cost of claims notified but not settled and for claims incurred but not yet reported. In addition, in line with the requirements of the Insurance Companies (Reserves) Act 1995, claims equalisation provisions are maintained in relation to property, credit and suretyship business. The majority of provisions in respect of claims will be settled in the following year, although new provisions will then be required in respect of claims arising from that year. The level of the claims equalisation provision will be adjusted annually, taking into account the guidelines contained in the legislation, and such provisions will be held for as long as the Group continues to write the relevant types of general insurance business.

The Group also carries provisions in respect of its obligations relating to UIC Insurance Company Limited ('UIC'), which is partly owned by the Group. The Group has indemnified a third party against losses in the event that UIC does not honour its obligations under a re-insurance contract, which is subject to asbestosis and pollution claims in the US. The ultimate exposure to claims in respect of the insurance business of UIC is uncertain. Accordingly, the provision has been based upon an actuarial estimate of prospective claims, taking account of re-insurance arrangements protecting UIC and UIC's available assets. Given the long-term nature of many of the claims to which UIC is exposed, it is expected to be many years before the Group's ultimate liability can be assessed with certainty.

Vacant leasehold property and other
Vacant leasehold property provisions are made by reference to a prudent estimate of expected sub-let income and the possibility of disposing of the Group's interest in the lease, taking into account conditions in the property market. These provisions are reassessed on an annual basis and will normally run off over the remaining life of the leases concerned, currently averaging five years; where a property is disposed of earlier than anticipated, any remaining balance in the provision relating to that property is released.

39 Subordinated liabilities

	Notes	Group 2002 £m	Group 2001* £m	Company 2002 £m	Company 2001 £m
Undated loan capital (see below)		**5,496**	4,102	**497**	–
Dated loan capital (see below)		**4,672**	4,006	**873**	413
Total subordinated liabilities		**10,168**	8,108	**1,370**	413

**Undated loan capital:*	Notes	Group 2002 £m	Group 2001* £m	Company 2002 £m	Company 2001 £m
Primary Capital Undated Floating Rate Notes:	a				
Series 1 (US$750 million)		**466**	516	**–**	–
Series 2 (US$500 million)		**311**	344	**–**	–
Series 3 (US$600 million)		**373**	412	**–**	–
11¾% Perpetual Subordinated Bonds		**100**	100	**–**	–
6.625% Perpetual Capital Securities (€750 million)	b	**482**	451	**–**	–
6.90% Perpetual Capital Securities callable 2007 (US$1,000 million)	c, k	**610**	–	**–**	–
5⅝% Undated Subordinated Step-up Notes callable 2009 (€1,250 million)	h	**807**	757	**–**	–
Undated Step-up Floating Rate Notes callable 2009 (€150 million)	a	**97**	91	**–**	–
6⅝% Undated Subordinated Step-up Notes callable 2010	f	**406**	406	**–**	–
6.35% Step-up Perpetual Capital Securities callable 2013 (€500 million)	d, h, k	**322**	–	**–**	–
5.57% Undated Subordinated Step-up Coupon Notes callable 2015 (¥20 billion)	i	**104**	105	**–**	–
6½% Undated Subordinated Step-up Notes callable 2019	f	**267**	266	**–**	–
8% Undated Subordinated Step-up Notes callable 2023	f	**199**	199	**–**	–
6½% Undated Subordinated Step-up Notes callable 2029	f	**455**	455	**–**	–
6% Undated Subordinated Step-up Guaranteed Bonds callable 2032	f, k	**497**	–	**497**	–
		5,496	4,102	**497**	–

*restated (see note 1)

39 Subordinated liabilities (continued)

	Notes	Group 2002 £m	Group 2001 £m	Company 2002 £m	Company 2001 £m
Dated loan capital:					
Eurocurrency Zero Coupon Bonds 2003 (¥3 billion)	e	**14**	15	**14**	15
Subordinated Fixed Rate Bonds 2003 (NZ$151 million)	g	**48**	43	**–**	–
Subordinated Floating Rate Notes 2004	a	**10**	15	**–**	–
7⅜% Subordinated Bonds 2004		**400**	399	**–**	–
Subordinated Floating Rate Notes 2004	a, j	**100**	100	**–**	–
8½% Subordinated Bonds 2006		**249**	249	**249**	249
7¾% Subordinated Bonds 2007		**299**	299	**–**	–
Subordinated Fixed Rate Bonds 2007 (NZ$150 million)	g	**–**	43	**–**	–
5¼% Subordinated Notes 2008 (DM750 million)		**249**	234	**–**	–
10⅝% Guaranteed Subordinated Loan Stock 2008	e	**100**	100	**–**	–
9½% Subordinated Bonds 2009		**99**	99	**–**	–
Subordinated Step-up Floating Rate Notes 2009 callable 2004 (US$500 million)	a	**310**	343	**–**	–
Subordinated Fixed Rate Bonds 2010 (NZ$100 million)	g	**33**	29	**–**	–
6¼% Subordinated Notes 2010 (€400 million)		**259**	244	**–**	–
Subordinated Floating Rate Notes 2010 (US$400 million)	a	**248**	274	**–**	–
12% Guaranteed Subordinated Bonds 2011	e	**100**	100	**–**	–
9⅛% Subordinated Bonds 2011		**149**	149	**149**	149
4¾% Subordinated Notes 2011 (€850 million)		**532**	498	**–**	–
Subordinated Fixed Rate Bonds 2011 (NZ$100 million)	g	**33**	28	**–**	–
Subordinated Fixed Rate Bonds 2012 (NZ$125 million)	g, k	**41**	–	**–**	–
Subordinated Fixed Rate Bonds 2012 (NZ$125 million)	g, k	**41**	–	**–**	–
5⅞% Subordinated Guaranteed Bonds 2014 (€750 million)	k	**461**	–	**461**	–
5⅞% Subordinated Notes 2014	k	**148**	–	**–**	–
6⅝% Subordinated Notes 2015		**344**	343	**–**	–
Subordinated Floating Rate Notes 2020 (€100 million)	a	**65**	61	**–**	–
9⅝% Subordinated Bonds 2023		**340**	341	**–**	–
		4,672	4,006	**873**	413

These liabilities will, in the event of the winding-up of the issuer, be subordinated to the claims of depositors and all other creditors of the issuer.

**In certain circumstances, these notes and bonds would acquire the characteristics of preference share capital.

a) These notes bear interest at rates fixed periodically in advance based on London Interbank rates.

b) In certain circumstances the interest payments on these securities can be deferred although in this case neither Lloyds TSB Bank plc nor Lloyds TSB Group plc can declare or pay a dividend until any deferred payments have been made. In the event of a winding up of Lloyds TSB Bank plc, these securities will acquire the characteristics of preference shares. The securities can be redeemed at par at the option of Lloyds TSB Bank plc on or after 25 October 2006.

c) In certain circumstances the interest payments on these securities can be deferred although in this case neither Lloyds TSB Bank plc nor Lloyds TSB Group plc can declare or pay a dividend until payments are resumed. Any deferred payments will be made good on redemption of the securities. In the event of a winding up of Lloyds TSB Bank plc, these securities will acquire the characteristics of preference shares. The securities can be redeemed at par at the option of Lloyds TSB Bank plc on or after 22 November 2007.

d) In certain circumstances the interest payments on these securities can be deferred although in this case neither Lloyds TSB Bank plc nor Lloyds TSB Group plc can declare or pay a dividend until any deferred payments have been made. In the event of a winding up of Lloyds TSB Bank plc, these securities will acquire the characteristics of preference shares. The securities can be redeemed at par at the option of Lloyds TSB Bank plc on or after 25 February 2013.

e) Issued by a group undertaking under the Company's subordinated guarantee and, in the case of the Eurocurrency Zero Coupon Bonds 2003, on-lent to the Company on a subordinated basis.

f) At the callable date the coupon on these Notes will be reset by reference to the applicable five year benchmark gilt rate.

g) These bonds bear interest, to be reset 5 years before redemption date, at a fixed margin over New Zealand Government stocks.

h) In the event that these Notes are not redeemed at the callable date, the coupon will be reset to a floating rate.

i) In the event that these Notes are not redeemed at the callable date, the coupon will be reset to a fixed margin over the then 5 year Yen swap rate.

j) Exchangeable at the election of the Group for further subordinated floating rate notes.

k) Issued during 2002 primarily to finance the general business of the Group.

39 Subordinated liabilities (continued)

Dated subordinated liabilities are repayable as follows:

	Group 2002 £m	Group 2001 £m	Company 2002 £m	Company 2001 £m
1 year or less	**67**	5	**14**	–
2 years or less but over 1 year	**505**	63	**–**	15
5 years or less but over 2 years	**548**	753	**249**	249
Over 5 years	**3,552**	3,185	**610**	149
	4,672	4,006	**873**	413

40 Non-equity minority interests

Non-equity minority interests comprise:

	2002 £m	2001* £m
Euro Step-up Non-Voting Non-Cumulative Preferred Securities (€430 million) callable 2012**	**278**	261
Sterling Step-up Non-Voting Non-Cumulative Preferred Securities callable 2015†	**248**	248
Capital instruments	**526**	509
European Financial Institution Investments Partnership•	**123**	–
LM ABS Investment Partnership¤	**45**	–
	694	509

*restated (see note 1)

**These securities constitute limited partnership interests in Lloyds TSB Capital 1 L.P., a Jersey limited partnership in which Lloyds TSB (General Partner) Limited, a wholly owned subsidiary, is the general partner. Non-cumulative income distributions accrue at a fixed rate of 7.375 per cent per annum up to 7 February 2012; thereafter they will accrue at a rate of 2.33 per cent above EURIBOR, to be set annually.

†These securities constitute limited partnership interests in Lloyds TSB Capital 2 L.P., a Jersey limited partnership in which Lloyds TSB (General Partner) Limited, a wholly owned subsidiary, is the general partner. Non-cumulative income distributions accrue at a fixed rate of 7.834 per cent per annum up to 7 February 2015; thereafter they will accrue at a rate of 3.50 per cent above a rate based on the yield of specified UK government stock.

Both of the above issues were made under the limited subordinated guarantee of Lloyds TSB Bank plc. In certain circumstances these preferred securities will be mandatorily exchanged for preference shares in Lloyds TSB Group plc. Lloyds TSB Group plc has entered into an agreement whereby dividends may only be paid on its ordinary shares if sufficient distributable profits are available for distributions due in the financial year on these preferred securities.

•These securities constitute interests in European Financial Institution Investments Partnership, an English law general partnership in which the principal partner is Langbourn Holdings Limited, a wholly owned subsidiary of the Group. The minority interests are entitled to 90 per cent of the partnership's profits. In the event of a winding-up, at least 90 per cent of the capital of the partnership would be returned to Langbourn Holdings Limited.

¤These securities constitute interests in LM ABS Investment Partnership, an English law general partnership in which the principal partner is Lime Street Holdings Limited, a wholly owned subsidiary of the Group. The minority interests are entitled to 95 per cent of the partnership's profits. In the event of a winding-up, at least 85 per cent of the capital of the partnership would be returned to Lime Street Holdings Limited.

41 Called-up share capital

	2002 £m	2001 £m
Authorised:		
Sterling		
Ordinary shares of 25p each	**1,728**	1,728
Limited voting ordinary shares of 25p each	**20**	20
Preference shares of 25p each	**44**	44
	1,792	1,792
US dollars	**US$m**	US$m
Preference shares of US25 cents each	**40**	40
Euro	**€m**	€m
Preference shares of €25 cents each	**40**	40
Japanese yen	**¥m**	¥m
Preference shares of ¥25 each	**1,250**	1,250

	Ordinary shares of 25p each £m	Limited voting ordinary shares of 25p each £m	Total £m
Issued and fully paid:			
At 1 January 2002	**1,391**	**20**	**1,411**
Issued to the QUEST (note 27)	**5**	**–**	**5**
At 31 December 2002	**1,396**	**20**	**1,416**

The limited voting ordinary shares are held by the Lloyds TSB Foundations. These shares carry no rights to dividends but rank pari passu with the ordinary shares in respect of other distributions and in the event of winding up. These shares do not have any right to vote at general meetings other than on resolutions concerning acquisitions or disposals of such importance that they require shareholder consent, or for the winding up of the Company, or for a variation in the class rights of the limited voting ordinary shares.

Lloyds TSB Group plc has entered into deeds of covenant with the Lloyds TSB Foundations, under the terms of which the Company makes annual donations to the foundations equal, in total, to 1 per cent of the Group's pre-tax profits (after certain adjustments) averaged over three years. The deeds of covenant can be cancelled by the Company at nine years' notice.

At 31 December 2002, options to acquire 126 million Lloyds TSB Group ordinary shares of 25p each were outstanding under the executive share option schemes, the share retention plan, and the staff sharesave share option schemes exercisable up to 2012. These include the option, described on page 54, to acquire 216,763 shares under the share retention plan: otherwise the options are exercisable at prices ranging from 160p to 888p per share.

42 Reserves

	Group £m	Company £m
Share premium account:		
At 1 January 2002	**959**	**959**
Premium arising on issue of shares	**134**	**134**
At 31 December 2002	**1,093**	**1,093**
Revaluation reserve:		
At 1 January 2002		**5,894**
Decrease in net tangible assets of subsidiary undertakings		**(2,869)**
At 31 December 2002		**3,025**
Merger reserve:		
At 1 January 2002 and 31 December 2002	**343**	**–**
Profit and loss account:		
At 1 January 2002 – as previously reported	**8,047**	**2,496**
Prior year adjustment (note 1)	**(404)**	**–**
At 1 January 2002 – restated	**7,643**	**2,496**
Exchange and other adjustments	**(3)**	**–**
Actuarial losses recognised in post-retirement benefit schemes (note 44)	**(2,331)**	**–**
Charge in respect of the QUEST (note 27)	**(62)**	**(62)**
(Loss) profit for the year	**(127)**	**4**
At 31 December 2002	**5,120**	**2,438**

The Group profit and loss account reserves at 31 December 2002 include £1,310 million (2001: £1,222 million) not presently available for distribution representing the Group's share of the value of long-term assurance business in force and the surplus retained within the long-term assurance funds. The Group profit and loss account reserves at 31 December 2002 are stated after including a deficit of £2,077 million relating to the Group's post-retirement defined benefit schemes (2001: surplus of £281 million).

The cumulative amount of premiums on acquisitions written off against reserves during previous years amounts to £2,271 million of which £1,823 million was within the last 10 years.

43 Related party transactions

a Transactions, arrangements and agreements involving directors and others

At 31 December 2002, transactions, arrangements and agreements entered into by the Group's banking subsidiaries with directors and connected persons and with officers included:

	2002 Number of persons	**2002 Total £000**	2001 Number of persons	2001 Total £000
Loans and credit card transactions:				
Directors and connected persons	**4**	**3,334**	7	1,343
Officers	**31**	**3,930**	28	4,113

During the year three officers purchased cars from the Group for a total consideration of £37,000.

b Group undertakings

Details of the principal group undertakings are given in note 21. In accordance with FRS 8, transactions or balances with group entities that have been eliminated on consolidation are not reported.

c Joint ventures

Details of the Group's joint ventures are provided in note 20. Information relating to transactions entered into between Group undertakings and the joint ventures and details of outstanding balances at 31 December 2002 are also shown in note 20.

d Long-term assurance business

The Group enters into certain transactions with its long-term assurance businesses, which cannot be eliminated in the consolidated accounts because of the basis of accounting used for the Group's long-term assurance businesses. After taking into account legally enforceable netting agreements, at 31 December 2002 Group entities owed £1,372 million (2001: £1,186 million) and were owed £145 million (2001: £299 million); these amounts are included in customer accounts and loans and advances to customers respectively. In addition, fees of £76 million (2001: £62 million) were received, and fees of £35 million (2001: £28 million) were paid, in respect of asset management services.

Certain administrative properties used by Scottish Widows are owned by the long-term assurance funds. During 2002 Scottish Widows paid rent to the long-term assurance funds amounting to £5 million (2001: £4 million). In addition, at 31 December 2002, the long-term assurance funds owned 31 million ordinary shares in the Company (2001: 31 million shares).

e Pension funds

Group entities provide a number of banking and other services to the Group's pension funds, which are conducted on similar terms to third party transactions. At 31 December 2002, the Group's pension funds had call deposits with Lloyds TSB Bank plc amounting to £89 million (2001: £572 million).

44 Pensions and other post-retirement benefits

The pension costs included in administrative expenses are comprised as follows:

	2002 £m	2001 £m
Defined contribution schemes	**25**	18
Defined benefit schemes	**293**	329
	318	347

The majority of the Group's employees are members of the defined benefit sections of Lloyds TSB Group Pension Schemes No's 1 and 2. During the years ended 31 December 2001 and 2002, the Group made no contributions to these schemes. Since the defined benefit sections of these schemes are now closed to new members and the age profile of the active members is increasing, under the projected unit method, the current service cost will increase as the members of the schemes approach retirement.

The latest full valuations of the schemes were carried out as at 30 June 2002; these have been updated to 31 December 2002 by qualified independent actuaries. The last full valuations of other group schemes were carried out on a number of different dates; these have been updated to 31 December 2002 by qualified independent actuaries or, in the case of the Scottish Widows Retirement Benefits Scheme, by a qualified actuary employed by Scottish Widows.

The principal assumptions used in the scheme valuations were as follows:

	31 December 2002 %	31 December 2001 %
Rate of inflation	**2.30**	2.50
Rate of salary increases	**3.83**	4.04
Rate of increase for pensions in payment and deferred pensions	**2.30**	2.50
Discount rate	**5.60**	6.00

In addition, the Group operates a number of schemes which provide post-retirement healthcare benefits to certain employees, retired employees and their dependent relatives. The principal scheme relates to former Lloyds Bank staff and under this scheme the Group has undertaken to meet the cost of post-retirement healthcare for all eligible former employees (and their dependants) who retired prior to 1 January 1996. For retirements subsequent to this date, the Group will meet a reducing proportion of the cost until 31 December 2004, after which date the only obligation will be in respect of the pre 1 January 1996 retirements.

Included within other finance income is an interest cost of £4 million (2001: £3 million) in respect of these defined benefit post-retirement healthcare schemes.

For the principal post-retirement healthcare scheme, the latest actuarial valuation of the liability was carried out at 31 December 2000; this valuation has been updated to 31 December 2002 by qualified independent actuaries. The principal assumptions used were as set out above, except that the rate of increase in healthcare premiums has been assumed at 4.86 per cent.

The assets of the Group's defined benefit schemes and the expected rates of return are summarised as follows:

	Fair value at 31 December 2002 £m	Expected long-term rate of return at 31 December 2002 %	Fair value at 31 December 2001 £m	Expected long-term rate of return at 31 December 2001 %
Market values of scheme assets:				
Equities	**7,175**	**8.4**	7,779	8.0
Fixed interest securities	**557**	**4.5**	1,835	5.1
Property	**791**	**6.9**	798	7.1
Other	**560**	**5.4**	714	4.1
Total fair value of scheme assets	**9,083**		11,126	

Other finance income is comprised of:

	2002 £m	2001 £m
Expected return on scheme assets	**817**	844
Interest cost of scheme liabilities	**(652)**	(537)
	165	307

The pension and other post-retirement benefit cost in respect of defined benefit schemes is comprised of:

	2002 £m	2001 £m
Current service cost	**244**	212
Past service costs	**49**	117
Defined benefit costs	**293**	329

The amounts recognised in the statement of total recognised gains and losses are comprised of:

	2002 £m	2001 £m
Actual return less expected return on scheme assets	**(2,582)**	(2,015)
Experience gains and losses arising on scheme liabilities	**(240)**	(71)
Effect of changes in demographic and financial assumptions	**(477)**	(787)
Actuarial losses recognised	**(3,299)**	(2,873)
Deferred tax thereon	**968**	863
Amount recognised in the statement of total recognised gains and losses	**(2,331)**	(2,010)

44 Pensions and other post-retirement benefits (continued)

The experience gains and losses recognised can also be interpreted as follows:

	2002 £m	2001 £m
Actual return less expected return on scheme assets		
Amount	**(2,582)**	(2,015)
Percentage of scheme assets at balance sheet date	**28.4%**	18.1%
Experience gains and losses arising on scheme liabilities		
Amount	**(240)**	(71)
Percentage of scheme liabilities at balance sheet date	**2.0%**	0.7%
Total amount recognised in the statement of total recognised gains and losses		
Amount	**(3,299)**	(2,873)
Percentage of scheme liabilities at balance sheet date	**27.5%**	26.9%

The amounts reported on the Group's balance sheet are comprised as follows:

	2002 £m	2001 £m
Market value of assets	**9,083**	11,126
Present value of scheme liabilities	**(12,014)**	(10,693)
(Deficit) surplus in the schemes	**(2,931)**	433
Related deferred tax asset (liability)	**854**	(152)
Net post-retirement benefit (liability) asset	**(2,077)**	281
Disclosed in the accounts as follows:		
Post-retirement benefit asset	**–**	356
Post-retirement benefit liability	**(2,077)**	(75)
	(2,077)	281

The movements in the (deficit) surplus in the schemes over the year have been as follows:

	2002 £m	2001 £m
Surplus at beginning of year	**433**	3,325
Exchange and other adjustments	**26**	–
Other finance income	**165**	307
Current service costs	**(244)**	(212)
Contributions	**37**	3
Past service costs	**(49)**	(117)
Actuarial loss	**(3,299)**	(2,873)
(Deficit) surplus at end of year	**(2,931)**	433

45 Contingent liabilities and commitments

a Contingent liabilities and commitments arising out of banking transactions	2002 £m	2001 £m
Contingent liabilities:		
Acceptances and endorsements	**1,879**	2,243
Guarantees	**5,927**	3,789
Other:		
Other items serving as direct credit substitutes	**1,103**	460
Performance bonds and other transaction-related contingencies	**1,436**	1,469
Other contingent liabilities	**1**	2
	2,540	1,931
	10,346	7,963
Commitments:		
Documentary credits and other short-term trade-related transactions	**289**	354
Forward asset purchases and forward forward deposits placed	**394**	783
Undrawn note issuing and revolving underwriting facilities	**32**	35
Undrawn formal standby facilities, credit lines and other commitments to lend:		
Less than 1 year maturity	**49,417**	42,594
1 year or over maturity	**14,372**	9,576
	64,504	53,342

b Contingent liabilities arising out of past sales of savings and investment products

In common with other companies providing savings and investment products to retail consumers, matters arise from time to time as a result of customer complaints or investigations by the regulator requiring remedial action to be taken, which may include the payment of compensation.

One such matter relates to the sale of life assurance products related to the repayment of residential mortgages. Falling investment returns have led to increased concern that the value of some of these policies will be less than the amount required to repay the mortgage. Certain customers have complained that this risk was not properly explained to them at the time of sale. Following a review of past sales made by Abbey Life a provision of £165 million has been made for the estimated cost of redress (note 30e).

Other complaints, including those related to the sale of life assurance products, are dealt with on a case by case basis and where appropriate compensation is paid. Provision has been made, based upon the level of complaints for the estimated cost of redress which is not significant. If the position changes, further provisions may be required.

Concerns have also been expressed over the appropriateness of certain sales of stockmarket related savings products. In this regard the Group is carrying out, in conjunction with the regulator, an investigation into the sales of the Extra Income & Growth Plan. This investigation is expected to be completed during 2003 when the Group will be in a position to estimate the financial effect.

46 Derivatives and other financial instruments

Information about the Group's use of financial instruments and management of the associated risks is given on pages 31 to 41 in the financial review.

a Derivatives

The Group uses derivatives as part of its trading activities and to reduce its own exposure to fluctuations in interest and exchange rates.

Trading
The notional principal amounts and fair values (which, after netting, are the carrying values) of trading instruments entered into with third parties were as follows:

31 December 2002	Notional principal amount £m	Fair values Assets £m	Fair values Liabilities £m
Exchange rate contracts:			
Spot, forwards and futures	**94,250**	**2,064**	**2,735**
Currency swaps	**8,556**	**232**	**304**
Options purchased	**4,468**	**87**	**8**
Options written	**4,303**	**–**	**103**
	111,577	**2,383**	**3,150**
Interest rate contracts:			
Interest rate swaps	**258,523**	**5,473**	**5,808**
Forward rate agreements	**41,768**	**35**	**37**
Options purchased	**8,248**	**105**	**–**
Options written	**4,899**	**–**	**152**
Futures	**18,963**	**–**	**–**
	332,401	**5,613**	**5,997**
Equity contracts	**5,662**	**608**	**491**
Effect of netting		**(5,176)**	**(5,176)**
Balances arising from off-balance sheet financial instruments		**3,428**	**4,462**

31 December 2001	Notional principal amount £m	Fair values Assets £m	Fair values Liabilities £m
Exchange rate contracts:			
Spot, forwards and futures	95,895	1,035	1,038
Currency swaps	6,737	223	152
Options purchased	3,825	11	–
Options written	3,492	–	9
	109,949	1,269	1,199
Interest rate contracts:			
Interest rate swaps	286,617	4,085	4,535
Forward rate agreements	54,171	78	84
Options purchased	8,887	73	–
Options written	3,993	–	58
Futures	35,112	–	–
	388,780	4,236	4,677
Equity contracts	4,580	428	255
Effect of netting		(3,843)	(3,843)
Balances arising from off-balance sheet financial instruments		2,090	2,288

Non-trading
Through intra company and intra group transactions, Group companies establish non-trading derivatives positions with the Group's independent trading operations, which then enter into similar positions with third parties. The notional principal amounts and fair values of non-trading instruments entered into with third parties were as follows:

31 December 2002	Notional principal amount £m	Fair values Positive £m	Fair values Negative £m
Exchange rate contracts:			
Spot, forwards and futures	**146**	**16**	**4**
Currency swaps	**59**	**4**	**1**
	205	**20**	**5**
Interest rate contracts:			
Interest rate swaps	**17,261**	**129**	**223**
Forward rate agreements	**1,279**	**2**	**2**
Options written	**41**	**–**	**1**
	18,581	**131**	**226**
Effect of netting		**(36)**	**(36)**
		115	**195**

31 December 2001	Notional principal amount £m	Fair values Positive £m	Fair values Negative £m
Exchange rate contracts:			
Spot, forwards and futures	146	3	1
Currency swaps	70	9	1
	216	12	2
Interest rate contracts:			
Interest rate swaps	2,919	164	68
Forward rate agreements	62	–	–
	2,981	164	68
Effect of netting		(39)	(39)
		137	31

The Company held non-trading derivatives with a notional principal amount of £1,852 million (2001: £400 million).

The aggregate carrying value of non-trading derivatives with a positive fair value was an asset of £54 million (2001: an asset of £18 million) and with a negative fair value was an asset of £9 million (2001: an asset of £1 million).

46 Derivatives and other financial instruments (continued)

a Derivatives (continued)

The maturity of the notional principal amounts and replacement cost of both trading and non-trading instruments entered into with third parties was:

	Under 1 year £m	1 to 5 years £m	Over 5 years £m	Total £m
31 December 2002				
Exchange rate contracts:				
Notional principal amount	**102,559**	**6,888**	**2,335**	**111,782**
Replacement cost	**2,209**	**108**	**86**	**2,403**
Interest rate contracts:				
Notional principal amount	**150,883**	**149,381**	**50,718**	**350,982**
Replacement cost	**850**	**2,682**	**2,212**	**5,744**
Equity contracts:				
Notional principal amount	**1,130**	**3,714**	**818**	**5,662**
Replacement cost	**3**	**531**	**74**	**608**
Total:				
Notional principal amount	**254,572**	**159,983**	**53,871**	**468,426**
Replacement cost	**3,062**	**3,321**	**2,372**	**8,755**
31 December 2001				
Exchange rate contracts:				
Notional principal amount	102,130	6,260	1,775	110,165
Replacement cost	1,087	152	42	1,281
Interest rate contracts:				
Notional principal amount	187,570	155,079	49,112	391,761
Replacement cost	1,300	1,796	1,304	4,400
Equity contracts:				
Notional principal amount	738	3,394	448	4,580
Replacement cost	75	330	23	428
Total:				
Notional principal amount	290,438	164,733	51,335	506,506
Replacement cost	2,462	2,278	1,369	6,109

The notional principal amount does not represent the Group's real exposure to credit risk, which is limited to the current cost of replacing contracts at current market rates should the counterparties default.

Net replacement cost represents the total positive fair value of all derivative contracts at the balance sheet date, after allowing for the offset of all negative fair values where the Group has a legal right of set-off with the counterparty concerned.

An analysis of the net replacement cost of both trading and non-trading instruments entered into with third parties by counterparty type is set out below; the Group's exposure is further reduced by qualifying collateral held.

	2002 £m	2001 £m
OECD banks	**1,939**	1,425
Other	**1,604**	802
Net replacement cost	**3,543**	2,227
Qualifying collateral held	**(521)**	(339)
Potential credit risk exposure	**3,022**	1,888

46 Derivatives and other financial instruments (continued)

b Interest rate sensitivity gap analysis for the non-trading book

The table below summarises the repricing mismatches of the Group's non-trading assets and liabilities. Items are allocated to time bands by reference to the earlier of the next contractual interest rate repricing date and the maturity date.

As at 31 December 2002	3 months or less £m	6 months or less but over 3 months £m	1 year or less but over 6 months £m	5 years or less but over 1 year £m	Over 5 years £m	Non-interest bearing £m	Trading book £m	Total £m
Assets:								
Treasury bills and other eligible bills	**1,759**	**23**	**94**	**1**	**2**	**–**	**530**	**2,409**
Loans and advances to banks	**12,363**	**1,362**	**761**	**775**	**200**	**666**	**1,402**	**17,529**
Loans and advances to customers	**88,349**	**4,997**	**8,233**	**26,787**	**7,210**	**(1,732)**	**630**	**134,474**
Debt securities and equity shares	**6,093**	**1,049**	**312**	**1,972**	**2,516**	**(42)**	**17,620**	**29,520**
Other assets	**130**	**25**	**25**	**243**	**48**	**16,536**	**6,479**	**23,486**
Total assets	**108,694**	**7,456**	**9,425**	**29,778**	**9,976**	**15,428**	**26,661**	**207,418**
Liabilities:								
Deposits by banks	**21,572**	**817**	**240**	**377**	**112**	**248**	**2,077**	**25,443**
Customer accounts	**103,996**	**1,318**	**1,193**	**3,829**	**2,008**	**3,140**	**850**	**116,334**
Debt securities in issue	**19,169**	**5,526**	**2,002**	**1,212**	**1,224**	**–**	**1,122**	**30,255**
Other liabilities	**353**	**–**	**6**	**–**	**–**	**9,136**	**7,020**	**16,515**
Subordinated liabilities – loan capital	**2,692**	**1,140**	**12**	**1,183**	**5,141**	**–**	**–**	**10,168**
Minority interests and shareholders' funds	**–**	**–**	**–**	**–**	**–**	**8,855**	**(152)**	**8,703**
Internal funding of trading business	**(7,973)**	**(198)**	**(1,545)**	**(5,148)**	**(880)**	**–**	**15,744**	**–**
Total liabilities	**139,809**	**8,603**	**1,908**	**1,453**	**7,605**	**21,379**	**26,661**	**207,418**
Off-balance sheet items	**10,942**	**5,939**	**(10,082)**	**(8,830)**	**2,031**	**–**	**–**	**–**
Interest rate repricing gap	**(20,173)**	**4,792**	**(2,565)**	**19,495**	**4,402**	**(5,951)**	**–**	**–**
Cumulative interest rate repricing gap	**(20,173)**	**(15,381)**	**(17,946)**	**1,549**	**5,951**	**–**	**–**	**–**

As at 31 December 2001*	3 months or less £m	6 months or less but over 3 months £m	1 year or less but over 6 months £m	5 years or less but over 1 year £m	Over 5 years £m	Non-interest bearing £m	Trading book £m	Total £m
Assets:								
Treasury bills and other eligible bills	2,709	37	26	4	6	–	1,630	4,412
Loans and advances to banks	11,311	1,621	1,076	142	289	452	333	15,224
Loans and advances to customers	74,361	5,252	8,798	28,497	7,108	(1,353)	272	122,935
Debt securities and equity shares	2,545	1,662	718	1,940	4,168	(6)	13,423	24,450
Other assets	154	9	8	4	15	16,545	5,648	22,383
Total assets	91,080	8,581	10,626	30,587	11,586	15,638	21,306	189,404
Liabilities:								
Deposits by banks	19,226	1,859	666	512	90	681	1,276	24,310
Customer accounts	92,834	1,644	1,172	3,228	2,299	7,633	306	109,116
Debt securities in issue	16,453	3,957	1,333	600	890	–	1,187	24,420
Other liabilities	350	–	3	–	5	6,838	5,352	12,548
Subordinated liabilities – loan capital	1,069	714	–	641	5,684	–	–	8,108
Minority interests and shareholders' funds	–	–	–	–	–	10,800	102	10,902
Internal funding of trading business	(3,736)	(741)	(1,171)	(6,051)	(1,384)	–	13,083	–
Total liabilities	126,196	7,433	2,003	(1,070)	7,584	25,952	21,306	189,404
Off-balance sheet items	21,937	(10,861)	(7,509)	(2,896)	(671)	–	–	–
Interest rate repricing gap	(13,179)	(9,713)	1,114	28,761	3,331	(10,314)	–	–
Cumulative interest rate repricing gap	(13,179)	(22,892)	(21,778)	6,983	10,314	–	–	–

The table above does not take into account the effect of interest rate options used by the Group to hedge its exposure; details of options are given in note 46a.

*restated (see note 1)

46 Derivatives and other financial instruments (continued)

c Fair value analysis

The table below shows a comparison by category of book values and fair values of the Group's on-balance sheet financial assets and liabilities.

	Trading book		Non-trading book	
As at 31 December 2002	Book value £m	Fair value £m	Book value £m	Fair value £m
Assets:				
Treasury bills and other eligible bills	**530**	**530**	**1,879**	**1,878**
Loans and advances to banks and customers	**2,032**	**2,032**	**149,971**	**151,526**
Debt securities and equity shares	**17,620**	**17,620**	**11,900**	**11,932**
Liabilities:				
Deposits by banks and customers	**2,927**	**2,927**	**138,850**	**138,428**
Debt securities in issue	**1,122**	**1,122**	**29,133**	**29,005**
Subordinated liabilities	**–**	**–**	**10,168**	**11,156**

	Trading book		Non-trading book	
As at 31 December 2001*	Book value £m	Fair value £m	Book value £m	Fair value £m
Assets:				
Treasury bills and other eligible bills	1,630	1,630	2,782	2,780
Loans and advances to banks and customers	605	605	137,554	138,287
Debt securities and equity shares	13,423	13,423	11,027	11,269
Liabilities:				
Deposits by banks and customers	1,582	1,582	131,844	131,813
Debt securities in issue	1,187	1,187	23,233	23,266
Subordinated liabilities	–	–	8,108	8,544

*restated (see note 1)

The disclosures in this note cover all on-balance sheet financial instruments; fair values of all derivative instruments are disclosed in note 46a.

Fair values are determined by reference to quoted market prices or, where no market price is available, using internal models which discount expected future cashflows at prevailing interest rates.

Fair values have not been calculated for sundry debtors and creditors in the trading book.

d Currency exposures

Structural currency exposures
The Group's main overseas operations are in New Zealand, the Americas and Europe. Details of the Group's structural foreign currency exposures are as follows:

	2002 £m	2001 £m
Functional currency of Group operation		
New Zealand dollar	**921**	748
Euro	**304**	286
US dollar	**259**	147
Swiss franc	**100**	104
Other non-sterling	**323**	438
	1,907	1,723

Non-structural currency exposures
All foreign exchange exposures in the non-trading book are transferred to the trading area where they are monitored and controlled.

Information about the management of market risk in the Group's trading activities is given on pages 36 and 37 in the financial review.

e Unrecognised gains and losses on hedging instruments

The Group uses a variety of financial instruments to hedge exposures in its banking book; these hedges are accounted for on an accruals basis, in line with the underlying instruments being hedged. Any gains or losses that would occur if these instruments were carried at market value are therefore not recognised.

At 31 December 2002, the unrecognised gains on financial instruments used for hedging were £518 million (2001: £242 million) and unrecognised losses were £744 million (2001: £820 million).

The net losses arising in 2001 and earlier years and recognised in 2002 amounted to £344 million. Net losses of £6 million arose in 2002 but were not recognised in the year.

Of the net losses of £226 million at 31 December 2002, £38 million of net losses are expected to be recognised in the year ending 31 December 2003 and £188 million of net losses in later years.

f Value at risk in trading activities

Details of value at risk in the Group's global trading activities are given on page 36 in the financial review.

Notes to the accounts

47 Acquisitions

a) On 18 April 2002 the Group's subsidiary, Lloyds TSB Asset Finance Division Limited, completed the acquisition of First National Vehicle Holdings and Abbey National Vehicle Finance, both previously wholly owned subsidiaries of Abbey National plc operating in the UK contract hire and fleet management market; the results of these businesses have been consolidated in full from that date, the effect on the results of the Group is not material. The premium on acquisition of £86 million has been capitalised and will be written off to the profit and loss account over its estimated useful life of 20 years.

A summarised profit and loss account for First National Vehicle Holdings and Abbey National Vehicle Finance for the period from 1 January 2002 to 17 April 2002 is set out below:

	£m
Net interest income	6
Other income	25
Total income	31
Operating expenses	38
Provisions for bad and doubtful debts	1
Loss on ordinary activities before tax	(8)
Tax	2
Loss after tax for the period to 17 April 2002	(6)
Profit after tax for the year ended 31 December 2001	–

All recognised gains and losses are included in the profit and loss account.

The combined balance sheet of First National Vehicle Holdings and Abbey National Vehicle Finance at 18 April 2002 was as follows:

	Book value at 18 April 2002 £m	Fair value adjustments £m	Fair value at acquisition £m
Loans and advances to customers	64	–	64
Tangible fixed assets	355	(8)	347
Other assets and prepayments	63	–	63
Deposits by banks	(405)	–	(405)
Other liabilities and accruals	(107)	(6)	(113)
Net liabilities acquired	(30)	(14)	(44)
Goodwill			86
Consideration			42

An initial cash payment of £47 million has been made, however following the preparation of the completion accounts it is believed that this should be subject to a downward adjustment of £5 million. Accordingly a receivable of this amount has been recognised in the Group's balance sheet. The fair value adjustments principally reflect adjustments to the carrying value of operating lease assets and related taxation. Negotiations regarding the completion of this acquisition are still ongoing and, whilst no further significant adjustments to consideration or fair value adjustments are expected, in accordance with the requirements of paragraph 27 of Financial Reporting Standard 6, it is noted that the fair value of the net assets of the acquired businesses and the goodwill arising shown above are provisional.

b) On 17 October 2002 the Group's subsidiary, Lloyds TSB Bank (No. 5) Limited, completed the purchase of the business of Accucard, a credit card technology development and marketing company. The consideration for the purchase was £9 million, of which £7 million was settled in cash with a further £1 million payable in 2003 and £1 million payable in 2004. The premium on acquisition of £7 million has been capitalised and will be written off to the profit and loss account over its estimated useful life of 5 years. There were no fair value adjustments made to the assets acquired. The results of this business have been consolidated in full from the date of acquisition, the effect on the results of the Group is not material.

c) On 16 December 2002 the Group's subsidiary, Lloyds TSB Asset Finance Division Limited, completed the purchase of the business of the Dutton-Forshaw Group, a motor dealer which has a network of 38 franchised dealerships representing 14 motor vehicle manufacturers. The consideration for the purchase was £49 million which was settled in cash. The premium on acquisition of £10 million has been capitalised and will be written off to the profit and loss account over its estimated useful life of 20 years. Fair value adjustments were made to the carrying value of tangible fixed assets and in respect of certain liabilities. Negotiations regarding the completion of this acquisition are still ongoing and, whilst no further significant adjustments to consideration or fair value adjustments are expected, in accordance with the requirements of paragraph 27 of Financial Reporting Standard 6, it is noted that the goodwill arising stated above is provisional. The results of this business have been consolidated in full from the date of acquisition, the effect on the results of the Group is not material.

48 Consolidated cash flow statement

a Reconciliation of operating profit to net cash inflow from operating activities	**2002 £m**	2001* £m
Operating profit	**2,618**	3,132
Increase in prepayments and accrued income	**(21)**	(285)
Increase (decrease) in accruals and deferred income	**113**	(439)
Provisions for bad and doubtful debts	**1,029**	747
Net advances written off	**(675)**	(691)
Insurance claims	**233**	174
Insurance claims paid	**(210)**	(178)
Amounts written off fixed asset investments	**87**	60
Income from long-term assurance business	**303**	29
Transfer from long-term assurance business	**–**	155
Interest on subordinated liabilities (loan capital)	**537**	515
Interest element of finance lease rental payments	**–**	1
Depreciation and amortisation	**701**	550
Other non-cash movements	**(189)**	(376)
Net cash inflow from trading activities	**4,526**	3,394
Net increase in loans and advances	**(11,970)**	(9,340)
Net increase in investments other than investment securities	**(2,494)**	(5,664)
Net increase in other assets	**(683)**	(327)
Net increase in deposits by banks	**1,018**	7,689
Net increase in customer accounts	**6,900**	7,525
Net increase in debt securities in issue	**5,904**	6,557
Net increase in other liabilities	**1,511**	109
Net decrease (increase) in items in course of collection/transmission	**147**	(17)
Other non-cash movements	**535**	1
Net cash inflow from operating activities	**5,394**	9,927

b Analysis of cash as shown in the balance sheet	**2002 £m**	2001 £m
Cash and balances with central banks	**1,140**	1,240
Loans and advances to banks repayable on demand	**4,313**	2,443
	5,453	3,683

The Group is required to maintain balances with the Bank of England which, at 31 December 2002, amounted to £165 million (2001: £156 million).

48 Consolidated cash flow statement (continued)

c Analysis of changes in cash during the year

	2002 £m	2001 £m
At 1 January	**3,683**	3,821
Net cash inflow (outflow) before adjustments for the effect of foreign exchange movements	**1,766**	(100)
Effect of foreign exchange movements	**4**	(38)
At 31 December	**5,453**	3,683

d Analysis of changes in financing during the year

	Share capital (including premium and merger reserve) 2002 £m	2001 £m
At 1 January	**2,713**	2,334
Cash inflow from financing	**139**	379
At 31 December	**2,852**	2,713

	Capital securities issued by subsidiary undertakings 2002 £m	2001* £m
At 1 January	**509**	515
Effect of foreign exchange movements	**17**	(6)
At 31 December	**526**	509

	Minority investment in subsidiaries 2002 £m	2001 £m
At 1 January	**–**	–
Cash inflow from financing	**167**	–
Retained profit	**1**	–
At 31 December	**168**	–

	Subordinated liabilities and finance leases 2002 £m	2001* £m
At 1 January	**8,111**	7,533
Effect of foreign exchange movements	**(5)**	(13)
Cash inflow from financing	**2,065**	611
Capital repayments	**(4)**	(20)
Adjustments on acquisition	**2**	–
At 31 December	**10,169**	8,111

e Analysis of the net cash outflow in respect of the acquisition of group undertakings

	2002 £m	2001 £m
Cash consideration paid (see f)	**103**	1
Payments to former members of Scottish Widows Fund and Life Assurance Society acquired during 2000	**14**	179
Net cash outflow	**117**	180

f Acquisition of group undertakings

	2002 £m	2001 £m
Net assets acquired:		
Loans and advances	**66**	–
Other assets	**137**	15
Tangible fixed assets	**384**	–
Deposits by banks and other liabilities	**(590)**	(13)
	(3)	2
Goodwill arising on consolidation	**103**	8
	100	10
Satisfied by:		
Amounts receivable	**(5)**	–
Issue of loan notes	**–**	9
Deferred consideration	**2**	–
Cash	**103**	1
	100	10

g Disposal of group undertakings and businesses

	2002 £m	2001 £m
Sundry net assets disposed of	**–**	1
Profit on sale	**–**	39
Cash consideration received	**–**	40

*restated (see note 1)

Information for shareholders

Analysis of shareholders

at 31 December 2002

Size of shareholding	Shareholders Number	Shareholders %	Number of ordinary shares Millions	Number of ordinary shares %
1 – 99	68,103	7.00	2.3	0.04
100 – 499	448,759	46.10	150.7	2.70
500 – 999	295,111	30.32	186.8	3.35
1,000 – 4,999	126,484	12.99	244.8	4.38
5,000 – 9,999	18,626	1.91	127.8	2.29
10,000 – 49,999	13,647	1.41	247.3	4.43
50,000 – 99,999	843	0.09	57.0	1.02
100,000 – 999,999	1,289	0.13	409.3	7.33
1,000,000 and over	506	0.05	4,157.1	74.46
	973,368	100.00	5,583.1*	100.00

**Includes 710 million shares (12.7%) registered in the names of some 864,000 individuals. 203 million shares (3.6%) are held by over 67,000 staff and Group pensioners, or on their behalf by the trustee of the staff profit sharing schemes.*

Substantial shareholdings
At the date of this report notification had been received that Legal & General Investment Management Limited has an interest in 3% of the nominal value of the issued share capital. No other notification has been received that anyone has an interest in 3% or more of the nominal value of the issued share capital.

Share price information
In addition to information published in the financial pages of the press, the latest price of Lloyds TSB shares on the London Stock Exchange can be obtained by telephoning 0906 8771515. These telephone calls are charged at 60p per minute, including VAT, or visit www.londonstockexchange.com.

Share dealing facilities
The Company provides a low cost, execution only, postal dealing service for the purchase and sale of Lloyds TSB shares through Lloyds TSB Registrars. The current rate of commission is 0.75%, for both purchases and sales, no minimum. For full details please contact Lloyds TSB Registrars. Telephone 0870 2424244.

The Company also provides a telephone dealing service through Lloyds TSB Stockbrokers for the purchase and sale of Lloyds TSB shares on preferential commission terms. The current rate for both purchases and sales is 0.75%, minimum £18.50 maximum £75, for transactions up to £75,000. For full details please contact Lloyds TSB Stockbrokers. Telephone 0845 7888100.

American Depositary Receipts (ADRs)
Lloyds TSB shares are traded in the USA through an NYSE-listed sponsored ADR facility, with The Bank of New York as the depositary. The ADRs are traded on the New York Stock Exchange under the symbol LYG. The CUSIP number is 539439109 and the ratio of ADRs to ordinary shares is 1:4. For details please contact The Bank of New York, Investor Relations, PO Box 11258, Church Street Station, New York, NY 10286-1258. Telephone (1) 888 BNY ADRS (US toll free), international callers (1) 610 312 5315. Visit www.adrbny.com or email shareowner–svcs@bankofny.com

Individual Savings Accounts (ISAs)
The Company provides a facility for investing in Lloyds TSB shares through an ISA. For details please contact Lloyds TSB Private Banking ISAs, Freepost, PO Box 149, Haywards Heath, West Sussex RH16 3BR. Telephone 0845 7418418.

The community and our business
Information about the Group's role in the community and copies of the Group's code of business conduct and its environmental report may be obtained by writing to Public Affairs, Lloyds TSB Group plc, 71 Lombard Street, London EC3P 3BS. This information is also available on the Group's website (see below).

The Better Payment Practice Code
A copy of the code and information about it may be obtained from the DTI Publications Orderline 0870 1502500, quoting ref URN 01/621.

Shareholder enquiries
The Company's share register is maintained by Lloyds TSB Registrars, The Causeway, Worthing, West Sussex BN99 6DA. Telephone 0870 6003990; textphone 0870 6003950. Please contact them if you have enquiries about your Lloyds TSB shareholding, including those concerning the following matters:

- change of name or address
- loss of share certificate, dividend warrant or tax voucher
- to obtain a form for dividends to be paid directly to your bank or building society account (tax vouchers will still be sent to your registered address unless you request otherwise)
- to obtain details of the dividend reinvestment plan which enables you to use your cash dividends to buy Lloyds TSB shares in the market
- request for copies of the report and accounts in alternative formats for shareholders with disabilities.

Lloyds TSB Registrars operates a web based enquiry and portfolio management service for shareholders. Visit www.shareview.co.uk for details.

Financial calendar 2003

14 February
Results for 2002 announced

26 February
Ex-dividend date for 2002 final dividend

28 February
Record date for final dividend

9 April
Final date for joining or leaving the dividend reinvestment plan for the final dividend

16 April
Annual general meeting in Glasgow

7 May
Final dividend paid

1 August
Results for half-year to 30 June 2003 announced

13 August
Ex-dividend date for 2003 interim dividend

15 August
Record date for interim dividend

10 September
Final date for joining or leaving the dividend reinvestment plan for the interim dividend

8 October
Interim dividend paid

Head office
71 Lombard Street
London EC3P 3BS

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