Bank of Scotland plc

2020 Half-Year Results

Member of the Lloyds Banking Group

FORWARD LOOKING STATEMENTS

This document contains certain forward looking statements within the meaning of Section 21E of the US Securities Exchange Act of 1934, as amended, and section 27A of the US Securities Act of 1933, as amended, with respect to the business, strategy, plans and/or results of Bank of Scotland plc together with its subsidiaries (the Group) and its current goals and expectations relating to its future financial condition and performance. Statements that are not historical facts, including statements about the Group's or its directors' and/or management's beliefs and expectations, are forward looking statements. Words such as 'believes', 'anticipates', 'estimates', 'expects', 'intends', 'aims', 'potential', 'will', 'would', 'could', 'considered', 'likely', 'estimate' and variations of these words and similar future or conditional expressions are intended to identify forward looking statements but are not the exclusive means of identifying such statements. Examples of such forward looking statements include, but are not limited to: projections or expectations of the Group's future financial position including profit attributable to shareholders, provisions, economic profit, dividends, capital structure, portfolios, net interest margin, capital ratios, liquidity, risk-weighted assets (RWAs), expenditures or any other financial items or ratios; litigation, regulatory and governmental investigations; the Group's future financial performance; the level and extent of future impairments and write-downs; statements of plans, objectives or goals of the Group or its management including in respect of statements about the future business and economic environments in the UK and elsewhere including, but not limited to, future trends in interest rates, foreign exchange rates, credit and equity market levels and demographic developments; statements about competition, regulation, disposals and consolidation or technological developments in the financial services industry; and statements of assumptions underlying such statements. By their nature, forward looking statements involve risk and uncertainty because they relate to events and depend upon circumstances that will or may occur in the future. Factors that could cause actual business, strategy, plans and/or results (including but not limited to the payment of dividends) to differ materially from forward looking statements made by the Group or on its behalf include, but are not limited to: general economic and business conditions in the UK and internationally; market related trends and developments; fluctuations in interest rates, inflation, exchange rates, stock markets and currencies; any impact of the transition from IBORs to alternative reference rates; the ability to access sufficient sources of capital, liquidity and funding when required; changes to the credit ratings of the Group or any of the Group's immediate or ultimate parent entities; the ability to derive cost savings and other benefits including, but without limitation as a result of any acquisitions, disposals and other strategic transactions; the ability to achieve strategic objectives; changing customer behaviour including consumer spending, saving and borrowing habits; changes to borrower or counterparty credit quality; concentration of financial exposure; management and monitoring of conduct risk; instability in the global financial markets, including Eurozone instability, instability as a result of uncertainty surrounding the exit by the UK from the European Union (EU) and as a result of such exit and the potential for other countries to exit the EU or the Eurozone and the impact of any sovereign credit rating downgrade or other sovereign financial issues; political instability including as a result of any UK general election; technological changes and risks to the security of IT and operational infrastructure, systems, data and information resulting from increased threat of cyber and other attacks; natural, pandemic (including but not limited to the coronavirus disease (COVID-19) outbreak) and other disasters, adverse weather and similar contingencies outside the control of the Group or any of the Group's immediate or ultimate parent entities; inadequate or failed internal or external processes or systems; acts of war, other acts of hostility, terrorist acts and responses to those acts, geopolitical, pandemic or other such events; risks relating to climate change; changes in laws, regulations, practices and accounting standards or taxation, including as a result of the exit by the UK from the EU, or a further possible referendum on Scottish independence; changes to regulatory capital or liquidity requirements and similar contingencies outside the control of the Group or any of the Group's immediate or ultimate parent entities; the policies, decisions and actions of governmental or regulatory authorities or courts in the UK, the EU, the US or elsewhere including the implementation and interpretation of key legislation and regulation together with any resulting impact on the future structure of the Group; the ability to attract and retain senior management and other employees and meet its diversity objectives; actions or omissions by the Group's directors, management or employees including industrial action; changes to the Group's post-retirement defined benefit scheme obligations; the extent of any future impairment charges or write-downs caused by, but not limited to, depressed asset valuations, market disruptions and illiquid markets; the value and effectiveness of any credit protection purchased by the Group; the inability to hedge certain risks economically; the adequacy of loss reserves; the actions of competitors, including non-bank financial services, lending companies and digital innovators and disruptive technologies; and exposure to regulatory or competition scrutiny, legal, regulatory or competition proceedings, investigations or complaints. Please refer to the latest Annual Report on Form 20-F filed by Lloyds Banking Group plc with the US Securities and Exchange Commission for a discussion of certain factors and risks together with examples of forward looking statements. Lloyds Banking Group may also make or disclose written and/or oral forward looking statements in reports filed with or furnished to the US Securities and Exchange Commission, Lloyds Banking Group annual reviews, half-year announcements, proxy statements, offering circulars, prospectuses, press releases and other written materials and in oral statements made by the directors, officers or employees of Lloyds Banking Group to third parties, including financial analysts.

Except as required by any applicable law or regulation, the forward looking statements contained in this document are made as of today's date, and the Group expressly disclaims any obligation or undertaking to release publicly any updates or revisions to any forward looking statements contained in this document to reflect any change in the Group's expectations with regard thereto or any change in events, conditions or circumstances on which any such statement is based. The information, statements and opinions contained in this document do not constitute a public offer under any applicable law or an offer to sell any securities or financial instruments or any advice or recommendation with respect to such securities or financial instruments.

CONTENTS

FINANCIAL REVIEW

Principal activities

Bank of Scotland plc (the Bank) and its subsidiaries (together, the Group) provide a wide range of banking and financial services in the UK and overseas.

The Group's revenue is earned through interest and fees on a broad range of financial services products including current and savings accounts, personal loans, credit cards and mortgages within the retail market; loans and other products to commercial, corporate and asset finance customers; and private banking.

Review of results

Income statement

The Group's profit before tax for the six months ended 30 June 2020 was £11 million, down from £962 million in the six months to 30 June 2019 and profit for the period was £180 million, down from £625 million in the first half of 2019 with both being impacted by a significantly increased impairment charge in the period of £1,465 million.

In the challenging external environment total income fell by £170 million, to £2,846 million in the six months to 30 June 2020 compared to £3,016 million in the six months to 30 June 2019, and was impacted by both lower net interest income and lower other income.

Net interest income of £2,634 million in the half-year to 30 June 2020 was down 3 per cent on the half-year to 30 June 2019 reflecting the lower rate environment, actions taken to support customers including free overdrafts and reduced levels of customer demand during the coronavirus pandemic.

Other income of £212 million in the half-year to 30 June 2020 was £97 million lower compared to £309 million in the half-year to 30 June 2019 as a result of lower customer activity and a subdued demand during the coronavirus lockdown period.

Total operating expenses reduced by £471 million to £1,370 million in period compared to £1,841 million in the half-year to 30 June 2019 with a £234 million decrease in regulatory provisions and a £237 million decrease in other operating expenses. Regulatory provisions comprised £98 million for the six months to 30 June 2020 relating to a number of items across existing programmes; the £280 million charge for PPI in the first half of 2019 was not repeated. Other operating expenses were £237 million lower at £1,272 million in the half-year to 30 June 2020 compared to £1,509 million in the half-year to 30 June 2020, driven by continued cost discipline, efficiencies gained through digitalisation and other process improvements and a reduction in costs recharged to the Group by fellow Lloyds Banking Group undertakings.

The impairment charge increased significantly in the first six months of the year to £1,465 million compared to a charge in the six months to 30 June 2019 of £213 million. The additional charge was primarily driven by updates to the Group's economic outlook and provisions taken on existing restructuring cases where recovery strategies have been directly impacted by the coronavirus outbreak.

The Group recognised a tax credit of £169 million in the period, primarily as a result of an uplift in the value of deferred tax assets of £182 million following the announcement by the UK Government that it would maintain the corporation tax rate at 19 per cent, which was substantively enacted on 17 March 2020.

FINANCIAL REVIEW (continued)

Balance sheet and capital

Total assets at 30 June 2020 were £1,079 million lower at £374,695 million compared to £375,774 million at 31 December 2019 with increases in balances due from fellow Lloyds Banking Group undertakings being more than offset by reductions in the mortgage and credit card books as customer demand reduced during the coronavirus lockdown as well as lower derivative assets.

Total liabilities were £1,236 million lower at £361,448 million at 30 June 2020 compared to £362,684 million at 31 December 2019 with increases in customer deposits which have been driven by growth in current accounts as a result of reduced consumer spending during the coronavirus lockdown period, being more than offset by reductions in amounts owed to fellow Lloyds Banking Group undertakings and lower derivative financial liabilities.

Total equity has increased by £157 million from £13,090 million at 31 December 2019 to £13,247 million at 30 June 2020, with total comprehensive income for the period of £215 million and other movements more than offsetting distributions on other equity instruments of £80 million.

The Bank's common equity tier 1 capital ratio increased to 14.0 per cent[1] (31 December 2019: 13.5 per cent) and the tier 1 capital ratio increased to 18.5 per cent[1] (31 December 2019: 18.2 per cent), as the impact of the impairment charge on the Bank's profits was largely mitigated through the increase in IFRS 9 transitional relief for capital. The resultant increase in the capital ratios was offset in part by an increase in deferred tax assets deducted from capital and an increase in risk-weighted assets. The total capital ratio reduced to 21.7 per cent[1] (31 December 2019: 22.0 per cent), largely reflecting the reduction in the regulatory value of tier 2 capital instruments and the increase in risk-weighted assets, offset in part by the increase in tier 1 capital and an increase in eligible provisions.

Risk-weighted assets increased by £1,310 million, or 2 per cent, to £62,643 million at 30 June 2020 compared to £61,333 million at 31 December 2019, largely reflecting the impact of credit migrations and retail model calibrations, offset in part by the reduction in lending balances.

[1] Incorporating profits for the period that remain subject to formal verification in accordance with the Capital Requirements Regulation.

FINANCIAL REVIEW (continued)

Capital position at 30 June 2020

Following a change in approach the capital position of Bank of Scotland plc is now presented on the basis of the Bank where previously this was presented on the basis of the Group. Prior year comparatives reflect the position of the Bank at 31 December 2019.

The Bank's capital position as at 30 June 2020, incorporating profits for the period that remain subject to formal verification in accordance with the Capital Requirements Regulation and applying CRD IV transitional rules and IFRS 9 transitional arrangements, is set out in the following section.

Capital ratios (Bank)

Capital resources (transitional)	At 30 June 2020 £m	At 31 Dec 2019 £m
Common equity tier 1		
Shareholders' equity per Bank balance sheet	**10,095**	9,972
Cash flow hedging reserve	**27**	41
Other adjustments	**762**	246
	10,884	10,259
Less: deductions from common equity tier 1		
Goodwill and other intangible assets	**(469)**	(461)
Prudent valuation adjustment	**(88)**	(92)
Removal of defined benefit pension surplus	**(56)**	(37)
Deferred tax assets	**(1,504)**	(1,362)
Common equity tier 1 capital	**8,767**	8,307
Additional tier 1		
Additional tier 1 instruments	**2,840**	2,872
Total tier 1 capital	**11,607**	11,179
Tier 2		
Tier 2 instruments	**2,010**	2,572
Eligible provisions and other adjustments	**(8)**	(232)
Total tier 2 capital	**2,002**	2,340
Total capital resources	**13,609**	13,519
Risk-weighted assets	**62,643**	61,333
Common equity tier 1 capital ratio[1]	**14.0%**	13.5%
Tier 1 capital ratio[1]	**18.5%**	18.2%
Total capital ratio[1]	**21.7%**	22.0%

[1] Reflecting the full impact of IFRS 9 at 30 June 2020, without the application of transitional arrangements, the Bank's common equity tier 1 capital ratio would be 12.7 per cent, the tier 1 capital ratio would be 17.3 per cent and the total capital ratio would be 20.9 per cent.

FINANCIAL REVIEW (continued)

	At 30 June 2020 £m	At 31 Dec 2019 £m
Risk-weighted assets (Bank)		
Foundation Internal Ratings Based (IRB) Approach	**4,256**	4,500
Retail IRB Approach	**38,243**	36,696
Other IRB Approach	**2,069**	1,778
IRB Approach	**44,568**	42,974
Standardised Approach	**6,947**	7,278
Credit risk	**51,515**	50,252
Counterparty credit risk	**535**	481
Credit valuation adjustment risk	**92**	78
Operational risk	**9,486**	9,357
Market risk	**338**	492
Underlying risk-weighted assets	**61,966**	60,660
Threshold risk-weighted assets	**677**	673
Total risk-weighted assets	**62,643**	61,333

PRINCIPAL RISKS AND UNCERTAINTIES

The significant risks faced by the Group are detailed below. There has been no change to the description of these risks since disclosed in the Group’s 2019 Annual Report and Accounts.

The external risks faced by the Group may also impact the success of delivering against the Group’s long-term strategic objectives. They include, but are not limited to the coronavirus pandemic, global macro-economic conditions, regulatory developments and the exit of the UK from the European Union.

Through the coronavirus pandemic, the Group has offered help and support to customers with a range of measures, for example with payment holidays and government lending schemes, and continues to actively monitor the outcomes to ensure fair customer treatment. Support has been prioritised for those customers in the most vulnerable situations and those who need help urgently. The Group has also been required to take a series of unprecedented actions to protect colleagues, and has been proactive in limiting the impact with a number of mitigating actions to support colleagues’ safety and wellbeing. Transition planning, including continued engagement with colleagues, remains a key focus in ensuring that the Group continues to protect colleagues and services to customers as the situation continues to evolve, and any lessons learned from the pandemic can be embedded into our future working practices.

The Group’s key cyber controls have continued to operate effectively during the coronavirus pandemic. During this period, the Group has also enhanced monitoring of key suppliers to protect the services received by Group and its ability to protect and maintain service to customers. The Group continues to work with the regulators constructively with regular engagement to ensure they are aware of the impacts on, and mitigating actions taken by the Group.

The Group’s principal risks and uncertainties are reviewed and reported regularly to the Board in alignment with Lloyds Banking Group’s Enterprise Risk Management Framework. Climate risk is being proposed to be introduced as a principal risk category, reflecting the focus in this key area, and work already undertaken by the Group.

Change / Execution – The risk that, in delivering the change agenda, the Group fails to ensure compliance with laws and regulation, maintain effective customer service and availability, and/or operate within the Group’s approved risk appetite.

Data – The risk that the Group fails to effectively govern, manage, and control data (including data processed by third party suppliers) leading to unethical decisions, poor customer outcomes, loss of value to the Group and mistrust.

Operational Resilience – The risk that the Group fails to design resilience into business operations, underlying infrastructure and controls (people, process, technology) so that it is able to withstand external or internal events which could impact the continuation of operations, and fails to respond in a way which meets customer and stakeholder expectations and needs when the continuity of operations is compromised.

Strategic – The risks which result from strategic plans which do not adequately reflect trends in external factors, ineffective business strategy execution, or failure to respond in a timely manner to external environments or changes in stakeholder behaviours and expectations.

Credit – The risk that parties with whom the Group has contracted, fail to meet their financial obligations (both on and off balance sheet). For example observed, anticipated or unexpected changes in the economic environment could impact profitability due to an increase in delinquency, defaults, write-downs and/or expected credit losses.

PRINCIPAL RISKS AND UNCERTAINTIES (continued)

Regulatory and Legal – The risk of financial penalties, regulatory censure, criminal or civil enforcement action or customer detriment as a result of failure to identify, assess, correctly interpret, comply with, or manage regulatory and/or legal requirements.

Conduct – The risk of customer detriment across the customer lifecycle including: failures in product management, distribution and servicing activities; from other risks materialising, or other activities which could undermine the integrity of the market or distort competition, leading to unfair customer outcomes, regulatory censure, reputational damage or financial loss.

Operational – The risk of loss from inadequate or failed internal processes, people and systems, or from external events.

People – The risk that the Group fails to provide an appropriate colleague and customer-centric culture, supported by robust reward and wellbeing policies and processes; effective leadership to manage colleague resources; effective talent and succession management; and robust control to ensure all colleague-related requirements are met.

Capital – The risk that the Bank has a sub-optimal quantity or quality of capital or that capital is inefficiently deployed across Lloyds Banking Group.

Funding and Liquidity – Funding risk is the risk that the Group does not have sufficiently stable and diverse sources of funding or the funding structure is inefficient. Liquidity risk is the risk that the Group does not have sufficient financial resources to meet commitments when they fall due, or can only secure them at excessive cost.

Governance – The risk that the organisational infrastructure fails to provide robust oversight of decision making and the control mechanisms to ensure strategies and management instructions are implemented effectively.

Market – The risk that the Group's capital or earnings profile is affected by adverse market rates, in particular interest rates and credit spreads in the banking business, and credit spreads in Lloyds Banking Group's defined benefit pension schemes.

Model – The risk of financial loss, regulatory censure, reputational damage or customer detriment, as a result of deficiencies in the development, application and ongoing operation of models and rating systems.

Credit risk

Economic conditions have worsened in the first half of 2020 as the coronavirus crisis impact is felt. Given the challenging external environment and expectations of further economic deterioration, the impairment charge has increased significantly during the first half of 2020, predominantly driven by updates to the Group's economic outlook as well as the impact on restructuring cases and single name charges. As a result, expected credit loss allowances increased. There are a number of headwinds which have the potential to further impact the portfolios, including uncertainty around future UK and global economic conditions with a risk of an increase in unemployment and further business failures as the various UK Government schemes wind down in the third quarter, the risk of a second wave of the virus and further, perhaps deeper, measures worsening the economy and the financial health of customers. Outside of these, the possibility still remains of a no-deal end to the transition period of the UK exit from the European Union. In the context of the uncertainty, the Group's risk appetite and risk management approach continues to help ensure that the Group takes timely and proactive actions.

CONDENSED CONSOLIDATED HALF-YEAR FINANCIAL STATEMENTS
CONSOLIDATED INCOME STATEMENT (UNAUDITED)

	Note	**Half-year to 30 June 2020 £m**	Half-year to 30 June 2019 £m
Interest and similar income		**3,977**	4,308
Interest and similar expense		**(1,343)**	(1,601)
Net interest income		**2,634**	2,707
Fee and commission income		**237**	293
Fee and commission expense		**(107)**	(146)
Net fee and commission income	2	**130**	147
Net trading income		**5**	90
Other operating income		**77**	72
Other income		**212**	309
Total income		**2,846**	3,016
Regulatory provisions	10	**(98)**	(332)
Other operating expenses		**(1,272)**	(1,509)
Total operating expenses	3	**(1,370)**	(1,841)
Trading surplus		**1,476**	1,175
Impairment	4	**(1,465)**	(213)
Profit before tax		**11**	962
Tax credit (expense)	5	**169**	(337)
Profit for the period		**180**	625
Profit attributable to ordinary shareholders		**100**	575
Profit attributable to other equity holders		**80**	50
Profit for the period		**180**	625

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (UNAUDITED)

	Half-year to 30 June 2020 £m	Half-year to 30 June 2019 £m
Profit for the period	**180**	625
Other comprehensive income		
Items that will not subsequently be reclassified to profit or loss:		
Post-retirement defined benefit scheme remeasurements:		
Remeasurements before tax	**31**	–
Tax	**(9)**	–
	22	–
Items that may subsequently be reclassified to profit or loss:		
Movement in revaluation reserve in respect of debt securities held at fair value through other comprehensive income:		
Change in fair value	**9**	6
Income statement transfers in respect of disposals	**2**	–
Impairment recognised in the income statement	**1**	–
Tax	**(4)**	(2)
	8	4
Movement in cash flow hedging reserve:		
Effective portion of changes in fair value	**15**	30
Net income statement transfers	**3**	19
Tax	**(4)**	(13)
	14	36
Currency translation differences (tax: nil)	**(9)**	(13)
Other comprehensive income for the period, net of tax	**35**	27
Total comprehensive income for the period	**215**	652
Total comprehensive income attributable to ordinary shareholders	**135**	602
Total comprehensive income attributable to other equity shareholders	**80**	50
Total comprehensive income for the period	**215**	652

CONSOLIDATED BALANCE SHEET

	Note	At 30 June 2020 (unaudited) £m	At 31 Dec 2019 (audited) £m
Assets			
Cash and balances at central banks		**2,608**	2,492
Items in course of collection from banks		**58**	40
Financial assets at fair value through profit or loss	6	**468**	463
Derivative financial instruments		**8,479**	10,338
Loans and advances to banks		**443**	311
Loans and advances to customers		**254,114**	258,315
Debt securities		**19**	–
Due from fellow Lloyds Banking Group undertakings		**101,118**	97,534
Financial assets at amortised cost	7	**355,694**	356,160
Financial assets at fair value through other comprehensive income		**3,013**	2,253
Goodwill		**325**	325
Other intangible assets		**149**	138
Property, plant and equipment		**1,300**	1,407
Current tax recoverable		**528**	104
Deferred tax assets		**1,791**	1,652
Retirement benefit assets		**77**	46
Other assets		**205**	356
Total assets		**374,695**	375,774

CONSOLIDATED BALANCE SHEET (continued)

	Note	**At 30 June 2020 (unaudited) £m**	At 31 Dec 2019 (audited) £m
Equity and liabilities			
Liabilities			
Deposits from banks		**16,118**	16,472
Customer deposits		**158,665**	151,845
Due to fellow Lloyds Banking Group undertakings		**157,521**	161,618
Items in course of transmission to banks		**108**	143
Financial liabilities at fair value through profit or loss		**47**	47
Derivative financial instruments		**9,387**	11,352
Notes in circulation		**1,256**	1,079
Debt securities in issue	9	**9,839**	11,204
Other liabilities		**1,647**	1,831
Current tax liabilities		**3**	15
Other provisions	10	**734**	977
Subordinated liabilities		**6,123**	6,101
Total liabilities		**361,448**	362,684
Equity			
Share capital		**5,847**	5,847
Other reserves		**2,032**	2,019
Retained profits		**2,660**	2,516
Shareholders' equity		**10,539**	10,382
Other equity instruments		**2,700**	2,700
Total equity excluding non-controlling interests		**13,239**	13,082
Non-controlling interests		**8**	8
Total equity		**13,247**	13,090
Total equity and liabilities		**374,695**	375,774

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY (UNAUDITED)

	Attributable to ordinary shareholders						
	Share capital £m	Other reserves £m	Retained profits £m	Total £m	Other equity instruments £m	Non-controlling interests £m	Total £m
Balance at 1 January 2020	**5,847**	**2,019**	**2,516**	**10,382**	**2,700**	**8**	**13,090**
Comprehensive income							
Profit for the period	–	–	100	100	80	–	180
Other comprehensive income							
Post-retirement defined benefit scheme remeasurements, net of tax	–	–	22	22	–	–	22
Movements in revaluation reserve in respect of debt securities held at fair value through other comprehensive income, net of tax	–	8	–	8	–	–	8
Movements in cash flow hedging reserve, net of tax	–	14	–	14	–	–	14
Currency translation differences (tax: nil)	–	(9)	–	(9)	–	–	(9)
Total other comprehensive income	–	13	22	35	–	–	35
Total comprehensive income[1]	–	13	122	135	80	–	215
Transactions with owners							
Distributions on other equity instruments	–	–	–	–	(80)	–	(80)
Capital contribution received	–	–	22	22	–	–	22
Total transactions with owners	–	–	22	22	(80)	–	(58)
Balance at 30 June 2020	5,847	2,032	2,660	10,539	2,700	8	13,247

[1] Total comprehensive income attributable to owners of the parent for the half-year to 30 June 2020 was £215 million (half-year to 30 June 2019: £652 million; half-year to 31 December 2019: £166 million).

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY (UNAUDITED) (continued)

	Attributable to ordinary shareholders						
	Share capital £m	Other reserves £m	Retained profits £m	Total £m	Other equity instruments £m	Non-controlling interests £m	Total £m
Balance at 1 January 2019	5,847	1,892	2,373	10,112	1,500	8	11,620
Comprehensive income							
Profit for the period	–	–	575	575	50	–	625
Other comprehensive income							
Movements in revaluation reserve in respect of debt securities held at fair value through other comprehensive income, net of tax	–	4	–	4	–	–	4
Movements in cash flow hedging reserve, net of tax	–	36	–	36	–	–	36
Currency translation differences (tax: nil)	–	(13)	–	(13)	–	–	(13)
Total other comprehensive income	–	27	–	27	–	–	27
Total comprehensive income	–	27	575	602	50	–	652
Transactions with owners							
Dividends	–	–	(500)	(500)	–	–	(500)
Distributions on other equity instruments	–	–	–	–	(50)	–	(50)
Capital contribution received	–	–	27	27	–	–	27
Total transactions with owners	–	–	(473)	(473)	(50)	–	(523)
Balance at 30 June 2019	5,847	1,919	2,475	10,241	1,500	8	11,749

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY (UNAUDITED) (continued)

	Attributable to ordinary shareholders						
	Share capital £m	Other reserves £m	Retained profits £m	Total £m	Other equity instruments £m	Non-controlling interests £m	Total £m
Balance at 1 July 2019	5,847	1,919	2,475	10,241	1,500	8	11,749
Comprehensive income							
(Loss) profit for the period	–	–	(2)	(2)	51	–	49
Other comprehensive income							
Post-retirement defined benefit scheme remeasurements, net of tax	–	–	17	17	–	–	17
Movements in revaluation reserve in respect of debt securities held at fair value through other comprehensive income, net of tax	–	–	–	–	–	–	–
Movements in cash flow hedging reserve, net of tax	–	(7)	–	(7)	–	–	(7)
Currency translation differences (tax: nil)	–	107	–	107	–	–	107
Total other comprehensive income	–	100	17	117	–	–	117
Total comprehensive income	–	100	15	115	51	–	166
Transactions with owners							
Distributions on other equity instruments	–	–	–	–	(51)	–	(51)
Issue of other equity instruments	–	–	–	–	1,200	–	1,200
Capital contribution received	–	–	26	26	–	–	26
Total transactions with owners	–	–	26	26	1,149	–	1,175
Balance at 31 December 2019	5,847	2,019	2,516	10,382	2,700	8	13,090

CONSOLIDATED CASH FLOW STATEMENT (UNAUDITED)

	Half-year to 30 June 2020 £m	Half-year to 30 June 2019 £m
Profit before tax	**11**	962
Adjustments for:		
Change in operating assets	**1,241**	(5,564)
Change in operating liabilities	**(1,008)**	6,680
Non-cash and other items	**1,104**	(214)
Tax paid	**(421)**	(159)
Net cash provided by operating activities	**927**	1,705
Cash flows from investing activities		
Purchase of financial assets	**(1,178)**	(1,171)
Proceeds from sale and maturity of financial assets	**424**	184
Purchase of fixed assets	**(64)**	(129)
Proceeds from sale of fixed assets	**22**	55
Net cash used in investing activities	**(796)**	(1,061)
Cash flows from financing activities		
Dividends paid to ordinary shareholders	**–**	(500)
Distributions on other equity instruments	**(80)**	(50)
Interest paid on subordinated liabilities	**(90)**	(116)
Repayment of subordinated liabilities	**–**	(328)
Net cash used in financing activities	**(170)**	(994)
Effects of exchange rate changes on cash and cash equivalents	**2**	–
Change in cash and cash equivalents	**(37)**	(350)
Cash and cash equivalents at beginning of period	**759**	1,003
Cash and cash equivalents at end of period	**722**	653

Cash and cash equivalents comprise cash and balances at central banks (excluding mandatory deposits) and amounts due from banks with a maturity of less than three months.

NOTES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1. Accounting policies, presentation and estimates

These condensed consolidated half-year financial statements as at and for the period to 30 June 2020 have been prepared in accordance with the Disclosure Guidance and Transparency Rules of the Financial Conduct Authority (FCA) and with International Accounting Standard 34 (IAS 34), *Interim Financial Reporting* as adopted by the European Union and comprise the results of Bank of Scotland plc (the Bank) together with its subsidiaries (the Group). They do not include all of the information required for full annual financial statements and should be read in conjunction with the Group's consolidated financial statements as at and for the year ended 31 December 2019 which were prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union. Copies of the 2019 Annual Report and Accounts are available on the Lloyds Banking Group's website and are available upon request from Investor Relations, Lloyds Banking Group plc, 25 Gresham Street, London EC2V 7HN.

The directors consider that it is appropriate to continue to adopt the going concern basis in preparing the condensed consolidated half-year financial statements. In reaching this assessment, the directors have considered the implications of the coronavirus pandemic upon the Group's performance and projected funding and capital position and also taken into account the impact of further stress scenarios. On this basis, the directors are satisfied that the Group will maintain adequate levels of funding and capital for the foreseeable future.

The accounting policies are consistent with those applied by the Group in its 2019 Annual Report and Accounts.

Future accounting developments

The IASB has issued a number of minor amendments to IFRSs effective 1 January 2021 and 1 January 2022 (including IFRS 9 *Financial Instruments* and IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*). These amendments are not expected to have a significant impact on the Group.

Critical accounting estimates and judgements

The preparation of the Group's financial statements requires management to make judgements, estimates and assumptions that impact the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Due to the inherent uncertainty in making estimates, actual results reported in future periods may include amounts which differ from those estimates. Estimates, judgements and assumptions are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The Group's significant judgements, estimates and assumptions are unchanged, compared to those applied at 31 December 2019, except as detailed below.

Allowance for impairment losses

At 30 June 2020 the Group's expected credit loss allowance (ECL) was £3,360 million (31 December 2019: £2,148 million), of which £3,227 million (31 December 2019: £2,092 million) was in respect of drawn balances. The calculation of the Group's ECL allowances and its provisions against loan commitments and guarantees under IFRS 9 requires the Group to make a number of judgements, assumptions and estimates.

Forward-looking information

The measurement of expected credit losses is required to reflect an unbiased probability-weighted range of possible future outcomes. In order to do this, the Group has developed an economic model to project a wide range of key impairment drivers using information derived mainly from external sources. These drivers include factors such as the unemployment rate, the house price index, commercial property prices and corporate credit spreads. The model-generated economic scenarios for the six years beyond 2020 are mapped to industry-wide historical loss data by portfolio. Combined losses across portfolios are used to rank the scenarios by severity of loss.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (continued)

1. Accounting policies, presentation and estimates (continued)

Alongside a defined central economic scenario, reflecting the Group's base case assumptions used for medium-term planning purposes, three further economic scenarios are generated to represent the range of future outcomes. The upside, downside and severe downside scenarios are produced by averaging across a group of constituent scenarios around the 15th, 75th and 95th percentiles of the estimated loss distribution around the central case, with the central case expected to lie in the vicinity of the 45th percentile. These locations correspond to scenario weightings that allow for the inclusion of a relatively unlikely severe downside scenario associated with relatively large credit losses. At 31 December 2019 and 30 June 2020, the base case, upside and downside scenarios each carry a 30 per cent weighting, while the severe downside scenario is weighted at 10 per cent. The weights reflect the location of the economic scenarios on the estimated loss distribution.

Following review of the severe downside scenario generated by the modelled approach described above, a judgement was made to increase the severity of GDP and unemployment dispersion from the base case. Whilst the modelled approach gives an unbiased method of creating a loss distribution, it is built on historic experience that does not yet fully capture the unprecedented complexities of the current economic environment and the risk of inflated near-term shocks. The impact of this change has been reflected as a central overlay to reflect the incremental ECL estimated outside the core ECL calculation process. The following economic assumptions include both the modelled severe scenario – used in portfolio level ECL and staging assessment, and the adjusted severe downside - used to generate the final ECL through a central overlay in recognition of more adverse economic outcomes.

The key UK economic assumptions made by the Group are shown below. Compounded growth rates have been calculated on a geometric average basis, they were previously calculated on an arithmetic average basis:

Impact of economic assumptions

	Base case %	**Upside %**	**Downside %**	**Modelled severe %**	**Adjusted severe %**
At 30 June 2020					
GDP	**0.4**	**0.8**	**0.3**	**(0.4)**	**(0.8)**
Interest rate	**0.15**	**1.06**	**0.16**	**0.03**	**0.03**
Unemployment rate	**6.0**	**5.5**	**7.1**	**8.1**	**8.8**
House price growth	**0.4**	**4.7**	**(4.8)**	**(9.6)**	**(9.6)**
Commercial real estate price growth	**(0.6)**	**2.7**	**(3.5)**	**(8.0)**	**(8.0)**
At 31 December 2019					
GDP	1.4	1.7	1.2	0.5	n/a
Interest rate	1.25	2.04	0.49	0.11	n/a
Unemployment rate	4.3	3.9	5.8	7.2	n/a
House price growth	1.0	4.8	(3.2)	(7.7)	n/a
Commercial real estate price growth	0.0	1.8	(3.8)	(7.1)	n/a

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (continued)

1. Accounting policies, presentation and estimates (continued)

The five-year averages shown do not fully reveal the extent of peaks and troughs in the stated assumptions over the period. The tables below illustrate the variability of the assumptions from the start of the scenario period to the peak and trough.

Economic assumptions – start to peak

	Base case %	Upside %	Downside %	Modelled severe %	Adjusted severe %
At 30 June 2020					
GDP	**1.9**	**4.0**	**1.7**	**(1.8)**	**(2.0)**
Interest rate	**0.25**	**1.50**	**0.21**	**0.10**	**0.10**
Unemployment rate	**9.0**	**8.6**	**9.2**	**9.7**	**12.5**
House price growth	**2.1**	**25.8**	**0.4**	**0.4**	**0.4**
Commercial real estate price growth	**(2.7)**	**14.8**	**(2.7)**	**(2.7)**	**(2.7)**
At 31 December 2019					
GDP	7.0	8.6	6.2	2.7	n/a
Interest rate	1.75	2.56	0.75	0.75	n/a
Unemployment rate	4.6	4.6	6.9	8.3	n/a
House price growth	5.2	26.3	(1.9)	(2.3)	n/a
Commercial real estate price growth	0.1	10.4	(0.6)	(1.1)	n/a

Economic assumptions – start to trough

	Base case %	Upside %	Downside %	Modelled severe %	Adjusted severe %
At 30 June 2020					
GDP	**(19.7)**	**(19.5)**	**(19.8)**	**(20.2)**	**(26.1)**
Interest rate	**0.10**	**0.10**	**0.08**	**0.01**	**0.01**
Unemployment rate	**3.9**	**3.9**	**3.9**	**3.9**	**3.9**
House price growth	**(6.1)**	**(3.8)**	**(21.6)**	**(39.7)**	**(39.7)**
Commercial real estate price growth	**(20.0)**	**(11.5)**	**(27.2)**	**(42.3)**	**(42.3)**
At 31 December 2019					
GDP	0.4	0.7	0.2	(2.7)	n/a
Interest rate	0.75	0.75	0.35	0.01	n/a
Unemployment rate	3.8	3.4	3.9	3.9	n/a
House price growth	(2.7)	(0.8)	(14.8)	(33.1)	n/a
Commercial real estate price growth	(0.9)	0.3	(17.5)	(30.9)	n/a

The Group's base case economic scenario has been materially revised in light of the impact of the coronavirus pandemic in the UK and globally. The estimated impact reflects judgements on the net effect of restrictions on economic activity unprecedented in peacetime, large-scale and previously untried government interventions, and lasting behavioural changes by households and businesses.

Although the UK economy has begun to recover as restrictions are eased, there is considerable uncertainty about the pace and eventual extent of the recovery. The Group's base case assumptions reflect an expectation of some enduring scarring as the economy works through the sharp contraction in economic activity in 2020. Consistent with this, and despite the support provided by the Government's Coronavirus Job Retention Scheme and other income and lending assistance, the base case outlook entails a rise in the unemployment rate and weakness in residential and commercial property prices. The Group considers that risks to its base case economic view lie in both directions, reflecting both epidemiological and other developments, including vis-à-vis the UK's transition to new trading arrangements with the European Union.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (continued)

1. Accounting policies, presentation and estimates (continued)

Scenarios by year

	2020 %	2021 %	2022 %	2020-22 %
Base Case				
GDP	**(10.0)**	**6.0**	**3.0**	**(1.8)**
Interest rate	**0.10**	**0.10**	**0.10**	**0.10**
Unemployment rate	**7.2**	**7.0**	**5.7**	**6.7**
House price growth	**(6.0)**	**(0.1)**	**2.9**	**(3.3)**
Commercial real estate price growth	**(20.0)**	**10.0**	**4.0**	**(8.5)**
Upside				
GDP	**(9.5)**	**7.5**	**3.1**	**0.3**
Interest rate	**0.21**	**1.15**	**1.42**	**0.92**
Unemployment rate	**7.1**	**6.2**	**4.9**	**6.1**
House price growth	**(3.7)**	**5.0**	**9.0**	**10.2**
Commercial real estate price growth	**(8.4)**	**18.6**	**3.4**	**12.4**
Downside				
GDP	**(10.2)**	**5.8**	**3.1**	**(2.0)**
Interest rate	**0.09**	**0.12**	**0.19**	**0.13**
Unemployment rate	**7.3**	**7.7**	**6.8**	**7.3**
House price growth	**(8.0)**	**(6.1)**	**(4.5)**	**(17.5)**
Commercial real estate price growth	**(27.2)**	**4.0**	**2.9**	**(22.1)**
Severe downside - Modelled				
GDP	**(10.9)**	**3.0**	**2.2**	**(6.2)**
Interest rate	**0.06**	**0.01**	**0.02**	**0.03**
Unemployment rate	**7.5**	**8.9**	**8.4**	**8.3**
House price growth	**(9.5)**	**(11.5)**	**(11.7)**	**(29.2)**
Commercial real estate price growth	**(36.2)**	**(7.8)**	**(1.4)**	**(41.9)**
Severe downside - Adjusted				
GDP	**(17.2)**	**4.1**	**5.2**	**(9.4)**
Interest rate	**0.06**	**0.01**	**0.02**	**0.03**
Unemployment rate	**8.0**	**11.6**	**9.2**	**9.6**
House price growth	**(9.5)**	**(11.5)**	**(11.7)**	**(29.2)**
Commercial real estate price growth	**(36.2)**	**(7.8)**	**(1.4)**	**(41.9)**

Base Case Scenario by Quarter

	2020 Q1 %	2020 Q2 %	2020 Q3 %	2020 Q4 %	2021 Q1 %	2021 Q2 %	2021 Q3 %	2021 Q4 %
Base Case								
GDP	**(1.6)**	**(19.3)**	**(10.9)**	**(8.1)**	**(4.7)**	**18.1**	**7.7**	**5.1**
Interest rate	**0.10**	**0.10**	**0.10**	**0.10**	**0.10**	**0.10**	**0.10**	**0.10**
Unemployment rate	**3.9**	**7.5**	**8.5**	**9.0**	**8.0**	**7.4**	**6.6**	**6.2**
House price growth	**2.8**	**0.9**	**(2.4)**	**(6.0)**	**(6.3)**	**(4.0)**	**(1.1)**	**(0.1)**
Commercial real estate price growth	**(5.0)**	**(12.3)**	**(19.9)**	**(20.0)**	**(14.4)**	**(3.7)**	**7.7**	**10.0**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (continued)

1. Accounting policies, presentation and estimates (continued)

Post-model adjustments

Limitations in the Group's impairment models or input data may be identified through the on-going assessment and validation of the output of the models. In these circumstances, management make appropriate adjustments to the Group's allowance for impairment losses to ensure the overall provision adequately reflects all material risks. These adjustments are generally determined taking into account the particular attributes of the exposure which have not been adequately captured by the primary impairment models.

Significant increase in credit risk

An assessment of whether credit risk has increased significantly since initial recognition considers the change in the risk of default occurring over the remaining expected life of the financial instrument. In determining whether there has been a significant increase in credit risk, the Group uses quantitative tests based on relative and absolute probability of default movements linked to internal credit ratings together with qualitative indicators such as watchlists and other indicators of historical delinquency, credit weakness or financial difficulty. These quantitative tests are carried out on both observed and forward-looking probabilities of default (PDs) to determine whether a customer has triggered the required deterioration appropriate for their PD at origination. For each major product grouping, models have been developed which utilise historical credit loss data to produce probabilities of default for each scenario; and it is the overall weighted-average forward-looking PD that is used to assist in determining the staging of financial assets.

There have been no changes to the quantitative or qualitative triggers used at 30 June 2020. The Group considers these to continue to perform adequately under the current economic conditions and notably with the widespread use of payment holidays. The use of a payment holiday in itself has not been judged to indicate a significant increase in credit risk, with the underlying long-term credit risk deemed to be driven by economic conditions and captured through the use of forward-looking models. These portfolio level models are capturing the anticipated volume of increased defaults and therefore an appropriate assessment of staging and expected credit loss.

Definition of default

The probability of default (PD) of an exposure, both over a 12 month period and over its lifetime, is a key input to the measurement of the ECL allowance. Default has occurred when there is evidence that the customer is experiencing significant financial difficulty which is likely to affect the ability to repay amounts due. The Group uses a 90 day past due backstop for all of its products except for UK mortgages where a backstop of 180 days past due is in place. The use of payment holidays is not considered to be an automatic trigger of regulatory default and therefore does not automatically trigger Stage 3. Days past due will also not accumulate on any accounts that have taken a payment holiday including those already past due.

Loss given default

The calculation of the ECL allowance also requires an estimate to be made of the loss that will be incurred in the event of a default. The loss given default (LGD) is based on market recovery rates and internal credit assessments. The LGD for customers utilising government funding schemes incorporates an appropriate level of recovery dependent upon the individual scheme and corresponding level of guarantee being used. The use of forecast collateral value indices in determining LGDs continues to be effective despite the temporarily low volumes of transactions upon which those indices are based.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (continued)

1. Accounting policies, presentation and estimates (continued)

Financial instrument valuations

The Group categorises financial instruments carried on the balance sheet at fair value using a three level hierarchy. Financial instruments categorised as level 1 are valued using quoted market prices and therefore minimal estimates are made in determining fair value. The fair value of financial instruments categorised as level 2 and, in particular, level 3 is determined using valuation techniques which involve management judgement and estimates the extent of which depends on the complexity of the instrument and the availability of market observable information.

The principal judgements made by the Group in determining the fair value of its financial assets and liabilities classified as level 3 are primarily related to interest rate spreads and interest rate volatility. Further details on the valuation of level 3 assets and liabilities, including significant unobservable inputs used in the valuation models, together with the effects of reasonably possible alternative assumptions, are given in note 12.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (continued)

2. Net fee and commission income

	Half-year to 30 June 2020 £m	Half-year to 30 June 2019 £m
Fee and commission income:		
Current accounts	**101**	103
Credit and debit card fees	**89**	110
Other	**47**	80
Total fee and commission income	**237**	293
Fee and commission expense	**(107)**	(146)
Net fee and commission income	**130**	147

3. Operating expenses

	Half-year to 30 June 2020 £m	Half-year to 30 June 2019 £m
Administrative expenses		
Staff costs	**605**	641
Premises and equipment	**92**	87
Other expenses	**458**	663
	1,155	1,391
Depreciation and amortisation	**117**	118
Total operating expenses, excluding regulatory provisions	**1,272**	1,509
Regulatory provisions:		
Payment protection insurance provision (note 10)	**–**	280
Other regulatory provisions (note 10)	**98**	52
	98	332
Total operating expenses	**1,370**	1,841

4. Impairment

	Half-year to 30 June 2020 £m	Half-year to 30 June 2019 £m
Impairment charge on drawn balances	**1,387**	209
Loan commitments and financial guarantees	**77**	4
Financial assets at fair value through other comprehensive income	**1**	–
Total impairment charge	**1,465**	213

The Group's impairment charge in the half-year to 30 June 2020 included £91 million (half-year to 30 June 2019: £6 million) in respect of amounts due from fellow Lloyds Banking Group undertakings.

In the half-year to 30 June 2020 the Group's impairment charge included a central adjustment to the severe scenario of £100 million.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (continued)

5. Taxation

In accordance with IAS 34, the Group's income tax expense for the half-year to 30 June 2020 is based on the best estimate of the weighted-average annual income tax rate expected for the full financial year. The tax effects of one-off items are not included in the weighted-average annual income tax rate, but are recognised in the relevant period.

An explanation of the relationship between tax expense and accounting profit is set out below:

	Half-year to 30 June 2020 £m	Half-year to 30 June 2019 £m
Profit before tax	**11**	962
UK corporation tax thereon at 19 per cent (2019: 19 per cent)	**(2)**	(183)
Impact of surcharge on banking profits	**(7)**	(95)
Non-deductible costs: conduct charges	**(3)**	(54)
Other non-deductible costs	**(30)**	(16)
Non-taxable income	**9**	1
Tax relief on coupons on other equity instruments	**15**	10
Remeasurement of deferred tax due to rate changes	**182**	–
Differences in overseas tax rates	**3**	–
Adjustments in respect of prior years	**2**	–
Tax credit (expense)	**169**	(337)

6. Financial assets at fair value through profit or loss

	At 30 June 2020 £m	At 31 Dec 2019 £m
Loans and advances to customers	**468**	463

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (continued)

7. Financial assets at amortised cost

Half-year to 30 June 2020

	Stage 1 £m	Stage 2 £m	Stage 3 £m	Total £m
Loans and advances to banks				
At 1 January 2020	311	–	–	311
Exchange and other movements	18	–	–	18
Additions (repayments)	114	–	–	114
At 30 June 2020	443	–	–	443
Allowance for impairment losses	–	–	–	–
Total loans and advances to banks	443	–	–	443
Loans and advances to customers				
At 1 January 2020	229,741	24,996	5,663	260,400
Exchange and other movements	163	1	(2)	162
Additions (repayments)	(536)	(1,248)	(473)	(2,257)
Transfers to Stage 1	1,620	(1,614)	(6)	–
Transfers to Stage 2	(19,209)	19,637	(428)	–
Transfers to Stage 3	(162)	(1,220)	1,382	–
	(17,751)	16,803	948	–
Recoveries			40	40
Disposal of businesses	(796)	(6)	–	(802)
Financial assets that have been written off			(300)	(300)
At 30 June 2020	210,821	40,546	5,876	257,243
Allowance for impairment losses	(425)	(1,154)	(1,550)	(3,129)
Total loans and advances to customers	210,396	39,392	4,326	254,114
Debt securities				
At 1 January 2020	–	–	1	1
Additions (repayments)	19	–	–	19
Financial assets that have been written off			–	–
At 30 June 2020	19	–	1	20
Allowance for impairment losses	–	–	(1)	(1)
Total debt securities	19	–	–	19
Due from fellow Lloyds Banking Group undertakings				
At 30 June 2020	101,216	–	–	101,216
Allowance for impairment losses	(98)	–	–	(98)
Total due from fellow Lloyds Banking Group undertakings	101,118	–	–	101,118
Total financial assets at amortised cost	311,976	39,392	4,326	355,694

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (continued)

7. Financial assets at amortised cost (continued)

Year ended 31 December 2019

	Stage 1 £m	Stage 2 £m	Stage 3 £m	Total £m
Loans and advances to banks				
At 1 January 2019	471	–	–	471
Exchange and other movements	(20)	–	–	(20)
Additions (repayments)	(140)	–	–	(140)
At 31 December 2019	311	–	–	311
Allowance for impairment losses	–	–	–	–
Total loans and advances to banks	311	–	–	311
Loans and advances to customers				
At 1 January 2019	232,951	25,345	6,143	264,439
Exchange and other movements	(265)	(15)	25	(255)
Additions (repayments)	7,162	(2,583)	(1,102)	3,477
Transfers to Stage 1	4,524	(4,515)	(9)	–
Transfers to Stage 2	(7,591)	8,502	(911)	–
Transfers to Stage 3	(677)	(1,378)	2,055	–
	(3,744)	2,609	1,135	–
Recoveries			169	169
Disposal of businesses	(6,363)	(360)	(42)	(6,765)
Financial assets that have been written off			(665)	(665)
At 31 December 2019	229,741	24,996	5,663	260,400
Allowance for impairment losses	(149)	(749)	(1,187)	(2,085)
Total loans and advances to customers	229,592	24,247	4,476	258,315
Debt securities				
At 1 January 2019	–	–	13	13
Financial assets that have been written off			(12)	(12)
At 31 December 2019	–	–	1	1
Allowance for impairment losses	–	–	(1)	(1)
Total debt securities	–	–	–	–
Due from fellow Lloyds Banking Group undertakings				
At 31 December 2019	97,541	–	–	97,541
Allowance for impairment losses	(7)	–	–	(7)
Total due from fellow Lloyds Banking Group undertakings	97,534	–	–	97,534
Total financial assets at amortised cost	327,437	24,247	4,476	356,160

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (continued)

7. Financial assets at amortised cost (continued)

The movement tables are compiled by comparing the position at the reporting date to that at the beginning of the year.

Transfers between stages are deemed to have taken place at the start of the reporting period, with all other movements shown in the stage in which the asset is held at the period end.

Additions (repayments) comprise new loans originated and repayments of outstanding balances throughout the reporting period. Loans which are written off in the period are first transferred to Stage 3 before acquiring a full allowance and subsequent write-off.

Loans and advances to customers include advances securitised under the Group's securitisation and covered bond programmes (see note 9).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (continued)

8. Allowance for impairment losses

Half-year to 30 June 2020

	Stage 1 £m	Stage 2 £m	Stage 3 £m	Total £m
In respect of drawn balances				
At 1 January 2020	156	749	1,188	2,093
Exchange and other movements	–	–	16	16
Transfers to Stage 1	39	(38)	(1)	–
Transfers to Stage 2	(19)	58	(39)	–
Transfers to Stage 3	(3)	(88)	91	–
Impact of transfers between stages	(23)	254	114	345
	(6)	186	165	345
Other items charged to the income statement	373	220	449	1,042
Charge to the income statement (note 4)	367	406	614	1,387
Advances written off			(300)	(300)
Disposal of businesses	–	(1)	–	(1)
Recoveries of advances written off in previous years			40	40
Discount unwind			(7)	(7)
At 30 June 2020	523	1,154	1,551	3,228
In respect of undrawn balances				
At 1 January 2020	26	28	1	55
Transfers to Stage 1	3	(3)	–	–
Transfers to Stage 2	(1)	1	–	–
Transfers to Stage 3	–	(3)	3	–
Impact of transfers between stages	(1)	12	11	22
	1	7	14	22
Other items charged to the income statement	34	22	(1)	55
Charge to the income statement (note 4)	35	29	13	77
At 30 June 2020	61	57	14	132
Total allowance for impairment losses	584	1,211	1,565	3,360
In respect of:				
Loans and advances to customers	425	1,154	1,550	3,129
Debt securities	–	–	1	1
Amounts due from fellow Lloyds Banking Group undertakings	98	–	–	98
Financial assets at amortised cost	523	1,154	1,551	3,228
Provisions in relation to loan commitments and financial guarantees	61	57	14	132
Total allowance for impairment losses	584	1,211	1,565	3,360

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (continued)

8. Allowance for impairment losses (continued)

Year ended 31 December 2019

	Stage 1 £m	Stage 2 £m	Stage 3 £m	Total £m
In respect of drawn balances				
At 1 January 2019	160	858	1,121	2,139
Exchange and other movements	–	(7)	64	57
Transfers to Stage 1	80	(76)	(4)	–
Transfers to Stage 2	(22)	115	(93)	–
Transfers to Stage 3	(10)	(118)	128	–
Impact of transfers between stages	(65)	129	130	194
	(17)	50	161	194
Other items charged to the income statement	19	(143)	375	251
Charge to the income statement	2	(93)	536	445
Advances written off			(677)	(677)
Disposal of businesses	(6)	(9)	(14)	(29)
Recoveries of advances written off in previous years			169	169
Discount unwind			(11)	(11)
At 31 December 2019	156	749	1,188	2,093
In respect of undrawn balances				
At 1 January 2019	24	23	3	50
Transfers to Stage 1	5	(5)	–	–
Transfers to Stage 2	(1)	1	–	–
Transfers to Stage 3	–	(1)	1	–
Impact of transfers between stages	(4)	6	(1)	1
	–	1	–	1
Other items charged to the income statement	2	4	(2)	4
Charge to the income statement	2	5	(2)	5
At 31 December 2019	26	28	1	55
Total allowance for impairment losses	182	777	1,189	2,148
In respect of:				
Loans and advances to customers	149	749	1,187	2,085
Debt securities	–	–	1	1
Amounts due from fellow Lloyds Banking Group undertakings	7	–	–	7
Financial assets at amortised cost	156	749	1,188	2,093
Provisions in relation to loan commitments and financial guarantees	26	28	1	55
Total allowance for impairment losses	182	777	1,189	2,148

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (continued)

8. Allowance for impairment losses (continued)

The Group's income statement charge comprises:

	Half-year to 30 June 2020 £m	Year ended 31 Dec 2019 £m
Drawn balances	**1,387**	445
Undrawn balances	**77**	5
Financial assets at fair value through other comprehensive income	**1**	–
Total	**1,465**	450

Transfers between stages are deemed to have taken place at the start of the reporting period, with all other movements shown in the stage in which the asset is held at the period end. As assets are transferred between stages, the resulting change in expected credit loss of £345 million for drawn balances, and £22 million for undrawn balances, is presented separately as Impact of transfers between stages, in the stage in which the expected credit loss is recognised at the end of the reporting period.

Other items charged to the income statement include the movements in the expected credit loss as a result of new loans originated and repayments of outstanding balances throughout the reporting period. Loans which are written off in the period are first transferred to Stage 3 before acquiring a full allowance and subsequent write-off. Consequently, recoveries on assets previously written-off also occur in Stage 3 only.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (continued)

9. Debt securities in issue

	At 30 June 2020			At 31 December 2019		
	At fair value through profit or loss £m	**At amortised cost £m**	**Total £m**	At fair value through profit or loss £m	At amortised cost £m	Total £m
Medium-term notes issued	**–**	**2,188**	**2,188**	–	1,106	1,106
Covered bonds	**–**	**3,356**	**3,356**	–	4,529	4,529
Securitisation notes	**47**	**4,295**	**4,342**	47	5,569	5,616
Total debt securities in issue	**47**	**9,839**	**9,886**	47	11,204	11,251

The notes issued by the Group's securitisation and covered bond programmes are held by external parties and by subsidiaries of the Group.

Securitisation programmes
At 30 June 2020, external parties held £4,342 million (31 December 2019: £5,616 million) and the Group's subsidiaries held £23,413 million (31 December 2019: £23,632 million) of total securitisation notes in issue of £27,755 million (31 December 2019: £29,248 million). The notes are secured on loans and advances to customers and debt securities classified at amortised cost amounting to £28,494 million (31 December 2019: £30,417 million), the majority of which have been sold by subsidiary companies to bankruptcy remote structured entities. The structured entities are consolidated fully and all of these loans are retained on the Group's balance sheet.

Covered bond programmes
At 30 June 2020, external parties held £3,356 million (31 December 2019: £4,529 million) and the Group's subsidiaries held £100 million (31 December 2019: £100 million) of total covered bonds in issue of £3,456 million (31 December 2019: £4,629 million). The bonds are secured on certain loans and advances to customers amounting to £6,006 million (31 December 2019: £6,758 million) that have been assigned to bankruptcy remote limited liability partnerships. These loans are retained on the Group's balance sheet.

Cash deposits of £1,757 million (31 December 2019: £2,000 million) which support the debt securities issued by the structured entities, the term advances related to covered bonds and other legal obligations are held by the Group.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (continued)

10. Provisions for liabilities and charges

	Provisions for commitments £m	**Payment protection insurance £m**	**Other regulatory provisions £m**	**Other £m**	**Total £m**
At 31 December 2019	55	596	232	94	977
Exchange and other movements	–	–	–	**1**	**1**
Provisions applied	–	**(279)**	**(153)**	**(22)**	**(454)**
Charge for the period	**77**	–	**98**	**35**	**210**
At 30 June 2020	**132**	**317**	**177**	**108**	**734**

Payment protection insurance

The Group has made provisions for PPI costs totalling £6,421 million, no additional charge has been made in the first half of 2020. Good progress has been made with the review of PPI information requests received and the conversion rate remains low and consistent with the provision assumption of around 10 per cent, albeit operations have been impacted by the coronavirus pandemic in the second quarter.

At 30 June 2020, a provision of £317 million remained unutilised relating to complaints and associated administration costs. Total cash payments were £279 million during the six months to 30 June 2020.

The total amount provided for PPI represents the Group's best estimate of the likely future cost. A number of risks and uncertainties remain including processing the remaining outstanding complaints. These may also be impacted by any further regulatory changes. The cost could therefore differ from the Group's estimates and the assumptions underpinning them, and could result in a further provision being required.

For every 1 per cent increase in PIR conversion rate on the stock as at the industry deadline, the Group would expect an additional charge of approximately £40 million.

Other provisions for legal actions and regulatory matters

In the course of its business, the Group is engaged in discussions with the PRA, FCA and other UK and overseas regulators and other governmental authorities on a range of matters. The Group also receives complaints in connection with its past conduct and claims brought by or on behalf of current and former employees, customers, investors and other third parties and is subject to legal proceedings and other legal actions. Where significant, provisions are held against the costs expected to be incurred in relation to these matters and matters arising from related internal reviews. During the six months to 30 June 2020 the Group charged a further £98 million in respect of legal actions and other regulatory matters, and the unutilised balance at 30 June 2020 was £177 million (31 December 2019: £232 million). The most significant items are as follows.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (continued)

10. Provisions for liabilities and charges (continued)

Arrears handling related activities

The Group has provided an additional £19 million during the half-year to 30 June 2020 for arrears handling related activities, bringing the total provided to date to £649 million; the unutilised balance at 30 June 2020 was £45 million.

HBOS Reading – review

The Group completed its compensation assessment for all 71 business customers within the customer review in the fourth quarter of 2019. In total more than £109 million of compensation has been accepted by victims of the HBOS Reading fraud, in addition to £14 million for ex-gratia payments and £6 million for the re-imbursements of legal fees. Sir Ross Cranston's Quality Assurance review was concluded on 10 December 2019 and made a number of recommendations, including a re-assessment of direct and consequential losses by an independent panel, an extension of debt relief, and a wider definition of de facto directors. Details of the panel were announced on 3 April 2020 and the panel's full scope and methodology was published on 7 July 2020. Details of an appeal process for the further assessments of debt relief and de facto director status have also been announced. The Group has begun its assessment of customer claims for further debt relief and de facto director status. The Group has committed to implementing Sir Ross's recommendations in full. It is not possible to estimate at this stage what the financial impact will be.

11. Contingent liabilities, commitments and guarantees

Interchange fees

With respect to multi-lateral interchange fees (MIFs), the Lloyds Banking Group is not involved in the ongoing litigation which involves card schemes such as Visa and Mastercard (as described below). However, the Lloyds Banking Group is a member / licensee of Visa and Mastercard and other card schemes. The litigation in question is as follows:

- litigation brought by retailers against both Visa and Mastercard which continues in the English Courts (this includes a judgment of the Supreme Court in June 2020 upholding the Court of Appeal's finding in 2018 that historic interchange arrangements of Mastercard and Visa infringed competition law); and
- litigation brought on behalf of UK consumers in the English Courts against Mastercard (judgment is awaited from the Supreme Court on whether the collective proceedings may be permissible).

Any impact on the Lloyds Banking Group of the litigation against Visa and Mastercard remains uncertain at this time. Insofar as Visa is required to pay damages to retailers for interchange fees set prior to June 2016, contractual arrangements to allocate liability have been agreed between various UK banks (including the Lloyds Banking Group) and Visa Inc, as part of Visa Inc's acquisition of Visa Europe in 2016. These arrangements cap the maximum amount of liability to which the Lloyds Banking Group may be subject, and this cap is set at the cash consideration received by the Lloyds Banking Group for the sale of its stake in Visa Europe to Visa Inc in 2016.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (continued)

11. Contingent liabilities, commitments and guarantees (continued)

LIBOR and other trading rates

In July 2014, the Lloyds Banking Group announced that it had reached settlements totalling £217 million (at 30 June 2014 exchange rates) to resolve with UK and US federal authorities legacy issues regarding the manipulation several years ago of Group companies' submissions to the British Bankers' Association (BBA) London Interbank Offered Rate (LIBOR) and Sterling Repo Rate. The Swiss Competition Commission concluded its investigation against Lloyds Bank plc in June 2019. However, the Group continues to cooperate with various other government and regulatory authorities, including a number of US State Attorneys General, in conjunction with their investigations into submissions made by panel members to the bodies that set LIBOR and various other interbank offered rates.

Certain Lloyds Banking Group companies, together with other panel banks, have also been named as defendants in private lawsuits, including purported class action suits, in the US in connection with their roles as panel banks contributing to the setting of US Dollar, Japanese Yen and Sterling LIBOR and the Australian BBSW Reference Rate. Certain of the plaintiffs' claims have been dismissed by the US Federal Court for Southern District of New York (subject to appeals).

Certain Lloyds Banking Group companies are also named as defendants in (i) UK based claims; and (ii) two Dutch class actions, raising LIBOR manipulation allegations. A number of the claims against the Lloyds Banking Group in relation to the alleged mis-sale of interest rate hedging products also include allegations of LIBOR manipulation.

It is currently not possible to predict the scope and ultimate outcome on the Group of the various outstanding regulatory investigations not encompassed by the settlements, any private lawsuits or any related challenges to the interpretation or validity of any of the Lloyds Banking Group's contractual arrangements, including their timing and scale.

Tax authorities

The Lloyds Banking Group has an open matter in relation to a claim for group relief of losses incurred in its former Irish banking subsidiary, which ceased trading on 31 December 2010. In 2013 HMRC informed the Lloyds Banking Group that their interpretation of the UK rules which allow the offset of such losses denies the claim for group relief of losses. If HMRC's position is found to be correct, management estimate that this would result in an increase in the Group's current tax liabilities of approximately £175 million (including interest). The Lloyds Banking Group does not agree with HMRC's position and, having taken appropriate advice, does not consider that this is a case where additional tax will ultimately fall due.

Other legal actions and regulatory matters

In addition, during the ordinary course of business the Group is subject to other complaints and threatened or actual legal proceedings (including class or group action claims) brought by or on behalf of current or former employees, customers, investors or other third parties, as well as legal and regulatory reviews, challenges, investigations and enforcement actions, both in the UK and overseas. All such material matters are periodically reassessed, with the assistance of external professional advisers where appropriate, to determine the likelihood of the Group incurring a liability. In those instances where it is concluded that it is more likely than not that a payment will be made, a provision is established to management's best estimate of the amount required at the relevant balance sheet date. In some cases it will not be possible to form a view, for example because the facts are unclear or because further time is needed to assess properly the merits of the case, and no provisions are held in relation to such matters. In these circumstances, specific disclosure in relation to a contingent liability will be made where material. However the Group does not currently expect the final outcome of any such case to have a material adverse effect on its financial position, operations or cash flows.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (continued)

11. Contingent liabilities, commitments and guarantees (continued)

Contingent liabilities, commitments and guarantees arising from the banking business

	At 30 June 2020 £m	At 31 Dec 2019 £m
Contingent liabilities		
Acceptances and endorsements	**–**	1
Other:		
Other items serving as direct credit substitutes	**32**	20
Performance bonds and other transaction-related contingencies	**175**	199
	207	219
Total contingent liabilities	**207**	220
Commitments and guarantees		
Documentary credits and other short-term trade-related transactions	**1**	–
Forward asset purchases and forward deposits placed	**55**	14
Undrawn formal standby facilities, credit lines and other commitments to lend:		
Less than 1 year original maturity:		
Mortgage offers made	**12,550**	11,271
Other commitments and guarantees	**25,216**	24,217
	37,766	35,488
1 year or over original maturity	**2,225**	2,410
Total commitments and guarantees	**40,047**	37,912

Of the amounts shown above in respect of undrawn formal standby facilities, credit lines and other commitments to lend, £15,345 million (31 December 2019: £14,478 million) was irrevocable.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (continued)

12. Fair values of financial assets and liabilities

The valuations of financial instruments have been classified into three levels according to the quality and reliability of information used to determine those fair values. Note 40 to the Group's 2019 financial statements describes the definitions of the three levels in the fair value hierarchy.

Valuation control framework

Key elements of the valuation control framework, which covers processes for all levels in the fair value hierarchy including level 3 portfolios, include model validation (incorporating pre-trade and post-trade testing), product implementation review and independent price verification. Formal committees meet quarterly to discuss and approve valuations in more judgemental areas.

Transfers into and out of level 3 portfolios

Transfers out of level 3 portfolios arise when inputs that could have a significant impact on the instrument's valuation become market observable; conversely, transfers into the portfolios arise when sources of data cease to be observable.

Valuation methodology

For level 2 and level 3 portfolios, there is no significant change to the valuation methodology (techniques and inputs) disclosed in the Group's 2019 Annual Report and Accounts applied to these portfolios.

The table below summarises the carrying values of financial assets and liabilities presented on the Group's balance sheet. The fair values presented in the table are at a specific date and may be significantly different from the amounts which will actually be paid or received on the maturity or settlement date.

	At 30 June 2020		At 31 December 2019	
	Carrying value £m	**Fair value £m**	Carrying value £m	Fair value £m
Financial assets				
Financial assets at fair value through profit or loss	**468**	**468**	463	463
Derivative financial instruments	**8,479**	**8,479**	10,338	10,338
Loans and advances to banks	**443**	**444**	311	311
Loans and advances to customers	**254,114**	**257,178**	258,315	261,438
Debt securities	**19**	**19**	–	–
Due from fellow Lloyds Banking Group undertakings	**101,118**	**101,118**	97,534	97,534
Financial assets at amortised cost:	**355,694**	**358,759**	356,160	359,283
Financial assets at fair value through other comprehensive income	**3,013**	**3,013**	2,253	2,253
Financial liabilities				
Deposits from banks	**16,118**	**16,118**	16,472	16,472
Customer deposits	**158,665**	**158,836**	151,845	152,038
Due to fellow Lloyds Banking Group undertakings	**157,521**	**157,521**	161,618	161,618
Financial liabilities at fair value through profit or loss	**47**	**47**	47	47
Derivative financial instruments	**9,387**	**9,387**	11,352	11,352
Debt securities in issue	**9,839**	**10,162**	11,204	11,146
Subordinated liabilities	**6,123**	**6,170**	6,101	6,133

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (continued)

12. Fair values of financial assets and liabilities (continued)

The carrying amount of the following financial instruments is a reasonable approximation of fair value: cash and balances at central banks, items in the course of collection from banks, items in course of transmission to banks and notes in circulation.

The Group manages valuation adjustments for its derivative exposures on a net basis; the Group determines their fair values on the basis of their net exposures. In all other cases, fair values of financial assets and liabilities measured at fair value are determined on the basis of their gross exposures.

The following tables provide an analysis of the financial assets and liabilities of the Group that are carried at fair value in the Group's consolidated balance sheet, grouped into levels 1 to 3 based on the degree to which the fair value is observable.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (continued)

12. Fair values of financial assets and liabilities (**continued**)

Financial assets

	Level 1 £m	**Level 2 £m**	**Level 3 £m**	**Total £m**
At 30 June 2020				
Loans and advances to customers at fair value through profit or loss	**–**	**–**	**468**	**468**
Debt securities at fair value through other comprehensive income	**–**	**3,013**	**–**	**3,013**
Derivative financial instruments	**–**	**8,466**	**13**	**8,479**
Total financial assets carried at fair value	**–**	**11,479**	**481**	**11,960**

	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
At 31 December 2019				
Loans and advances to customers at fair value through profit or loss	–	–	463	463
Debt securities at fair value through other comprehensive income	–	2,253	–	2,253
Derivative financial instruments	–	10,338	–	10,338
Total financial assets carried at fair value	–	12,591	463	13,054

Financial liabilities

	Level 1 £m	**Level 2 £m**	**Level 3 £m**	**Total £m**
At 30 June 2020				
Financial liabilities designated at fair value through profit or loss	**–**	**–**	**47**	**47**
Derivative financial instruments	**–**	**9,090**	**297**	**9,387**
Total financial liabilities carried at fair value	**–**	**9,090**	**344**	**9,434**

	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
At 31 December 2019				
Financial liabilities designated at fair value through profit or loss	–	–	47	47
Derivative financial instruments	–	11,055	297	11,352
Total financial liabilities carried at fair value	–	11,055	344	11,399

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (continued)

12. Fair values of financial assets and liabilities (continued)

Movements in level 3 portfolio

The tables below analyse movements in the level 3 financial assets portfolio.

	Financial assets at fair value through profit or loss £m	**Derivative assets £m**	**Total financial assets carried at fair value £m**
At 1 January 2020	**463**	**–**	**463**
Gains recognised in the income statement within other income	**18**	**2**	**20**
Sales	**(13)**	–	**(13)**
Transfers into the level 3 portfolio	**–**	**11**	**11**
At 30 June 2020	**468**	**13**	**481**
Gains recognised in the income statement within other income relating to those assets held at 30 June 2020	**9**	**–**	**9**

	Financial assets at fair value through profit or loss £m	Derivative assets £m	Total financial assets carried at fair value £m
At 1 January 2019	110	–	110
(Losses) gains recognised in the income statement within other income	(1)	1	–
Additions	–	1	1
Sales	(8)	–	(8)
Transfers into the level 3 portfolio	399	11	410
At 30 June 2019	500	13	513
Gains recognised in the income statement within other income relating to those assets held at 30 June 2019	–	–	–

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (continued)

12. Fair values of financial assets and liabilities (continued)

Movements in level 3 portfolio

The tables below analyse movements in the level 3 financial liabilities portfolio.

	Financial liabilities at fair value through profit or loss £m	**Derivative liabilities £m**	**Total financial liabilities carried at fair value £m**
At 1 January 2020	**47**	**297**	**344**
Losses recognised in the income statement within other income	**1**	**8**	**9**
Redemptions	**(1)**	**(8)**	**(9)**
At 30 June 2020	**47**	**297**	**344**
Gains recognised in the income statement within other income relating to those liabilities held at 30 June 2020	**–**	**–**	**–**

	Financial liabilities at fair value through profit or loss £m	Derivative liabilities £m	Total financial liabilities carried at fair value £m
At 1 January 2019	–	–	–
Redemptions	(1)	(12)	(13)
Transfers into the level 3 portfolio	53	344	397
At 30 June 2019	52	332	384
Gains recognised in the income statement within other income relating to those liabilities held at 30 June 2019	–	–	–

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (continued)

12. Fair values of financial assets and liabilities (continued)

The tables below set out the effects of reasonably possible alternative assumptions for categories of level 3 financial assets and financial liabilities.

				At 30 June 2020		
					Effect of reasonably possible alternative assumptions[1]	
	Valuation technique(s)	**Significant unobservable inputs**	**Range[2]**	**Carrying value £m**	**Favourable changes £m**	**Unfavourable changes £m**
Financial assets at fair value through profit or loss:						
Interest rate derivatives	Option pricing model	Interest rate volatility	**32% / 58%**	**13**	**–**	**–**
Loans and advances to customers	Discounted cash flows	Interest rate spreads	**50 bps / 103 bps**	**468**	**22**	**(22)**
Financial assets carried at fair value				**481**		
Financial liabilities at fair value through profit or loss:						
Debt securities in issue	Discounted cash flows	Interest rate spreads	**+/- 50 bps**	**47**	**1**	**(1)**
Derivative financial liabilities:						
Interest rate derivatives	Market values – property valuation	HPI	**+/- 5 bps**	**297**	**17**	**(17)**
Financial liabilities carried at fair value				**344**		

[1] Where the exposure to an unobservable input is managed on a net basis, only the net impact is shown in the table.

[2] The range represents the highest and lowest inputs used in the level 3 valuations.

				At 31 December 2019		
					Effect of reasonably possible alternative assumptions[1]	
	Valuation technique(s)	Significant unobservable inputs	Range[2]	Carrying value £m	Favourable changes £m	Unfavourable changes £m
Financial assets at fair value through profit or loss:						
Loans and advances to customers	Discounted cash flows	Interest rate spreads	50bps / 102bps	463	22	(22)
Financial assets carried at fair value				463		
Financial liabilities at fair value through profit or loss:						
Debt securities in issue	Discounted cash flows	Interest rate spreads	+/- 50 bps	47	1	(1)
Derivative financial liabilities:						
Interest rate derivatives	Market values – property valuation	HPI	+/- 5 bps	297	17	(17)
Financial liabilities carried at fair value				344		

[1] Where the exposure to an unobservable input is managed on a net basis, only the net impact is shown in the table.

[2] The range represents the highest and lowest inputs used in the level 3 valuations.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (continued)

12. Fair values of financial assets and liabilities (continued)

Unobservable inputs

Significant unobservable inputs affecting the valuation of debt securities, unlisted equity investments and derivatives are unchanged from those described in the Group's 2019 financial statements.

Reasonably possible alternative assumptions

Valuation techniques applied to many of the Group's level 3 instruments often involve the use of two or more inputs whose relationship is interdependent. The calculation of the effect of reasonably possible alternative assumptions included in the table above reflects such relationships and are unchanged from those described in the Group's 2019 financial statements.

13. Related party transactions

Balances and transactions with Lloyds Banking Group plc and fellow Lloyds Banking Group undertakings

The Bank and its subsidiaries have balances due to and from the Bank's ultimate parent company, Lloyds Banking Group plc, and fellow Lloyds Banking Group undertakings. These are included on the balance sheet as follows:

	At 30 June 2020 £m	At 31 Dec 2019 £m
Assets		
Derivative financial instruments	**4,751**	7,026
Due from fellow Lloyds Banking Group undertakings	**101,118**	97,534
Liabilities		
Due to fellow Lloyds Banking Group undertakings	**157,521**	161,618
Derivative financial instruments	**7,368**	9,107
Debt securities in issue	**1,224**	45
Subordinated liabilities	**5,529**	5,502

During the half-year to 30 June 2020 the Group earned £260 million (half-year ended 30 June 2019: £274 million) of interest income and incurred £1,018 million (half-year ended 30 June 2019: £1,105 million) of interest expense on balances and transactions with Lloyds Banking Group plc and fellow Lloyds Banking Group undertakings.

In addition, during the half-year to 30 June 2020 the Group incurred expenditure of £20 million (half-year ended 30 June 2019: £28 million) on behalf of fellow Lloyds Banking Group undertakings which was recharged to those undertakings; and fellow Lloyds Banking Group undertakings incurred expenditure of £331 million (half-year ended 30 June 2019: £446 million) on behalf of the Group which has been recharged to the Group.

Other related party transactions

Other related party transactions for the half-year to 30 June 2020 are similar in nature to those for the year ended 31 December 2019.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (continued)

14. Ultimate parent undertaking

Bank of Scotland plc's ultimate parent undertaking and controlling party is Lloyds Banking Group plc which is incorporated in Scotland. Lloyds Banking Group plc has published consolidated accounts for the year ended 31 December 2019 and copies may be obtained from Investor Relations, Lloyds Banking Group, 25 Gresham Street, London EC2V 7HN and are available for download from www.lloydsbankinggroup.com

15. Other information

The financial information included in these condensed consolidated half-year financial statements does not constitute statutory accounts within the meaning of section 434 of the Companies Act 2006. Statutory accounts for the year ended 31 December 2019 have been delivered to the Registrar of Companies. The auditors' report on those accounts was unqualified, did not include an emphasis of matter paragraph and did not include a statement under section 498 of the Companies Act 2006.

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The directors listed below (being all the directors of Bank of Scotland plc) confirm that to the best of their knowledge these condensed consolidated half-year financial statements have been prepared in accordance with International Accounting Standard 34, *Interim Financial Reporting*, as adopted by the European Union, and that the half-year results herein includes a fair review of the information required by DTR 4.2.7R and DTR 4.2.8R, namely:

- an indication of important events that have occurred during the six months ended 30 June 2020 and their impact on the condensed consolidated half-year financial statements, and a description of the principal risks and uncertainties for the remaining six months of the financial year; and
- material related party transactions in the six months ended 30 June 2020 and any material changes in the related party transactions described in the last annual report.

Signed on behalf of the board by

António Horta-Osório
Group Chief Executive
29 July 2020

Bank of Scotland plc board of directors:
António Horta-Osório (Executive Director and Group Chief Executive)
William Chalmers (Executive Director and Chief Financial Officer)
Juan Colombás (Executive Director and Chief Operating Officer)
Lord Blackwell (Chairman)
Alan Dickinson (Deputy Chairman)
Sarah Bentley
Brendan Gilligan
Simon Henry
Nigel Hinshelwood (Senior Independent Director)
Sarah Legg
Lord Lupton CBE
Amanda Mackenzie OBE
Nick Prettejohn
Stuart Sinclair
Sara Weller CBE
Catherine Woods

INDEPENDENT REVIEW REPORT TO BANK OF SCOTLAND PLC

Report on the condensed consolidated half-year financial statements

Our conclusion

We have reviewed Bank of Scotland plc's condensed consolidated half-year financial statements (the ‘interim financial statements’) in the 2020 Half-Year Results of Bank of Scotland plc (the ‘Company’) for the six month period ended 30 June 2020. Based on our review, nothing has come to our attention that causes us to believe that the interim financial statements are not prepared, in all material respects, in accordance with International Accounting Standard 34, ‘Interim Financial Reporting’, as adopted by the European Union and the Disclosure Guidance and Transparency Rules sourcebook of the United Kingdom’s Financial Conduct Authority.

What we have reviewed

The interim financial statements comprise:

- the consolidated balance sheet as at 30 June 2020;
- the consolidated income statement and consolidated statement of comprehensive income for the period then ended;
- the consolidated cash flow statement for the period then ended;
- the consolidated statement of changes in equity for the period then ended; and
- the explanatory notes to the interim financial statements.

The interim financial statements included in the 2020 Half-Year Results have been prepared in accordance with International Accounting Standard 34, ‘Interim Financial Reporting’, as adopted by the European Union and the Disclosure Guidance and Transparency Rules sourcebook of the United Kingdom’s Financial Conduct Authority.

As disclosed in note 1 to the interim financial statements, the financial reporting framework that has been applied in the preparation of the full annual financial statements of the Group is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

Responsibilities for the interim financial statements and the review

Our responsibilities and those of the directors

The 2020 Half-Year Results, including the interim financial statements, is the responsibility of, and has been approved by, the directors. The directors are responsible for preparing the 2020 Half-Year Results in accordance with the Disclosure Guidance and Transparency Rules sourcebook of the United Kingdom’s Financial Conduct Authority.

Our responsibility is to express a conclusion on the interim financial statements in the 2020 Half-Year Results based on our review. This report, including the conclusion, has been prepared for and only for the Company for the purpose of complying with the Disclosure Guidance and Transparency Rules sourcebook of the United Kingdom’s Financial Conduct Authority and for no other purpose. We do not, in giving this conclusion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

What a review of interim financial statements involves

We conducted our review in accordance with International Standard on Review Engagements (UK and Ireland) 2410, ‘Review of Interim Financial Information Performed by the Independent Auditor of the Entity’ issued by the Auditing Practices Board for use in the United Kingdom. A review of interim financial information consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures.

A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing (UK) and, consequently, does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

We have read the other information contained in the 2020 Half-Year Results and considered whether it contains any apparent misstatements or material inconsistencies with the information in the interim financial statements.

PricewaterhouseCoopers LLP
Chartered Accountants
London
29 July 2020

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