HBOS plc

2023 Half-Year Results

26 July 2023

Member of the Lloyds Banking Group

CONTENTS

FINANCIAL REVIEW

Principal activities

HBOS plc (the Company) and its subsidiaries (together, the Group) provide a wide range of banking and financial services. 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 and loans and other products to commercial and corporate customers.

Income statement

The Group made a loss before tax for the half-year to 30 June 2023 of £33 million, compared to a profit before tax of £1,190 million for the same period in 2022, as a result of lower net interest income and a higher impairment charge. Profit after tax was £32 million (half-year to 30 June 2022: £886 million).

Total income for the half-year to 30 June 2023 was £1,785 million, a decrease of 33 per cent on the first half of 2022. Net interest income was £1,601 million, compared to £2,482 million for the same period in 2022. This was impacted by higher funding costs on intra-group borrowing which more than offset the benefits from UK Bank Rate increases and effects of average interest-earning asset growth.

Other income of £184 million was 2 per cent higher than the first half of 2022, driven by increases in both net fee and commission income and other operating income. Net fee and commission income for the period was £184 million compared to £154 million in the first half of 2022, reflecting improved credit and debit card performance. Other operating income in the period of £56 million was up £28 million.

Operating expenses of £1,439 million were 1 per cent lower than in the first half of 2022, due to higher depreciation given increased strategic investment, partly offset by lower staff costs. The Group recognised remediation costs of £11 million (half-year to 30 June 2022: £2 million). There have been no further charges relating to HBOS Reading and the provision held continues to reflect the Group's best estimate of its full liability, albeit uncertainties remain.

The impairment charge was £379 million compared with a £18 million charge in the half-year to 30 June 2022. The increase reflects the expected credit loss (ECL) allowance build from Stage 1 loans rolling forward into a more adverse economic outlook, as well as increased flows to default primarily in legacy variable rate mortgage portfolios and the inclusion of MBNA limited following the transfer from Lloyds Bank plc in November 2022. This increase was partly offset by a lower charge from economic outlook revisions. The Group's ECL allowance increased to £3,399 million, compared to £3,324 million at 31 December 2022 resulting from the Stage 3 increases in the mortgages and commercial portfolios alongside low levels of write offs in the period. Asset quality remains resilient with only modest deterioration to date from a low base, with credit performance similar, or remaining favourable, to pre-pandemic experience.

The Group recognised a tax credit of £65 million in the period, compared to an expense of £304 million in the first half of 2022.

Balance sheet

The Group's balance sheet has remained broadly stable compared to 31 December 2022. Total assets of £319,559 million were down £8 million compared to £319,567 million at 31 December 2022. Financial assets at amortised cost were £747 million lower at £305,922 million compared to £306,669 million at 31 December 2022 with debt securities £1,957 million higher, offset by a reduction in balances due from fellow Lloyds Banking Group undertakings of £584 million and loans and advances to customers of £2,172 million to £290,244 million. The reduction in loans and advances to customers was largely as a result of the exit of £2.5 billion of legacy mortgage loans.

Total liabilities of £301,848 million were down £297 million compared to £302,145 million at 31 December 2022 driven by a reduction in customer deposits of £3,951 million in the period to £162,412 million. The reduction in the first half included a decrease in current account balances from tax payments, higher spend and a more competitive market, partly offset by growth in savings balances. This was partially offset by increases in balances due to fellow Lloyds Banking Group undertakings of £2,366 million and debt securities in issue of £1,455 million.

Total equity increased by £289 million from £17,422 million at 31 December 2022 to £17,711 million at 30 June 2023.

Capital

Neither the Company nor the Group are regulated from a capital perspective. Regulatory capital is instead managed in the Company's principal banking subsidiary, Bank of Scotland plc.

PRINCIPAL RISKS AND UNCERTAINTIES

The most important risks faced by the Group are detailed below. The external risks faced by the Group may impact the success of delivering against the Group's long-term strategic objectives. They include, but are not limited to macroeconomic uncertainty; high interest rates and high inflation which are contributing to the cost of living increases and associated implications for UK consumers and businesses.

Heightened monitoring is in place across the Group's portfolios to identify signs of affordability stress. The Group has experienced only modest deterioration in credit performance across its portfolio to date, most notably in UK mortgages where new to arrears and flows to default have increased on legacy variable rate loans. The Group continues to work with its customers to proactively support them through cost of living pressures, the impact from rising interest rates and any deterioration in broader economic conditions.

The Group remains committed to the effective implementation and embedding of Consumer Duty into its purpose, strategy and culture in order to deliver good outcomes for our customers throughout their journeys. This activity seeks to align and enhance the Group's approach to supporting all customers, including those who may be vulnerable and customers in financial difficulty.

CRD IV model changes reflecting the revised regulatory standards introduced in 2022 remain subject to approval by the PRA with the resultant risk-weighted asset and expected loss outcome dependent upon this. An adjustment to risk-weighted assets has been taken in the second quarter, to reflect the anticipated impact of CRD IV models, following a further iteration of model development. On that basis final impacts remain uncertain and further increases could be required.

There have been minor changes to the definition of these risks compared to those disclosed in the Group's 2022 Annual Report and Accounts, such as clarifying third party and outsourced arrangements. The Group continues to conduct a detailed review of its Enterprise Risk Management Framework, which may result in a reclassification of the principal risks.

The Group's principal risks and uncertainties are reviewed and reported regularly to the Board in alignment with the Group's Enterprise Risk Management Framework.

Capital risk – The risk that an insufficient quantity or quality of capital is held to meet regulatory requirements or to support business strategy, an inefficient level of capital is held or that capital is inefficiently deployed across the Group.

Change and execution risk – The risk that, in delivering its change agenda, the Group fails to ensure compliance with laws and regulation, maintain available and effective customer and colleague services, and/or operate within the Group's risk appetite.

Climate risk – The risk that the Group experiences losses and/or reputational damage, either from the impacts of climate change and the transition to net zero, or as a result of the Group's responses to tackling climate change.

Conduct risk – 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. Customer harm or detriment is defined as consumer loss, distress or inconvenience to customers due to breaches of regulatory or internal requirements or our wider duty to act fairly and reasonably.

Credit risk – The risk that parties with whom the Group has contracted fail to meet their financial obligations (both on and off-balance sheet).

Data risk – The risk of the Group failing to effectively govern, manage and protect its data throughout its lifecycle, including data processed by third parties, or failure to drive value from data; leading to unethical decision making, poor customer outcomes, loss of value to the Group and mistrust.

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

Market risk – The risk that the Group's capital or earnings profile is affected by adverse market rates or prices, in particular interest rates, and equity prices.

PRINCIPAL RISKS AND UNCERTAINTIES (continued)

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

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

Operational resilience risk – The risk that the Group fails to design resilience into business operations including those that are outsourced, underlying infrastructure and controls (people, property, 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 customers and stakeholder expectations and needs when the continuity of operations is compromised.

People risk – 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.

Regulatory and legal risk – 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.

Strategic risk – The risk which results from:

- Incorrect assumptions about internal or external operating environments
- Failure to understand the potential impact of strategic responses and business plans on existing risk types
- Failure to respond or the inappropriate strategic response to material changes in the external or internal operating environments

STATUTORY INFORMATION

Condensed consolidated half-year financial statements (unaudited)

Notes

CONSOLIDATED INCOME STATEMENT (UNAUDITED)

	Note	**Half-year to 30 Jun 2023 £m**	Half-year to 30 Jun 2022 £m
Interest income		**5,455**	3,712
Interest expense		**(3,854)**	(1,230)
Net interest income		**1,601**	2,482
Fee and commission income		**347**	310
Fee and commission expense		**(163)**	(156)
Net fee and commission income	3	**184**	154
Net trading losses		**(56)**	(2)
Other operating income		**56**	28
Other income		**184**	180
Total income		**1,785**	2,662
Operating expenses	4	**(1,439)**	(1,454)
Impairment	5	**(379)**	(18)
(Loss) profit before tax		**(33)**	1,190
Tax credit (expense)	6	**65**	(304)
Profit for the period		**32**	886
(Loss) profit attributable to ordinary shareholders		**(56)**	829
Profit attributable to non-controlling interests		**88**	57
Profit for the period		**32**	886

The accompanying notes are an integral part of the condensed consolidated half-year financial statements.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (UNAUDITED)

	Half-year to 30 Jun 2023 £m	Half-year to 30 Jun 2022 £m
Profit for the period	**32**	886
Other comprehensive income		
Items that will not subsequently be reclassified to profit or loss:		
Post-retirement defined benefit scheme remeasurements		
Remeasurements before tax	**(6)**	(373)
Tax	**(3)**	67
	(9)	(306)
Items that may subsequently be reclassified to profit or loss:		
Movements in revaluation reserve in respect of debt securities held at fair value through other comprehensive income:		
Change in fair value	**(5)**	(26)
Tax	**1**	6
	(4)	(20)
Movements in cash flow hedging reserve:		
Effective portion of changes in fair value taken to other comprehensive income	**(6)**	12
Net income statement transfers	**(6)**	(5)
Tax	**4**	(5)
	(8)	2
Total other comprehensive loss for the period, net of tax	**(21)**	(324)
Total comprehensive income for the period	**11**	562
Total comprehensive (loss) income attributable to ordinary shareholders	**(77)**	505
Total comprehensive income attributable to non-controlling interests	**88**	57
Total comprehensive income for the period	**11**	562

The accompanying notes are an integral part of the condensed consolidated half-year financial statements.

CONSOLIDATED BALANCE SHEET (UNAUDITED)

	Note	At 30 Jun 2023 £m	At 31 Dec 2022 £m
Assets			
Cash and balances at central banks		**2,941**	3,004
Financial assets at fair value through profit or loss		**300**	291
Derivative financial instruments		**3,345**	3,477
Loans and advances to banks		**323**	271
Loans and advances to customers	8	**290,244**	292,416
Debt securities		**1,957**	–
Due from fellow Lloyds Banking Group undertakings		**13,398**	13,982
Financial assets at amortised cost		**305,922**	306,669
Financial assets at fair value through other comprehensive income		**103**	103
Goodwill		**452**	452
Current tax recoverable		**1,197**	542
Deferred tax assets		**1,417**	1,501
Retirement benefit assets	11	**1,852**	1,513
Other assets[1]		**2,030**	2,015
Total assets		**319,559**	319,567
Liabilities			
Deposits from banks		**176**	195
Customer deposits		**162,412**	166,363
Repurchase agreements		**30,332**	30,210
Due to fellow Lloyds Banking Group undertakings		**90,546**	88,180
Financial liabilities at fair value through profit or loss		**25**	26
Derivative financial instruments		**4,430**	4,544
Notes in circulation		**1,342**	1,280
Debt securities in issue	10	**7,578**	6,123
Other liabilities[1]		**1,948**	1,719
Retirement benefit obligations	11	**72**	76
Other provisions	12	**796**	973
Subordinated liabilities		**2,191**	2,456
Total liabilities		**301,848**	302,145
Equity			
Share capital		**3,778**	3,778
Share premium account		**585**	585
Other reserves		**11,161**	11,173
Retained profits		**(386)**	(337)
Shareholders' equity		**15,138**	15,199
Non-controlling interests		**2,573**	2,223
Total equity		**17,711**	17,422
Total equity and liabilities		**319,559**	319,567

[1] See note 1 regarding changes to presentation.

The accompanying notes are an integral part of the condensed consolidated half-year financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY (UNAUDITED)

	Attributable to ordinary shareholders					
	Share capital and premium £m	Other reserves £m	Retained profits £m	Total £m	Non-controlling interests £m	Total £m
At 1 January 2023	**4,363**	**11,173**	**(337)**	**15,199**	**2,223**	**17,422**
Comprehensive income						
Profit for the period	**–**	**–**	**(56)**	**(56)**	**88**	**32**
Other comprehensive income						
Post-retirement defined benefit scheme remeasurements, net of tax	**–**	**–**	**(9)**	**(9)**	**–**	**(9)**
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	**–**	**(8)**	**–**	**(8)**	**–**	**(8)**
Total other comprehensive loss	**–**	**(12)**	**(9)**	**(21)**	**–**	**(21)**
Total comprehensive (loss) income[1]	**–**	**(12)**	**(65)**	**(77)**	**88**	**11**
Transactions with owners						
Distributions to non-controlling interests	**–**	**–**	**–**	**–**	**(88)**	**(88)**
Changes in non-controlling interests	**–**	**–**	**–**	**–**	**350**	**350**
Capital contributions received	**–**	**–**	**16**	**16**	**–**	**16**
Total transactions with owners	**–**	**–**	**16**	**16**	**262**	**278**
At 30 June 2023[2]	**4,363**	**11,161**	**(386)**	**15,138**	**2,573**	**17,711**

1 Total comprehensive income attributable to owners of the parent was a loss of £77 million.

2 Total equity attributable to owners of the parent was £15,138 million.

The accompanying notes are an integral part of the condensed consolidated half-year financial statements.

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

	Attributable to ordinary shareholders					
	Share capital and premium £m	Other reserves £m	Retained profits £m	Total £m	Non-controlling interests £m	Total £m
At 1 January 2022	3,763	10,165	(562)	13,366	2,223	15,589
Comprehensive income						
Profit for the period	–	–	829	829	57	886
Other comprehensive income						
Post-retirement defined benefit scheme remeasurements, net of tax	–	–	(306)	(306)	–	(306)
Movements in revaluation reserve in respect of debt securities held at fair value through other comprehensive income, net of tax	–	(20)	–	(20)	–	(20)
Movements in cash flow hedging reserve, net of tax	–	2	–	2	–	2
Total other comprehensive loss	–	(18)	(306)	(324)	–	(324)
Total comprehensive (loss) income[1]	–	(18)	523	505	57	562
Transactions with owners						
Distributions to non-controlling interests	–	–	–	–	(57)	(57)
Capital contributions received	–	–	23	23	–	23
Total transactions with owners	–	–	23	23	(57)	(34)
At 30 June 2022[2]	3,763	10,147	(16)	13,894	2,223	16,117
Comprehensive income						
Profit for the period	–	–	189	189	65	254
Other comprehensive income						
Post-retirement defined benefit scheme remeasurements, net of tax	–	–	(514)	(514)	–	(514)
Movements in revaluation reserve in respect of debt securities held at fair value through other comprehensive income, net of tax	–	(24)	–	(24)	–	(24)
Movements in cash flow hedging reserve, net of tax	–	(4)	–	(4)	–	(4)
Total other comprehensive loss	–	(28)	(514)	(542)	–	(542)
Total comprehensive (loss) income[1]	–	(28)	(325)	(353)	65	(288)
Transactions with owners						
Distributions to non-controlling interests	–	–	–	–	(65)	(65)
Issue of ordinary shares	600	–	–	600	–	600
Capital contributions received	–	1,054	23	1,077	–	1,077
Adjustment on transfer of subsidiary	–	–	(19)	(19)	–	(19)
Total transactions with owners	600	1,054	4	1,658	(65)	1,593
At 31 December 2022[2]	4,363	11,173	(337)	15,199	2,223	17,422

1 Total comprehensive income attributable to owners of the parent for the half-year to 30 June 2022 was a surplus of £505 million (half-year to 31 December 2022: loss of £353 million)

2 Total equity attributable to owners of the parent at 30 June 2022 was £13,894 million (31 December 2022: £15,199 million).

The accompanying notes are an integral part of the condensed consolidated half-year financial statements.

CONSOLIDATED CASH FLOW STATEMENT (UNAUDITED)

	Half-year to 30 Jun 2023 £m	Half-year to 30 Jun 2022 £m
Cash flows from operating activities		
(Loss) profit before tax	**(33)**	1,190
Adjustments for:		
Change in operating assets	**681**	(3,993)
Change in operating liabilities	**136**	4,184
Non-cash and other items	**(122)**	(556)
Tax paid (net)	**(506)**	(333)
Net cash provided by operating activities	**156**	492
Cash flows from investing activities		
Purchase of financial assets	**(5)**	(558)
Proceeds from sale and maturity of financial assets	**–**	179
Purchase of fixed assets	**(76)**	(68)
Proceeds from sale of fixed assets	**12**	–
Net cash used in investing activities	**(69)**	(447)
Cash flows from financing activities		
Distributions to non-controlling interests	**(88)**	(57)
Interest paid on subordinated liabilities	**(85)**	(61)
Proceeds from changes in non-controlling interests	**350**	–
Repayment of subordinated liabilities	**(226)**	(58)
Net cash used in financing activities	**(49)**	(176)
Change in cash and cash equivalents	**38**	(131)
Cash and cash equivalents at beginning of period	**2,087**	2,185
Cash and cash equivalents at end of period	**2,125**	2,054

The accompanying notes are an integral part of the condensed consolidated half-year financial statements.

Cash and cash equivalents comprise cash and non-mandatory balances with central banks and amounts due from banks with an original maturity of less than three months.

NOTES TO THE CONDENSED CONSOLIDATED HALF-YEAR FINANCIAL STATEMENTS

Note 1: Basis of preparation and accounting policies

These condensed consolidated half-year financial statements as at and for the period to 30 June 2023 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 United Kingdom and comprise the results of HBOS plc (the Company) 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 2022 which complied with international accounting standards in conformity with the requirements of the Companies Act 2006 and were prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB). Copies of the 2022 Annual Report and Accounts are available on the Lloyds Banking Group's website and are also 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 these condensed consolidated half-year financial statements. In reaching this assessment, the directors have taken into account the uncertainties affecting the UK economy and their potential effects upon the Group's performance and projected funding and capital position; the impact of further stress scenarios has also been considered. On this basis, the directors are satisfied that the Group will maintain adequate levels of funding and capital for the foreseeable future.

The Group's accounting policies are consistent with those applied by the Group in its financial statements for the year ended 31 December 2022 and there have been no changes in the Group's methods of computation.

Presentational changes

The following changes have been made to the presentation of the Group's balance sheet:

- items in the course of collection from banks are reported within other assets rather than separately on the face of the balance sheet; and
- items in the course of transmission to banks are reported within other liabilities rather than separately on the face of the balance sheet.

There has been no change in the basis of accounting for any of the underlying transactions. Comparatives have been presented on a consistent basis.

Future accounting developments

The IASB has issued a number of minor amendments to IFRSs effective 1 January 2024, including IFRS 16 *Lease liability in a sale and leaseback*, IAS 1 *Non-current liabilities with covenants*, and IAS 1 *Classification of liabilities as current or non-current*. These amendments are not expected to have a significant impact on the Group and, apart from the amendments relating to IFRS 16 *Lease liability in a sale and leaseback*, have not been endorsed for use in the UK.

HBOS 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 to 31 December 2022 and copies may be obtained from Investor Relations, Lloyds Banking Group plc, 25 Gresham Street, London EC2V 7HN and are available for download from www.lloydsbankinggroup.com.

The financial information contained in this document does not constitute statutory accounts within the meaning of section 434 of the Companies Act 2006 (the Act). The statutory accounts for the year ended 31 December 2022 were approved by the directors on 7 March 2023 and were delivered to the Registrar of Companies on 6 April 2023. The auditors' report on those accounts was unqualified and did not include a statement under sections 498(2) (accounting records or returns inadequate or accounts not agreeing with records and returns) or 498(3) (failure to obtain necessary information and explanations) of the Act.

NOTES TO THE CONDENSED CONSOLIDATED HALF-YEAR FINANCIAL STATEMENTS (continued)

Note 2: Critical accounting judgements and key sources of estimation uncertainty

The preparation of the Group's financial statements in accordance with IFRS requires management to make judgements, estimates and assumptions in applying the accounting policies that affect the reported amounts of assets, liabilities, income and expenses. Due to the inherent uncertainty in making estimates, actual results reported in future periods may be based upon amounts which differ from these 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. In preparing the financial statements, the Group has considered the impact of climate-related risks on its financial position and performance. While the effects of climate change represent a source of uncertainty, the Group does not consider there to be a material impact on its judgements and estimates from the physical, transition and other climate-related risks in the short term.

Except for the removal of the judgements and estimates in respect of capitalised software enhancements, the Group's significant judgements, estimates and assumptions are unchanged compared to those applied at 31 December 2022. Further information on the critical accounting judgements and key sources of estimation uncertainty for the allowance for expected credit losses is set out in note 9.

Note 3: Net fee and commission income

	Half-year to 30 Jun 2023 £m	Half-year to 30 Jun 2022 £m
Fee and commission income:		
Current accounts	**96**	103
Credit and debit card fees	**202**	157
Other fees and commissions	**49**	50
Total fee and commission income	**347**	310
Fee and commission expense	**(163)**	(156)
Net fee and commission income	**184**	154

Note 4: Operating expenses

	Half-year to 30 Jun 2023 £m	Half-year to 30 Jun 2022 £m
Staff costs	**432**	531
Premises and equipment costs	**94**	72
Amounts paid to fellow Lloyds Banking Group undertakings and other expenses	**780**	744
Depreciation and amortisation	**133**	107
Total operating expenses	**1,439**	1,454

NOTES TO THE CONDENSED CONSOLIDATED HALF-YEAR FINANCIAL STATEMENTS (continued)

Note 5: Impairment

	Half-year to 30 Jun 2023 £m	Half-year to 30 Jun 2022 £m
Impact of transfers between stages	**295**	201
Other changes in credit quality	**155**	(134)
Additions and repayments	**(77)**	(47)
Other items	**6**	(2)
	84	(183)
Total impairment	**379**	18
In respect of:		
Loans and advances to customers	**378**	5
Due from fellow Lloyds Banking Group undertakings	**–**	5
Financial assets held at amortised cost	**378**	10
Loan commitments and financial guarantees	**1**	8
Total impairment	**379**	18

The Group's impairment charge comprises the following:

Impact of transfers between stages

The net impact on the impairment charge of transfers between stages.

Other changes in credit quality

Changes in loss allowance as a result of movements in risk parameters that reflect changes in customer credit quality, but which have not resulted in a transfer to a different stage. This also contains the impact on the impairment charge of write-offs and recoveries, where the related loss allowances are reassessed to reflect the view of credit quality at the balance sheet date and therefore the ultimate realisable or recoverable value.

Additions and repayments

Expected loss allowances are recognised on origination of new loans or further drawdowns of existing facilities. Repayments relate to the reduction of loss allowances resulting from the repayment of outstanding balances that have been provided against.

Note 6: Tax expense

In accordance with IAS 34, the Group's income tax credit (expense) for the half-year to 30 June 2023 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 credit (expense) and accounting profit is set out below:

	Half-year to 30 Jun 2023 £m	Half-year to 30 Jun 2022 £m
(Loss) profit before tax	**(33)**	1,190
UK corporation tax thereon at 23.5 per cent (2022: 19.0 per cent)	**8**	(226)
Impact of surcharge on banking profits	**15**	(87)
Non-deductible costs: conduct charges	**(1)**	–
Other non-deductible costs	**(6)**	3
Non-taxable income	**–**	(1)
Tax relief on coupons on other equity instruments	**21**	–
Tax-exempt gains on disposals	**22**	–
Remeasurement of deferred tax due to rate changes	**–**	(6)
Adjustments in respect of prior years	**6**	13
Tax credit (expense)	**65**	(304)

NOTES TO THE CONDENSED CONSOLIDATED HALF-YEAR FINANCIAL STATEMENTS (continued)

Note 7: 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 35 to the Group's financial statements for the year ended 31 December 2022 details the definitions of the three levels in the fair value hierarchy.

Financial instruments classified as financial assets at fair value through profit or loss, derivative financial instruments, financial assets at fair value through other comprehensive income and financial liabilities at fair value through profit or loss are recognised at fair value.

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. There were no significant transfers between level 1 and level 2 during the period.

Financial assets	**Level 1 £m**	**Level 2 £m**	**Level 3 £m**	**Total £m**
At 30 June 2023				
Loans and advances to customers at fair value through profit or loss	**–**	**–**	**300**	**300**
Debt securities at fair value through other comprehensive income	**103**	**–**	**–**	**103**
Derivative financial instruments	**–**	**3,345**	**–**	**3,345**
Total financial assets carried at fair value	**103**	**3,345**	**300**	**3,748**
At 31 December 2022				
Loans and advances to customers at fair value through profit or loss	–	–	291	291
Debt securities at fair value through other comprehensive income	103	–	–	103
Derivative financial instruments	–	3,477	–	3,477
Total financial assets carried at fair value	103	3,477	291	3,871

Financial liabilities	**Level 1 £m**	**Level 2 £m**	**Level 3 £m**	**Total £m**
At 30 June 2023				
Financial liabilities designated at fair value through profit or loss	**–**	**–**	**25**	**25**
Derivative financial instruments	**–**	**4,269**	**161**	**4,430**
Total financial liabilities carried at fair value	**–**	**4,269**	**186**	**4,455**
At 31 December 2022				
Financial liabilities designated at fair value through profit or loss	–	–	26	26
Derivative financial instruments	–	4,394	150	4,544
Total financial liabilities carried at fair value	–	4,394	176	4,570

NOTES TO THE CONDENSED CONSOLIDATED HALF-YEAR FINANCIAL STATEMENTS (continued)

Note 7: Fair values of financial assets and liabilities (continued)

Valuation control framework

Key elements of the valuation control framework include model validation (incorporating pre-trade and post-trade testing), product implementation review and independent price verification. The framework covers processes for all 3 levels in the fair value hierarchy. 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 financial statements for the year ended 31 December 2022 applied to these portfolios.

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 2023	**291**	**–**	**291**
Gains recognised in the income statement within other income	**17**	**–**	**17**
Repayments of customer loans	**(8)**	**–**	**(8)**
At 30 June 2023	**300**	**–**	**300**
Gains recognised in the income statement, within other income, relating to the change in fair value of those assets held at 30 June 2023	**17**	**–**	**17**
At 1 January 2022	362	–	362
Losses recognised in the income statement within other income	(5)	–	(5)
Repayments of customer loans	(27)	–	(27)
At 30 June 2022	330	–	330
Losses recognised in the income statement, within other income, relating to the change in fair value of those assets held at 30 June 2022	(5)	–	(5)

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 2023	**26**	**150**	**176**
(Gains) losses recognised in the income statement within other income	**(1)**	**16**	**15**
Redemptions	**–**	**(5)**	**(5)**
At 30 June 2023	**25**	**161**	**186**
(Gains) losses recognised in the income statement, within other income, relating to the change in fair value of those liabilities held at 30 June 2023	**(1)**	**16**	**15**
At 1 January 2022	33	176	209
(Gains) losses recognised in the income statement within other income	(2)	6	4
Redemptions	(2)	(11)	(13)
At 30 June 2022	29	171	200
(Gains) losses recognised in the income statement, within other income, relating to the change in fair value of those liabilities held at 30 June 2022	(2)	5	3

NOTES TO THE CONDENSED CONSOLIDATED HALF-YEAR FINANCIAL STATEMENTS (continued)

Note 7: Fair values of financial assets and liabilities (continued)

Sensitivity of level 3 valuations

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

				Effect of reasonably possible alternative assumptions[1]	
At 30 June 2023	**Valuation techniques**	**Significant unobservable inputs[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)	**300**	**24**	**(24)**
Level 3 financial assets carried at fair value			**300**		
Financial liabilities at fair value through profit or loss					
Securitisation notes	Discounted cash flows	Interest rate spreads (+/- 50bps)	**25**	**1**	**(1)**
Derivative financial liabilities					
Shared appreciation rights	Market values – property valuation	HPI (+/- 1%)	**161**	**15**	**(16)**
Level 3 financial liabilities carried at fair value			**186**		
At 31 December 2022					
Financial assets at fair value through profit or loss					
Loans and advances to customers	Discounted cash flows	Interest rate spreads (+/- 50bps)	291	25	(23)
Level 3 financial assets carried at fair value			291		
Financial liabilities at fair value through profit or loss					
Securitisation notes	Discounted cash flows	Interest rate spreads (+/- 50bps)	26	1	(1)
Derivative financial liabilities					
Shared appreciation rights	Market values – property valuation	HPI (+/- 1%)	150	16	(16)
Level 3 financial liabilities carried at fair value			176		

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

2 Ranges are shown where appropriate and represent the highest and lowest inputs used in the level 3 valuations.

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 financial statements for the year ended 31 December 2022.

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 is unchanged from that described in note 35 to the Group's financial statements for the year ended 31 December 2022.

NOTES TO THE CONDENSED CONSOLIDATED HALF-YEAR FINANCIAL STATEMENTS (continued)

Note 7: Fair values of financial assets and liabilities (continued)

The table below summarises the carrying values of financial assets and liabilities measured at amortised cost in the Group's consolidated 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 2023		At 31 December 2022	
	Carrying value £m	**Fair value £m**	Carrying value £m	Fair value £m
Financial assets				
Loans and advances to banks	**323**	**323**	271	271
Loans and advances to customers	**290,244**	**282,280**	292,416	285,540
Debt securities	**1,957**	**1,752**	–	–
Due from fellow Lloyds Banking Group undertakings	**13,398**	**13,398**	13,982	13,982
Financial assets at amortised cost	**305,922**	**297,753**	306,669	299,793
Financial liabilities				
Deposits from banks	**176**	**176**	195	195
Customer deposits	**162,412**	**162,408**	166,363	166,264
Repurchase agreements	**30,332**	**30,332**	30,210	30,210
Due to fellow Lloyds Banking Group undertakings	**90,546**	**90,546**	88,180	88,180
Debt securities in issue	**7,578**	**7,575**	6,123	6,122
Subordinated liabilities	**2,191**	**2,218**	2,456	2,475

The carrying amount of cash and balances at central banks and notes in circulation is a reasonable approximation of fair value.

NOTES TO THE CONDENSED CONSOLIDATED HALF-YEAR FINANCIAL STATEMENTS (continued)

Note 8: Loans and advances to customers

Half-year to 30 June 2023

	Gross carrying amount				**Allowance for expected credit losses**			
	Stage 1 £m	**Stage 2 £m**	**Stage 3 £m**	**Total £m**	**Stage 1 £m**	**Stage 2 £m**	**Stage 3 £m**	**Total £m**
At 1 January 2023	**243,873**	**44,226**	**7,514**	**295,613**	**284**	**1,132**	**1,781**	**3,197**
Exchange and other adjustments	**(2)**	**(4)**	**–**	**(6)**	**–**	**–**	**66**	**66**
Transfers to Stage 1	**8,739**	**(8,735)**	**(4)**	**–**	**144**	**(142)**	**(2)**	**–**
Transfers to Stage 2	**(13,290)**	**13,785**	**(495)**	**–**	**(24)**	**73**	**(49)**	**–**
Transfers to Stage 3	**(212)**	**(1,379)**	**1,591**	**–**	**(3)**	**(118)**	**121**	**–**
Impact of transfers between stages	**(4,763)**	**3,671**	**1,092**	**–**	**(95)**	**242**	**146**	**293**
					22	**55**	**216**	**293**
Other changes in credit quality					**11**	**1**	**149**	**161**
Additions and repayments	**2,216**	**(905)**	**(506)**	**805**	**7**	**(41)**	**(42)**	**(76)**
Charge to the income statement					**40**	**15**	**323**	**378**
Disposals and derecognition[1]	**(1,314)**	**(887)**	**(447)**	**(2,648)**	**(1)**	**(35)**	**(85)**	**(121)**
Advances written off			**(308)**	**(308)**			**(308)**	**(308)**
Recoveries of advances written off in previous years			**61**	**61**			**61**	**61**
At 30 June 2023	**240,010**	**46,101**	**7,406**	**293,517**	**323**	**1,112**	**1,838**	**3,273**
Allowance for impairment losses	**(323)**	**(1,112)**	**(1,838)**	**(3,273)**				
Net carrying amount	**239,687**	**44,989**	**5,568**	**290,244**				
Drawn ECL coverage[2] (%)	**0.1**	**2.4**	**24.8**	**1.1**				

Year ended 31 December 2022

	Gross carrying amount				Allowance for expected credit losses			
	Stage 1 £m	Stage 2 £m	Stage 3 £m	Total £m	Stage 1 £m	Stage 2 £m	Stage 3 £m	Total £m
At 1 January 2022	250,007	26,420	5,561	281,988	392	810	1,377	2,579
Exchange and other adjustments	8	–	–	8	–	–	55	55
Acquisition of business[3]	5,345	875	125	6,345	61	110	57	228
Transfers to Stage 1	5,473	(5,422)	(51)	–	75	(71)	(4)	–
Transfers to Stage 2	(24,077)	24,327	(250)	–	(31)	64	(33)	–
Transfers to Stage 3	(498)	(2,722)	3,220	–	(5)	(163)	168	–
Impact of transfers between stages	(19,102)	16,183	2,919	–	(57)	401	161	505
					(18)	231	292	505
Other changes in credit quality					(187)	(14)	329	128
Additions and repayments	7,615	748	(835)	7,528	36	(5)	(73)	(42)
Charge (credit) to the income statement					(169)	212	548	591
Advances written off			(350)	(350)			(350)	(350)
Recoveries of advances written off in previous years			94	94			94	94
At 31 December 2022	243,873	44,226	7,514	295,613	284	1,132	1,781	3,197
Allowance for impairment losses	(284)	(1,132)	(1,781)	(3,197)				
Net carrying amount	243,589	43,094	5,733	292,416				
Drawn ECL coverage[2] (%)	0.1	2.6	23.7	1.1				

[1] Relates to the exit of legacy mortgage loans.

[2] Allowance for expected credit losses on loans and advances to customers as a percentage of gross loans and advances to customers.

[3] On 30 November 2022 the Group acquired MBNA Limited, formerly a subsidiary of Lloyds Bank plc, a fellow Lloyds Banking Group undertaking.

NOTES TO THE CONDENSED CONSOLIDATED HALF-YEAR FINANCIAL STATEMENTS (continued)

Note 8: Loans and advances to customers (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 and 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 10).

Note 9: Allowance for expected credit losses

The Group recognises an allowance for expected credit losses (ECLs) for loans and advances to customers and banks, other financial assets held at amortised cost, financial assets measured at fair value through other comprehensive income and certain loan commitment and financial guarantee contracts. At 30 June 2023 the Group's expected credit loss allowance was £3,399 million (31 December 2022: £3,324 million), of which £3,283 million (31 December 2022: £3,209 million) was in respect of drawn balances.

The Group's total allowances for expected credit losses were as follows:

	Allowance for expected credit losses			
At 30 June 2023	**Stage 1 £m**	**Stage 2 £m**	**Stage 3 £m**	**Total £m**
In respect of:				
Loans and advances to customers	**323**	**1,112**	**1,838**	**3,273**
Debt securities	**–**	**–**	**1**	**1**
Due from fellow Lloyds Banking Group undertakings	**9**	**–**	**–**	**9**
Drawn balances	**332**	**1,112**	**1,839**	**3,283**
Provisions in relation to loan commitments and financial guarantees	**54**	**61**	**1**	**116**
Total	**386**	**1,173**	**1,840**	**3,399**
At 31 December 2022				
In respect of:				
Loans and advances to customers	284	1,132	1,781	3,197
Debt securities	–	–	1	1
Due from fellow Lloyds Banking Group undertakings	11	–	–	11
Drawn balances	295	1,132	1,782	3,209
Provisions in relation to loan commitments and financial guarantees	53	61	1	115
Total	348	1,193	1,783	3,324

NOTES TO THE CONDENSED CONSOLIDATED HALF-YEAR FINANCIAL STATEMENTS (continued)

Note 9: Allowance for expected credit losses (continued)

The calculation of the Group’s expected credit loss allowances and provisions against loan commitments and guarantees under IFRS 9 requires the Group to make a number of judgements, assumptions and estimates. These are set out in detail in the note 14 to the Group’s financial statements for the year ended 31 December 2022. The principal changes made in the half-year to 30 June 2023 are as follows:

Base case and MES economic assumptions

The Group’s updated base case scenario has three conditioning assumptions: first, the war in Ukraine remains contained within its borders; second, the financial stress emerging from some weak bank/insurer business models in the context of rising bond yields does not become systemic; and third, the Bank of England will continue to tighten policy until it is clear that inflation is returning to target.

Based on these assumptions and incorporating the economic data published in the second quarter of 2023, the Group’s base case scenario is for a slow expansion of economic activity alongside a gradual rise in the unemployment rate. Increases in UK Bank Rate in response to persistent inflationary pressures trigger further declines in residential and commercial property prices. Risks around this base case economic view lie in both directions and are largely captured by the generation of alternative economic scenarios.

The Group has taken into account the latest available information at the reporting date in defining its base case scenario and generating alternative economic scenarios. The scenarios include forecasts for key variables in the second quarter of 2023, for which actuals may have since emerged prior to publication.

The Group’s approach to generating alternative economic scenarios is set out in detail in note 14 to the financial statements for the year ended 31 December 2022. For June 2023, the Group continues to judge it appropriate to include a non-modelled severe downside scenario for Group ECL calculations. This adjusted scenario is considered to better reflect the risks around the Group’s base case view in an economic environment where past supply shocks continue to unwind slowly.

Scenarios by year

The key UK economic assumptions made by the Group are shown in the following tables across a number of measures explained below.

Annual assumptions

Gross domestic product (GDP) and Consumer Price Index (CPI) inflation are presented as an annual change, house price growth and commercial real estate price growth are presented as the growth in the respective indices over each year. Unemployment rate and UK Bank Rate are averages over the year.

Five-year average

The five-year average reflects the average annual growth rate, or level, over the five-year period. It includes movements within the current reporting year, such that the position as of 30 June 2023 covers the five years 2023 to 2027. The inclusion of the reporting year within the five-year period reflects the need to predict variables which remain unpublished at the reporting date and recognises that credit models utilise both level and annual changes. The use of calendar years maintains a comparability between the annual assumptions presented.

NOTES TO THE CONDENSED CONSOLIDATED HALF-YEAR FINANCIAL STATEMENTS (continued)

Note 9: Allowance for expected credit losses (continued)

At 30 June 2023	2023 %	2024 %	2025 %	2026 %	2027 %	2023 to 2027 average %
Upside						
Gross domestic product	0.8	1.6	0.9	1.5	2.0	1.3
Unemployment rate	3.3	2.7	3.0	3.4	3.3	3.1
House price growth	(3.3)	2.4	7.8	7.5	7.3	4.3
Commercial real estate price growth	2.3	6.5	1.8	2.4	3.8	3.4
UK Bank Rate	5.39	7.00	6.57	5.76	5.63	6.07
CPI inflation	7.9	4.2	3.7	3.3	3.3	4.5
Base case						
Gross domestic product	0.2	0.3	0.7	1.5	2.1	0.9
Unemployment rate	4.1	4.7	5.2	5.3	5.0	4.9
House price growth	(5.4)	(3.2)	0.8	2.8	4.8	(0.1)
Commercial real estate price growth	(3.9)	(0.2)	(0.3)	1.2	3.8	0.1
UK Bank Rate	5.06	5.44	4.63	3.69	3.50	4.46
CPI inflation	7.9	4.0	3.0	2.2	2.0	3.8
Downside						
Gross domestic product	(0.6)	(1.5)	0.4	1.4	2.1	0.4
Unemployment rate	4.9	7.1	7.7	7.6	7.1	6.9
House price growth	(6.9)	(8.2)	(6.3)	(2.5)	2.2	(4.4)
Commercial real estate price growth	(9.2)	(7.0)	(3.7)	(1.4)	2.2	(3.9)
UK Bank Rate	4.73	3.67	2.37	1.30	1.04	2.62
CPI inflation	7.9	3.8	2.3	0.9	0.4	3.1
Severe downside						
Gross domestic product	(1.5)	(2.8)	0.3	1.2	1.8	(0.2)
Unemployment rate	6.1	9.8	10.4	10.1	9.5	9.2
House price growth	(9.3)	(14.6)	(14.3)	(9.1)	(1.8)	(9.9)
Commercial real estate price growth	(17.5)	(16.5)	(9.0)	(6.1)	(0.4)	(10.1)
UK Bank Rate – modelled	4.26	1.73	0.48	0.08	0.04	1.32
UK Bank Rate – adjusted[1]	5.69	7.00	4.94	3.88	3.50	5.00
CPI inflation – modelled	7.9	3.5	1.4	(0.5)	(1.3)	2.2
CPI inflation – adjusted[1]	9.8	7.4	5.5	4.2	3.9	6.2
Probability-weighted						
Gross domestic product	0.0	(0.2)	0.6	1.4	2.0	0.8
Unemployment rate	4.3	5.3	5.8	5.9	5.5	5.4
House price growth	(5.6)	(4.1)	(0.7)	1.4	4.1	(1.1)
Commercial real estate price growth	(5.0)	(1.9)	(1.5)	0.1	2.9	(1.1)
UK Bank Rate – modelled	4.98	5.00	4.12	3.23	3.05	4.08
UK Bank Rate – adjusted[1]	5.12	5.53	4.56	3.61	3.40	4.45
CPI inflation – modelled	7.9	4.0	2.8	1.9	1.6	3.6
CPI inflation – adjusted[1]	8.1	4.3	3.2	2.3	2.1	4.0

[1] The adjustment to UK Bank Rate and CPI inflation in the severe downside is considered to better reflect the risks to the Group's base case view in an economic environment where supply shocks are the principal concern.

NOTES TO THE CONDENSED CONSOLIDATED HALF-YEAR FINANCIAL STATEMENTS (continued)

Note 9: Allowance for expected credit losses (continued)

At 31 December 2022	2022 %	2023 %	2024 %	2025 %	2026 %	2022 to 2026 average %
Upside						
Gross domestic product	4.1	0.1	1.1	1.7	2.1	1.8
Unemployment rate	3.5	2.8	3.0	3.3	3.4	3.2
House price growth	2.4	(2.8)	6.5	9.0	8.0	4.5
Commercial real estate price growth	(9.4)	8.5	3.5	2.6	2.3	1.3
UK Bank Rate	1.94	4.95	4.98	4.63	4.58	4.22
CPI inflation	9.0	8.3	4.2	3.3	3.0	5.5
Base case						
Gross domestic product	4.0	(1.2)	0.5	1.6	2.1	1.4
Unemployment rate	3.7	4.5	5.1	5.3	5.1	4.8
House price growth	2.0	(6.9)	(1.2)	2.9	4.4	0.2
Commercial real estate price growth	(11.8)	(3.3)	0.9	2.8	3.1	(1.8)
UK Bank Rate	1.94	4.00	3.38	3.00	3.00	3.06
CPI inflation	9.0	8.3	3.7	2.3	1.7	5.0
Downside						
Gross domestic product	3.9	(3.0)	(0.5)	1.4	2.1	0.8
Unemployment rate	3.8	6.3	7.5	7.6	7.2	6.5
House price growth	1.6	(11.1)	(9.8)	(5.6)	(1.5)	(5.4)
Commercial real estate price growth	(13.9)	(15.0)	(3.7)	0.4	1.4	(6.4)
UK Bank Rate	1.94	2.93	1.39	0.98	1.04	1.65
CPI inflation	9.0	8.2	3.3	1.3	0.3	4.4
Severe downside						
Gross domestic product	3.7	(5.2)	(1.0)	1.3	2.1	0.1
Unemployment rate	4.1	9.0	10.7	10.4	9.7	8.8
House price growth	1.1	(14.8)	(18.0)	(11.5)	(4.2)	(9.8)
Commercial real estate price growth	(17.3)	(28.8)	(9.9)	(1.3)	3.2	(11.6)
UK Bank Rate – modelled	1.94	1.41	0.20	0.13	0.14	0.76
UK Bank Rate – adjusted[1]	2.44	7.00	4.88	3.31	3.25	4.18
CPI inflation – modelled	9.0	8.2	2.6	(0.1)	(1.6)	3.6
CPI inflation – adjusted[1]	9.7	14.3	9.0	4.1	1.6	7.7
Probability-weighted						
Gross domestic product	4.0	(1.8)	0.2	1.5	2.1	1.2
Unemployment rate	3.7	5.0	5.8	5.9	5.7	5.2
House price growth	1.9	(7.7)	(3.2)	0.7	2.9	(1.2)
Commercial real estate price growth	(12.3)	(5.8)	(0.8)	1.6	2.3	(3.1)
UK Bank Rate – modelled	1.94	3.70	2.94	2.59	2.60	2.76
UK Bank Rate – adjusted[1]	1.99	4.26	3.41	2.91	2.91	3.10
CPI inflation – modelled	9.0	8.3	3.6	2.1	1.4	4.9
CPI inflation – adjusted[1]	9.1	8.9	4.3	2.5	1.7	5.3

[1] The adjustment to UK Bank Rate and CPI inflation in the severe downside is considered to better reflect the risks to the Group's base case view in an economic environment where supply shocks are the principal concern.

NOTES TO THE CONDENSED CONSOLIDATED HALF-YEAR FINANCIAL STATEMENTS (continued)

Note 9: Allowance for expected credit losses (continued)

Base case scenario by quarter

Gross domestic product is presented quarter-on-quarter. House price growth, commercial real estate price growth and CPI inflation are presented year-on-year, i.e. from the equivalent quarter in the previous year. Unemployment rate and UK Bank Rate are presented as at the end of each quarter.

At 30 June 2023	**First quarter 2023 %**	**Second quarter 2023 %**	**Third quarter 2023 %**	**Fourth quarter 2023 %**	**First quarter 2024 %**	**Second quarter 2024 %**	**Third quarter 2024 %**	**Fourth quarter 2024 %**
Gross domestic product	**0.1**	**(0.1)**	**0.1**	**(0.1)**	**0.1**	**0.1**	**0.1**	**0.2**
Unemployment rate	**3.9**	**4.0**	**4.2**	**4.4**	**4.5**	**4.7**	**4.8**	**4.9**
House price growth	**1.6**	**(2.5)**	**(6.4)**	**(5.4)**	**(9.1)**	**(9.5)**	**(6.2)**	**(3.2)**
Commercial real estate price growth	**(18.8)**	**(21.4)**	**(17.9)**	**(3.9)**	**(3.5)**	**(3.5)**	**(2.0)**	**(0.2)**
UK Bank Rate	**4.25**	**5.00**	**5.50**	**5.50**	**5.50**	**5.50**	**5.50**	**5.25**
CPI inflation	**10.2**	**8.7**	**7.3**	**5.3**	**4.8**	**3.6**	**3.8**	**3.7**

At 31 December 2022	First quarter 2022 %	Second quarter 2022 %	Third quarter 2022 %	Fourth quarter 2022 %	First quarter 2023 %	Second quarter 2023 %	Third quarter 2023 %	Fourth quarter 2023 %
Gross domestic product	0.6	0.1	(0.3)	(0.4)	(0.4)	(0.4)	(0.2)	(0.1)
Unemployment rate	3.7	3.8	3.6	3.7	4.0	4.4	4.7	4.9
House price growth	11.1	12.5	9.8	2.0	(3.0)	(8.4)	(9.8)	(6.9)
Commercial real estate price growth	18.0	18.0	8.4	(11.8)	(16.9)	(19.8)	(15.9)	(3.3)
UK Bank Rate	0.75	1.25	2.25	3.50	4.00	4.00	4.00	4.00
CPI inflation	6.2	9.2	10.0	10.7	10.0	8.9	8.0	6.1

ECL sensitivity to economic assumptions

The table below shows the Group's ECL for the probability-weighted, upside, base case, downside and severe downside scenarios, with the severe downside scenario incorporating adjustments made to CPI inflation and UK Bank Rate paths. The stage allocation for an asset is based on the overall scenario probability-weighted PD and hence the staging of assets is constant across all the scenarios. In each economic scenario the ECL for individual assessments and post-model adjustments is typically held constant reflecting the basis on which they are evaluated. However, post-model adjustments in Commercial Banking have been apportioned across the scenarios to better reflect the sensitivity of these adjustments to each scenario. Judgements applied through changes to model inputs are reflected in the scenario ECL sensitivities. The probability-weighted view shows the extent to which a higher ECL allowance has been recognised to take account of multiple economic scenarios relative to the base case; the uplift being £472 million for 30 June 2023 and £440 million at 31 December 2022.

ECL allowance	**Probability-weighted £m**	**Upside £m**	**Base case £m**	**Downside £m**	**Severe downside £m**
At 30 June 2023	**3,399**	**2,479**	**2,927**	**3,638**	**6,862**
At 31 December 2022	3,324	2,482	2,884	3,602	6,340

NOTES TO THE CONDENSED CONSOLIDATED HALF-YEAR FINANCIAL STATEMENTS (continued)

Note 9: Allowance for expected credit losses (continued)

The impact of changes in the UK unemployment rate and House Price Index (HPI) have also been assessed. Although such changes would not be observed in isolation, as economic indicators tend to be correlated in a coherent scenario, this gives insight into the sensitivity of the Group's ECL to gradual changes in these two critical economic factors. The assessment has been made against the base case with the reported staging unchanged and is assessed through the direct impact on modelled ECL only.

The table below shows the impact on the Group's ECL resulting from a 1 percentage point (pp) increase or decrease in the UK unemployment rate. The increase or decrease is presented based on the adjustment phased evenly over the first ten quarters of the base case scenario. An immediate increase or decrease would drive a more material ECL impact as it would be fully reflected in both 12-month and lifetime PDs.

	At 30 June 2023		At 31 December 2022	
	1pp increase in unemployment	**1pp decrease in unemployment**	1pp increase in unemployment	1pp decrease in unemployment
ECL impact, £m	**78**	**(67)**	73	(70)

The table below shows the impact on the Group's ECL in respect of UK mortgages resulting from an increase or decrease in loss given default for a 10 percentage point (pp) increase or decrease in the UK House Price Index (HPI). The increase or decrease is presented based on the adjustment phased evenly over the first ten quarters of the base case scenario.

	At 30 June 2023		At 31 December 2022	
	10pp increase in HPI	**10pp decrease in HPI**	10pp increase in HPI	10pp decrease in HPI
ECL impact, £m	**(203)**	**328**	(207)	341

Application of judgement in adjustments to modelled ECL

Impairment models fall within the Group's model risk framework with model monitoring, periodic validation and back testing performed on model components (i.e. probability of default, exposure at default and loss given default). Limitations in the Group's impairment models or data inputs may be identified through the ongoing 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 that the overall provision adequately reflects all material risks. These adjustments are determined by considering the particular attributes of exposures which have not been adequately captured by the impairment models and range from changes to model inputs and parameters, at account level, through to more qualitative post-model adjustments.

During 2022 the intensifying inflationary pressures, alongside rising interest rates within the Group's outlook created further risks not deemed to be fully captured by ECL models. This has required judgements to be added to capture affordability risks from inflationary and rising interest rate pressures. These risks have increased further in the first half of 2023 with additional judgemental adjustments taken. At 30 June 2023 total management judgement resulted in additional ECL allowances of £337 million (31 December 2022: £402 million).

The table below analyses total ECL allowance, separately identifying the amounts that have been modelled, those that have been individually assessed and those arising through the application of management judgement.

			Judgements due to:		
	Modelled ECL £m	**Individually assessed £m**	**Inflationary and interest rate risk £m**	**Other £m**	**Total ECL £m**
At 30 June 2023	**2,128**	**934**	**186**	**151**	**3,399**
At 31 December 2022	2,045	877	137	265	3,324

NOTES TO THE CONDENSED CONSOLIDATED HALF-YEAR FINANCIAL STATEMENTS (continued)

Note 9: Allowance for expected credit losses (continued)

Judgements due to inflationary and interest rate risk

Inflationary and interest rate pressures: £186 million (31 December 2022: £137 million)

There has been modest evidence of credit deterioration in the UK mortgages portfolio through the first half of 2023 despite the high levels of inflation and the rising interest rate environment. Increases in new to arrears and defaults that have emerged are mainly driven by variable-rate customers, who have experienced material increases in their monthly payment. Mortgage ECL models use bank base rate as a driver of predicted defaults and that has contributed materially to the elevated levels of ECL at 30 June 2023. However, there remains a potential risk to affordability from continued inflationary pressures combined with higher interest rates, and that this may not be fully captured by the Group's ECL models. This risk is to customers maturing from low fixed rate deals, the building impact on variable rate product holders, lower levels of real household income and rental cover value.

The level of risk is somewhat mitigated from stressed affordability assessments applied at loan origination which means most customers are anticipated to be able to absorb payment shocks. A judgemental uplift in ECL has therefore been taken in specific segments of the mortgages portfolio, either where inflation is expected to present a more material risk, or where segments within the model do not recognise bank base rate as a material driver of predicted defaults. The increase in judgemental ECL during the period recognises the heightened risk within the interest-only segment and potential default suppression due to increased monthly payments diluting the relative scale of amounts in arrears.

Other judgements

These adjustments principally comprise:

Increase in time to repossession: £144 million (31 December 2022: £159 million)

Due to the Group suspending mortgage litigation activity between late-2014 and mid-2018 due to policy changes for the treatment of arrears, and as collections strategy normalises post COVID-19 pandemic, the Group's experience of possessions data on which our models rely on is limited. This reflects an adjustment made to allow for an increase in the time assumed between default and repossession. Provision coverage is therefore uplifted to the equivalent levels of those accounts already in repossession on an estimated shortfall of balances expected to flow to possession. A further adjustment is made to accounts which have been in default for more than 24 months, with an arrears balance increase in the last six months. These accounts have their probability of possession set to 70 per cent based on observed historical losses incurred on accounts that were of an equivalent status.

Asset recovery values: £108 million (31 December 2022: £93 million)

Due to low repossession volumes, sales data informing the estimated level of discount in the event of repossessions has been limited, impacting the ability to update model parameters. Despite these low volumes, since 2020 the observed asset recovery sale values have remained broadly the same on the limited volumes seen, however the indexed valuation within the model has shown an increasing trend due to HPI increases, therefore management consider it appropriate to uplift ECL to reflect expected recovery values. The increase in the judgement reflects an enhancement in the assessment approach as well as increased volumes of predicted defaults against which the adjustment is applied.

Adjustment for specific segments: £26 million (31 December 2022: £27 million)

The Group monitors risks across specific segments of its portfolios which may not be fully captured through wider collective models. The judgement for fire safety and cladding uncertainty has been maintained. Though experience remains limited the risk is considered sufficiently material to address through judgement, given that there is evidence of assessed cases having defective cladding, or other fire safety issues.

Adjustment for Stage 2 oversensitivity: £(69) million (31 December 2022: £nil)

The observed mortgages ECL model oversensitivity to the economic forecast movements is driven by model limitations such as lack of forward looking origination PD and movement from application to behaviour scorecards, amplified by the worsening economic outlook. Management have applied a judgement to mitigate the Stage 2 oversensitivity in recent vintages where the impact is most materially observed.

NOTES TO THE CONDENSED CONSOLIDATED HALF-YEAR FINANCIAL STATEMENTS (continued)

Note 9: Allowance for expected credit losses (continued)

Other judgements (continued)

Lifetime extension on revolving products: £54 million (31 December 2022: £63 million)

An adjustment is required to extend the lifetime used for Stage 2 exposures on unsecured revolving products from a three year modelled lifetime, which reflected the outcome data available when the ECL models were developed. Incremental defaults beyond year three are calculated through the extrapolation of the default trajectory observed throughout the three years and beyond. The judgement has reduced slightly in the period following refinement to the discounting methodology applied.

Adjustments to loss given defaults (LGDs): £(92) million (31 December 2022: £(76) million)

A number of adjustments have been made to the loss given default assumptions used within unsecured credit models. These include largely favourable impacts on ECL in relation to the alignment of MBNA credit card cure rates as collection strategies harmonise and adjustments to capture recent improvements in observed cure rates across all portfolios. These adjustments will be released once incorporated into models through future recalibration which is pending model development. The additional benefit in the period is driven by a greater proportion of charged off accounts being eligible for debt sale.

Following a review on the loss given default approach for commercial exposures management deem ECL should be adjusted to mitigate limitations identified in the approach which are causing loss given defaults to be inflated. These include the benefit from amortisation of exposures relative to collateral values at default and a move to an exposure-weighted approach being adopted. These temporary adjustments will be addressed through future model development.

Note 10: Debt securities in issue

	At 30 June 2023			At 31 December 2022		
	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	**–**	**5,739**	**5,739**	–	4,876	4,876
Covered bonds	**–**	**500**	**500**	–	500	500
Securitisation notes	**25**	**1,339**	**1,364**	26	747	773
	25	**7,578**	**7,603**	26	6,123	6,149

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 2023, external parties held £1,364 million (31 December 2022: £773 million) of the Group's securitisation notes in issue; these notes, together with those held internally, are secured on loans and advances to customers and debt securities held at amortised cost amounting to £26,630 million (31 December 2022: £24,811 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 2023, external parties held £500 million (31 December 2022: £500 million) of the Group's covered bonds in issue; these bonds, together with those held internally, are secured on certain loans and advances to customers amounting to £867 million (31 December 2022: £831 million) that have been assigned to bankruptcy remote limited liability partnerships. These loans are retained on the Group's balance sheet.

The Group holds cash deposits of £1,235 million (31 December 2022: £1,501 million) which support the debt securities issued by the structured entities, the term advances related to covered bonds and other legal obligations.

NOTES TO THE CONDENSED CONSOLIDATED HALF-YEAR FINANCIAL STATEMENTS (continued)

Note 11: Retirement benefit obligations

The Group's post-retirement defined benefit scheme obligations are comprised as follows:

	At 30 Jun 2023 £m	At 31 Dec 2022 £m
Defined benefit pension schemes:		
Present value of funded obligations	**(9,267)**	(9,706)
Fair value of scheme assets	**11,061**	11,157
Net pension scheme asset	**1,794**	1,451
Other post-retirement schemes	**(14)**	(14)
Net retirement benefit asset	**1,780**	1,437
Recognised on the balance sheet as:		
Retirement benefit assets	**1,852**	1,513
Retirement benefit obligations	**(72)**	(76)
Net retirement benefit asset	**1,780**	1,437

Movements in the Group's net post-retirement defined benefit scheme asset during the period were as follows:

	£m
Asset at 1 January 2023	**1,437**
Income statement charge	**11**
Employer contributions	**338**
Remeasurement	**(6)**
Asset at 30 June 2023	**1,780**

The principal assumptions used in the valuations of the defined benefit pension schemes were as follows:

	At 30 Jun 2023 %	At 31 Dec 2022 %
Discount rate	**5.39**	4.93
Rate of inflation:		
Retail Price Index (RPI)	**3.09**	2.99
Consumer Price Index (CPI)	**2.78**	2.68
Rate of salary increases	**0.00**	0.00
Weighted-average rate of increase for pensions in payment	**3.06**	3.01

NOTES TO THE CONDENSED CONSOLIDATED HALF-YEAR FINANCIAL STATEMENTS (continued)

Note 12: Other provisions

	Provisions for financial commitments and guarantees £m	**Regulatory and legal provisions £m**	**Other £m**	**Total £m**
At 1 January 2023	**115**	**709**	**149**	**973**
Exchange and other adjustments	**–**	**–**	**(4)**	**(4)**
Provisions applied	**–**	**(187)**	**(19)**	**(206)**
Charge for the period	**1**	**11**	**21**	**33**
At 30 June 2023	**116**	**533**	**147**	**796**

Regulatory and legal provisions

In the course of its business, the Group engages in discussions with the PRA, FCA and other UK and overseas regulators and other governmental authorities on a range of matters on a regular basis, including legal and regulatory reviews and, from time to time, enforcement investigations (including in relation to compliance with applicable laws and regulations, such as those relating to prudential regulation, consumer protection, investment advice, business conduct, systems and controls, competition/antitrust, tax, anti-bribery, anti-money laundering and sanctions). Any matters discussed or identified during such discussions and inquiries may result in, among other things, further inquiry or investigation, other action being taken by governmental and/or regulatory authorities, increased costs being incurred by the Group, remediation of systems and controls, public or private censure, restriction of the Group's business activities and/or fines. 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 from time to time. Any events or circumstances mentioned herein or below could have a material adverse effect on the Group's financial position, operations or cash flows. Where significant, provisions are held against the costs and/or liabilities expected to be incurred in relation to these matters and matters arising from related internal reviews. However, the impact of such matters cannot always be predicted with certainty and the ultimate liability of the Group may be significantly more, or less, than the amount of any provision recognised. During the half-year to 30 June 2023 the Group charged a further £11 million in respect of legal actions and other regulatory matters. The unutilised balance at 30 June 2023 was £533 million (31 December 2022: £709 million). The most significant items are as follows:

HBOS Reading – review

The Group continues to apply the recommendations from Sir Ross Cranston's review, issued in December 2019, including a reassessment of direct and consequential losses by an independent panel (the Foskett Panel), an extension of debt relief and a wider definition of de facto directors. The Foskett Panel's full scope and methodology was published on 7 July 2020. The Foskett Panel's stated objective is to consider cases via a non-legalistic and fair process and to make their decisions in a generous, fair and common sense manner, assessing claims against an expanded definition of the fraud and on a lower evidential basis.

The provision, unchanged from 2022, includes operational costs in relation to Dame Linda Dobbs's review, which is considering whether the issues relating to HBOS Reading were investigated and appropriately reported by the Group during the period from January 2009 to January 2017, and other programme costs. A significant proportion of the provision relates to the estimated future awards from the Foskett Panel, and is materially dependent on the assumption that the number of awards to date are representative of the full population of cases.

In June 2022, the Foskett Panel announced an alternative option, in the form of a fixed sum award which could be accepted as an alternative to participation in the full re-review process, to support earlier resolution of claims for those deemed by the Foskett Panel to be victims of the fraud. Around three-quarters of the population have now had outcomes via this new process. Notwithstanding the settled claims and the increase in coverage which builds confidence in the full estimated cost, uncertainties remain and the final outcome could be different from the current provision once the re-review is concluded by the Foskett Panel. There is no confirmed timeline for the completion of the Foskett Panel re-review process nor the review by Dame Linda Dobbs. The Group is committed to implementing Sir Ross's recommendations in full.

Payment protection insurance

The Group has incurred costs for PPI over a number of years totalling £6,356 million. The Group continues to challenge PPI litigation cases, with mainly legal fees and operational costs associated with litigation activity recognised within regulatory and legal provisions. PPI litigation remains inherently uncertain, with a number of key court judgments due to be delivered in 2023.

NOTES TO THE CONDENSED CONSOLIDATED HALF-YEAR FINANCIAL STATEMENTS (continued)

Note 13: Related party transactions

Balances and transactions with fellow Lloyds Banking Group undertakings

The Company and its subsidiaries have balances due to and from the Company'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 Jun 2023 £m	At 31 Dec 2022 £m
Assets, included within:		
Derivative financial instruments	**2,941**	2,901
Financial assets at amortised cost: due from fellow Lloyds Banking Group undertakings	**13,398**	13,982
	16,339	16,883
Liabilities, included within:		
Due to fellow Lloyds Banking Group undertakings	**90,546**	88,180
Derivative financial instruments	**3,899**	4,063
Debt securities in issue	**5,091**	4,196
Subordinated liabilities	**1,504**	1,564
	101,040	98,003

During the half-year to 30 June 2023 the Group earned £268 million (half-year to 30 June 2022: £82 million) of interest income and incurred £2,383 million (half-year to 30 June 2022: £983 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 2023 the Group incurred expenditure of £26 million (half-year ended 30 June 2022: £23 million) on behalf of fellow Lloyds Banking Group undertakings which was recharged to those undertakings; and fellow Lloyds Banking Group undertakings incurred expenditure of £605 million (half-year ended 30 June 2022: £597 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 2023 are similar in nature to those for the year ended 31 December 2022.

Note 14: Contingent liabilities, commitments and guarantees

Interchange fees

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

- Litigation brought by or on behalf of retailers against both Visa and Mastercard in the English Courts, in which retailers are seeking damages on grounds that Visa and Mastercard's MIFs breached competition law (this includes a judgment of the Supreme Court in June 2020 upholding the Court of Appeal's finding in 2018 that certain historic interchange arrangements of Mastercard and Visa infringed competition law)
- Litigation brought on behalf of UK consumers in the English Courts against Mastercard

Any impact on the Group of the litigation against Visa and Mastercard remains uncertain at this time, such that it is not practicable for the Group to provide an estimate of any potential financial effect. 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. In 2016, the Lloyds Banking Group received Visa preference shares as part of the consideration for the sale of its shares in Visa Europe. A release assessment is carried out by Visa on certain anniversaries of the sale (in line with the Visa Europe sale documentation) and as a result, some Visa preference shares may be converted into Visa Inc Class A common stock from time to time. Any such release and any subsequent sale of Visa common stock does not impact the contingent liability.

NOTES TO THE CONDENSED CONSOLIDATED HALF-YEAR FINANCIAL STATEMENTS (continued)

Note 14: Contingent liabilities, commitments and guarantees (continued)

LIBOR and other trading rates

Certain Lloyds Banking Group companies, together with other panel banks, have been named as defendants in ongoing 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 London Interbank Offered Rate and the Australian BBSW reference rate.

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 claims against the Lloyds Banking Group in the UK relating 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 ongoing private lawsuits or any related challenges to the interpretation or validity of any of the Group's contractual arrangements, including their timing and scale. As such, it is not practicable to provide an estimate of any potential financial effect.

Tax authorities

The 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 Group that its interpretation of the UK rules means that the group relief is not available. In 2020, HMRC concluded their enquiry into the matter and issued a closure notice. The Group's interpretation of the UK rules has not changed and hence it appealed to the First Tier Tax Tribunal, with a hearing having taken place in May 2023. If the final determination of the matter by the judicial process is that HMRC's position is correct, management estimate that this would result in an increase in current tax liabilities of approximately £390 million (including interest). The Group, having taken appropriate advice, does not consider that this is a case where additional tax will ultimately fall due.

There are a number of other open matters on which the Lloyds Banking Group is in discussions with HMRC (including the tax treatment of certain costs arising from the divestment of TSB Banking Group plc), none of which is expected to have a material impact on the financial position of the Group.

Other legal actions and regulatory matters

In addition, in the course of its 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, enquiries and examinations, requests for information, audits, challenges, investigations and enforcement actions, which could relate to a number of issues, including financial, environmental, compliance, conduct or other regulatory matters, some of which may be beyond the Group's control, both in the UK and overseas. Where material, such 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 based on management's best estimate of the amount required at the relevant balance sheet date, although the recognition of a provision does not amount to an admission of liability or wrongdoing on the part of the Group. 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. 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. Where there is a contingent liability related to an existing provision the relevant disclosures are included within note 12.

Contingent liabilities, commitments and guarantees arising from the banking business

At 30 June 2023 total contingent liabilities were £105 million (31 December 2022: £97 million). Total commitments and guarantees were £64,564 million (31 December 2022: £65,188 million), of which £17,549 million (2022: £17,458 million) was irrevocable.

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The directors listed below (being all the directors of HBOS plc) confirm that to the best of their knowledge these condensed consolidated half-year financial statements have been prepared in accordance with UK adopted International Accounting Standard 34, *Interim Financial Reporting*, and that the half-year management report 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 2023 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 2023 and any material changes in the related party transactions described in the last annual report.

Signed on behalf of the Board by

Charlie Nunn
Group Chief Executive
25 July 2023

HBOS plc Board of Directors:

Executive directors:
Charlie Nunn *(Group Chief Executive)*
William Chalmers *(Chief Financial Officer)*

Non-executive directors:
Sir Robin Budenberg CBE *(Chair)*
Alan Dickinson *(Deputy Chair)*
Sarah Legg
Lord Lupton CBE
Amanda Mackenzie LVO OBE
Harmeen Mehta
Cathy Turner
Scott Wheway
Catherine Woods

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 HBOS plc together with its subsidiaries (the Group) and its current goals and expectations. Statements that are not historical or current facts, including statements about the Group's or its directors' and/or management's beliefs and expectations, are forward looking statements. Words such as, without limitation, 'believes', 'achieves', 'anticipates', 'estimates', 'expects', 'targets', 'should', 'intends', 'aims', 'projects', 'plans', 'potential', 'will', 'would', 'could', 'considered', 'likely', 'may', 'seek', 'estimate', 'probability', 'goal', 'objective', 'deliver', 'endeavour', 'prospects', 'optimistic' and similar expressions or variations on these expressions are intended to identify forward looking statements. These statements concern or may affect future matters, including but 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; the Group's ESG targets and/or commitments; statements of plans, objectives or goals of the Group or its management and other statements that are not historical fact; expectations about the impact of COVID-19; 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 include, but are not limited to: general economic and business conditions in the UK and internationally; political instability including as a result of any UK general election and any further possible referendum on Scottish independence; acts of hostility or terrorism and responses to those acts, or other such events; geopolitical unpredictability; the war between Russia and Ukraine; the tensions between China and Taiwan; market related risks, trends and developments; exposure to counterparty risk; instability in the global financial markets, including within the Eurozone, and as a result of the exit by the UK from the European Union (EU) and the effects of the EU-UK Trade and Cooperation Agreement; the ability to access sufficient sources of capital, liquidity and funding when required; changes to the Group's credit ratings; fluctuations in interest rates, inflation, exchange rates, stock markets and currencies; volatility in credit markets; volatility in the price of the Group's securities; tightening of monetary policy in jurisdictions in which the Group operates; natural pandemic (including but not limited to the COVID-19 pandemic) and other disasters; risks concerning borrower and counterparty credit quality; longevity risks affecting defined benefit pension schemes; risks related to the uncertainty surrounding the integrity and continued existence of reference rates; changes in laws, regulations, practices and accounting standards or taxation; changes to regulatory capital or liquidity requirements and similar contingencies; the policies and actions of governmental or regulatory authorities or courts together with any resulting impact on the future structure of the Group; risks associated with the Group's compliance with a wide range of laws and regulations; assessment related to resolution planning requirements; risks related to regulatory actions which may be taken in the event of a bank or Group failure; exposure to legal, regulatory or competition proceedings, investigations or complaints; failure to comply with anti-money laundering, counter terrorist financing, anti-bribery and sanctions regulations; failure to prevent or detect any illegal or improper activities; operational risks; conduct risk; 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; technological failure; inadequate or failed internal or external processes or systems; risks relating to ESG matters, such as climate change (and achieving climate change ambitions), including the Group's ability along with the government and other stakeholders to measure, manage and mitigate the impacts of climate change effectively, and human rights issues; the impact of competitive conditions; failure to attract, retain and develop high calibre talent; the ability to achieve strategic objectives; the ability to derive cost savings and other benefits including, but without limitation, as a result of any acquisitions, disposals and other strategic transactions; inability to capture accurately the expected value from acquisitions; assumptions and estimates that form the basis of the Group's financial statements; and potential changes in dividend policy. A number of these influences and factors are beyond the control of the Group or any of the Group's immediate or ultimate parent entities (if applicable). Please refer to the latest Annual Report on Form 20-F filed by Lloyds Bank plc with the US Securities and Exchange Commission (the SEC), which is available on the SEC's website at www.sec.gov, for a discussion of certain factors and risks. Lloyds Banking Group plc may also make or disclose written and/or oral forward-looking statements in other written materials and in oral statements made by the directors, officers or employees of Lloyds Banking Group plc 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 whether as a result of new information, future events or otherwise. 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.

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