Lloyds Bank Corporate Markets plc

Report and Accounts
2020

Member of Lloyds Banking Group

Contents

Strategic report

The directors present their Strategic report on Lloyds Bank Corporate Markets plc (the Bank) and its subsidiary undertakings (the Group) for the year ended 31 December 2020.

The Bank and the Group provide a wide range of banking and financial services through branches and offices in the UK, the Crown Dependencies, the USA, Singapore and Germany. The Bank was established in response to the Financial Services (Banking Reform) Act 2013 for the purpose of carrying on elements of the commercial banking business of Lloyds Banking Group plc (also referred to herein as LBG) along with the banking business of LBG in territories outside the EEA. The Group contributes to the financial results of the Commercial Banking Division of LBG.

Principal activities

The Group supports a diverse range of customers and provides a broad range of banking products to help them achieve their financial goals. The Group's revenues are earned through the provision of financing and risk management solutions to commercial customers; and current accounts, savings accounts, mortgages, car finance and personal loans in the Retail market in our Crown Dependencies businesses.

The target market for these products and services in the UK and internationally is made up of large corporates, financial institutions, commercial customers plus, in the Crown Dependencies, retail customers and includes the following product propositions:

- Commercial lending (including fixed rates loans, revolving credit facilities, variable loans and business mortgages)
- Trade and working capital management (including trade services, trade finance, supply chain finance and asset finance)
- Bonds and structured finance (including bonds, structured lending and asset securitisation)
- Risk management (including FX, rates, credit, commodities and liabilities management)
- Retail banking services (including mortgages, personal current accounts, personal loans and motor finance) in the Crown Dependencies

Key performance indicators

The Group's strategic purpose as part of LBG is to Help Britain Recover as part of Helping Britain Prosper through operating a responsible business that focuses on delighting our customers and delivering long-term sustainable success. Key to the success of the Group's strategy is the focus on delighting our customers and success is measured via customer focussed objectives such as customer satisfaction and complaint levels monitored through a range of customer insight and feedback. Our ongoing commitment to treat customers fairly and consistently delivering great service is central to our ways of working. Our customer focused business model continues to provide a competitive advantage with the diversity and strength of our client franchise enabling scalable business propositions, relative cost efficiencies and sustainable returns on capital deployed. We have developed a culture to attract, retain and develop the right capability for the future. The Group has a diversified and high quality balance sheet and is Helping Britain Prosper through a simple digitised business underpinned by a strong brand, credit rating and capital position. The shared service model we utilise leverages LBG capabilities to meet the needs of our customers and we are transforming the business to deliver a leading customer experience.

The Bank's Board of Directors (the Board) regularly monitors key performance indicators which include business performance, appropriate levels of capital, funding and liquidity, and delighting our customers. The Board notes the following with regard to strategic process and indicators of performance:

- Appropriate levels of capital, liquidity and funding have been maintained and metrics are noted in tables 1 and 2 on page 4
- Support provided to our customers during COVID-19. Despite the disruption encountered during 2020, the Group has continued to support customers and provide assistance
- Continued targeted investment in a number of areas across the period to benefit both customers and colleagues, including investing in our markets proposition and technology roll out in our Crown Dependencies business to enhance capability and grow the commercial franchise
- Mortgage growth in our Retail business with now over £1 billion lent in our Crown Dependencies
- Build out of our Frankfurt subsidiary Lloyds Bank Corporate Markets Wertpapierhandelsbank GmbH to enable securities trading in the Eurozone after the UK exit from the European Union
- The seamless continuity of operations across our business both in the UK and internationally with most colleagues moving to home working in the period (both within the Group and our shared service provider teams)
- The wellbeing of team members throughout our businesses with measures taken to ensure our branch based customer facing colleagues were able to operate in a safe way in addition to the provision of IT and other equipment to facilitate office based colleagues working from home
- Development of new ways of working across our teams to support home working, caring and schooling responsibilities and the deployment of online collaboration technologies and applications
- Colleague development, learning hours and engagement measured through our annual survey
- Decisive management action to reduce controllable costs and funding and liquidity risk. This included the delivery of optimisation activity in our lending business in the USA where the Group has strategically exited certain facilities, including the sale of a portfolio of eligible facilities to Lloyds Bank plc
- Successful divestment of the Group's Jersey based investment management business to Brooks MacDonald, enabling the Group to focus on core service propositions (the Group will no longer operate in this particular market). A subsidiary of the Group, Lloyds Investment Fund Managers Limited was sold along with the customers and assets under management from Lloyds Bank International Limited
- Good progress towards IBOR transition

Future developments

The Group's long term customer and strategic priorities remain unchanged. We will grow the business in core Retail and Commercial franchises through product and service enhancements; in Markets we will continue to respond to the industry pace of change to remain competitive and meet our customers' evolving needs. Further digitisation will simplify our operating model, increase efficiency and deliver a stronger proposition for customers. Focus continues on having optimal levels of funding, capital and costs to deliver sustainable returns on equity. In the short to medium term, we will also continue to support our customers through COVID-19 and the recovery of the UK economy and the international territories in which the Group operates.

Financial performance

Overall, 2020 has seen a very resilient performance of the Group's diversified business despite the difficult environment and challenging market conditions. Although COVID-19 has impacted the Group's results, the Board considers the decisive actions taken in response to the global pandemic as a key measure of performance in the year. The Group's expected credit loss (ECL) on loans and commitments, calculated under IFRS 9, requires the use of a range of possible future outcomes. The projected impacts on the markets in which we operate has resulted in significant increases in ECL charges recognised through the impairment line of the Income Statement. This along with fair value write downs on derivatives recognised through net trading income, has impacted profitability, despite diligent management of costs and capital.

During the year ended 31 December 2020, the Group recorded a profit before tax of £45 million compared with £368 million in 2019. Regulatory capital adequacy remains strong with a common equity tier 1 (CET1) capital ratio of 14.8%, reflecting the stability of the business and strength of the Group's client franchise.

Income

Total income was £544 million compared to £819 million in 2019, comprising net interest income of £74 million compared to £221 million in 2019, net fee and commission income of £191 million compared to £188 million in 2019 and net trading income of £279 million compared to £410 million in 2019. The COVID-19 pandemic has had an effect on the global economy and financial markets with net interest income being adversely impacted through increased costs of funding and a continued low interest rate environment. Within the 2020 net trading income of £279 million, the Group has taken a fair value write down of £88 million on derivative positions. This was concentrated in a single counterparty that has only derivative exposure with the Group entering administration during the pandemic. Net fee and commission income has shown a resilient performance year on year.

Operating expenses & tax

Operating expenses were £428 million compared to £462 million in 2019, predominantly consisting of management charges relating to the Intra Group Agreement (IGA) and staff costs payable to Lloyds Bank plc. This represents a reduction of £34 million as a result of management action and specific cost control initiatives.

The Group recorded a tax expense of £1 million compared to £85 million in 2019 reflecting lower profitability in 2020.

Impairment

The other key impact of the economic implications of COVID-19 has been an increase in the ECL with a net impairment expense of £71 million recognised compared to a net release of £11 million in 2019. This ECL charge is driven by the forward looking nature of IFRS9 (stage 1 and 2 impairment) and the forecast deterioration in the economic outlook. This has shown a small improvement since half year but remains a significant element of financial performance. There have been no significant new credit impaired cases (stage 3 impairment) in the year.

Assets

Total assets of the Group were £92,429 million at 31 December 2020, £12,768 million higher than the assets at 31 December 2019 of £79,661 million. The largest movement is in cash and balances at central banks which increased by £7,119 million from £16,250 million at 31 December 2019 to £23,369 million at 31 December 2020 reflecting prudent management action to increase liquidity to serve customer needs and should the impact of COVID-19 cause further market distress.

Financial assets at fair value through profit or loss increased in the year by £2,780 million to £20,926 million compared to £18,146 million at 31 December 2019 driven by increases in reverse repurchase agreements. Derivative financial instruments increased in the year by £2,921 million to £21,757 million compared to £18,836 million at 31 December 2019 mainly due to a fall in the market yield curves. Financial assets at amortised cost decreased to £25,087 million compared to £25,899 million at 31 December 2019, this includes Loans and Advances to Customers of £18,452 million compared to £20,264 million at 31 December 2019 reflecting optimisation activity.

Liabilities

Total liabilities of the Group were £88,800 million at 31 December 2020 compared to £75,385 million at 31 December 2019 driven by increases in financial liabilities at fair value through profit or loss, derivative financial instruments and debt securities in issue.

Customer deposits of £25,497 million increased by £1,018 million from £24,479 million at 31 December 2019. Financial liabilities at fair value through profit or loss of £15,815 million increased by £2,031 million compared to £13,784 million at 31 December 2019 reflecting an increase in repurchase agreements. Derivative financial instruments of £21,233 million compared to £17,762 million at 31 December 2019 increased by £3,471 million mainly as a result of a fall in market yield curves.

Debt securities in issue of £15,602 million increased in the year by £3,173 million compared to £12,429 million at 31 December 2019 mainly due to new issuances during 2020 of commercial paper and in the Lloyds Bank Corporate Markets plc European Medium-term Note programme. This resulted in increased liquidity in addition to improving the liability maturity profile.

Total equity at the year end was £3,629 million compared to £4,276 million at 31 December 2019. This movement largely reflects that during the year the Board approved the payment of an interim dividend of £700 million to the Group's parent company LBG.

The Bank's common equity tier 1 capital ratio increased to 14.8 per cent (31 December 2019: 14.0 per cent) and the tier 1 capital ratio increased to 19.4 per cent (31 December 2019: 18.4 per cent), largely due to the reduction in risk-weighted assets and the removal of the securitisation deduction, partially offset by the accrual for foreseeable dividends.

The total capital ratio increased to 22.5 per cent (31 December 2019: 21.6 per cent) largely reflecting the reduction in risk-weighted assets and the net increase in tier 1 capital.

Risk-weighted assets reduced by £411 million, or 2.4 per cent, to £16,610 million at 31 December 2020, compared to £17,021 million at 31 December 2019, largely reflecting optimisation activity and a change in mix of the portfolio offset, by increases in market risk and counterparty-credit risk.

Capital position at 31 December 2020

Following a change in approach the capital position of Lloyds Bank Corporate Markets 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 31 December 2020, applying current IFRS 9 transitional arrangements, is set out in the following section.

Table 1: Bank capital resources (audited)

	2020 £m	2019 £m
Common equity tier 1		
Shareholder's equity per balance sheet	**2,914**	3,593
Adjustment to retained earnings for foreseeable dividends	**(200)**	(700)
Cash flow hedging reserve	**(105)**	(56)
Debit valuation adjustment	**(25)**	(25)
Other adjustments	**34**	3
Sub-total	**2,618**	2,815
Less: deductions from common equity tier 1		
Prudent valuation adjustment	**(156)**	(179)
Excess of expected losses over impairment provisions and value adjustments	**–**	(16)
Securitisation deductions	**–**	(185)
Deferred tax assets	**–**	(2)
Significant investments	**–**	(52)
Common equity tier 1 capital	**2,462**	2,381
Additional tier 1		
Additional tier 1 instruments	**757**	757
Total tier 1 capital	**3,219**	3,138
Tier 2		
Tier 2 instruments	**635**	645
Other adjustments	**(109)**	(98)
Total tier 2 capital	**526**	547
Total capital resources	**3,745**	3,685
Risk-weighted assets	**16,610**	17,021
Common equity tier 1 capital ratio[1]	**14.8%**	14.0%
Tier 1 capital ratio[1]	**19.4%**	18.4%
Total capital ratio[1]	**22.5%**	21.6%

1 Reflecting the full impact of IFRS 9 at 31 December 2020, without the application of transitional arrangements, the Bank's common equity tier 1 capital ratio would be 14.6 per cent, the tier 1 capital ratio would be 19.2 per cent and the total capital ratio would be 22.5 per cent.

Table 2: Bank risk-weighted assets (unaudited)

	2020 £m	2019 £m
Foundation Internal Ratings Based (IRB) Approach	**6,566**	7,270
Other IRB Approach	**267**	433
IRB Approach	**6,833**	7,703
Standardised Approach	**1,961**	2,262
Credit risk	**8,794**	9,965
Counterparty credit risk	**3,948**	3,477
Credit valuation adjustment risk	**324**	313
Operational risk	**952**	1,062
Market risk	**1,982**	1,588
Underlying risk-weighted assets	**16,000**	16,405
Threshold risk-weighted assets	**610**	616
Total risk-weighted assets	**16,610**	17,021

Section 172(1) statement and statement of engagement with employees and other stakeholders

In accordance with the Companies Act 2006 (the Act) (as amended by the Companies (Miscellaneous Reporting) Regulations 2018), the directors provide the following statement describing how they have had regard to the matters set out in section 172(1) of the Act, when performing their duty to promote the success of the Bank under section 172. Further details on key actions in this regard are also contained within the Directors' report on page 12 and the Corporate Governance Report on pages 12 to 14.

In accordance with the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (as amended by the Companies (Miscellaneous Reporting) Regulations 2018), the following statement also provides details of how the directors have engaged with and had regard to the interests of key stakeholders. The Bank is a subsidiary of LBG, and as such adopts many of the processes and practices of LBG, which are further referred to in this statement where relevant.

The directors acknowledge that one of the primary responsibilities of the Board is to ensure the strategy of the Bank, as aligned to that of LBG, achieves long-term success and generates sustainable returns, central to which is ensuring engagement with stakeholders, and considering in all instances the long-term implications of decisions made, acting at all times to maintain the highest possible standards of conduct. This year interaction with stakeholders was adapted to comply with the UK Government's measures in relation to COVID-19 and has been undertaken virtually as necessary.

Customers

The Board's deep understanding of customers' needs is vital in setting and achieving the Bank's goals. Delighting our customers and identifying their needs through a customer-centric approach remains therefore a key consideration in Board decisions.

COVID-19 response

The Group's response to the COVID pandemic has been a central focus for the Board since the start of the outbreak which has magnified existing challenges for customers. The Board has remained fully focused on helping customers and the UK economy recover by supporting businesses across the jurisdictions in which the Group operates. The Group has actively supported the UK Government through increased participation in the Debt Management Office Gilt Issuance and Asset Purchase Facility buy-back schemes and has supported customers in the Crown Dependencies through the governments' Coronavirus Business Interruption Loan schemes and payment holidays.

The directors ensure the Bank works towards achieving its customers ambitions, treating customers fairly, and making it easy for customers to find, understand and access products that are suitable for their needs. The Board is committed to providing meaningful support to meet the needs of customers, aiming to provide positive outcomes, and working to mitigate or reduce the risk of financial harm. Ensuring a smooth customer transition was a key focus in the Board's decision making when considering the divestment of the Group's Jersey based investment management business to Brooks MacDonald, and the delivery of the optimisation activity in the lending business in the USA where the Group has strategically exited certain facilities.

To ensure directors truly understand the needs of customers, customer feedback and related management information is regularly considered including as part of the directors' strategic decision-making process. The Bank proactively engages with customers by conducting customer feedback surveys, including the Client 360 Feedback Programmes, and Greenwich surveys. The Board exercises oversight of customer satisfaction through updates from the output of these surveys and the level of complaints within the business.

The Bank regularly benchmarks its performance and the performance of its business units amongst its customers. The directors use this insight along with a range of internal and external research to ensure ongoing improvement in customer experience. The directors ensure the Bank plays an active part in LBG's wider customer ambitions, as acknowledged in the Bank's strategy, and where appropriate during the course of the year this has included the ongoing development of market leading digital propositions, more personalised customer propositions and better experience for customers across all channels.

In line with the Group's purpose of Helping Britain Prosper, the primary focus during the current pandemic has been to support and do what is right for our customers and this has been central to the activities of the directors.

Shareholders

The Bank is a wholly owned subsidiary of LBG, forming part of its Commercial Banking Division. As a wholly owned subsidiary, the Board ensures that the strategy, priorities, processes and practices of the Group are aligned where appropriate to those of LBG, ensuring that its interests as the Bank's shareholder are duly acknowledged. The Bank's Corporate Governance Framework sets out the Bank's relationship with LBG and the reporting of material matters to the LBG Chair, LBG Board and LBG Chief Executive Officer.

Two senior leaders of LBG serve as directors on the Bank's Board in a non-executive capacity and the Chair of the Bank's Board serves also on the Board of LBG. The Board of LBG and its Board Risk and Audit Committees and the Group Executive Committee receive regular updates from the LBCM Board and its Committees on the Bank's activities and performance. The LBG Chief Executive Officer and LBG Chair aim to attend at least one Bank Board meeting each year to hold an open discussion on such matters as the Bank's strategy in the context of LBG and the operation of the shared service model. In 2020 this also included discussion on the support for customers and colleagues during the COVID-19 pandemic. LBG's Non-Executive Directors are invited to attend Board and Committee meetings during the year at which the Board can share insights and hear the LBG perspective increasing shareholder engagement. These arrangements ensure the Bank's Board has a clear understanding of the views of its shareholder.

Further information in respect of the relationship of LBG with its shareholders is included in the Strategic Report within the Lloyds Banking Group Annual Report and Accounts for 2020, available on the Lloyds Banking Group website.

Colleagues

The Board considers that maintaining open dialogue is crucial in informing its thinking, allowing directors to hear first-hand colleague views on the matters most important to them, and to the Group. Throughout 2020 the Board received regular updates on workforce[1] engagement and on colleague matters generally including key themes raised by colleagues and trends on people matters, including for example absence or attrition and the Group's response to the COVID pandemic. The Board's focus on colleague matters has included engagement, culture, succession and people risks.

During the year there were plenty of opportunities for two-way communication between the Board and the workforce. These included informal colleague breakfast and lunch meetings held virtually by the Chairman and Non-Executive Directors. Virtual Town Hall sessions were hosted by both the Chairman and the Chief Executive. These were complemented by engagement sessions led by the Chief Executive and other senior members of his Executive team with members of the Board participating in Q&A sessions. These sessions were particularly helpful in allowing colleagues the opportunity to ask questions, share their views and receive a direct answer in real time. The Board considered the feedback from these sessions which provided useful insights into colleague sentiment.

During the year, the Board gained further understanding of colleague views through a number of surveys completed by colleagues across the Group. These included the annual colleague survey, ad hoc 'Pulse' surveys, and participation by colleagues in the external survey of the Banking Standards Board.

The directors consider these arrangements invaluable in giving them an understanding of the views of the workforce and encouraging meaningful dialogue between the Board and the workforce.

During the year the Group also communicated directly with colleagues detailing its performance and that of LBG, changes in the economic and regulatory environment, and updates on key strategic initiatives. The Board was especially mindful of the impacts on colleagues of the strategic changes made during the year, in particular in the Crown Dependencies and the USA, ensuring colleagues were kept informed and supported throughout the process. Meetings were also held throughout the year between LBG representatives and our recognised unions.

Our colleagues are remunerated by LBG and UK colleagues are eligible to participate in HMRC approved share plans which promote share ownership by giving employees an opportunity to invest in LBG shares. A one-off £250 cash recognition award was paid in July 2020 to c500 predominantly customer-facing colleagues. The impact of the pandemic on LBG's financial results has meant there was no Group Performance Share pool for 2020. In order to keep with the approach of timely, open and honest communication, this was communicated to colleagues in December 2020. This is in no way reflective of the hard work, commitment and sacrifice colleagues have made throughout the year to keep business running and helping customers. To recognise further the considerable role that all colleagues have played in supporting customers in 2020, and the part they will play in delivering the next phase of the strategy, every permanent colleague will receive a £400 share award. Further information can be found in the Directors' Remuneration Report within the LBG Annual Report and Accounts for 2020, available on the LBG website.

COVID-19 response

During 2020, the Bank has continued to provide essential financial services to its customers by implementing business changes to manage the pandemic and have reviewed every iteration of the Government advice in the UK and local advice across the jurisdictions in which it operates. In response to changing customer demands, changing colleague needs and expectations, a fluctuating and less stable business environment, and significant economic issues the Group has had to reimagine ways of working. Health and safety of colleagues was a key COVID-19 consideration with a response which included supporting colleagues to work from home with the appropriate technology, equipment and IT assistance and ensuring offices that were open complied with regulations.

Colleagues are vital to the delivery of the Group's strategy and ambitions. This is recognised by the Board in its engagement with colleagues throughout the year. Whilst the COVID-19 pandemic has been challenging for our customers, it has also posed challenges for our colleagues. The Board was therefore keen to ensure colleagues received all the support the Group could give.

During the COVID-19 period the Chief Executive held regular Board calls to keep the Board updated on pertinent COVID-19 issues impacting the Group and the wider external environment where the Board could provide support to the Chief Executive's initiatives. Regular engagement has continued throughout the pandemic.

Regular and open engagement with colleagues has been crucial, with the Chief Executive undertaking a series of updates and calls to keep colleagues informed of developments.

This was supported by regular updates from the senior Executive team. The Chairman and Chief Executive delivered podcasts and held colleague Q&A sessions where colleagues posed the questions which mattered to them most. In addition, the LBG Chief Executive, senior Executive team and Group People Director have delivered regular communications to colleagues in the form of video broadcasts and updates.

The Board has considered how colleague working practices will develop beyond the COVID crisis including how more flexible and efficient ways of working, seen during 2020, could be retained.

1 The definition of 'workforce' as agreed by the Board is permanent employees, contingent workers and third-party suppliers that work on LBG premises delivering services to customers and supporting key business operations.

Diversity

The Board believes a diverse workforce is vital to the Group's success and values the differences each colleague brings to their role, making the Group stronger and better able to meet the needs of its customers. The Bank continues to have focus on its gender targets whilst also interlocking with LBG's Race Action plan which was introduced in July 2020 designed to drive race related cultural change, recruitment and progression and is putting in appropriate action plans to meet the target to increase Black representation in senior roles to at least 3 per cent by 2025. The Board's focus on inclusion and diversity has extended to all the jurisdictions in which the Group operates which have their own demographic profile.

Communities

The directors acknowledge that the Group, as part of one of the largest financial service providers in the UK, has responsibilities to invest in the communities in which it operates, to help them prosper economically and build a more sustainable future. As such the directors receive regular updates on responsible and sustainable business activities. The Group participates in related LBG initiatives, with the directors ensuring the Group plays an appropriate role in LBG's related Helping Britain Recover ambition as part of the Helping Britain Prosper plan.

The directors have regard to the Group's sustainable business activity which continues to support delivery of LBG's ambition to be a leading UK bank in the Green/Sustainable Bonds market through the Bank's Green bond activity. Since 2017 the Group has acted as bookrunner on more Environmental, Social and Governance (ESG) transactions from UK Corporate Issuers than any other bank, making LBG number three in the league table during this period.

More broadly, the Group continues to invest in the communities in which it operates through initiatives such as development of onshore and offshore wind towers, wind farm projects and solar energy project funding.

As part of the regular updates to the Board on sustainable business activity information is shared on how the Group has established an international working forum. The focus has been to promote and support the reduction of its own Carbon Footprint through initiatives related to travel. The Group is also active in reducing the carbon emissions it funds which contributes to the LBG target of at least 50 per cent reduction by 2030.

The Board also receives updates on how the Group is progressing on supporting its communities. Initiatives include, for example, the Group's work with LBG's charitable foundations to help local communities in the Crown Dependencies such as the Lloyds Bank Foundation for the Channel Islands which supported a number of charities through grants, and provided a wide range of developmental support, including training and mentoring. The Group has also been actively engaged in the Digital skills initiative and other volunteering events across its jurisdictions in Singapore, the USA and the Crown Dependencies. The #StayConnected initiative offers older and vulnerable customers in the Crown Dependencies access to tablets to keep in touch with their families and emergency funding was provided to help set up devices, share digital skills and organise Lloyds branches as collection points for device donations.

The Board acknowledges the contribution that colleagues have made to local communities through volunteering and fundraising activities focussing support on assisting communities during the COVID-19 pandemic.

Within the local community, the Crown Dependencies business operates "Bringing Banking to You", supporting customers in their workplace through offering individual financial reviews for their workforce. Over 4,000 customers and around 200 businesses have benefited from this service since its conception.

Suppliers
The Board recognises the importance of partners who provide aspects of our operations and customer service provision through the shared service model with LBG. The Bank's approach to external supplier management follows that of LBG, working with suppliers of varying sizes, most in professional services sectors such as IT, cyber, operations, management consultancy, legal, HR, marketing, and communication. The supply chain is crucial to the way the Bank and LBG serves its customers, and through it the reach is considerable. The impacts of the COVID crisis and EU exit have been no less material within LBG's supply chain, with the Board keen to ensure that whilst the services are received via the Intra Group Agreement (IGA), these important relationships are not unduly impacted.

The Bank and LBG seek to improve the experience of suppliers, with feedback regularly sought on related assurance processes to ensure continued improvement in the process. Suppliers are also encouraged to express their satisfaction or otherwise and have access to LBG and the Bank's whistleblowing service.

Importance is placed on having the right supplier framework to operate responsibly. LBG's Sourcing & Supply Chain Management Policy applies to all businesses, divisions, and subsidiaries of LBG, including the Bank, with the directors assuming ultimate responsibility for its application as relevant to the Bank. This Policy has been designed to assist in managing the inherent risk in outsourcing services, and in dealing with third party suppliers. Suppliers are required to adhere to relevant LBG policies and comply with LBG's Code of Supplier Responsibility which can be found on the LBG website. This defines expectations for responsible business behaviour, underpinning the efforts of the Bank and LBG to share and extend good practice. All material contracts are subject to rigorous cost management governance with regular review of key supplier risks.

The operation of the Group's supply chain is through LBG. The Board supports LBG's zero tolerance attitude towards modern slavery in LBG's supply chain and an assurance process of the measures which address the risk of human trafficking and modern slavery in the wider supply chain is undertaken by the Group.

Regulators
The Bank and its directors have an open, and transparent relationship with relevant regulators and other authorities and liaise regularly both directly and as part of LBG to ensure the business is aligned to the evolving regulatory framework. Engagement has been needed with the regulators and other authorities in response to the COVID crisis. Key areas of focus have included ensuring robust prudential standards and supervision arrangements are in place, ensuring the fair treatment of customers, adapting to changes in regulatory requirements, recovery and resolution, preparations for the UK's withdrawal from the EU and the Bank's ongoing response to market changes.

The Chairman and individual directors have in the ordinary course of business had continuing discussions with the FCA and PRA on a number of aspects of the regulatory agenda.

The Board in turn reviewed regular updates on regulatory engagement and key areas of regulatory focus as listed above, alongside progress being made in addressing key regulatory priorities. During the year such changes have included not only the response to COVID, but LIBOR cessation, climate change responsibilities, and the Bank's ongoing financial and operational resilience.

Board members, in the ordinary course of business, proactively engage with regulators across all these areas in addition to regular updates at Board Risk Committee. These updates cover all aspects of the regulatory agenda including emerging regulatory and legal risks. This provides a focused view of areas of priority.

The Board continues to closely monitor the status of the Bank's regulatory relationships across all the jurisdictions in which it has a presence, seeking to enhance engagement particularly in key areas of regulatory change. During the coming year, this is expected to continue to include the ongoing impacts of COVID, IBOR cessation, EU exit transition, credit risk including the standardised approach to counterparty credit risk (SA-CCR), and climate risk management.

Principal risks and uncertainties
2020 has been a year of significant uncertainty, including that arising from the spread of COVID-19 and its impact on global and domestic economies and the UK's exit from the European Union. The unprecedented events of this year have demonstrated how individual risks can combine to place pressure on the Group's strategy, business model and performance.

COVID-19 has had a significant impact on all risk types in 2020, and understanding and managing the impacts dynamically has been a major area of focus. The Group reacted quickly to the challenges faced, putting in place risk mitigation strategies and refining its investment and strategic plans. Since March 2020, the Group has adopted remote working and other new ways of working to ensure customer needs and expectations are met during and after the COVID-19 pandemic (people risk). The Group has adapted quickly to evolving regulatory expectations and has engaged with regulatory authorities throughout. The Group continues to monitor, assess the risks, and address the impacts on its customers and colleagues. The macroeconomic environment remains highly uncertain across all the jurisdictions that the Group operates in, including the UK where a third national lockdown is in place and is expected to be lifted through H1 2021 based on conditions defined by the UK government. Individual criteria have to be met for the next step of the lockdown easing to progress. The effectiveness of vaccines and the government's ability to deliver them to the majority of the populace will be key factors in restricting the spread of the virus in 2021. In addition, as the macroeconomic outlook remains uncertain, aggressive fiscal policies implemented to respond to the pandemic have led to elevated government indebtedness in advanced economies and limited headroom for conventional monetary policy. These circumstances may spur the wider adoption of less conventional monetary policies such as negative interest rates. Negative interest rates could have an adverse impact on the Group's net interest income and profitability. In many countries, interest rates have already turned negative or are very close to zero and governments, including the UK, are borrowing at negative yields. Conversely, there may be upward pressure on inflation and interest rates due to COVID-19 impacts around the world. Higher interest rates could trigger vulnerabilities within highly indebted companies and households, and to asset prices which have been boosted by high levels of liquidity provided by central banks.

In addition to the risks mentioned above, COVID-19 has had, and could continue to have, an adverse impact across risks including the Group's credit portfolio with increasing levels of impairment. Linked to this, there is increased model risk as the effect of government-led customer support initiatives have weakened established relationships between model inputs and outputs, reducing the ability to forecast using models alone. While underlying model drivers are expected to remain valid in the longer term, year end impairment reporting contains a greater element of governed judgement that reflects current conditions. In addition, the Group continues to assess and address the impact of data and operational risk created by the business disruptions, capital risk impacts linked to impairments and RWAs, funding and liquidity risk through higher funding costs and the potential threat of a credit rating downgrade.

The UK and EU agreed the EU-UK Trade and Cooperation Agreement (TCA), which was written into UK law on December 31st 2020 through the European Union (Future Relationship) Act 2020. The trade agreement primarily allows the tariff and quota free movement of goods between the UK and EU, but trade is no longer frictionless at borders. The deal only covers services in very narrow areas. As a result of these changes, UK companies have lost the ability to passport into the EU. However, negotiations on financial services are expected to continue with both sides aiming to agree and sign a Memorandum of Understanding establishing a framework for Financial Services Regulatory Cooperation by the 31st March 2021. The Group continues to consider the ongoing impact of the TCA on its customers, colleagues, products and business strategy including the potential legal, regulatory, tax, financial and capital implications. The Group operates in the European Union through its subsidiary in Germany, Lloyds Bank Corporate Markets Wertpapierhandelsbank GmbH (LBCMW) which offers a set of products to meet the current clients' needs in the EU. With LBG, the Group continues to work closely with regulatory authorities and industry bodies to ensure that the Group can identify and respond to the evolving regulatory and legal landscape and meet clients' demands with appropriate products and service offerings.

Additionally, the Group continues its transition from IBORs to Alternative Risk Free Reference Rates in anticipation of London Interbank Offered Rate (LIBOR) cessation announcements in 2021. As a result, existing benchmark rates may be discontinued or the basis on which they are calculated may change, impacting pricing, market risk and valuations. Uncertainty as to the nature of such potential changes, including the impact of the UK Government's Tough Legacy Legislation, may adversely affect the value of a broad array of financial products, including any LIBOR-based securities, loans and derivatives. These changes could have important implications for the Group's customers by necessitating amendments to existing documents and contracts and thereby creating differentials in performance of benchmark rates and financial products which reference them. The Group is working closely with LBG on the transition away from IBORs.

The most significant risks that could impact the Group's ability to deliver its long-term strategic objectives, and the approach to managing each risk, are detailed below. These principal risks and uncertainties are reviewed and reported to the Board Risk Committee regularly.

The provision of services to the Group supporting the business, operations and support functions is out sourced to Lloyds Bank plc via a shared service provision model. References below to the Group's shared service provider refers to this arrangement.

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

Key mitigating actions
- Credit policy, incorporating prudent lending criteria, aligned with the Board approved risk appetite, to manage risk effectively
- Robust risk assessment and credit sanctioning to ensure appropriate and responsible lending
- Extensive and thorough credit processes and controls to ensure effective and timely risk identification, management and oversight
- Effective governance processes delivered by the shared service and supported by independent credit risk assurances
- Early identification of signs of stress leading to engagement with the customer

Regulatory and legal risk
The risk arising from the failure to identify, assess, correctly interpret, comply with, or manage regulatory and/or legal requirements, leading to customer detriment, failure to prevent fraud and financial crime, financial penalties, regulatory censure, criminal or civil enforcement action.

Key mitigating actions
- The Board has established a risk appetite metric for regulatory and legal risk
- Effective, well established compliance and legal risk management policies and procedures which ensure appropriate controls and systems are in place to comply with applicable laws, rules and regulations
- Robust framework and processes are in place to monitor on-going compliance with new legislation
- Continued investment in people, processes, training and IT to assess impact and help meet our legal and regulatory commitments
- Ongoing horizon scanning to identify and address changes in regulatory and legal requirements
- Effective engagement with regulatory authorities and industry bodies on forthcoming regulatory changes, market reviews and investigations
- Effective mechanisms for the business are in place to identify, assess and monitor risks, providing appropriate management information, and with robust oversight and escalation routes

Conduct risk
The risk of 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.

Key mitigating actions
- Simplified and enhanced conduct policies and procedures are in place to ensure appropriate controls and systems that deliver fair customer outcomes and support market integrity and competition requirements
- Conduct risk appetite metrics provide a granular view of how our products and services are performing for customers through the customer lifecycle
- Product approval, continuous product review processes and customer outcome testing (across products and services) supported by conduct management information
- Root cause analysis, enhanced complaint management and clear customer accountabilities for colleagues, with rewards driven by customer-centric metrics
- Further enhancements and embedding of our framework to support all customers, including, in particular, those in vulnerable circumstances
- Achieving a values led culture through a focus on behaviours to ensure we are transforming our culture for success in a digital world. This is supported by strong direction and tone from senior executives and the Board
- Review and oversight of thematic conduct agenda items at senior committees, ensuring holistic consideration of key conduct risks
- Robust recruitment and training, with a continued focus on how the Group manages colleagues' performance with clear customer accountabilities
- Ongoing engagement with third-parties involved in serving the Group's customers to ensure consistent delivery

Operational risk
The risk of inadequate or failed internal processes, people, systems or from external events (including cyber-related and fraud and financial crime prevention challenges) leading to loss.

Key mitigating actions
- Continued investment in the Group's control environment by both the Group and its shared service provider, with an emphasis on automated preventative and real-time detective controls
- Deployment of enhanced cyber controls to detect, protect against and respond to threats to the confidentiality or integrity of information assets, or the availability of systems, and to ensure effective third-party assurance
- Enhancing technology infrastructure and the resilience of systems (including focus on simplification of IT architecture and the decommissioning of legacy systems) that support critical business processes
- Application of a risk based approach to mitigate financial crime and both internal and external fraud risk
- Working with industry bodies and law enforcement agencies to identify and combat fraud and money laundering
- Rigorous oversight of relevant management at business area and entity-level committees
- Explicit focus on the effectiveness of these mitigants in the context of changes arising from/in response to COVID-19

Operational risk: shared services model (SSM)
LBG's chosen ring-fencing operating model introduces risk for the Group in the execution of that model as a shared service recipient.

Key risks include
- Key reliance on the SSM increases the prominence of internal service provision risk
- Business process risk (i.e. non-adherence to key processes, including those relating to market, operational, capital, credit, fraud and financial crime prevention and funding and liquidity)
- Information security and cyber risk including access management, records, data protection and cyber
- IT Systems risk
- Reliance on the SSM to operate key controls designed to detect and prevent fraud and financial crime
- Operational Risk around business resilience, change activity and sourcing

Key mitigating actions
The Group has arrangements in place to assess, monitor and take action on risks arising from the SSM which includes:

- Service performance and reporting to ensure that management information is provided to the Group's executive to monitor and respond to the effectiveness of the service provision
- Service agreements in the form of a legally binding Intra-Group Agreement (IGA) is in place to ensure required standard for services
- Service governance arrangements to ensure that the Group can manage, monitor and escalate service risks to relevant Boards
- Service audit rights are incorporated within the IGA, allowing the Group to audit the services provided by Lloyds Banking Group

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

Key mitigating actions
- Designing resilience into the Group's operations to enable it to be able to withstand and recover from unexpected events
- Identification of critical business processes and investing in technology to enhance the resilience of systems supporting them, primarily through the LBG technology resilience programme
- Continued investment, through LBG, to improve identification and access management, improving capability to detect and respond to cyber-attacks and improved ability to manage vulnerabilities across the estate
- Setting recovery targets for those processes in line with regulatory guidance
- Ensuring resilience capability for those services
- Testing that capability regularly
- Ensuring that the operational resilience risk profile needs are reassessed and prioritised in line with strategic change
- Setting, monitoring and operating within the Board level risk appetite
- Continued optimisation and investment in people controls and processes, property and sourcing programmes

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 control framework to ensure all colleague related requirements are met.

Key mitigating actions
The Group has sought to implement mitigating actions with respect to people risk; these have been significant areas of focus in light of the increased challenge provided by COVID-19. Key objectives of this effort have included:

- Focusing on leadership and colleague engagement, through delivery of strategies to attract, retain and develop high calibre people together with implementation of rigorous succession planning
- Continued focus on the Group's culture by developing and delivering initiatives that reinforce the appropriate behaviours which generate the best possible long-term outcomes for customers and colleagues
- Managing organisational capability and capacity to ensure that the Group have the right skills and resources to meet our customers' needs and deliver our strategic plan
- Evolving remuneration arrangements effectively to ensure they promote an appropriate culture and colleague behaviours that meet customer needs and regulatory expectations
- Ensuring colleague wellbeing strategies and support are in place to meet colleague needs, and that the skills and capability growth required to build a workforce for the 'Bank of the Future' are achieved
- Ensuring compliance with legal and regulatory requirements related to Senior Manager & Certification Regime (SM&CR), embedding compliant and appropriate colleague behaviours in line with Group policies, values and its people risk priorities
- Key people resources provided under the SSM are managed by a People Services Agreement

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

Key mitigating actions
- A comprehensive capital management framework that includes setting of capital risk appetite and dividend policy
- Close monitoring of capital and leverage ratios to ensure the Bank and Group meet regulatory requirements, remain within Board risk appetite and deploy capital resources efficiently
- Comprehensive stress testing analyses in place to evidence capital adequacy
- Maintaining a recovery plan setting out a range of potential mitigating actions that could be taken in response to a stress

Funding and liquidity risk
The risk that the Group does not have sufficiently stable and diverse sources of funding or financial resources are insufficient to meet commitments as they fall due.

Key mitigating actions
- Ensuring that the Group's liquidity risk management framework is adequate with regard to the internal risk appetite, strategy and regulatory requirements. Liquidity policies and procedures are subject to independent internal oversight by the Risk team
- Holding a liquidity buffer to cover potential cash and collateral net outflows calibrated to support strategic and operational needs as well as regulatory requirements
- Undertaking daily monitoring against a number of market and entity specific early warning indicators complemented with stress testing analysis
- Maintaining a contingency funding plan detailing actions and strategies available in stressed conditions
- Diversified funding sources including the Lloyds Bank Corporate Markets plc Euro Medium Term Notes programme

Governance risk
The risk that our organisational infrastructure fails to provide robust oversight of decision making and the control mechanisms to ensure strategies and management instructions are implemented effectively. Against a background of increased regulatory focus on governance and risk management, the most significant challenges arise from the continuing evolution of the SM&CR, including incorporating senior manager function allocation for financial risks arising from climate change.

Key mitigating actions
The Group's Risk Management Framework (RMF) establishes robust arrangements for risk governance, in particular by:

- Defining individual and collective accountabilities for risk management, risk oversight and risk assurance through a three lines of defence model which supports the discharge of responsibilities to customers, shareholders and regulators
- Ongoing monitoring of governance arrangements and key activities to ensure appropriateness, and compliance against regulatory requirements which includes, but is not limited to, the corporate governance framework (the Board, its committees and the executive committees), shared service and Credit Governance
- Regular monitoring of the governance risk profile and performance, and reporting through the consolidated risk report to the Group's Risk Committee, Board Risk Committee and the Board
- Supporting a consistent approach to LBG wide behaviour and risk decision-making through the adoption of the LBG policy framework which helps everyone understand their responsibilities by clearly articulating and communicating rules, standards, boundaries and risk appetite measures which can be controlled, enforced and monitored
- Effective implementation of the RMF mutually reinforces and is reinforced by LBG and the Group's risk culture, which is embedded in its approach to recruitment, selection, training, performance management and reward

Market risk
The risk that our capital or earnings profile is affected by adverse market rates, in particular changes and volatility in interest and foreign exchange rates, inflation rates, commodity prices and credit spreads through activity in the banking and markets businesses.

Key mitigating actions
- Setting an appropriate market risk policy in line with risk appetite, operating within its parameters and the supplementary procedures that underpin it
- Undertaking regular monitoring of market risk positions versus limits and triggers to ensure they remain within limits which are calibrated in line with risk appetite
- Mitigating actions vary depending on exposure but, in general, seek to reduce risk in a cost effective manner including the externalisation to financial markets where market liquidity allows
- Structural hedge programmes implemented to manage liability margins and margin compression

Model risk
The risk of financial loss, regulatory censure, reputational damage or customer detriment from deficiencies in developing, applying and operating models and rating systems.

Key mitigating actions
A comprehensive model risk management framework established by and with continued oversight from the second line of defence, provides the foundation for managing and mitigating model risk within the Group including:

- Defined roles and responsibilities, with clear ownership and accountability
- Principles regarding the requirements of data integrity, development, validation, implementation and ongoing maintenance
- Regular model monitoring
- Independent review of models
- Periodic validation and re-approval of models

Climate risk
Climate risk is defined as the risk that the Group experiences losses and /or reputational damage as a result of climate change, either directly or through its customers. These losses may be realised from physical events, the required adaptation in transitioning to a lower carbon economy, or as a consequence of the responses to managing these changes.

Key risks include:
- Physical risks – changes in climate or weather patterns which are acute, event driven (e.g. flood), or chronic, longer term shifts (e.g. rising sea levels)
- Transition risks – associated with the move towards a lower carbon economy, e.g. changes to policy, legislation and regulation, technology and changes to customer preferences
- Climate risk manifests through, and has potential to impact, the Group's existing primary financial and non-financial risks. For example, physical and transition risk, the impairment of asset values, may impact the creditworthiness of our clients, and result in currently profitable business deteriorating over the term of agreed facilities. The focus on these risks by key stakeholders including businesses, clients and investors, governments and regulators is aligned to the evolving societal, regulatory and political landscape. An analysis has been undertaken by our parent company of how the primary risks across LBG are impacted by climate change. For further information, see the 2020 Lloyds Banking Group ESG Report
- There also remains a risk that campaign groups or other bodies could seek to take legal action (including indirect action) against the Group, Lloyds Banking Group and/or the financial services industry for investing in or lending to organisations that they deem to be responsible for, or contributing to, climate change.

Key mitigating actions

- The Group applies the approach agreed with LBG, our parent company and service provider, which has taken a strategic approach to align with the UK Government's Clean Growth Strategy and has committed to adopting the approach set out by the Financial Stability Board's Task Force on Climate-related Financial Disclosures (TCFD) by 2022
- The Group applies the 12 external sector statements defined by LBG that help articulate appropriate areas of environment, our approach to the risk assessment of our customers; also in 2020, the Group approved a climate related risk appetite. These statements continue to be refined and enhanced
- The Group is integrating risk management of financial risks posed by climate change through our existing enterprise risk management framework, including our policies, risk appetite, controls and models
- As part of LBG's credit risk policy, mandatory requirements to consider environmental risks have been introduced in key risk management activities. In Commercial Banking Division, relationship managers and credit risk officers must ensure that climate risk is considered for all new and renewal facilities
- The Group continues to identify new opportunities to support customers and clients and to finance the UK's transition to a lower carbon economy

Data risk

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

Key mitigating actions

- Introduction of advanced data management practices to deliver compliance with BCBS 239, based on standards consistently applied by the Group and (where appropriate) LBG as a service provider, a data first culture supported by enhancements to enterprise data platforms and the simplification of IT architecture
- Ensuring that risks are identified, measured, managed, monitored and reported using the risk and control self-assessment process
- Employing the infrastructure delivered via the general data protection programme
- Developing capability by investing in professional training for data privacy managers
- Enhancing assurance over third party suppliers
- Improving controls and processes for data retention and destruction

Change / execution risk

The risk that, in delivering its 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 risk appetite.

Key mitigating actions

- Setting (and operating within) the Board level risk appetite for change and execution risk. The Group monitors metrics provided by LBG as a service provider at sub-board level.
- Ensuring compliance with the change policy and associated policies and procedures, which set out the principles and key controls that apply across the business and are aligned to the Group's risk appetite
- Assessment by the business of the potential impacts of undertaking any change activity on its ability to execute effectively, and the potential consequences for the existing risk profiles
- Implementation of effective governance and control frameworks to ensure the adequacy of controls to manage the change activity and act to mitigate the change/execution risks identified
- Escalation of events related to change activities to ensure that they are managed appropriately in line with risk framework guidance

Strategic risk

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.

Key mitigating actions

- Continued digitisation of customer journeys, thereby enabling the delivery of market leading customer experiences that are seamless, accessible and personal
- Robust operating and contingency planning to ensure potential impacts of strategic initiatives and external drivers are mitigated
- Continued focus on increasing the efficiency of the business' operations to ensure investment capacity, responsiveness and effectiveness to respond to external trends

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Financial risk management objectives and policies

Information regarding the financial risk management objectives and policies of the Group, in relation to the use of financial instruments, is given in note 34 to the accounts. The Group's approach to risk management including risk policies, risk appetite, measurement bases and sensitivities, in particular for credit risk, market risk and liquidity risk, is aligned to those of Lloyds Banking Group plc, the Bank's ultimate parent. Further information can be found in the Lloyds Banking Group plc annual report.

The Group maintains risk management systems and internal controls relating to the financial reporting processes designed to:

- ensure that accounting policies are appropriately and consistently applied
- enable the calculation, preparation and reporting of financial outcomes in line with applicable standards
- ensure that disclosures are made on a timely basis in accordance with statutory and regulatory requirements

The 2020 Strategic report has been approved by the Board.

On behalf of the Board

Eduardo J Stock da Cunha
Director
Lloyds Bank Corporate Markets plc
11 March 2021

Directors' report

The directors present their annual report and audited consolidated financial statements for the year ended 31 December 2020.

Information included in the Strategic report incorporated by reference
The following additional information forms part of the Directors' report, and is incorporated by reference.

Content	Pages
Engagement with colleagues	page 5
Engagement with customers, suppliers and others	pages 5 to 7
Principal risks and uncertainties	pages 7 to 11

Results
The consolidated income statement on page 26 shows a statutory profit before tax from continuing operations for the year ended 31 December 2020 of £45 million (2019: £368 million).

Dividends
During the year the Bank paid an interim dividend of £700 million, which was paid in April 2020 (2019: £nil). The directors have not recommended a final dividend for the year ended 31 December 2020. In March 2021, the directors approved the payment of an interim dividend of £200 million, which will be paid by the end of April 2021.

Post balance sheet events
Details of events since the balance sheet date are set out in note 37.

Going concern
The going concern of the Bank and the Group is dependent upon successfully maintaining adequate levels of capital and funding. In order to satisfy themselves that the Bank and the Group have adequate resources to continue to operate for the foreseeable future, the directors have considered the implications of the COVID-19 pandemic and EU exit upon the Bank and Group's performance and projected funding and capital positions and also taken account of the impact of further stress scenarios as well as a number of other key dependencies which are set out in the risk management section under principal risks and uncertainties and capital position set out in the Strategic report on pages 2 to 11. The directors conclude that the Bank and the Group have adequate resources to continue in operational existence for a period of at least 12 months from the date of the approval of the financial statements and therefore it is appropriate to continue to adopt the going concern basis in preparing the accounts.

Corporate governance report
Approach to corporate governance
In accordance with the "Large and Medium-sized Companies and Group (Accounts and Reports) Regulations 2008 (as amended by the Companies (Miscellaneous Reporting) Regulations 2018)" (the Regulations), for the year ended 31 December 2020, the Bank and Group has in its corporate governance arrangements applied the Wates Corporate Governance Principles for Large Private Companies (the Principles). The following section explains the Bank's approach to corporate governance, and its application of the Principles.

Fundamental to the Bank and Group's strategy are high standards of corporate governance. A Corporate Governance Framework is in place for the Bank, which sets the approach and applicable standards in respect of the Bank's corporate governance arrangements whilst addressing the matters set out in the Principles.

This includes the matters reserved to the Board, and the matters the Board has chosen to delegate to management, including decision making on operational matters such as those relating to credit, liquidity and the day-to-day management of risk, and the governance requirements of the operation of the Bank as an entity outside of LBG's Ring Fenced Bank. Governance arrangements, including the Corporate Governance Framework, are reviewed at least annually to ensure they remain fit for purpose. The Corporate Governance Framework of the Bank further addresses the requirements of the Principles as follows.

Principle One – purpose and leadership
The Board is collectively responsible for the long-term success of the Bank. It achieves this by agreeing the Bank's strategy, within the wider strategy of LBG, and overseeing delivery against it. The Bank's strategy is discussed further in the Strategic report on pages 2 to 11. The Board also assumes responsibilities for setting the culture, values and wider standards of the Bank, within the equivalent standards set by LBG.

The COVID-19 pandemic has had a profound effect on the way we live. The Board has monitored the impact of the pandemic on the Group's business and its stakeholders and the Group's response as the situation evolved, seeking to ensure that the risks posed by the pandemic are mitigated. All Board meetings have been held virtually since the March 2020 Board meeting with Board and Board Committee agendas flexed to consider COVID-related matters. The Board received frequent COVID-19 updates from management (both formally and informally) as events unfolded covering matters such as the impact on customers, colleagues, suppliers and other stakeholders and on funding and liquidity.

Consideration of the needs of all stakeholders is fundamental to the way the Bank operates, as is maintaining the highest standards of business conduct, which along with ensuring delivery for customers is a vital part of the corporate culture. The Bank's approach is further influenced by the need to build a culture in which everyone feels included, empowered and inspired to do the right thing for customers. To this end, the Board plays a lead role in establishing, promoting and monitoring the Bank's corporate culture and values, with the Corporate Governance Framework ensuring such matters receive the level of prominence in Board and Executive decision making which they require. The Board receives regular updates on the Group's culture including progress on the cultural transformation journey which is closely aligned to those of LBG, which are discussed in more detail on page 92 of the LBG Annual Report and Accounts for 2020.

Principle two – Board composition
The Board is chaired by a Non-Executive member of the LBG Board and contains a balance of independent Non-Executive Directors, LBG executives (serving as Non-Executives) and Executive Directors. This composition supports its legal and regulatory requirements for independent decision making within the overall framework of LBG policies and controls. Further details of the directors can be found on page 14.

There were a number of changes to the Board during the year, all of which were overseen by the Nomination and Governance Committee. As disclosed in last year's Annual report, Mark Grant retired as Chief Executive Officer and Executive Director of the Bank on 31 January 2020 and was succeeded by Eduardo J Stock da Cunha on 1 February 2020. Jennifer Tippin resigned as Non-Executive Director on 24 April 2020 and was succeeded by Letitia Smith on 26 October 2020. Eve Henrikson was appointed to the Board as an additional independent Non-Executive Director and member of the Board Risk Committee on 1 September 2020.

The Nomination and Governance Committee led a thorough selection and recruitment process to identify and assess candidates. Eduardo J Stock da Cunha was selected on the basis of his strong banking experience and has brought a wealth of knowledge to the Bank. Following a review of the size, diversity and skills of the Board, the Chairman led the process for the recruitment of an additional independent Non-Executive Director with digital transformation skills.

Eve Henrikson's appointment brings wide experience in digital transformation and has broadened the overall skills mix of the Board. Letitia Smith's risk and compliance experience complements and enhances the skills of the Board.

Christopher Edis will be leaving the Board this year to take up another position within LBG and Letitia Smith announced that she plans to leave LBG in June 2021 and will resign from the Board at that time. The Nomination and Governance Committee is leading the process for refreshing the Board.

The Nomination and Governance Committee continues to keep under review, on an ongoing basis, the structure, size and composition of the Board and its committees, making recommendations to the Board as appropriate. Consideration is given to the need to ensure the appropriate mix of knowledge, skills and experience, and diversity.

The Board has adopted the LBG Board Diversity Policy and LBG Board Diversity Objectives as applicable to the Bank and reflecting the relative size of the Board. The Board has continued its commitment to maintaining at least two female board members so long as the board size is eight directors. With the appointment of Eve Henrikson the Board size has increased to nine directors of which three are female. Further, the Board supports the overall aspirations of the Hampton-Alexander and Parker Review goals reflecting that the Bank is a subsidiary and not a listed entity. The Board will continue to take opportunities to increase ethnic diversity and the number of female board members over time where this is consistent with other skills and diversity requirements and is proportionate to the size of the Board and the Bank.

Reflecting the size and complexity of the business, the Board has established a committee structure comprising a Board Risk Committee, Audit Committee, Remuneration Committee and Nomination and Governance Committee (Committees). The Committees make recommendations to the Board on matters delegated to them, in particular in relation to internal control, risk, financial reporting and remuneration matters. Each Committee has written terms of reference setting out its delegated responsibilities and comprises independent Non-Executive Directors with appropriate skills and experiences and chaired by an experienced Chair. The Committee Chairs report to the Board at each Board meeting.

The Board undertakes an annual review of its effectiveness, which provides an opportunity to consider ways of identifying greater efficiencies, ways to maximise strengths and highlights areas of further development. During the year under review, the Board commissioned an independent external evaluator, Board Level Partners Ltd (BLP), to carry out a detailed evaluation of the effectiveness of the Board, its Committees and the individual directors. The process included confidential, unattributable interviews between BLP and each director, as well as senior Group and LBG executives. BLP observed Board and Committee meetings, and reviewed relevant board papers. The external evaluation included an appraisal of Lord Lupton, as Chairman; this was led separately by the Senior Independent Director.

The external evaluation concluded that the Board oversees the management of the Group effectively and has the appropriate skills and expertise to protect the interests of all stakeholders. Its directors benefit from diverse but complementary skills and experience in financial markets and institutions, technology and consumer-facing businesses in the UK and overseas, and all make valuable contributions to the Board. While the evaluation did not highlight any material weaknesses or concerns, it identified some areas of focus in the future, including the successful implementation of the Board succession programme that is now in train, further development of the Group's long-term strategic plan, and continued fine tuning of the Board papers and processes.

The external Board evaluation also considered the activities of the Audit, the Board Risk, the Nomination and Governance, and Remuneration Committees. It concluded that the Committees were operating effectively, with the right balance of membership, experience and skills.

Principle three – director responsibilities

The Board has established and maintains corporate governance practices that provide clear lines of accountability and responsibility to support effective decision-making through the Corporate Governance Framework. This also helps clarify the relationship between the Bank and its parent company in order to deliver long-term sustainable success. Policies are also in place in relation to potential conflicts of interest which may arise.

The Board is supported by its Committees which make recommendations on matters delegated to them under the Corporate Governance Framework. The management of all Committees is in keeping with the basis on which meetings of the Board are managed, with open debate, and adequate time for members to consider proposals which are put forward. The Chairman of the Board and each Board Committee assumes responsibility with support from the Company Secretary for the provision to each meeting of accurate and timely information.

Principle four – opportunity and risk

The Board oversees the development and implementation of the Bank's strategy, within the context of the wider strategy of LBG. Consideration is given to strategic opportunities, and the Board's annual cycle of meetings includes sessions dedicated to debating strategic priorities, as well as one meeting focused on strategy.

The Board is also responsible for the long term sustainable success of the Bank, ensuring it generates value for its shareholder and delivers a positive contribution to society. The Board agrees the Bank's culture, purpose, values and strategy within those set by LBG, and sets expectations for risk management, financial performance and reporting. The specific aims and objectives of the Board are formalised within the Bank's Corporate Governance Framework, which also sets out the key decisions and matters reserved for the Board's approval.

Strong risk management is central to the Bank's strategy along with a robust risk control framework which acts as the foundation for sustainable business growth. The Board agrees the Bank's risk appetite, within the overarching risk appetite of LBG, and monitors the effectiveness of risk management with the support of the Board Risk Committee. Board level engagement, coupled with the direct involvement of senior management ensures that escalated risk issues are promptly addressed and remediation plans are initiated where required.

The Bank's risk appetite, principles, policies, procedures, controls and reporting are managed in conjunction with those of LBG, and are regularly reviewed to ensure they remain fully in line with regulations, law, corporate governance and industry best practice. The Bank's principal risks are discussed further on pages 7 to 11.

Principle five – remuneration
The Remuneration Committee of the Board is responsible for reviewing and making recommendations to the Board on the remuneration policy for the Bank. This includes reviewing performance and approving remuneration arrangements ranging from the remuneration of directors and members of the Executive to that of all other colleagues where the regulators require the Bank to implement a specific approach to their remuneration, such as Senior Managers and other material risk takers. The activities of the Remuneration Committee extend to matters of remuneration relevant to subsidiaries of the Group, taking into account the principles, policies and governance requirements of LBG and the recommendations of LBG's Group Remuneration Committee.

Principle six – stakeholders
The Bank, as part of LBG, operates under LBG's wider Responsible Business approach, which acknowledges that the Bank has a responsibility to help address the economic, social and environmental challenges which the UK faces, and as part of this understand the needs of the Bank's external stakeholders, including in the development and implementation of strategy. Central to this is LBG's Helping Britain Recover commitments, as part of the Helping Britain Prosper plan, in which the Bank participates, to help the UK, and stakeholders across the jurisdictions in which the Group operates, recover from the impact of coronavirus as overseen by LBG's Responsible Business Committee.

In 2020, the Responsible Business Committee determined that the Bank and LBG continued to demonstrate responsibility as a key priority, including focus on Inclusions & Diversity, keeping customers' data safe, supporting vulnerable customers, responding to climate change, lending responsibly, supporting businesses and working with suppliers. The Committee will seek to ensure that the Helping Britain Recover commitments are fully embedded into business plans and that they remain flexible to respond to the changing needs. The workforce, as a key stakeholder, includes the Bank's permanent employees, contingent workers and third-party suppliers delivering services to customers and supporting key business operations. This also includes LBG colleagues providing services to the Bank under the Shared Service Model. The Board's approach to workforce engagement includes an annual programme of engagement activity and oversight of policies on remuneration structures and practices that take account of the broader operating context, including the pay and conditions of the wider workforce and the Bank's response to matters such as any gender pay gap.

Appointment and retirement of directors

The appointment of directors is governed by the Bank's articles of association and the Companies Act 2006. The Bank's articles of association may only be amended by a special resolution of the shareholders in a general meeting.

Directors
The names of the current directors are shown on page 17. Changes to the composition of the Board since 1 January 2020 up to the date of this report are shown in the table below:

	Joined the Board	Resigned from the Board
Mark A Grant		31 January 2020
Eduardo J Stock da Cunha	1 February 2020	
Jennifer L Tippin		24 April 2020
Eve A Henrikson	1 September 2020	
Letitia M Smith	26 October 2020	

Directors' indemnities and Directors' and Officers' liability insurance
The directors of the Bank, including the former directors, have entered into individual deeds of indemnity with LBG which constitutes 'qualifying third party indemnity provisions' for the purposes of the Companies Act 2006. The deeds were in force during the whole of the financial year or from the date of appointment in respect of the directors who joined the Board during 2020. Directors no longer in office but who served on the Board at any time in the financial year had the benefit of this deed of indemnity during that period of service. The indemnity remains in force for the duration of a director's period of office. The deeds indemnify the directors to the maximum extent permitted by law. In addition, LBG has in place appropriate Directors and Officers Liability Insurance cover which was in place throughout the financial year.

Change of control
The Bank is not party to any significant agreements which take effect, alter or terminate upon a change of control of the Bank following a takeover bid. There are no agreements between the Bank and its directors or employees providing compensation for loss of office or employment that occurs because of a takeover bid.

Directors' interests
The directors do not have any direct interest in the shares of the Bank. Lord Lupton is also a director of LBG. Lord Lupton's interest in shares of LBG is shown in the report and accounts of that company.

Conflicts of interest
The Board has a comprehensive procedure for reviewing and, as permitted by the Companies Act 2006 and the Bank's articles of association, approving actual and potential conflicts of interest. Directors have a continuing duty to notify the Chairman and the Company Secretary as soon as they become aware of actual or potential conflict situations. Changes to the commitments of all directors are reported to the Board and a register of potential conflicts and time commitments is regularly reviewed and authorised by the Board to ensure the authorisation status remains appropriate.

Lord Lupton is a senior advisor to Greenhill Europe, an investment bank focused on providing financial advice on significant mergers, acquisitions, restructurings, financings and capital raising to corporations, partnerships, institutions and governments. The Board has recognised that potential conflicts may arise as a result of this position. The Board has authorised the potential conflicts and requires Lord Lupton to recuse himself from discussions, should the need arise.

Andrew McIntyre is Non-Executive Director, Senior Independent Director and Chair of the Audit and Risk Committee of C. Hoare & Co., a UK regulated private bank. The Board has recognised that potential conflicts may arise in relation to these positions. The Board has authorised the potential conflicts and requires Andrew McIntyre to recuse himself from discussions, should the need arise. Andrew McIntyre was Non-Executive Director, Chair of Audit Committee and Chair of Ethics and Culture Committee of National Bank of Greece S.A until 30 August 2020 and he was a member of the Financial Reporting Review Panel (FRRP), a sub-committee of the Financial Reporting Council (FRC) until 31 December 2020. As a former partner of EY, he continued to have a financial relationship with EY in the form of a fixed annuity until 30 June 2020.

John Cummins is Managing Director of Future Cities and interim acting Director of Regeneration, Legal and General Finance plc, director of Legal and General Finance plc and holds a number of director appointments with Legal and General Capital plc related entities. He is a director and trustee of Centre for Cities, a charitable company limited by guarantee set up as a think tank to improve the performance of UK city economies and conduct research into urban matters. In addition, John Cummins has personal investments in a Fintech company, Shieldpay, a developer and supplier of secure anti-fraud payment systems to banks and other organisations; and Auden Group Limited, a social lending company. The Board has recognised that potential conflicts may arise as a result of these positions. The Board has authorised the potential conflicts and requires John Cummins to recuse himself from discussions, should the need arise.

Christopher Edis is Non-Executive Director and member of the Risk and Assurance Committees of Stonewater Limited, a registered social housing provider, and Non-Executive Director of its subsidiary, Stonewater Funding plc. The Board has recognised that potential conflicts may arise as a result of these positions. The Board has authorised the potential conflicts and requires Christopher Edis to recuse himself from discussions, should the need arise.

The following Non-Executive Directors hold/held executive roles within LBG and whilst these are permitted interests under the Bank's articles of association, for the sake of good order the Board authorised the potential conflicts that may arise as a result of those roles and required the individuals listed below to recuse themselves from discussions, should the need arise. These individuals did not act as representative of the Group's sole shareholder, LBG, in their capacity as Non-Executive Directors of the Bank's Board:

Name	LBG Role
Jennifer Tippin	Group People and Productivity Director for LBG and member of Group Executive Committee (GEC) until April 2020
Carla Antunes da Silva	Group Strategy, Corporate Development and Investor Relations Director for LBG and attendee of GEC
Letitia Smith	Group Director, Conduct, Compliance & Operational Risk and attendee of GEC

Branches, future developments and financial risk management objectives and policies
The Bank and the Group provides a wide range of banking and financial services through branches and offices in the UK, Singapore, the USA, Germany and the Crown Dependencies. Information regarding future developments and financial risk management objectives and policies of the Group in relation to the use of financial instruments that would otherwise be required to be disclosed in the Directors' report, and which is incorporated into this report by reference, can be found in the Strategic report.

Share capital
Information about share capital is shown in note 24. This information is incorporated into this report by reference.

The Bank did not issue share capital and did not repurchase any of its own shares during the year. There are no restrictions on the transfer of shares in the Bank other than set out in the articles of association and certain restrictions which may from time to time be imposed by law and regulations.

The directors manage the business of the Bank under the powers set out in the Companies Act 2006 and the Bank's articles of association; these powers include those in relation to the issue or buy back of the Bank's shares. The Bank is a public company limited by shares.

Information required under DTR 7.2
Certain information is incorporated into this report by reference. Information about internal control and risk management systems relating to the financial reporting process can be found on page 11.

Information about share capital is shown in note 24 on page 66. The Bank is a wholly owned subsidiary of LBG, which holds all of the Bank's issued ordinary share capital.

The directors manage the business of the Bank under the powers set out in the Companies Act 2006 and the Bank's articles of association. These powers include those in relation to the issue or buy back of the Bank's shares.

Research and development activities
During the ordinary course of business the Group develops new products and services within its business units.

Emissions
Lloyds Banking Group (LBG), for which the Bank and Group are a part, has voluntarily reported greenhouse gas emissions (scope 1, 2 and 3) and environmental performance since 2009, and since 2013 this has been reported in line with the requirements of the Companies Act 2006 and its applicable regulations. The full details of LBG's greenhouse gas emissions, intensity ratio, carbon emissions, global energy use and energy efficiency can be found in the LBG Annual Report and Accounts for 2020.

Employees
The Group employed an average of 1,132 colleagues (note 7) during 2020 (2019: 1,196). This represents colleagues based in Singapore, the USA, Germany and the Crown Dependencies. Organisational changes in the Crown Dependencies and North America businesses account for the movement in the average number of colleagues year on year. Information concerning the employees of Lloyds Banking Group is available in the LBG's 2020 Annual Report and Accounts.

As part of LBG, the Bank is committed to creating an inclusive and diverse organisation where colleagues with disabilities or long-term health conditions feel valued and supported to reach their full potential. The Bank supports colleagues who have disclosed a disability in a range of ways. The Bank ensures full and fair consideration to applications from people with disabilities, and offers bespoke training, career development, promotions and adjustments for colleagues and applicants with disabilities, including those who became disabled while employed. This has been recognised through LBG holding the Business Disability Forum Gold Standard accreditation and retaining Disability Confident Leader status from the Department for Work and Pensions, which recognise the inclusive culture of LBG and the support provided to our colleagues identified as having a disability.

Significant contracts

The Group has a shared service contract with Lloyds Bank plc for the provision of services (note 7).

Details of related party transactions are set out in note 29.

Statement of directors' responsibilities in respect of the financial statements

The directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulation.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have prepared the Group and Bank financial statements in accordance with international accounting standards in conformity with the requirements of the Companies Act 2006. Additionally, the Financial Conduct Authority's Disclosure Guidance and Transparency Rules require the directors to prepare the group financial statements in accordance with international financial reporting standards adopted pursuant to Regulation (EC) No 1606/2002 as it applies in the European Union.

Under company law, directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and the Bank and of the profit or loss of the group for that period. In preparing the financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- state whether for the Group and the Bank, International accounting standards in conformity with the requirements of the Companies Act 2006 and, for the Group, international financial reporting standards adopted pursuant to Regulation (EC) No 1606/2002 as it applies in the European Union have been followed, subject to any material departures disclosed and explained in the financial statements;
- make judgements and accounting estimates that are reasonable and prudent; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group and the Bank will continue in business.

The directors are also responsible for safeguarding the assets of the Group and the Bank and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Group's and the Bank's transactions and disclose with reasonable accuracy at any time the financial position of the Group and the Bank and enable them to ensure that the financial statements comply with the Companies Act 2006 and, as regards the Group financial statements, international financial reporting standards adopted pursuant to Regulation (EC) No 1606/2002 as it applies in the European Union.

The directors are responsible for the maintenance and integrity of the Bank's financial statements published on the ultimate parent company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Directors' confirmations

Each of the directors, whose names and functions are listed in Directors' report confirm that, to the best of their knowledge:

- the Group and the Bank financial statements, which have been prepared in accordance with international accounting standards in conformity with the requirements of the Companies Act 2006. Additionally, the Financial Conduct Authority's Disclosure Guidance and Transparency Rules require the directors to prepare the Group financial statements in accordance with international financial reporting standards adopted pursuant to Regulation (EC) No 1606/2002 as it applies in the European Union, give a true and fair view of the assets, liabilities, financial position and profit of the Group and profit of the Bank; and
- the Strategic report includes a fair review of the development and performance of the business and the position of the Group and the Bank, together with a description of the principal risks and uncertainties that it faces.

In the case of each director in office at the date the directors' report is approved:

- so far as the director is aware, there is no relevant audit information of which the Group's and Bank's auditors are unaware; and
- they have taken all the steps that they ought to have taken as a director in order to make themselves aware of any relevant audit information and to establish that the Group's and Bank's auditors are aware of that information.

Independent auditors and audit information

Each person who is a director at the date of approval of this report confirms that, so far as the director is aware, there is no relevant audit information which the Group's and Bank's auditors are unaware and each director has taken all the steps that he or she ought to have taken as a director to make himself or herself aware of any relevant audit information and to establish that the Group's and Bank's auditors are aware of that information. This confirmation is given and should be interpreted in accordance with the provisions of the Companies Act 2006.

Resolutions concerning the appointment of Deloitte LLP as auditor will be proposed at the Bank's annual general meeting.

The Directors consider that the annual report and accounts as a whole, is fair, balanced and understandable and provides the information necessary for the shareholder to assess the Bank and the Group's position, performance, business model and strategy. The Directors have also separately reviewed and approved the strategic report.

The financial statements were approved by the Board and signed on its behalf by:

Christopher J K Edis
Director
11 March 2021

Lloyds Bank Corporate Markets plc
Registered in England & Wales
Company Number 10399850

Directors

John J Cummins *Non-Executive Director*

Eduardo J Stock da Cunha *Executive Director and Chief Executive Officer*

Christopher J K Edis *Executive Director and Chief Financial Officer*

Eve A Henrikson *Non-Executive Director*

Lord Lupton CBE *Non-Executive Director and Chairman*

Andrew J McIntyre *Non-Executive Director*

John S W Owen *Non-Executive Director and Senior Independent Director*

Carla A S Antunes da Silva *Non-Executive Director*

Letitia M Smith *Non-Executive Director*

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 Lloyds Bank Corporate Markets 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', 'achieves', 'anticipates', 'estimates', 'expects', 'targets', 'should', 'intends', 'aims', 'projects', 'plans', 'potential', 'will', 'would', 'could', 'considered', 'likely', 'may', 'seek', '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, statements or guidance relating 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 Lloyds Banking Group plc; 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; the Lloyds Banking Group's ESG targets and/or commitments; changing customer behaviour including consumer spending, saving and borrowing habits; changes to borrower or counterparty credit quality impacting the recoverability and value of balance sheet assets; concentration of financial exposure; management and monitoring of conduct risk; exposure to counterparty risk (including but not limited to third parties conducting illegal activities without the Group's knowledge); 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), the EU-UK Trade and Cooperation Agreement, 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 and any further possible referendum on Scottish independence; 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 COVID-19 pandemic) and other disasters, adverse weather and similar contingencies outside the control of the Group or Lloyds Banking Group plc; inadequate or failed internal or external processes or systems; acts of war, other acts of hostility, terrorist acts and responses to those acts, or other such events; geopolitical unpredictability; risks relating to climate change; changes in laws, regulations, practices and accounting standards or taxation, including as a result of the UK's exit from the EU; changes to regulatory capital or liquidity requirements (including regulatory measures to restrict distributions to address potential capital and liquidity stress) and similar contingencies outside the control of the Group or Lloyds Banking Group plc; 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 laws, 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 Lloyds Banking Group plc'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.

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.

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF LLOYDS BANK CORPORATE MARKETS PLC

Report on the audit of the financial statements

Opinion

In our opinion, Lloyds Bank Corporate Markets plc's group ("the Group") financial statements and Bank financial statements (the "financial statements"):

– give a true and fair view of the state of the Group's and of the Bank's affairs as at 31 December 2020 and of the Group's profit and the Group's and the Bank's cash flows for the year then ended;
– have been properly prepared in accordance with International accounting standards in conformity with the requirements of the Companies Act 2006; and
– have been prepared in accordance with the requirements of the Companies Act 2006.

We have audited the financial statements, included within the Report and Accounts (the "Annual Report"), which comprise: the Group and Bank balance sheets as at 31 December 2020; the Group consolidated income statement and the Group and Bank statements of comprehensive income, the Group and Bank cash flow statements, and the Group and Bank statements of changes in equity for the year then ended; and the notes to the financial statements, which include a description of the significant accounting policies.

Our opinion is consistent with our reporting to the Audit Committee.

Separate opinion in relation to international financial reporting standards adopted pursuant to Regulation (EC) No 1606/2002 as it applies in the European Union

As explained in note 1 to the financial statements, the Group, in addition to applying international accounting standards in conformity with the requirements of the Companies Act 2006, has also applied international financial reporting standards adopted pursuant to Regulation (EC) No 1606/2002 as it applies in the European Union.

In our opinion, the Group financial statements have been properly prepared in accordance with international financial reporting standards adopted pursuant to Regulation (EC) No 1606/2002 as it applies in the European Union.

Separate opinion in relation to IFRSs as issued by the IASB

As explained in note 1 to the financial statements, the Group, in addition to applying international accounting standards in conformity with the requirements of Companies Act 2006, has also applied international financial reporting standards (IFRSs) as issued by the International Accounting Standards Board (IASB).

In our opinion, the financial statements have been properly prepared in accordance with IFRSs as issued by the IASB.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities under ISAs (UK) are further described in the Auditors' responsibilities for the audit of the financial statements section of our report. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We remained independent of the Group in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, which includes the FRC's Ethical Standard, as applicable to public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

To the best of our knowledge and belief, we declare that non-audit services prohibited by the FRC's Ethical Standard were not provided to the group headed by Lloyds Banking Group plc, of which the Bank is a member.

Other than those disclosed in note 7 to the financial statements, we have provided no non-audit services to the Group in the period under audit.

Our audit approach

Context

The Group operates across a number of territories including the UK, the Crown Dependencies, Germany, Singapore and the USA. The Bank operates across a number of territories including the UK and through its branches in the Crown Dependencies, Singapore and the USA. For the purposes of our audit of the Bank, we considered the branches to be components of the Bank. The Group and Bank receive considerable operational support through shared service arrangements with other parts of the Lloyds Banking Group.

Overview

Audit scope

– The scope of our audit and the nature, timing and extent of audit procedures performed were determined by our risk assessment, the financial significance of components and other qualitative factors (including history of misstatement through fraud or error).
– We performed full scope audit procedures over components considered financially significant in the context of the Group and the Bank. These comprised components in the UK, the Crown Dependencies, the USA and Singapore. Any component which was not already included as a full scope audit component but was identified as being individually financially significant in respect of one or more account balances was subject to specific audit procedures over those account balances. We performed other procedures including testing entity level controls, information technology general controls and analytical review procedures to mitigate the risk of material misstatement in the residual components.

Key audit matters

– Valuation of complex financial instruments (Group and Bank)
– Determination of expected credit loss allowances (Group and Bank)
– Access to IT systems (Group and Bank)
– Hedge accounting (Group and Bank)
– Potential impact of COVID-19 (Group and Bank)

Materiality

– Overall Group materiality: £34,000,000 (2019: £37,800,000) based on 1% of Adjusted Tier 1 Capital Resources.
– Overall Bank materiality: £34,000,000 (2019: £37,800,000) based on 1% of Adjusted Tier 1 Capital Resources.
– Performance materiality: £25,500,000 (Group) and £25,500,000 (Bank).

The scope of our audit

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the financial statements.

Capability of the audit in detecting irregularities, including fraud
Irregularities, including fraud, are instances of non-compliance with laws and regulations. We design procedures in line with our responsibilities, outlined in the Auditors' responsibilities for the audit of the financial statements section, to detect material misstatements in respect of irregularities, including fraud. The extent to which our procedures are capable of detecting irregularities, including fraud, is detailed below.

Based on our understanding of the Group and industry, we identified that the principal risks of non-compliance with laws and regulations related to breaches of the rules of the Financial Conduct Authority ("FCA"), Prudential Regulatory Authority ("PRA"), UK tax legislation and equivalent laws and regulations applicable to significant components of the Group and Bank, and we considered the extent to which non-compliance might have a material effect on the financial statements. We also considered those laws and regulations that have a direct impact on the preparation of the financial statements such as the Companies Act 2006. We evaluated management's incentives and opportunities for fraudulent manipulation of the financial statements (including the risk of override of controls), and determined that the principal risks were related to posting manual journal entries to manipulate financial performance, management bias through judgements and assumptions in significant accounting estimates and significant one-off or unusual transactions. The group engagement team shared this risk assessment with the component auditors so that they could include appropriate audit procedures in response to such risks in their work. Audit procedures performed by the group engagement team and/or component auditors included:

- Performing enquiries with management and those charged with governance regarding any known or suspected instances of non-compliance with laws and regulation and fraud.
- Evaluation and testing of the operating effectiveness of management's entity level controls designed to prevent and detect irregularities, in particular their code of conduct and whistleblowing helpline.
- Assessment of matters reported on the Group's whistleblowing helpline and the results of management's investigation of such matters.
- Performing testing over period end adjustments.
- Incorporating unpredictability into the nature, timing and/or extent of our testing.
- Reviewing key correspondence with regulatory authorities, including the PRA and the FCA.
- Challenging assumptions and judgements made by management in their significant accounting estimates, in particular in relation to the determination of expected credit loss allowances and the valuation of complex financial instruments (see related key audit matters below).
- Identifying and testing journal entries, in particular any manual journal entries posted by infrequent or unexpected users and those posted late in the financial reporting process with a favourable impact on financial performance.

There are inherent limitations in the audit procedures described above. We are less likely to become aware of instances of non-compliance with laws and regulations that are not closely related to events and transactions reflected in the financial statements. Also, the risk of not detecting a material misstatement due to fraud is higher than the risk of not detecting one resulting from error, as fraud may involve deliberate concealment by, for example, forgery or intentional misrepresentations, or through collusion.

Key audit matters
Key audit matters are those matters that, in the auditors' professional judgement, were of most significance in the audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) identified by the auditors, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team. These matters, and any comments we make on the results of our procedures thereon, were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

This is not a complete list of all risks identified by our audit.

The key audit matters below are consistent with last year.

Key audit matter	How our audit addressed the key audit matter
Valuation of complex financial instruments **Group and Bank** Refer to page 33 (Note 2: Accounting policies), page 38 (Note 3: Critical accounting judgements and estimates) and page 71 (Note 31). The Group and Bank hold a portfolio of fair value assets and liabilities classified as level 3 instruments as their valuations are subjective and determined using bespoke models which rely on a range of unobservable inputs.	***Valuation of complex financial instruments*** **Group and Bank** We understood management's process and evaluated and tested the key controls around the financial instruments' valuation processes including the independent price verification and valuation governance controls. We found these key controls were designed, implemented and operated effectively, and therefore determined that we could place reliance on them for the purposes of our audit. With the support of our valuation experts, we performed the following further testing: – Tested the completeness of the level 3 population through review and testing of the methodology used by management to identify level 3 instruments; – Evaluated the appropriateness of management's valuation methodologies and tested their application; – Evaluated and tested key inputs and assumptions, with reference to matters including historic performance, market information and perspectives, servicer and trustee reports and investment prospectuses; and – Assessed the reasonableness of the valuations and performed sensitivity analyses over them. Based on the evidence obtained, we determined the methodologies, inputs and assumptions to be appropriate.

Determination of expected credit loss allowances
Group and Bank
Refer to page 35 (Note 2: Accounting policies), page 38 (Note 3: Critical accounting judgements and estimates) and page 45 (Note 8 Impairment (charge)/credit).

The determination of the allowance for expected credit loss ("ECL") is a judgemental area. A number of judgements and assumptions are outlined in the financial statements, including the application of forward looking information and overlays to the impairment model.

Application of forward looking information
Management's economics team develops future economic scenarios for each territory, as relevant.

The base case economic scenario is determined through the application of judgement. There is a high level of estimation uncertainty in the base case due to the inherent complexity in forecasting future economic outcomes. The impact of COVID-19 on the economy has significantly increased the level of uncertainty in the base case forecasts.

The outer scenarios are generated and selected through the use of a statistical model that is conditioned on the base case. The four economic scenarios represent distinct parts of the loss distribution which is developed based on historical experience. The scenarios, together with their weightings, are incorporated into the calculation of the allowance for ECL.

ECLs on Stage 1 and 2 positions
The allowance for ECL relating to 'good book' or non-credit impaired loans and advances (referred to as being in Stages 1 and 2) is determined on a collective basis, with the use of impairment models.

These models use a number of key assumptions including probability of default, loss given default and valuation of recoveries. Management also apply overlays where they believe the model calculated assumptions and allowances are not appropriate, either due to emerging trends or model limitations. An example of this is overlay's to the impairment model in respect of the PD limitation for Financial Institutions identified by management. There has been an increase in the use of expert judgement and overlays in the current year which reflects the fact that the historical data used in the development of the models does not capture all the conditions of the pandemic experienced during 2020.

Our work therefore focused on the appropriateness of modelling methodologies adopted and significant judgements made in determining overlays as well as the measurement of those overlays.

ECLs on Stage 3 positions
The allowance for ECL relating to credit impaired loans and advances (referred to herein also as being in Stage 3) is estimated on an individual basis. Judgement is required to determine when a loan is considered to be credit impaired, and then to estimate the expected future cash flows related to that loan under multiple weighted scenario outcomes.

Determination of expected credit loss allowances
Group and Bank
Application of forward looking information
We understood management's process and tested key controls relating to the generation, selection and weighting of economic scenarios. We engaged our internal economic experts and risk modelling specialists to assist us as we evaluated:

- The appropriateness of the base case economic scenario, focusing on the key UK economic assumptions (gross domestic product, UK Bank Rate, unemployment rate and commercial real estate price growth) and US economic assumptions (GDP and unemployment);
- The approach to the generation and selection of economic scenarios representing the upside, downside and severe downside;
- The Group's internally developed statistical model, including changes implemented during the year and the Group's model validation process; and
- The review, challenge and approval of the economic scenarios within the Group's governance processes.

We found the key controls were designed, implemented and operated effectively, and therefore determined that we could place reliance on these key controls for the purposes of our audit.

We critically assessed the key assumptions adopted in the base case economic scenario by comparing them to our independent view of the economic outlook and market consensus data. We investigated key economic variables outside of our thresholds. We also assessed the risk of bias in the forecasts, as well as the existence of contrary evidence.

We independently evaluated management's model by assessing the appropriateness of the code and independently applying it. We also assessed the appropriateness of the weightings adopted.

Based on the evidence obtained, we consider that the economic scenarios adopted reflect an unbiased, probability weighted view, that appropriately captures the impact of non-linearity.

ECLs on Stage 1 and 2 positions
We understood management's process and evaluated and tested key controls around the determination of ECL allowances, including controls relating to:

- The identification and assessment of the completeness and accuracy of critical data applied in the ECL calculation;
- The accuracy and timeliness of updates to credit risk ratings, which are applied in assessing whether loans have suffered a significant increase in credit risk since initial recognition;
- The governance over the ECL determination, including the validation of the ECL methodology, assumptions and inputs, and the annual model performance validation; and
- The review, challenge and approval processes in place to assess the overall reasonableness of the allowance for ECL together with other available credit risk related information within the Group.

We found these key controls were designed, implemented and operated effectively, and therefore determined that we could place reliance on these key controls for the purposes of our audit.

We performed the following procedures over the Stage 1 and 2 allowance for ECL:

- We critically assessed whether the methodology applied in the calculation is compliant with IFRS 9;
- We tested the formulae applied within the calculation, including the appropriateness, and application of, the quantitative and qualitative criteria used to assess significant increases in credit risk;
- We evaluated the accuracy and timing of the information being used to calculate a borrower's internal credit risk rating;
- We assessed whether the most recent internal credit risk rating assessment was performed closely enough to 31 December 2020 to sufficiently reflect the latest economic environment;
- We tested the completeness and accuracy of key data inputs, sourced from underlying systems that are applied in the calculation;
- We tested the reconciliation of loans and advances between underlying source systems and the allowance models; and
- We critically assessed the impact of identified model limitations and the justification for overlays applied by management.

	ECLs on Stage 3 positions: We understood management's process and evaluated and tested key controls around the determination of ECL allowances, including controls relating to: – The controls in place for the identification of credit impaired loans and subsequent transfer of these cases to the credit loss assessment team; and – The review, challenge and approval processes that are in place to assess the overall reasonableness of the allowance for ECL. We found these key controls were designed, implemented and operated effectively, and therefore determined that we could place reliance on these key controls for the purposes of our audit. We performed the following procedures to test the completeness of credit impaired assets requiring a Stage 3 allowance for ECL: – We critically assessed the criteria for determining whether a credit impairment event had occurred; and – We selected a sample of Stage 1 and 2 performing loans and we independently assessed whether there was evidence of any events of default which might lead to the loan moving into Stage 3, and therefore whether they were appropriately categorised as being performing. Based on the evidence assessed, we found the methodologies, modelled assumptions and data used within the allowance for ECL assessment to be appropriate and in line with the requirements of IFRS 9.
Access to IT systems **Group and Bank** The Group's financial reporting processes are reliant on automated processes, controls and data managed by IT systems. As part of our audit work in prior periods, we identified control matters in relation to the management of IT access to IT platforms and applications in-scope for financial reporting. While there is an ongoing programme of activities to address such control matters across the IT estate, the fact that these were open during the period meant there was a risk that automated functionality, reports or data from the specific systems are not reliable.	***Access to IT systems*** **Group and Bank** We evaluated the design, implementation and operating effectiveness of those automated and IT dependent controls that support the in-scope financial statement line items. We also tested the supporting IT General Computer Controls (ITGCs) that provide assurance over the effective operation of these controls as well as those controls that manage the integrity of relevant data repositories for the full financial reporting period. We tested the design and operating effectiveness of those key controls identified that manage IT access across the in-scope IT platforms and applications. Specifically, we tested foundational controls over: – Approval, recertification and timely removal of access from IT systems; and – The completeness and accuracy of the Access Control Lists for IT platforms and applications that are used in performing controls over user access. Where the testing above identified gaps in the foundational controls, we identified and tested mitigating controls including the following: – The onboarding and management of IT privileged accounts through the privileged access 'break-glass tool' (including static IT privileged accounts); and – The monitoring of security events on IT platforms by the Security Operations Centre. As part of our review, we identified a number of entitlements that had not been recertified on a timely basis during the period. Consequently we performed an assessment of each of the areas within our audit approach where we place reliance on automated functionality and data within IT systems. In each case we identified and tested a combination of mitigating IT and manual controls and performed substantive audit procedures in order to respond to the impact on our overall audit approach and reduce audit risk to an acceptably low level.

Hedge accounting **Group and Bank** Refer to page 34 (Note 2: Accounting policies) and page 50 (Note 12: Derivative financial instruments). The Group and Bank enter into derivative contracts in order to manage and economically hedge risks such as interest and foreign exchange rate risk. These arrangements create accounting mismatches which are addressed through designating instruments into fair value or cash flow hedge accounting relationships. Whilst there has been some automation of hedging accounting processes in the period, the application of hedge accounting in the year still relied upon a significant degree of manual processing, was largely manual in nature, which increases the risk of errors and hence the risk that financial reporting is not compliant with IFRS requirements.	***Hedge accounting*** **Group and Bank** We understood and tested key controls over the designation and ongoing management of hedge accounting relationships, including those over hedge documentation, hedge effectiveness testing and the recording of hedge accounting adjustments. We found these key controls were designed, implemented and operated effectively, and therefore determined that we could place reliance on these key controls for the purposes of our audit. Our other testing included the following: – Examining selected hedge documentation to assess whether it complied with the requirements of IFRS; – Testing the key year-end reconciliations between underlying source systems and the models used to manage hedging relationships; – Independently assessing whether management have captured and monitored all material sources of ineffectiveness, including any impact of reference interest rate reform; – Re-performing a sample of hedge effectiveness calculations in line with the requirements of IFRS; – Independently revaluing a sample of proxy derivatives which represent the designated hedged risk on the hedged items; – Independently revaluing a sample of hedging instruments used in hedging relationships; – Re-performing a sample of capacity assessment calculations; and – Testing a sample of manual adjustments posted to record ineffectiveness. Based on the evidence obtained, we determined the application of hedge accounting to be appropriate.
Potential impact of COVID-19 **Group and Bank** There is a global pandemic of COVID-19 which has taken hold in the UK and other territories in which the Group and Bank operate. This has been disruptive to financial markets and normal patterns of human behaviour. This translates into an adverse impact on the global economy. In response, the UK and other governments, and the respective central banks or similar authorities, have announced measures designed to ameliorate resulting adverse impacts on the economy. As at 31 December 2020, some vaccines have received regulatory approval and have begun to be administered to the population. These, and the development of other vaccines, create an expectation that the restrictions will be eased in the foreseeable future. However, there remains significant uncertainty over the future mutation and spread of the disease, the extent and impact of government measures and economic outlook. Management has considered the impact of COVID-19 when preparing the financial statements and, where relevant to a key audit matter or other area of this audit report, we have included our considerations therein.	***Potential impact of COVID-19*** **Group and Bank** Our planning and execution of our audit has given specific consideration to the impact of COVID-19 on the Group and Bank. In assessing management's consideration of the impact of COVID-19 on the financial statements, we have undertaken the following procedures: – In areas where management is required to estimate future financial performance of the Group and Bank when preparing the financial statements, we have challenged the forecasts and the extent to which they have been impacted by COVID-19; – Performed inquiries with management and the Group's regulators, including the Prudential Regulation Authority and the Financial Conduct Authority; – Assessed the impact of COVID-19 on estimates and the assumptions that underpin them, for example related to expected credit losses as detailed above; – Reviewed management's going concern assessment, which considered the potential impact of COVID-19 on future profitability; – Considered the impact of COVID-19 on the Group's internal control environment through our audit testing and inquiries of management; and – Evaluated the adequacy of the disclosures made in the financial statements with respect to the impact of COVID-19. As a result of these procedures, we concluded that the impact of COVID-19 has been appropriately evaluated and reflected in the preparation of the financial statements.

How we tailored the audit scope

We tailored the scope of our audits to ensure that we performed enough work to be able to give an opinion on the financial statements as a whole, taking into account the structure of the Group and the Bank, the accounting processes and controls, and the industry in which they operate.

The Group and Bank operate in a number of territories as described in the Context. The Group and Bank receive considerable operational support through shared service arrangements with other parts of the Lloyds Banking Group.

In establishing the overall approach to our audit of the financial statements, we determined the type of work that is required to be performed over the components by us, as the group engagement team, or auditors within PwC UK and from other PwC network firms operating under our instruction ('component auditors').

Where the work was performed by component auditors, we determined the level of involvement we needed to have in their audit work to be able to conclude whether sufficient appropriate audit evidence has been obtained as a basis for our opinion on the consolidated financial statements as a whole. This included regular communication with the component auditors throughout the audit, the issuance of instructions, a review of the results of their work and attendance at formal clearance meetings.

Any components which were considered individually financially significant in the context of the Group’s or Bank’s consolidated financial statements (defined as components that represent more than or equal to 10% of the total assets of the consolidated Group) were considered full scope components.

We considered the individual financial significance of other components in relation to primary statement account balances. We considered the presence of any significant audit risks and other qualitative factors (including history of misstatements through fraud or error). Any component which was not already included as a full scope audit component but was identified as being individually financially significant in respect of one or more account balances was subject to specific audit procedures over those account balances.

All remaining components were subject to procedures which mitigated the risk of material misstatement including testing of entity level controls, information technology general controls and Group, Bank and component level analytical review procedures.

Certain account balances were audited centrally by the group engagement team. In addition, we performed testing over certain activities and controls operating in the shared service centres across the Lloyds Banking Group.

Components within the scope of our Group audit contributed 99% of Group total assets and 92% of Group total income.

Materiality
The scope of our audit was influenced by our application of materiality. We set certain quantitative thresholds for materiality. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures on the individual financial statement line items and disclosures and in evaluating the effect of misstatements, both individually and in aggregate on the financial statements as a whole.

Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

	Financial statements - Group	Financial statements - Bank
Overall materiality	£34,000,000 (2019: £37,800,000).	£34,000,000 (2019: £37,800,000).
How we determined it	1% of Adjusted Tier 1 Capital Resources.	1% of Adjusted Tier 1 Capital Resources.
Rationale for benchmark applied	Tier 1 Capital Resources is used as a benchmark as it is a primary focus for the users of the financial statements. We have adjusted the benchmark amount to reinstate the foreseeable, but as yet unpaid and undeclared, dividend as it is a technical adjustment, not yet required to be given accounting recognition, and the resources remain in the Group at the year end.	Tier 1 Capital Resources is used as a benchmark as it is a primary focus for the users of the financial statements. We have adjusted the benchmark amount to reinstate the foreseeable, but as yet unpaid and undeclared, dividend as it is a technical adjustment, not yet required to be given accounting recognition, and the resources remain in the Bank at the year end.

For each component in the scope of our Group and Bank audits, we allocated a materiality that is less than our overall Group and Bank materiality. The range of materiality allocated across components was between £9,000,000 and £27,000,000. Certain components were audited to a local statutory audit materiality that was also less than our overall Group and Bank materiality.

We use performance materiality to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds overall materiality. Specifically, we use performance materiality in determining the scope of our audit and the nature and extent of our testing of account balances, classes of transactions and disclosures, for example in determining sample sizes. Our performance materiality was 75% of overall materiality, amounting to £25,500,000 for the Group financial statements and £25,500,000 for the Bank financial statements.

In determining the performance materiality, we considered a number of factors - the history of misstatements, risk assessment and aggregation risk and the effectiveness of controls - and concluded that an amount at the upper end of our normal range was appropriate.

We agreed with the Audit Committee that we would report to them misstatements identified during our audit above £1,700,000 (Group audit) (2019: £1,800,000) and £1,700,000 (Bank audit) (2019: £1,800,000) as well as misstatements below those amounts that, in our view, warranted reporting for qualitative reasons.

Conclusions relating to going concern
Our evaluation of the directors’ assessment of the Group’s and the Bank’s ability to continue to adopt the going concern basis of accounting included:

- Evaluation of management’s going concern assessment;
- Evaluation and testing of the control environment in place over liquidity and capital forecasting to the extent these are relevant to the going concern assessments performed by management;
- Evaluation of stress testing performed by management and consideration of whether the stresses applied are appropriate for assessing going concern;
- Evaluation of the Group’s and Bank’s forecast financial performance, liquidity and capital positions over the going concern period including an evaluation of the impact of COVID-19 on the financial outlook; and
- Review of credit rating agency ratings and actions.

Based on the work we have performed, we have not identified any material uncertainties relating to events or conditions that, individually or collectively, may cast significant doubt on the Group’s and the Bank’s ability to continue as a going concern for a period of at least twelve months from when the financial statements are authorised for issue.

In auditing the financial statements, we have concluded that the directors’ use of the going concern basis of accounting in the preparation of the financial statements is appropriate.

However, because not all future events or conditions can be predicted, this conclusion is not a guarantee as to the Group’s and the Bank’s ability to continue as a going concern.

Our responsibilities and the responsibilities of the directors with respect to going concern are described in the relevant sections of this report.

Reporting on other information
The other information comprises all of the information in the Annual Report other than the financial statements and our auditors' report thereon. The directors are responsible for the other information. Our opinion on the financial statements does not cover the other information and, accordingly, we do not express an audit opinion or, except to the extent otherwise explicitly stated in this report, any form of assurance thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If we identify an apparent material inconsistency or material misstatement, we are required to perform procedures to conclude whether there is a material misstatement of the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report based on these responsibilities.

With respect to the Strategic report and Directors' report, we also considered whether the disclosures required by the UK Companies Act 2006 have been included.

Based on our work undertaken in the course of the audit, the Companies Act 2006 requires us also to report certain opinions and matters as described below.

Strategic report and Directors' report
In our opinion, based on the work undertaken in the course of the audit, the information given in the Strategic report and Directors' report for the year ended 31 December 2020 is consistent with the financial statements and has been prepared in accordance with applicable legal requirements.

In light of the knowledge and understanding of the Group and Bank and their environment obtained in the course of the audit, we did not identify any material misstatements in the Strategic report and Directors' report.

Responsibilities for the financial statements and the audit
Responsibilities of the directors for the financial statements
As explained more fully in the Statement of directors' responsibilities, the directors are responsible for the preparation of the financial statements in accordance with the applicable framework and for being satisfied that they give a true and fair view. The directors are also responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the Group's and the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Group or the Bank or to cease operations, or have no realistic alternative but to do so.

Auditors' responsibilities for the audit of the financial statements
Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

Our audit testing might include testing complete populations of certain transactions and balances, possibly using data auditing techniques. However, it typically involves selecting a limited number of items for testing, rather than testing complete populations. We will often seek to target particular items for testing based on their size or risk characteristics. In other cases, we will use audit sampling to enable us to draw a conclusion about the population from which the sample is selected.

A further description of our responsibilities for the audit of the financial statements is located on the FRC's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditors' report.

Use of this report
This report, including the opinions, has been prepared for and only for the Bank's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, 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.

Other required reporting

Companies Act 2006 exception reporting
Under the Companies Act 2006 we are required to report to you if, in our opinion:

- we have not obtained all the information and explanations we require for our audit; or
- adequate accounting records have not been kept by the Bank, or returns adequate for our audit have not been received from branches not visited by us; or
- certain disclosures of directors' remuneration specified by law are not made; or
- the Bank financial statements are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.

Appointment
Following the recommendation of the Audit Committee, we were appointed by the directors on 28 September 2016 to audit the financial statements for the year ended 31 December 2017 and subsequent financial periods. The period of total uninterrupted engagement is 4 years, covering the years ended 31 December 2017 to 31 December 2020.

Darren Meek
(Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London

11 March 2021

Group consolidated income statement

for the year ended 31 December

	Note	2020 £m	2019 [1] £m
Interest and similar income		**444**	813
Interest and similar expense		**(370)**	(592)
Net interest income	4	**74**	221
Fee and commission income		**218**	230
Fee and commission expense		**(27)**	(42)
Net fee and commission income	5	**191**	188
Net trading income	6	**279**	410
Other income		**470**	598
Total income		**544**	819
Operating expenses	7	**(428)**	(462)
Impairment (charge)/credit	8	**(71)**	11
Profit before tax		**45**	368
Tax expense	10	**(1)**	(85)
Profit for the year		**44**	283
Profit attributable to ordinary shareholders		**4**	234
Profit attributable to other equity holders		**40**	49
Profit for the year		**44**	283

1 Restated, see note 1.

The accompanying notes are an integral part of the financial statements.

Statements of comprehensive income

for the year ended 31 December

The Group	**2020 £m**	2019 £m
Profit for the year	**44**	283
Other comprehensive (expense)/income		
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 assets:		
Change in fair value	**(2)**	(1)
Tax	**1**	(1)
	(1)	(2)
Movements in cash flow hedging reserve:		
Effective portion of changes in fair value taken to other comprehensive income	**93**	78
Net income statement transfers	**(17)**	(7)
Tax	**(27)**	(20)
	49	51
Movements in foreign currency translation (tax: nil)	**1**	(2)
Other comprehensive income for the year, net of tax	**49**	47
Total comprehensive income for the year	**93**	330
Total comprehensive income attributable to ordinary shareholders	**53**	281
Total comprehensive income attributable to other equity holders	**40**	49
Total comprehensive income for the year	**93**	330

The Bank	**2020 £m**	2019 £m
Profit for the year	**9**	397
Other comprehensive (expense)/income		
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 assets:		
Change in fair value	**(2)**	(1)
Tax	**1**	(1)
	(1)	(2)
Movements in cash flow hedging reserve:		
Effective portion of changes in fair value taken to other comprehensive income	**93**	78
Net income statement transfers	**(17)**	(7)
Tax	**(27)**	(20)
	49	51
Movements in foreign currency translation (tax: nil)	**4**	(1)
Other comprehensive income for the year, net of tax	**52**	48
Total comprehensive income for the year	**61**	445
Total comprehensive income attributable to ordinary shareholders	**21**	396
Total comprehensive income attributable to other equity holders	**40**	49
Total comprehensive income for the year	**61**	445

The accompanying notes are an integral part of the financial statements.

Balance sheets

at 31 December

	Note	The Group 2020 £m	The Group 2019 £m	The Bank 2020 £m	The Bank 2019 £m
Assets					
Cash and balances at central banks		**23,369**	16,250	**23,369**	16,250
Items in the course of collection from banks		**–**	21	**–**	21
Financial assets at fair value through profit or loss	11	**20,926**	18,146	**20,841**	18,059
Derivative financial instruments	12	**21,757**	18,836	**21,818**	18,892
Loans and advances to banks	13	**5,260**	4,813	**5,231**	4,792
Loans and advances to customers	13	**18,452**	20,264	**18,189**	19,986
Debt securities	13	**257**	112	**257**	112
Due from fellow Lloyds Banking Group undertakings	13	**1,118**	710	**1,218**	819
Financial assets at amortised cost	13	**25,087**	25,899	**24,895**	25,709
Financial assets at fair value through other comprehensive income	15	**149**	314	**149**	314
Property, plant and equipment	16	**78**	72	**61**	55
Current tax recoverable		**19**	2	**15**	–
Deferred tax asset	19	**19**	6	**18**	2
Investment in subsidiary undertakings	17	**–**	–	**223**	295
Other assets	18	**1,025**	115	**1,019**	105
Total assets		**92,429**	79,661	**92,408**	79,702

Equity and liabilities	Note	The Group 2020 £m	The Group 2019 £m	The Bank 2020 £m	The Bank 2019 £m
Liabilities					
Deposits from banks		**5,601**	3,970	**5,601**	3,970
Customer deposits		**25,497**	24,479	**25,061**	24,010
Due to fellow Lloyds Banking Group undertakings		**3,283**	1,638	**3,659**	2,084
Financial liabilities at fair value through profit or loss	20	**15,815**	13,784	**15,815**	13,784
Derivative financial instruments	12	**21,233**	17,762	**21,233**	17,762
Debt securities in issue	21	**15,602**	12,429	**15,602**	12,429
Current tax liability		**–**	30	**–**	24
Deferred tax liability	19	**38**	18	**35**	16
Other liabilities	22	**1,045**	577	**1,020**	550
Subordinated liabilities	23	**686**	698	**686**	698
Total liabilities		**88,800**	75,385	**88,712**	75,327
Equity					
Share capital	24	**120**	120	**120**	120
Other reserves	25	**81**	32	**83**	31
Retained profits[1]	26	**2,646**	3,342	**2,711**	3,442
Shareholder's equity		**2,847**	3,494	**2,914**	3,593
Other equity instruments	27	**782**	782	**782**	782
Total equity		**3,629**	4,276	**3,696**	4,375
Total equity and liabilities		**92,429**	79,661	**92,408**	79,702

1 The Group has elected to take the exemption under section 408 of the Companies Act 2006 not to present the Bank's income statement. The Bank recorded a profit after tax for the year of £9 million (2019: £397 million).

The accompanying notes are an integral part of the financial statements.

The financial statements were approved by the Board of Directors and were signed on its behalf by:

Eduardo J Stock da Cunha
Director

Christopher J K Edis
Director

11 March 2021

Statements of changes in equity

for the year ended 31 December

The Group	Share capital £m	Other reserves £m	Retained earnings £m	Total £m	Other equity instruments £m	Total £m
Balance at 1 January 2020	**120**	**32**	**3,342**	**3,494**	**782**	**4,276**
Comprehensive income						
Profit for the year	**–**	**–**	**4**	**4**	**40**	**44**
Other comprehensive (expense)/income						
Movements in revaluation reserve in respect of financial assets held at fair value through other comprehensive income, net of tax:						
Debt securities	**–**	**(1)**	**–**	**(1)**	**–**	**(1)**
Movements in cash flow hedging reserve, net of tax	**–**	**49**	**–**	**49**	**–**	**49**
Currency translation differences (tax: nil)	**–**	**1**	**–**	**1**	**–**	**1**
Total other comprehensive income	**–**	**49**	**–**	**49**	**–**	**49**
Total comprehensive income	**–**	**49**	**4**	**53**	**40**	**93**
Transactions with owners						
Dividends (note 28)	**–**	**–**	**(700)**	**(700)**	**–**	**(700)**
Distributions on other equity instruments	**–**	**–**	**–**	**–**	**(40)**	**(40)**
Total transactions with owners	**–**	**–**	**(700)**	**(700)**	**(40)**	**(740)**
Balance at 31 December 2020	**120**	**81**	**2,646**	**2,847**	**782**	**3,629**

The Group	Share capital £m	Other reserves £m	Retained earnings £m	Total £m	Other equity instruments £m	Total £m
Balance at 1 January 2019	120	(15)	3,105	3,210	782	3,992
Comprehensive income						
Profit for the year	–	–	234	234	49	283
Other comprehensive (expense)/income						
Movements in revaluation reserve in respect of financial assets held at fair value through other comprehensive income, net of tax:						
Debt securities	–	(2)	–	(2)	–	(2)
Movements in cash flow hedging reserve, net of tax	–	51	–	51	–	51
Currency translation differences (tax: nil)	–	(2)	–	(2)	–	(2)
Total other comprehensive income	–	47	–	47	–	47
Total comprehensive income	–	47	234	281	49	330
Transactions with owners						
Distributions on other equity instruments	–	–	–	–	(49)	(49)
Other adjustments	–	–	3	3	–	3
Total transactions with owners	–	–	3	3	(49)	(46)
Balance at 31 December 2019	120	32	3,342	3,494	782	4,276

Further details of movements in the Group's share capital and reserves are provided in notes 24, 25, 26 and 27.

The accompanying notes are an integral part of the financial statements.

Statements of changes in equity

for the year ended 31 December

The Bank	Share capital £m	Other reserves £m	Retained earnings £m	Total £m	Other equity instruments £m	Total £m
Balance at 1 January 2020	**120**	**31**	**3,442**	**3,593**	**782**	**4,375**
Comprehensive income						
Profit for the year	**–**	**–**	**(31)**	**(31)**	**40**	**9**
Other comprehensive (expense)/income						
Movements in revaluation reserve in respect of financial assets held at fair value through other comprehensive income, net of tax:						
Debt securities	**–**	**(1)**	**–**	**(1)**	**–**	**(1)**
Movements in cash flow hedging reserve, net of tax	**–**	**49**	**–**	**49**	**–**	**49**
Currency translation differences (tax: nil)	**–**	**4**	**–**	**4**	**–**	**4**
Total other comprehensive income	**–**	**52**	**–**	**52**	**–**	**52**
Total comprehensive income	**–**	**52**	**(31)**	**21**	**40**	**61**
Transactions with owners						
Dividends (note 28)	**–**	**–**	**(700)**	**(700)**	**–**	**(700)**
Distributions on other equity instruments	**–**	**–**	**–**	**–**	**(40)**	**(40)**
Total transactions with owners	**–**	**–**	**(700)**	**(700)**	**(40)**	**(740)**
Balance at 31 December 2020	**120**	**83**	**2,711**	**2,914**	**782**	**3,696**

The Bank	Share capital £m	Other reserves £m	Retained earnings £m	Total £m	Other equity instruments £m	Total £m
Balance at 1 January 2019	120	(17)	3,087	3,190	782	3,972
Comprehensive income						
Profit for the year	–	–	348	348	49	397
Other comprehensive (expense)/income						
Movements in revaluation reserve in respect of financial assets held at fair value through other comprehensive income, net of tax:						
Debt securities	–	(2)	–	(2)	–	(2)
Movements in cash flow hedging reserve, net of tax	–	51	–	51	–	51
Currency translation differences (tax: nil)	–	(1)	–	(1)	–	(1)
Total other comprehensive income	–	48	–	48	–	48
Total comprehensive income	–	48	348	396	49	445
Transactions with owners						
Distributions on other equity instruments	–	–	–	–	(49)	(49)
Other adjustments	–	–	7	7	–	7
Total transactions with owners	–	–	7	7	(49)	(42)
Balance at 31 December 2019	120	31	3,442	3,593	782	4,375

The accompanying notes are an integral part of the financial statements.

Cash flow statements

for the year ended 31 December

	Note	The Group 2020 £m	The Group 2019[1] £m	The Bank 2020 £m	The Bank 2019[1] £m
Profit before tax		**45**	368	**3**	473
Adjustments for:					
Change in operating assets	36a	**(5,462)**	2,406	**(5,476)**	(1,302)
Change in operating liabilities	36b	**13,609**	1,062	**13,574**	(2,103)
Non-cash and other items	36c	**103**	158	**111**	(23)
Tax paid		**(63)**	(81)	**(51)**	(72)
Net cash generated from/(used in) operating activities		**8,232**	3,913	**8,161**	(3,027)
Cash flows from investing activities					
Purchase of fixed assets		**(24)**	(5)	**(20)**	(1)
Dividends received from subsidiary undertakings		**–**	–	**57**	811
Acquisition of businesses		**–**	–	**–**	6,130
Net cash (used in)/generated from investing activities		**(24)**	(5)	**37**	6,940
Cash flows generated from financing activities					
Dividends paid to ordinary shareholders		**(700)**	–	**(700)**	–
Distributions on other equity instruments		**(40)**	(49)	**(40)**	(49)
Interest paid on subordinated liabilities		**(23)**	(32)	**(23)**	(32)
Net cash used in financing activities		**(763)**	(81)	**(763)**	(81)
Effect of exchange rate changes on cash and cash equivalents		**(169)**	(211)	**(167)**	(209)
Change in cash and cash equivalents		**7,276**	3,616	**7,268**	3,623
Cash and cash equivalents at beginning of year		**19,094**	15,478	**19,073**	15,450
Cash and cash equivalents at end of year	36d	**26,370**	19,094	**26,341**	19,073

1 Restated, see note 1.

The accompanying notes are an integral part of the financial statements.

1 Basis of preparation

The financial statements comply with international accounting standards in conformity with the requirements of the Companies Act 2006. The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS). IFRS comprises accounting standards prefixed IFRS issued by the International Accounting Standards Board (IASB) and those prefixed IAS issued by the IASB's predecessor body as well as interpretations issued by the IFRS Interpretations Committee (IFRS IC) and its predecessor body. On adoption of IFRS 9 in 2018, the Group (Lloyds Bank Corporate Markets plc and its subsidiaries) elected to continue applying hedge accounting under IAS 39. The financial statements are also compliant with IFRS adopted pursuant to Regulation (EC) No 1606/2002 as it applies in the European Union. The EU endorsed version of IAS 39 Financial Instruments: Recognition and Measurement relaxes some of the hedge accounting requirements; the Group has not taken advantage of this relaxation, and therefore there is no difference in application to the Group between IFRS as adopted by the EU and IFRS as issued by the IASB.

The financial information has been prepared under the historical cost convention, as modified by the revaluation of financial assets measured at fair value through other comprehensive income, trading securities and certain other financial assets and liabilities at fair value through profit or loss and all derivative contracts.

The going concern of the Bank and the Group is dependent on successfully funding their respective balance sheets and maintaining adequate levels of capital. In order to satisfy themselves that the Bank and the Group have adequate resources to continue to operate for the foreseeable future, the directors have considered a number of key dependencies which are set out in the Principal risks and uncertainties section under Funding and liquidity on page 10 and additionally have considered projections for the Group's capital and funding position. Taking all of these factors into account, the directors consider that it is appropriate to continue to adopt the going concern basis in preparing the financial statements. In reaching this assessment, the directors have considered the implications of the COVID-19 pandemic upon the Group's performance and projected funding and capital position and have 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.

Details of those IFRS pronouncements which will be relevant to the Group but which were not effective at 31 December 2020 and which have not been applied in preparing these financial statements are given in note 38.

A change of accounting policy took place in the year with respect to the treatment of interest income and expense on derivative instruments which are in hedge accounting relationships. This was done to better reflect the economic substance of the hedging arrangement. The result of which is that in the income statement, the 2019 comparative numbers have been restated to reflect a £51 million reclassification between net interest income (increased) and other income (decreased). This reclassification between lines within total income has no impact on overall total income reported or profit for the year.

The 2019 cashflow statement has been restated to correct the treatment of foreign exchange movements on the cash generated from operating activities. This correction has no impact on the closing cash positions.

In 2019 the Group adopted IFRS 16 and amendments to IAS 12 and early-adopted the hedge accounting amendments *Interest Rate Benchmark Reform* issued by the IASB.

2 Accounting policies

The accounting policies are set out below. These accounting policies have been applied consistently.

a Consolidation
The assets, liabilities and results of Group undertakings (including structured entities) are included in the financial statements on the basis of accounts made up to the reporting date. Details of the Bank's subsidiaries are given in note 40.

Subsidiaries
Subsidiaries are entities controlled by the Group. The Group controls an entity when it has power over the entity, is exposed to, or has rights to, variable returns from its involvement with the entity, and has the ability to affect those returns through the exercise of its power. This generally accompanies a shareholding of more than one half of the voting rights although in certain circumstances a holding of less than one half of the voting rights may still result in the ability of the Group to exercise control. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity. The Group reassesses whether or not it controls an entity if facts and circumstances indicate that there are changes to any of the above elements. Subsidiaries are consolidated from the date on which control is transferred to the Group; they are de-consolidated from the date that control ceases.

Structured entities are entities that are designed so that their activities are not governed by way of voting rights. In assessing whether the Group has power over such entities in which it has an interest, the Group considers factors such as the purpose and design of the entity; its practical ability to direct the relevant activities of the entity; the nature of the relationship with the entity; and the size of its exposure to the variability of returns of the entity.

Intercompany transactions, balances and unrealised gains and losses on transactions between Group companies are eliminated.

Predecessor accounting has been applied to the business transfers as described in note 32. The consideration for the acquisition of a subsidiary is the fair value of the assets transferred, the liabilities incurred and the equity interests issued by the Group. The consideration includes the fair value of any asset or liability resulting from a contingent consideration arrangement. Acquisition related costs are expensed as incurred except those relating to the issuance of debt instruments or share capital (see note 2l). Identifiable assets acquired and liabilities assumed in a business combination are measured initially at their fair value at the acquisition date.

b Revenue recognition
(1) Net interest income
Interest income and expense are recognised in the income statement for all interest-bearing financial instruments using the effective interest method, except for those classified at fair value through profit or loss. The effective interest method is a method of calculating the amortised cost of a financial asset or liability and of allocating the interest income or interest expense over the expected life of the financial instrument. The effective interest rate is the rate that exactly discounts the estimated future cash payments or receipts over the expected life of the financial instrument to the gross carrying amount of the financial asset (before adjusting for expected credit losses) or to the amortised cost of the financial liability, including redemption fees, and related penalties, and premiums and discounts that are an integral part of the overall return.

Direct incremental transaction costs related to the acquisition, issue or disposal of a financial instrument are also taken into account. Interest income from non-credit impaired financial assets is recognised by applying the effective interest rate to the gross carrying amount of the asset; for credit impaired financial assets, the effective interest rate is applied to the net carrying amount after deducting the allowance for expected credit losses. Impairment policies are set out in note 2f below.

(2) Fee and commission income and expense
Fees and commissions receivable which are not an integral part of the effective interest rate are recognised as income as the Group fulfils its performance obligations. The Group receives certain fees in respect of its asset finance business where the performance obligations are typically fulfilled towards the end of the customer contract; these fees are recognised in income on this basis. Where it is unlikely that the loan commitments will be drawn, loan commitment fees are recognised in fee and commission income over the life of the facility, rather than as an adjustment to the effective interest rate for loans expected to be drawn. Incremental costs incurred to generate fee and commission income are charged to fees and commissions expense as they are incurred.

(3) Other
Dividend income is recognised when the right to receive payment is established.

Revenue recognition policies specific to trading income are set out in 2c(3) below; those relating to leases are set out in 2h(2) below.

c Financial assets and liabilities
On initial recognition, financial assets are classified as measured at amortised cost, fair value through other comprehensive income or fair value through profit or loss, depending on the Group's business model for managing the financial assets and whether the cash flows represent solely payments of principal and interest. The Group assesses its business models at a portfolio level based on its objectives for the relevant portfolio, how the performance of the portfolio is managed and reported, and the frequency of asset sales. Financial assets with embedded derivatives are considered in their entirety when considering their cash flow characteristics. The Group reclassifies financial assets when and only when its business model for managing those assets changes. A reclassification will only take place when the change is significant to the Group's operations and will occur at a portfolio level and not for individual instruments; reclassifications are expected to be rare.

Equity investments are measured at fair value through profit or loss unless the Group elects at initial recognition to account for the instruments at fair value through other comprehensive income. For these instruments, dividends are recognised in profit or loss but fair value gains and losses are not subsequently reclassified to profit or loss following derecognition of the investment.

The Group initially recognises loans and advances, deposits, debt securities in issue and subordinated liabilities when the Group becomes a party to the contractual provisions of the instrument. Regular way purchases and sales of securities and other financial assets and trading liabilities are recognised on trade date, being the date that the Group is committed to purchase or sell an asset.

Financial assets are derecognised when the contractual right to receive cash flows from those assets has expired or when the Group has transferred its contractual right to receive the cash flows from the assets and either: substantially all of the risks and rewards of ownership have been transferred; or the Group has neither retained nor transferred substantially all of the risks and rewards, but has transferred control.

Financial liabilities are derecognised when the obligation is discharged, cancelled or expires.

2 Accounting policies (continued)

(1) Financial instruments measured at amortised cost
Financial assets that are held to collect contractual cash flows where those cash flows represent solely payments of principal and interest are measured at amortised cost. A basic lending arrangement results in contractual cash flows that are solely payments of principal and interest on the principal amount outstanding. Where the contractual cash flows introduce exposure to risks or volatility unrelated to a basic lending arrangement such as changes in equity prices or commodity prices, the payments do not comprise solely principal and interest. Financial assets measured at amortised cost are predominantly loans and advances to customers and banks together with certain debt securities used by the Group to manage its liquidity. Interest income is accounted for using the effective interest method (see note 2b above).

Financial liabilities are measured at amortised cost, except for trading liabilities and other financial liabilities designated at fair value through profit or loss on initial recognition which are held at fair value.

(2) Financial assets measured at fair value through other comprehensive income
Financial assets that are held to collect contractual cash flows and for subsequent sale, where the assets' cash flows represent solely payments of principal and interest, are recognised in the balance sheet at their fair value, inclusive of transaction costs. Gains and losses arising from changes in fair value are recognised directly in other comprehensive income, until the financial asset is either sold or matures, at which time the cumulative gain or loss previously recognised in other comprehensive income is recognised in the income statement other than in respect of equity shares, for which the cumulative revaluation amount is transferred directly to retained profits. Interest calculated using the effective interest method and foreign exchange gains and losses on assets denominated in foreign currencies are recognised in the income statement. In addition, the Group recognises a charge for expected credit losses in the income statement (see note 2f below). As the asset is measured at fair value, the charge does not adjust the carrying value of the asset, it is reflected in other comprehensive income.

(3) Financial instruments measured at fair value through profit or loss
Financial assets are classified at fair value through profit or loss where they do not meet the criteria to be measured at amortised cost or fair value through other comprehensive income or where they are designated at fair value through profit or loss to reduce an accounting mismatch. All derivatives are carried at fair value through profit or loss.

Trading securities, which are debt securities acquired principally for the purpose of selling in the short term or which are part of a portfolio which is managed for short-term gains, do not meet the criteria to be measured at amortised cost or fair value through other comprehensive income as they are managed on a fair value basis and accordingly are measured at fair value through profit or loss. Financial assets measured at fair value through profit or loss are recognised in the balance sheet at their fair value. Fair value gains and losses together with interest coupons and dividend income are recognised in the income statement within net trading income.

Financial liabilities are measured at fair value through profit or loss where they are trading liabilities or where they are designated at fair value through profit or loss in order to reduce an accounting mismatch; where the liabilities are part of a group of liabilities (or assets and liabilities) which is managed, and its performance evaluated, on a fair value basis; or where the liabilities contain one or more embedded derivatives that significantly modify the cash flows arising under the contract and would otherwise need to be separately accounted for. Financial liabilities measured at fair value through profit or loss are recognised in the balance sheet at their fair value. Fair value gains and losses are recognised in the income statement within net trading income in the period in which they occur.

The fair values of assets and liabilities traded in active markets are based on current bid and offer prices respectively. If the market is not active the Group establishes a fair value by using valuation techniques. The fair values of derivative financial instruments are adjusted where appropriate to reflect credit risk (via credit valuation adjustments (CVAs), debit valuation adjustments (DVAs) and funding valuation adjustments (FVAs)), market liquidity and other risks.

(4) Borrowings
Borrowings (which include deposits from banks, customer deposits, debt securities in issue and subordinated liabilities) are recognised initially at fair value, being their issue proceeds net of transaction costs incurred. These instruments are subsequently stated at amortised cost using the effective interest method.

Preference shares and other instruments which carry a mandatory coupon or are redeemable on a specific date are classified as financial liabilities. The coupon on these instruments is recognised in the income statement as interest expense. Securities which carry a discretionary coupon and have no fixed maturity or redemption date are classified as other equity instruments. Interest payments on these securities are recognised, net of tax, as distributions from equity in the period in which they are paid. An exchange of financial liabilities on substantially different terms is accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability. The difference between the carrying amount of a financial liability extinguished and the new financial liability is recognised in profit or loss together with any related costs or fees incurred.

When a financial liability is exchanged for an equity instrument, the new equity instrument is recognised at fair value and any difference between the carrying value of the liability and the fair value of the new equity is recognised in profit or loss.

(5) Sale and repurchase agreements (including securities lending and borrowing)
Securities sold subject to repurchase agreements (repos) continue to be recognised on the balance sheet where substantially all of the risks and rewards are retained. Funds received under these arrangements are included in deposits from banks, customer deposits, or trading liabilities. Conversely, securities purchased under agreements to resell (reverse repos), where the Group does not acquire substantially all of the risks and rewards of ownership, are recorded as loans and advances measured at amortised cost or trading assets. The difference between sale and repurchase price is treated as interest and accrued over the life of the agreements using the effective interest method.

Securities borrowing and lending transactions are typically secured; collateral takes the form of securities or cash advanced or received. Securities lent to counterparties are retained on the balance sheet. Securities borrowed are not recognised on the balance sheet, unless these are sold to third parties, in which case the obligation to return them is recorded at fair value as a trading liability. Cash collateral given or received is treated as a loan and advance measured at amortised cost or customer deposit.

d Derivative financial instruments and hedge accounting
As permitted by IFRS 9, the Group continues to apply the requirements of IAS 39 to its hedging relationships. All derivatives are recognised at their fair value. Derivatives are carried in the balance sheet as assets when their fair value is positive and as liabilities when their fair value is negative. Refer to note 31(3) (Financial instruments: Financial assets and liabilities carried at fair value) for details of valuation techniques and significant inputs to valuation models.

Changes in the fair value of all derivative instruments, other than those in effective cash flow and net investment hedging relationships, are recognised immediately in the income statement. As noted in (2) and (3) below, the change in fair value of a derivative in an effective cash flow or net investment hedging relationship is allocated between the income statement and other comprehensive income.

2 Accounting policies (continued)

Derivatives embedded in a financial asset are not considered separately; the financial asset is considered in its entirety when determining whether its cash flows are solely payments of principal and interest. Derivatives embedded in financial liabilities are treated as separate derivatives when their economic characteristics and risks are not closely related to those of the host contract and the host contract is not carried at fair value through profit or loss. These embedded derivatives are measured at fair value with changes in fair value recognised in the income statement.

Hedge accounting allows one financial instrument, generally a derivative such as a swap, to be designated as a hedge of another financial instrument such as a loan or deposit or a portfolio of such instruments. At the inception of the hedge relationship, formal documentation is drawn up specifying the hedging strategy, the hedged item, the hedging instrument and the methodology that will be used to measure the effectiveness of the hedge relationship in offsetting changes in the fair value or cash flow of the hedged risk. The effectiveness of the hedging relationship is tested both at inception and throughout its life and if at any point it is concluded that it is no longer highly effective, or forecast to be highly effective, in achieving its documented objective, hedge accounting is discontinued. Note 12 provides details of the types of derivatives held by the Group and presents separately those designated in hedge relationships. In respect of interest rate benchmark reform, the Group assumes that the interest rate benchmark on which the hedged cash flows and/or the hedged risk are based, or the interest rate benchmark on which the cash flows of the hedging instrument are based, are not altered as a result of interest rate benchmark reform. The Group does not discontinue a hedging relationship during the period of uncertainty arising from the interest rate benchmark reform solely because the actual results of the hedge are not highly effective.

(1) Fair value hedges
Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in the income statement, together with the changes in the fair value of the hedged asset or liability that are attributable to the hedged risk; this also applies if the hedged asset is classified as a financial asset at fair value through other comprehensive income. If the hedge no longer meets the criteria for hedge accounting, changes in the fair value of the hedged item attributable to the hedged risk are no longer identified and recognised in the income statement. The cumulative adjustment that has been made to the carrying amount of the hedged item is amortised to the income statement using the effective interest method over the period to maturity.

(2) Cash flow hedges
The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised in other comprehensive income in the cash flow hedging reserve. The gain or loss relating to the ineffective portion is recognised immediately in the income statement. Amounts accumulated in equity are reclassified to the income statement in the periods in which the hedged item affects profit or loss. When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognised in the income statement when the forecast transaction is ultimately recognised in the income statement. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the income statement.

(3) Net investment hedges
Hedges of net investments in foreign operations are accounted for similarly to cash flow hedges. Any gain or loss on the hedging instrument relating to the effective portion of the hedge is recognised in other comprehensive income, the gain or loss relating to the ineffective portion is recognised immediately in the income statement. Gains and losses accumulated in equity are included in the income statement when the foreign operation is disposed of. The hedging instrument used in net investment hedges may include non-derivative liabilities as well as derivative financial instruments.

e Offset
Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right of set-off and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously. Cash collateral on exchange traded derivative transactions is presented gross unless the collateral cash flows are always settled net with the derivative cash flows. In certain situations, even though master netting agreements exist, the lack of management intention to settle on a net basis results in the financial assets and liabilities being reported gross on the balance sheet.

f Impairment of financial assets
The impairment charge in the income statement includes the change in expected credit losses and including those arising from fraud. Expected credit losses are recognised 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 commitments and financial guarantee contracts. Expected credit losses are calculated as an unbiased and probability-weighted estimate using an appropriate probability of default, adjusted to take into account a range of possible future economic scenarios, and applying this to the estimated exposure of the Group at the point of default after taking into account the value of any collateral held, repayments, or other mitigants of loss and including the impact of discounting using the effective interest rate.

At initial recognition, allowance (or provision in the case of some loan commitments and financial guarantees) is made for expected credit losses resulting from default events that are possible within the next 12 months (12-month expected credit losses). In the event of a significant increase in credit risk since origination, allowance (or provision) is made for expected credit losses resulting from all possible default events over the expected life of the financial instrument (lifetime expected credit losses). Financial assets where 12-month expected credit losses are recognised are considered to be Stage 1; financial assets which are considered to have experienced a significant increase in credit risk since initial recognition are in Stage 2; and financial assets which have defaulted or are otherwise considered to be credit impaired are allocated to Stage 3.

Some Stage 3 assets are subject to individual rather than collective assessment. Such cases are subject to a risk-based impairment sanctioning process, and these are reviewed and updated at least quarterly, or more frequently if there is a significant change in the credit profile. The collective assessment of impairment aggregates financial instruments with similar risk characteristics such as whether the facility is revolving in nature or secured and the type of security against financial assets.

Predecessor accounting has been applied to the business transfers as described in note 32 and impairment allowances for financial assets were brought in to the financial statements at the predecessor carrying values.

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 (PD) movements linked to internal credit ratings together with qualitative indicators such as watchlists and other indicators of historic delinquency, credit weakness or financial difficulty. However, unless identified at an earlier stage, the credit risk of financial assets is deemed to have increased significantly when more than 30 days past due. Where the credit risk subsequently improves such that it no longer represents a significant increase in credit risk since initial recognition, the asset is transferred back to Stage 1.

Assets are transferred to Stage 3 when they have defaulted or are otherwise considered to be credit impaired. Default is considered to have occurred when there is evidence that the customer is experiencing financial difficulty which is likely to affect significantly the ability to repay the amount due. IFRS 9 contains a rebuttable presumption that default occurs no later than when a payment is 90 days past due. The Group uses this 90 day backstop for all its products in its Commercial business.

2 Accounting policies (continued)

In certain circumstances, the Group will renegotiate the original terms of a customer's loan, either as part of an ongoing customer relationship or in response to adverse changes in the circumstances of the borrower. In the latter circumstances, the loan will remain classified as either Stage 2 or Stage 3 until the credit risk has improved such that it no longer represents a significant increase since origination (for a return to Stage 1), or the loan is no longer credit impaired (for a return to Stage 2). On renegotiation the gross carrying amount of the loan is recalculated as the present value of the renegotiated or modified contractual cash flows, which are discounted at the original effective interest rate. Renegotiation may also lead to the loan and associated allowance being derecognised and a new loan being recognised initially at fair value.

A loan or advance is normally written off, either partially or in full, against the related allowance when the proceeds from realising any available security have been received or there is no realistic prospect of recovery and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off decrease the amount of impairment losses recorded in the income statement. For both secured and unsecured retail balances, the write-off takes place only once an extensive set of collections processes has been completed, or the status of the account reaches a point where policy dictates that continuing concessions are no longer appropriate. For commercial lending, a write-off occurs if the loan facility with the customer is restructured, the asset is under administration and the only monies that can be received are the amounts estimated by the administrator, the underlying assets are disposed and a decision is made that no further settlement monies will be received, or external evidence (for example, third party valuations) is available that there has been an irreversible decline in expected cash flows.

g Property, plant and equipment

Property, plant and equipment is included at cost less accumulated depreciation. The value of land (included in premises) is not depreciated. Depreciation on other assets is calculated using the straight-line method to allocate the difference between the cost and the residual value over their estimated useful lives, as follows: the shorter of 50 years and the remaining period of the lease for freehold/long and short leasehold premises; the shorter of 10 years and, if lease renewal is not likely, the remaining period of the lease for leasehold improvements; 10 to 20 years for fixtures and furnishings; and 2 to 8 years for other equipment and motor vehicles.

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

Assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. In the event that an asset's carrying amount is determined to be greater than its recoverable amount it is written down immediately. The recoverable amount is the higher of the asset's fair value less costs to sell and its value in use.

h Leases

Under IFRS 16, a lessor is required to determine whether a lease is a finance or operating lease. A lessee is not required to make this determination.

(1) As lessor

Assets leased to customers are classified as finance leases if the lease agreements transfer substantially all the risks and rewards of ownership to the lessee but not necessarily legal title. All other leases are classified as operating leases. When assets are subject to finance leases, the present value of the lease payments, together with any residual value, is recognised as a receivable, net of allowances for expected credit losses, within loans and advances to banks and customers. The difference between the gross receivable and the present value of the receivable is recognised as unearned finance lease income. Finance lease income is recognised in interest income over the term of the lease using the net investment method (before tax) so as to give a constant rate of return on the net investment in the leases. Unguaranteed residual values are reviewed regularly to identify any impairment.

Operating lease assets are included within property, plant and equipment at cost and depreciated over their estimated useful lives, which equates to the lives of the leases, after taking into account anticipated residual values. Operating lease rental income is recognised on a straight-line basis over the life of the lease.

The Group evaluates non-lease arrangements such as outsourcing and similar contracts to determine if they contain a lease which is then accounted for separately.

(2) As lessee

Leases are recognised as a right-of-use asset and a corresponding liability at the date at which the lease asset is available for use by the Group. Assets and liabilities arising from a lease are initially measured on a present value basis. The lease payments are discounted using the interest rate implicit in the lease, if that rate can be determined, or the Group's incremental borrowing rate appropriate for the right-of-use asset arising from the lease.

Lease payments are allocated between the liability and finance cost. The finance cost is charged to profit or loss over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period. The right-of-use assets is depreciated over the shorter of the asset's useful life and lease term on a straight-line basis.

Payments associated with short-term leases and leases of low-value assets are recognised on a straight-line basis as an expense in profit or loss. Short-term leases are leases with a lease term of twelve months or less. Low-value assets comprise IT equipment and small items of office furniture.

i Taxation

Tax expense comprises current and deferred tax. Current and deferred tax are charged or credited in the income statement except to the extent that the tax arises from a transaction or event which is recognised, in the same or a different period, outside the income statement (either in other comprehensive income, directly in equity, or through a business combination), in which case the tax appears in the same statement as the transaction that gave rise to it. The tax consequences of the Group's dividend payments (including distributions on other equity instruments), if any, are charged or credited to the statement in which the profit distributed originally arose.

Current tax is the amount of corporate income taxes expected to be payable or recoverable based on the profit for the period as adjusted for items that are not taxable or not deductible, and is calculated using tax rates and laws that were enacted or substantively enacted at the balance sheet date.

Provisions reflect management's best estimate of the ultimate liability based on their interpretation of tax law, precedent and guidance, informed by external tax advice as necessary. Changes in facts and circumstances underlying these provisions are reassessed at each balance sheet date, and the provisions are re-measured as required to reflect current information.

Deferred tax is recognised on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the balance sheet. Deferred tax is calculated using tax rates and laws that have been enacted or substantively enacted at the balance sheet date, and which are expected to apply when the related deferred tax asset is realised or the deferred tax liability is settled.

Deferred tax liabilities are generally recognised for all taxable temporary differences but not recognised for taxable temporary differences arising on investments in subsidiaries where the reversal of the temporary difference can be controlled and it is probable that the difference will not reverse in the foreseeable future.

2 Accounting policies (continued)

Deferred tax assets are recognised to the extent it is probable that taxable profits will be available against which the deductible temporary differences can be utilised, and are reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax assets and liabilities are not recognised in respect of temporary differences that arise on initial recognition of assets and liabilities acquired other than in a business combination. Deferred tax is not discounted.

j Foreign currency translation
Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the 'functional currency'). The functional currency of the Group and the Bank is sterling. Foreign currency transactions are translated into the appropriate functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement, except when recognised in other comprehensive income as qualifying cash flow or net investment hedges.

Non-monetary assets that are measured at fair value are translated using the exchange rate at the date that the fair value was determined. Translation differences on equities and similar non-monetary items held at fair value through profit and loss are recognised in profit or loss as part of the fair value gain or loss. Translation differences on non-monetary financial assets measured at fair value through other comprehensive income are included in the fair value reserve in equity unless the asset is a hedged item in a fair value hedge.

The results and financial position of all group entities that have a functional currency different from the presentation currency are translated into the presentation currency as follows: the assets and liabilities of foreign operations, including goodwill and fair value adjustments arising on the acquisition of a foreign entity, are translated into sterling at foreign exchange rates ruling at the balance sheet date; and the income and expenses of foreign operations are translated into sterling at average exchange rates unless these do not approximate to the foreign exchange rates ruling at the dates of the transactions in which case income and expenses are translated at the dates of the transactions.

Foreign exchange differences arising on the translation of a foreign operation are recognised in other comprehensive income and accumulated in a separate component of equity together with exchange differences arising from the translation of borrowings and other currency instruments designated as hedges of such investments (see note 2d(3) above). On disposal or liquidation of a foreign operation, the cumulative amount of exchange differences relating to that foreign operation are reclassified from equity and included in determining the profit or loss arising on disposal or liquidation.

k Provisions and contingent liabilities
Provisions are recognised in respect of present obligations arising from past events where it is probable that outflows of resources will be required to settle the obligations and they can be reliably estimated.

Contingent liabilities are possible obligations whose existence depends on the outcome of uncertain future events or those present obligations where the outflows of resources are uncertain or cannot be measured reliably. Contingent liabilities are not recognised in the financial statements but are disclosed unless they are remote.

Provision is made for expected credit losses in respect of irrevocable undrawn loan commitments and financial guarantee contracts (see note 2f above).

l Share capital
Incremental costs directly attributable to the issue of new shares or options or to the acquisition of a business are shown in equity as a deduction, net of tax, from the proceeds. Dividends paid on the Group's ordinary shares are recognised as a reduction in equity in the period in which they are paid.

m Cash and cash equivalents
For the purposes of the cash flow statement, cash and cash equivalents comprise cash and non-mandatory balances with central banks and amounts due from banks with a maturity of less than three months.

n Investment in subsidiaries of the bank
Investments in subsidiaries are carried at historical cost, less any provisions for impairment.

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3 Critical accounting estimates and judgements

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 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 estimates and judgements made by management in applying the Group's accounting policies and the key sources of estimation uncertainty in these financial statements, which together are deemed critical to the Group's results and financial position, are as follows:

3 Critical accounting estimates and judgements (continued)

Fair value of financial instruments
Key estimates: Interest rate spreads, earning multiples and interest rate volatility

At 31 December 2020, the carrying value of the Group's financial instrument assets held at fair value was £42,832 million (2019: £37,296 million), and its financial instrument liabilities held at fair value was £37,048 million (2019: £31,546 million). The carrying value of the Bank's financial instrument assets held at fair value was £42,808 million (2019: £37,265 million), and its financial instrument liabilities held at fair value was £37,048 million (2019: £31,546 million).

The valuation techniques for level 3 financial instruments involve management judgements and estimates, the extent of which depends on the complexity of the instrument and the availability of market observable information. In addition, in line with market practice, the Group applies credit, debit and funding valuation adjustments in determining the fair value of its uncollateralised derivative positions. A description of these adjustments is set out in note 31.

Allowance for expected credit losses
Key judgements: Determining an appropriate definition of default against which a probability of default, exposure at default and loss given default parameter can be evaluated.

The appropriate lifetime of an exposure to credit risk for the assessment of lifetime losses, notably on revolving products.

Establishing the criteria for a significant increase in credit risk.

The use of management judgement alongside impairment modelling processes to adjust inputs, parameters and outputs to reflect risks not captured by models.

Key estimates: Base case and multiple economic scenarios (MES) assumptions, including the rate of unemployment, required for creation of MES scenarios and forward looking credit parameters.

These judgements and estimates are subject to significant uncertainty.

The Group recognises an allowance for expected credit losses 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 31 December 2020 the Group's expected credit loss allowance was £83 million (2019: £91 million), of which £50 million (2019: £87 million) was in respect of drawn balances; and the Bank's expected credit loss allowance was £82 million (2019: £90 million), of which £49 million (2019: £86 million) was in respect of drawn balances.

The calculation of the Group's expected credit loss (ECL) allowances and provisions against loan commitments and guarantees under IFRS 9 requires the Group to make a number of judgements, assumptions and estimates. The most significant are set out below.

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 definition of default adopted by the Group is described in note 2(f) Impairment of financial assets.

Lifetime of an exposure
A range of approaches, segmented by product type, has been adopted by the Group to estimate a product's expected life. These include using the full contractual life and taking into account behavioural factors such as early repayments and refinancing. Changes to the assumed expected lives of the Group's assets could impact the ECL allowance recognised by the Group. The assessment of a significant increase in credit risk (SICR) and corresponding lifetime loss, and the PD, of a financial asset deemed to be Stage 2, or Stage 3, is dependent on its expected life.

Significant increase in credit risk
Performing assets are classified as either Stage 1 or Stage 2. An ECL allowance equivalent to 12 months expected losses is established against assets in Stage 1; assets classified as Stage 2 carry an ECL allowance equivalent to lifetime expected losses. Assets are transferred from Stage 1 to Stage 2 when there has been a SICR since initial recognition. Credit impaired assets are transferred to Stage 3 with a lifetime expected losses allowance. The Group uses both quantitative and qualitative indicators to determine whether there has been a SICR for an asset.

A doubling of PD with a minimum increase in PD of 1 per cent and a resulting change in the underlying grade is treated as a SICR. The Group uses the internal credit risk classification and watchlist as qualitative indicators to identify a SICR. The Group does not use the low credit risk exemption in its staging assessments.

All financial assets are assumed to have suffered a SICR if they are more than 30 days past due. Financial assets are classified as credit impaired if they are 90 days past due.

A Stage 3 asset that is no longer credit-impaired is transferred back to Stage 2 as no cure period is applied to Stage 3. If an exposure that is classified as Stage 2 no longer meets the SICR criteria, which in some cases include a minimum cure period, it is moved back to Stage 1.

The setting of precise trigger points combined with risk indicators requires judgement. The use of different trigger points may have a material impact upon the size of the ECL allowance. The Group monitors the effectiveness of SICR criteria on an ongoing basis.

3 Critical accounting estimates and judgements (continued)

Generation of Multiple Economic Scenarios (MES)

The measurement of expected credit losses is required to reflect an unbiased probability-weighted range of possible future outcomes. The Group considers the choice of approach used to generate the range of economic outcomes to be judgemental, given several methods can be adopted. In addition to a defined base case, as used for planning, the Group's approach relies on model-generated scenarios, reducing scope for bias in the selection of scenarios and their weightings. The conditioning assumptions underpinning the base case scenario reflect the Group's best view of future events. Where outcomes materially diverge from the conditioning assumptions adopted, the base case scenario is updated. The base case is therefore central to the range of outcomes created as no alternative conditioning assumptions are factored into the model generated scenarios.

The Group models a full distribution of economic scenarios around this base case, ranking them using estimated relationships with industrywide historical loss data. The full distribution is summarised by a practical number of scenarios to run through ECL models representing four sections: an upside, the base case, and a downside scenario weighted at 30 per cent each, with a severe downside scenario weighted at 10 per cent. With the base case already pre-defined, the other three scenarios are constructed as averages of constituent modelled scenarios around the 15th, 75th and 95th percentiles of the distribution. The scenario weights therefore represent the allocation to each summary segment of the distribution and not a subjective view on likelihood. The inclusion of a severe downside scenario with a smaller weighting but relatively large credit losses, ensures the non-linearity of losses in the tail of the distribution is captured when ECL based on the weighted result of the four scenarios is calculated.

A committee under the chairmanship of the LBG Chief Economist meets at least quarterly, to review and, if appropriate, recommend changes to the method by which economic scenarios are generated; for approval by the Group Chief Financial Officer and Group Chief Risk Officer. Findings dealing with all aspects of the expected credit loss calculation are presented to the Audit Committee. In 2020, a change was made to the way in which the distribution of scenarios is created. This change allows for a greater dispersal of economic outcomes in the early periods of the forecast, to recognise the increased near-term profile of risks present since the onset of the coronavirus pandemic. This change allows for a wider distribution of losses both on the upside and downside, although is most evident in the severe downside scenario, given it represents a more adverse segment of the distribution.

Base case and MES Economic Assumptions

The Group's base case economic scenario has continued to be revised in light of the impact of the coronavirus pandemic in the UK and globally. The scenario reflects judgements of the net effect of government-mandated restrictions on economic activity, large-scale government interventions, and behavioural changes by households and businesses that may persist beyond the rollout of coronavirus vaccination programmes.

Despite large-scale vaccination efforts commencing in the UK and globally, there remains considerable uncertainty about the pace and eventual extent of the post-pandemic recovery. The Group's current base case scenario builds in three key conditioning assumptions. First, the UK vaccine rollout successfully protects the elderly, key workers and the clinically vulnerable by mid-2021. Second, national lockdowns end by April 2021, allowing a phased return to a tiered system of restrictions that are progressively eased in the second quarter and second half of 2021, leaving only limited restrictions in place by the end of 2021. Third, government policy measures including specifically the job furlough scheme continue to provide support for the duration of severe economic restrictions, through to mid-2021.

Conditioned on the above assumptions, and despite the recovery in economic activity resuming from the second quarter of 2021, the Group's base case outlook assumes a rise in the unemployment rate and weakness in residential and commercial property prices. Risks around this base case economic view lie in both directions and are partly captured by the MES generated. But uncertainties relating to the key conditioning assumptions – including epidemiological developments and the effectiveness of vaccine rollouts are not specifically captured by the MES scenarios. These specific risks have been recognised outside the modelled scenarios published below.

The Group has accommodated the latest available information at the reporting date in defining its base case scenario and generating the MES. The scenarios include forecasts for key variables in the fourth quarter of 2020, for which actuals may have since emerged prior to publication.

Base case scenarios by quarter[1]

Base case[1]	**First quarter 2020 %**	**Second quarter 2020 %**	**Third quarter 2020 %**	**Fourth quarter 2020 %**	First quarter 2021 %	Second quarter 2021 %	Third quarter 2021 %	Fourth quarter 2021 %
UK Gross domestic product	**(3.0)**	**(18.8)**	**16.0**	**(1.9)**	(3.8)	5.6	3.6	1.5
UK Bank rate	**0.10**	**0.10**	**0.10**	**0.10**	0.10	0.10	0.10	0.10
UK Unemployment rate	**4.0**	**4.1**	**4.8**	**5.0**	5.2	6.5	8.0	7.5
UK Commercial real estate price growth	**(5.0)**	**(7.8)**	**(7.8)**	**(7.0)**	(6.1)	(2.9)	(2.2)	(1.7)
US Gross domestic product	**(1.3)**	**(9.0)**	**7.4**	**0.9**	0.8	0.8	0.8	0.7
US Unemployment rate	**3.8**	**13.0**	**8.8**	**7.6**	7.1	6.7	6.5	6.1

1 Gross domestic product presented quarter on quarter and commercial real estate growth presented year on year - i.e. from the equivalent quarter the previous year. Bank Rate is presented end quarter.

3 Critical accounting estimates and judgements (continued)

Scenarios by year

Key annual assumptions made by the Group are shown below. Gross domestic product is presented as an annual change and commercial real estate price growth is presented as the growth in the respective index within the period. UK Bank Rate and unemployment rates are averages in the period.

	2020 %	2021 %	2022 %	2023 %	2024 %
Upside					
UK Gross domestic product	**(10.5)**	3.7	5.7	1.7	1.5
UK Bank rate	**0.10**	1.14	1.27	1.20	1.21
UK Unemployment rate	**4.3**	5.4	5.4	5.0	4.5
UK Commercial real estate price growth	**(4.6)**	9.3	3.9	2.1	0.3
US Gross domestic product	**(3.4)**	8.0	5.1	0.2	(0.6)
US Unemployment rate	**8.3**	5.7	3.8	4.3	5.3
Base case					
UK Gross domestic product	**(10.5)**	3.0	6.0	1.7	1.4
UK Bank rate	**0.10**	0.10	0.10	0.21	0.25
UK Unemployment rate	**4.5**	6.8	6.8	6.1	5.5
UK Commercial real estate price growth	**(7.0)**	(1.7)	1.6	1.1	0.6
US Gross domestic product	**(3.5)**	3.9	2.6	2.0	1.8
US Unemployment rate	**8.3**	6.6	5.8	5.5	5.2
Downside					
UK Gross domestic product	**(10.6)**	1.7	5.1	1.4	1.4
UK Bank rate	**0.10**	0.06	0.02	0.02	0.03
UK Unemployment rate	**4.6**	7.9	8.4	7.8	7.0
UK Commercial real estate price growth	**(8.7)**	(10.6)	(3.2)	(0.8)	(0.8)
US Gross domestic product	**(3.7)**	1.2	0.3	2.5	3.3
US Unemployment rate	**8.3**	7.3	7.7	7.2	6.2
Severe downside					
UK Gross domestic product	**(10.8)**	0.3	4.8	1.3	1.2
UK Bank rate	**0.10**	0.00	0.00	0.01	0.01
UK Unemployment rate	**4.8**	9.9	10.7	9.8	8.7
UK Commercial real estate price growth	**(11.0)**	(21.4)	(9.8)	(3.9)	(0.8)
US Gross domestic product	**(3.9)**	(2.9)	(3.0)	3.8	5.9
US Unemployment rate	**8.4**	8.4	10.4	9.4	7.0

3 Critical accounting estimates and judgements (continued)

Economic assumptions - five year average

The key economic assumptions made by the Group averaged over a five-year period are shown below. The five-year period reflects movements within the current reporting year such that 31 December 2020 reflects five years 2020 to 2024. The prior year comparative data has been re-presented to align to the equivalent period, 2019 to 2023. 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 change in calculating ECL. The use of calendar years also maintains a comparability between tables disclosed.

	At 31 December 2020				At 31 December 2019			
Economic assumptions	Upside %	Base case %	Downside %	Severe downside %	Upside %	Base case %	Downside %	Severe downside %
UK Gross domestic product	0.3	0.1	(0.4)	(0.8)	1.6	1.3	1.0	0.3
UK Bank rate	0.98	0.15	0.05	0.02	1.87	1.15	0.51	0.17
UK Unemployment rate	5.0	5.9	7.1	8.8	3.9	4.3	5.5	6.7
UK Commercial real estate price growth	2.1	(1.1)	(4.9)	(9.7)	1.6	(0.3)	(3.9)	(7.3)
US Gross domestic product	1.8	1.3	0.7	(0.1)	2.1	1.9	1.3	0.7
US Unemployment rate	5.5	6.3	7.3	8.7	3.4	3.9	5.1	6.5

	At 31 December 2020				At 31 December 2019			
Economic assumptions – start to peak	Upside %	Base case %	Downside %	Severe downside %	Upside %	Base case %	Downside %	Severe downside %
UK Gross domestic product	1.4	0.8	(1.7)	(3.0)	8.4	6.6	5.5	1.8
UK Bank rate	1.44	0.25	0.10	0.10	2.56	1.75	0.75	0.75
Unemployment rate	6.5	8.0	9.3	11.5	4.4	4.6	6.9	8.3
UK Commercial real estate price growth	11.0	(2.7)	(2.7)	(2.7)	8.8	(0.8)	(0.8)	(0.8)
US Gross domestic product	9.4	6.5	3.8	0.5	10.5	9.5	6.9	3.8
US Unemployment rate	13.0	13.0	13.0	13.0	3.9	4.1	6.1	8.3

	At 31 December 2020				At 31 December 2019			
Economic assumptions – start to trough	Upside %	Base case %	Downside %	Severe downside %	Upside %	Base case %	Downside %	Severe downside %
UK Gross domestic product	(21.2)	(21.2)	(21.2)	(21.2)	0.3	0.3	0.3	(2.4)
UK Bank rate	0.10	0.10	0.01	0.00	0.75	0.75	0.35	0.01
UK Unemployment rate	4.0	4.0	4.0	4.0	3.4	3.8	3.8	3.8
UK Commercial real estate price growth	(6.9)	(9.0)	(22.2)	(39.9)	(1.4)	(2.3)	(17.9)	(31.4)
US Gross domestic product	(10.1)	(10.1)	(10.1)	(10.6)	0.8	0.8	0.8	(1.4)
US Unemployment rate	3.7	3.8	3.8	3.8	3.2	3.6	3.6	3.6

1 Gross domestic product presented quarter on quarter and commercial real estate growth presented year on year - i.e. from the equivalent quarter the previous year. Bank Rate is presented end quarter.

ECL sensitivity to economic assumptions

The table below shows the Group's ECL for the upside, base case, downside and severe downside scenarios. The stage allocation for an asset is based on the overall scenario probability-weighted PD and, hence, the Stage 2 allocation is constant across all the scenarios. ECL applied through individual assessments and post-model adjustments is reported flat against each economic scenario, reflecting the basis on which they are evaluated. Judgements applied through changes to inputs are reflected in the scenario sensitivities.

Impact of multiple economic scenarios	Probability Weighting £m	Upside £m	Base case £m	Downside £m	Severe downside £m
At 31 December 2020	**83**	**51**	**71**	**102**	**159**
At 31 December 2019	91	87	90	94	101

3 Critical accounting estimates and judgements (continued)

The table below shows the Group's ECL for the upside, base case, downside and severe downside scenarios, with stage allocation based on each specific scenario. ECL applied through individual assessments and post-model adjustments is reported flat against each economic scenario, reflecting the basis on which they are evaluated. Judgements applied through changes to inputs are reflected in the scenario sensitivities. A probability weighted scenario is not shown as this does not reflect the basis on which ECL is reported.

The table also shows the percentage of assets that would be recorded in Stage 2 for the upside, base case, downside and severe downside scenarios, if stage allocation was based on each specific scenario. Given additional data has been generated to support this new disclosure the prior year comparatives are not available.

Impact of multiple economic scenarios	Upside £m	Base case £m	Downside £m	Severe downside £m
At 31 December 2020	**45**	**71**	**104**	**165**
Percentage of assets in Stage 2	0.4%	1.6%	2.1%	3.3%

Individual assessments
Stage 3 ECL is largely assessed on an individual basis using bespoke assessment of loss for each specific customer. These assessments are carried out by the Business Support Unit based on detailed reviews and expected recovery strategies. While these assessments are based on the Group's latest economic view, the use of group-wide multiple economic scenarios and weightings is not considered appropriate for these cases due to their individual characteristics. In place of this a range of case specific outcomes are considered with any alternative better or worse outcomes that carry a 25 per cent likelihood taken into account in establishing a probability-weighted ECL. At 31 December 2020 individually assessed provisions for the Group were £1 million (2019: £74 million) which reflected a range of £1 million to £2 million (2019: £73 million to £84 million), based on these alternative outcomes.

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 model or data inputs may be identified through the ongoing assessment and validation of the output of the models. In these circumstances, management makes 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 overlays.

Judgements are not typically assessed under each distinct economic scenario used to generate ECL, but instead are applied on the basis of final modelled ECL which reflects the probability weighted view of all scenarios. All adjustments are reviewed quarterly and are subject to internal review and challenge, including by the Audit Committee, to ensure that amounts are appropriately calculated and that there are specific release criteria within a reasonable timeframe.

At 31 December 2020 the coronavirus pandemic and the various support measures that have been put in place have resulted in an economic environment which differs significantly from the historical economic conditions upon which the impairment models have been built. As a result there is a greater need for management judgements to be applied alongside the use of models. At 31 December 2020 management judgement resulted in additional ECL allowances totalling £50 million (2019: £nil). The table below analyses total ECL allowance at 31 December 2020, separately identifying the amounts that have been modelled, those that have been individually assessed and those arising through the application of management judgement.

£m	Modelled ECL	Individually assessed	Judgements due to COVID-19[1]	Other Judgements	Total ECL
As at 31 December 2020	**32**	**1**	**50**	**–**	**83**
As at 31 December 2019	17	74	–	–	91

1 Judgements introduced in 2020 due to the impact that COVID-19 and resulting interventions have had on the Group's economic outlook and observed loss experience, which have required additional model limitations to be addressed.

Post model adjustments have been raised to reflect uncertainty in the near term economic outlook and limitations in the models in dealing with this uncertainty but the impact on staging of assets has not been reflected.

Adjustment to PD models: £30 million
This is principally comprised of an adjustment to PD models reliant on GDP inputs. The credit models used to estimate US and Financial Institution defaults use GDP as a key input. Given the volatility seen in quarterly GDP the resulting anticipated recovery from the extraordinary low levels is judged to understate predicted defaults. Management has used an alternative approach in generating PDs and adjusted ECL to reflect equivalent movements seen in core models not reliant on GDP.

Economic impacts not captured by models: £20 million
A further management adjustment to increase ECL by £20 million is incorporated, to reflect the additional uncertainty of economic forecasts. This qualitative overlay is a management judgement to ensure the overall provision adequately reflects the current material risks; considering the range of the quarterly provision release, review of trends and provision coverage.

4 Net interest income

	2020 £m	2019[1] £m
Interest and similar income:		
Loans and advances to customers	**350**	567
Loans and advances to banks	**90**	239
Debt securities held at amortised cost	**2**	1
Interest receivable on financial assets held at amortised cost	**442**	807
Financial assets at fair value through other comprehensive income	**2**	6
Total interest and similar income[2]	**444**	813
Interest and similar expense:		
Deposits from banks	**(30)**	(10)
Customer deposits	**(161)**	(340)
Debt securities in issue	**(154)**	(208)
Subordinated liabilities	**(22)**	(31)
Lease liabilities	**(3)**	(3)
Total interest and similar expense[3]	**(370)**	(592)
Net interest income	**74**	221

1 Restated, see note 1.

2 Includes £1 million (2019: £nil) of interest income on liabilities with negative interest rates and £5 million (2019: £8 million) in respect of interest income on finance leases.

3 Includes £nil (2019: £nil) of interest expense on assets with negative interest rates.

Included within interest income is £1 million (2019: £2 million) in respect of credit impaired financial assets. Net interest income also includes a credit of £23 million (2019: £9 million) transferred from the cash flow hedging reserve (see note 25).

5 Net fee and commission income

	2020 £m	2019 £m
Fee and commission income:		
Commercial banking and treasury fees	**199**	213
Current accounts	**4**	5
Private banking and asset management	**5**	4
Credit and debit card fees	**2**	3
Other fees and commissions	**8**	5
Total fee and commission income	**218**	230
Fee and commission expense	**(27)**	(42)
Net fee and commission income	**191**	188

Fees and commissions which are an integral part of the effective interest rate form part of net interest income shown in note 4. Fees and commissions relating to instruments that are held at fair value through profit or loss are included within net trading income shown in note 6.

At 31 December 2020, the Group held on its balance sheet £6 million (31 December 2019: £4 million) in respect of services provided to customers after the balance sheet date.

6 Net trading income

	2020 £m	2019[1] £m
Foreign exchange translation losses	**(13)**	(12)
Gains on foreign exchange trading transactions	**108**	82
Total foreign exchange	**95**	70
Securities and other gains (see below)	**184**	340
Net trading income	**279**	410

Securities and other gains comprise net gains arising on assets and liabilities held at fair value through profit or loss and for trading as follows:

	2020 £m	2019[1] £m
Net income arising on assets and liabilities mandatorily held at fair value through profit or loss:		
Financial instruments held for trading	**147**	305
Other financial instruments mandatorily held at fair value through profit or loss:		
Debt securities, loans and advances	**34**	35
Equity shares	**3**	-
Securities and other gains	**184**	340

1 Restated, see note 1.

7 Operating expenses

	2020 £m	2019 £m
Staff costs:		
Salaries	**149**	138
Social security costs	**14**	11
Pensions and other post-retirement benefit schemes	**13**	12
Restructuring costs	**5**	4
Other staff costs	**6**	11
	187	176
Management charges payable	**186**	205
Depreciation and amortisation	**16**	19
Premises and equipment	**6**	9
Communications and data processing	**11**	12
Professional fees	**6**	8
Start up costs for Lloyds Bank Corporate Markets Wertpapierhandelsbank GmbH	**–**	14
Other operating expenses	**16**	19
Total operating expenses	**428**	462

Services are received by the Group from other parts of the Lloyds Banking Group via a shared service provision model. This is governed via Intra Group Agreement (IGA) contracts and includes the provision of services supporting the business, operations and support functions. Management charges payable were paid to Lloyds Bank plc in respect of these services. UK-based colleagues are employed through other Lloyds Banking Group companies and costs recharged via the IGA. The terms of the contract are negotiated and renewable to ensure market rate expense for services provided.

Additionally, the Group had an average of 1,132 (2019: 1,196) employees during the year based in Singapore, the USA, Germany and the Crown Dependencies.

7 Operating expenses (continued)

Fees payable to the Bank's auditors

	2020 £m	2019 £m
Fees payable for the audit of the Bank's current year annual report	**2.1**	2.2
Audit of the Bank's subsidiaries pursuant to legislation	**0.4**	0.5
Other services provided pursuant to legislation	**0.2**	0.2
Other services – audit related fees	**0.1**	0.2
Total fees payable to the Bank's auditors	**2.8**	3.1

The following types of services are included in the categories listed above:

Audit fees: This category includes fees in respect of the audit of the Group's annual financial statements and other services in connection with regulatory filings.

Audit related fees: This category includes fees in respect of services for assurance and related services that are reasonably related to the performance of the audit or review of the financial statements, for example acting as reporting accountants in respect of debt prospectuses required by listing rules.

8 Impairment (charge)/credit

	Stage 1 £m	Stage 2 £m	Stage 3 £m	Total £m
Year ended 31 December 2020				
Impact of transfers between stages	**1**	**(14)**	**–**	**(13)**
Other changes in credit quality	**(37)**	**(16)**	**(9)**	**(62)**
Additons (repayments)	**(20)**	**(3)**	**(1)**	**(24)**
Methodology and model changes	**13**	**–**	**–**	**13**
Other items	**–**	**–**	**15**	**15**
Total impairment	**(43)**	**(33)**	**5**	**(71)**
In respect of:				
Financial assets at amortised cost				
Loans and advances to banks	**(1)**	**–**	**–**	**(1)**
Loans and advances to customers	**(20)**	**(19)**	**5**	**(34)**
Loan commitments and financial guarantees	**(22)**	**(14)**	**–**	**(36)**
Total impairment	**(43)**	**(33)**	**5**	**(71)**

	Stage 1 £m	Stage 2 £m	Stage 3 £m	Total £m
Year ended 31 December 2019				
Other changes in credit quality	1	1	1	3
Additions (repayment)	(1)	(1)	10	8
Methodology and model changes	–	–	–	–
Total impairment	–	–	11	11
In respect of:				
Financial assets at amortised cost				
Loans and advances to customers	1	–	11	12
Loan commitments and financial guarantees	(1)	–	–	(1)
Total impairment	–	–	11	11

The Group's impairment (charge)/credit comprises the following items:

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 quality, but which have not resulted in a transfer to a different stage. This also contains the impact on the impairment charge as a result of write-offs and recoveries, where the related loss allowances are reassessed to reflect ultimate realisable or recoverable value.

8 Impairment (charge)/credit (continued)

Additions (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 as a result of repayments of outstanding balances.

Methodology and model changes
Increase or decrease in impairment charge as a result of adjustments to the models used for expected credit loss calculations; either as changes to the model inputs or to the underlying assumptions as well as the impact of changing the models used.

Movements in the Group's impairment allowances are shown in note 13.

9 Directors' emoluments
The directors' emoluments payable for services provided to the Bank are set out below:

	2020 £000s	2019 £000s
Executive directors	**1,294**	1,684
Non-executive directors	**717**	804
	2,011	2,488

Highest paid director:	**896**	1,095

10 Tax expense

a Analysis of tax expense for the year

	2020 £m	2019 £m
UK corporation tax:		
– Current tax on profit for the year	**6**	73
– Adjustments in respect of prior years	**2**	(3)
Foreign tax:		
– Current tax on profit for the year	**7**	16
– Adjustments in respect of prior years	**–**	–
Current tax expense	**15**	86
UK deferred tax:		
– Origination and reversal of temporary differences	**1**	(2)
– Adjustments in respect of prior years	**(1)**	1
Foreign deferred tax:		
– Origination and reversal of temporary differences	**(10)**	–
– Adjustments in respect of prior years	**(4)**	–
Deferred tax credit (see note 19)	**(14)**	(1)
Tax expense	**1**	85

UK corporation tax is calculated at a rate of 19 per cent (2019: 19 per cent) of the taxable profit for the year.

b Factors affecting the tax expense for the year
An explanation of the relationship between tax expense and accounting profit is set out below:

	2020 £m	2019 £m
Profit before tax	**45**	368
Tax thereon at UK corporation tax rate of 19% (2019: 19%)	**(9)**	(70)
Factors affecting (charge)/credit:		
– Bank levy	**(5)**	–
– Impact of surcharge on banking profits	**(2)**	(23)
– Non-deductible costs	**(1)**	(6)
– Tax relief on coupons on other equity instruments	**8**	9
– Non-taxable income and other deductions	**9**	–
– Recognition of temporary differences that arise in prior year	**6**	–
– Other adjustments in respect of prior years	**(3)**	2
– Temporary differences not recognised	**(3)**	–
– Differences in overseas tax rates	**(2)**	3
– Other	**1**	–
Tax expense on profit on ordinary activities	**(1)**	(85)
Effective rate	**2.2%**	23.1%

11 Financial assets at fair value through profit or loss

	The Group		The Bank	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Trading assets	**20,262**	17,732	**20,262**	17,732
Other financial assets mandatorily at fair value through profit or loss	**664**	414	**579**	327
Total	**20,926**	18,146	**20,841**	18,059

These assets are comprised as follows:

	The Group				The Bank			
	2020		2019		**2020**		2019	
	Trading assets £m	**Other financial assets mandatorily at fair value through profit or loss £m**	Trading assets £m	Other financial assets mandatorily at fair value through profit or loss £m	**Trading assets £m**	**Other financial assets mandatorily at fair value through profit or loss £m**	Trading assets £m	Other financial assets mandatorily at fair value through profit or loss £m
Loans and advances to customers	**12,766**	**353**	10,422	326	**12,766**	**353**	10,422	326
Loans and advances to banks	**229**	**–**	513	–	**229**	**–**	513	–
Debt securities:								
Government securities	**6,983**	**–**	6,501	–	**6,983**	**–**	6,501	–
Bank and building society certificates of deposit	**–**	**66**	–	68	**–**	**–**	–	–
Asset-backed securities:								
Mortgage-backed securities	**7**	**–**	6	–	**7**	**–**	6	–
Other asset-backed securities	**4**	**–**	17	–	**4**	**–**	17	–
Corporate and other debt securities	**273**	**223**	273	1	**273**	**223**	273	1
	7,267	**289**	6,797	69	**7,267**	**223**	6,797	1
Equity shares	**–**	**3**	–	–	**–**	**3**	–	–
Treasury bills and other bills	**–**	**19**	–	19	**–**	**–**	–	–
Total	**20,262**	**664**	17,732	414	**20,262**	**579**	17,732	327

At 31 December 2020 £7,633 million (2019: £6,885 million) of trading and other financial assets at fair value through profit or loss of the Group and £7,633 million (2019: £6,885 million) of the Bank had a contractual residual maturity of greater than one year.

For amounts included above which are subject to reverse repurchase agreements see note 31.

During the year the Group and Bank acquired financial assets at fair value through profit or loss of £nil (2019: £633 million).

12 Derivative financial instruments

The Group	2020 Contract/ notional amount £m	2020 Fair value assets £m	2020 Fair value liabilities £m	2019 Contract/ notional amount £m	2019 Fair value assets £m	2019 Fair value liabilities £m
Trading						
Exchange rate contracts:						
Spot, forwards and futures	**55,793**	**947**	**1,057**	41,339	533	654
Currency swaps	**377,768**	**5,001**	**4,959**	360,821	3,887	3,776
Options purchased	**5,769**	**428**	**–**	8,311	452	–
Options written	**7,560**	**–**	**489**	9,558	–	499
	446,890	**6,376**	**6,505**	420,029	4,872	4,929
Interest rate contracts:						
Interest rate swaps	**4,433,732**	**12,594**	**11,784**	3,500,882	11,678	10,406
Forward rate agreements	**554,066**	**12**	**6**	529,314	9	13
Options purchased	**24,507**	**2,572**	**–**	26,568	2,071	–
Options written	**21,053**	**–**	**2,711**	23,701	–	2,150
Futures	**273,727**	**1**	**9**	198,205	5	18
	5,307,085	**15,179**	**14,510**	4,278,670	13,763	12,587
Credit derivatives	**2,228**	**22**	**55**	11,674	9	71
Equity and other contracts	**3,390**	**174**	**160**	4,731	177	169
Total derivative assets/liabilities held for trading	**5,759,593**	**21,751**	**21,230**	4,715,104	18,821	17,756
Hedging						
Derivatives designated as fair value hedges:						
Interest rate swaps	**7,700**	**1**	**–**	4,126	2	–
Derivatives designated as cash flow hedges:						
Interest rate swaps	**9,750**	**5**	**3**	10,844	13	6
Total derivative assets/liabilities held for hedging	**17,450**	**6**	**3**	14,970	15	6
Total recognised derivative assets/liabilities	**5,777,043**	**21,757**	**21,233**	4,730,074	18,836	17,762

The notional amount of the contract does not represent the Group's exposure to credit risk which is limited to the current cost of replacing contracts with a positive value to the Group should the counterparty default. To reduce credit risk the Group uses a variety of credit enhancement techniques such as netting and collateralisation, where security is provided against the exposure; a large proportion of the Group's derivatives are held through exchanges such as London Clearing House and are collateralised through those exchanges. Further details are provided in note 34 Credit risk.

12 Derivative financial instruments (continued)

	2020			2019		
The Bank	**Contract/ notional amount £m**	**Fair value assets £m**	**Fair value liabilities £m**	Contract/ notional amount £m	Fair value assets £m	Fair value liabilities £m
Trading						
Exchange rate contracts:						
Spot, forwards and futures	**55,793**	**947**	**1,057**	41,339	533	654
Currency swaps	**377,768**	**5,001**	**4,959**	360,821	3,887	3,776
Options purchased	**5,769**	**428**	**–**	8,311	452	–
Options written	**7,560**	**–**	**489**	9,558	–	499
	446,890	**6,376**	**6,505**	420,029	4,872	4,929
Interest rate contracts:						
Interest rate swaps	**4,433,847**	**12,655**	**11,784**	3,500,997	11,734	10,406
Forward rate agreements	**554,066**	**12**	**6**	529,314	9	13
Options purchased	**24,507**	**2,572**	**–**	26,568	2,071	–
Options written	**21,053**	**–**	**2,711**	23,701	–	2,150
Futures	**273,727**	**1**	**9**	198,205	5	18
	5,307,200	**15,240**	**14,510**	4,278,785	13,819	12,587
Credit derivatives	**2,228**	**22**	**55**	11,674	9	71
Equity and other contracts	**3,390**	**174**	**160**	4,731	177	169
Total derivative assets/liabilities held for trading	**5,759,708**	**21,812**	**21,230**	4,715,219	18,877	17,756
Hedging						
Derivatives designated as fair value hedges:						
Interest rate swaps	**7,700**	**1**	**–**	4,126	2	–
Derivatives designated as cash flow hedges:						
Interest rate swaps	**9,750**	**5**	**3**	10,844	13	6
Total derivative assets/liabilities held for hedging	**17,450**	**6**	**3**	14,970	15	6
Total recognised derivative assets/liabilities	**5,777,158**	**21,818**	**21,233**	4,730,189	18,892	17,762

12 Derivative financial instruments (continued)

At 31 December 2020 £17,497 million of total recognised derivative assets of the Group (2019: £13,874 million) and £17,558 million of the Bank (2019: £13,874 million) and £16,992 million of total recognised derivative liabilities of the Group and the Bank (2019: £12,139 million) had a contractual residual maturity of greater than one year.

The amounts for the derivative assets and liabilities in the above tables include the amounts offset in note 33.

The principal derivatives used by the Group are as follows:

– Interest rate related contracts include interest rate swaps, forward rate agreements and options. An interest rate swap is an agreement between two parties to exchange fixed and floating interest payments, based upon interest rates defined in the contract, without the exchange of the underlying principal amounts. Forward rate agreements are contracts for the payment of the difference between a specified rate of interest and a reference rate, applied to a notional principal amount at a specific date in the future. An interest rate option gives the buyer, on payment of a premium, the right, but not the obligation, to fix the rate of interest on a future loan or deposit, for a specified period and commencing on a specified future date.

– Exchange rate related contracts include forward foreign exchange contracts, currency swaps and options. A forward foreign exchange contract is an agreement to buy or sell a specified amount of foreign currency on a specified future date at an agreed rate. Currency swaps generally involve the exchange of interest payment obligations denominated in different currencies; the exchange of principal can be notional or actual. A currency option gives the buyer, on payment of a premium, the right, but not the obligation, to sell specified amounts of currency at agreed rates of exchange on or before a specified future date.

The notional amount of the contract does not represent the Group's real exposure to credit risk which is limited to the current cost of replacing contracts with a positive value to the Group should the counterparty default.

To reduce credit risk the Group uses a variety of credit enhancement techniques such as netting and collateralisation, where security is provided against the exposure. Further details are provided in note 34 Credit risk.

Details of the Group's hedging instruments are set out below:

	Maturity					
The Group and the Bank – 31 December 2020	**Up to 1 month £m**	**1-3 months £m**	**3 months - 1 year £m**	**1-5 years £m**	**More than 5 years £m**	**Total £m**
Fair value hedges						
Interest rate						
Interest rate swap						
Notional	–	–	**575**	**5,076**	**2,049**	**7,700**
Average fixed interest rate	–	–	**0.40%**	**0.74%**	**1.37%**	
Cash flow hedges						
Interest rate						
Interest rate swap						
Notional	–	**165**	**1,016**	**4,633**	**3,936**	**9,750**
Average fixed interest rate	–	**0.98%**	**0.65%**	**0.87%**	**1.06%**	

	Maturity					
The Group and the Bank – 31 December 2019	Less than 1 month £m	1-3 months £m	3 months - 1 year £m	1-5 years £m	More than 5 years £m	Total £m
Fair value hedges						
Interest rate						
Interest rate swap						
Notional	–	–	–	2,958	1,168	4,126
Average fixed interest rate	–	–	–	0.27%	2.66%	
Cash flow hedges						
Interest rate						
Interest rate swap						
Notional	280	165	2,187	3,530	4,682	10,844
Average fixed interest rate	0.81%	0.91%	0.18%	1.03%	1.11%	

12 Derivative financial instruments (continued)

The carrying amounts of the Group's hedging instruments are as follows:

The Group and the Bank – 31 December 2020	Contract/notional amount £m	Carrying amount Assets £m	Carrying amount Liabilities £m	Changes in fair value used for calculating hedge ineffectiveness £m
Fair value hedges				
Interest rate				
Interest rate swaps	**7,700**	**1**	**–**	**121**
Cash flow hedges				
Interest rate				
Interest rate swaps	**9,750**	**5**	**3**	**80**

The Group and the Bank – 31 December 2019	Contract/notional amount £m	Carrying amount Assets £m	Carrying amount Liabilities £m	Changes in fair value used for calculating hedge ineffectiveness £m
Fair value hedges				
Interest rate				
Interest rate swaps	4,126	2	–	143
Cash flow hedges				
Interest rate				
Interest rate swaps	10,844	13	6	73

All amounts are held within derivative financial instruments.

The Group's hedged items are as follows:

The Group and the Bank – 31 December 2020	Carrying amount of the hedged item		Accumulated amount of fair value adjustment on the hedged item		Change in fair value of hedged item for ineffectiveness assessment £m	Cash flow hedge/currency translation reserve	
	Assets £m	Liabilities £m	Assets £m	Liabilities £m		Continuing hedges £m	Discontinued hedges £m
Fair value hedges							
Interest rate							
Fixed rate issuance[1]	**–**	**7,887**	**–**	**220**	**(123)**		
Cash flow hedges							
Interest rate							
Customer loans[2]					**(6)**	**31**	**(3)**
Central bank balances[3]					**(69)**	**116**	**–**

The Group and the Bank – 31 December 2019	Carrying amount of the hedged item		Accumulated amount of fair value adjustment on the hedged item		Change in fair value of hedged item for ineffectiveness assessment £m	Cash flow hedge/currency translation reserve	
	Assets £m	Liabilities £m	Assets £m	Liabilities £m		Continuing hedges £m	Discontinued hedges £m
Fair value hedges							
Interest rate							
Fixed rate issuance[1]	–	4,193	–	101	(147)		
Cash flow hedges							
Interest rate							
Customer loans[2]					(22)	29	–
Central bank balances[3]					(46)	46	–

1 Included within debt securities in issue.

2 Included within loans and advances to customers.

3 Included within cash and balances at central banks.

12 Derivative financial instruments (continued)

The accumulated amount of fair value hedge adjustments remaining in the statement of financial position for hedged items that have ceased to be adjusted for hedging gains and losses is £nil.

The cash flow hedge reserve in the previous table is calculated on a pre-deferred tax basis.

The accumulated amount of fair value hedge adjustments remaining in the balance sheet for hedged items that have ceased to be adjusted for hedging gains and losses is £nil (2019: £nil).

Gains and losses arising from hedge accounting are summarised as follows:

			Amounts reclassified from reserves to income statement as:	
The Group and the Bank – 31 December 2020	**Gain (loss) recognised in other comprehensive income £m**	**Hedge ineffectiveness recognised in the income statement[1] £m**	**Hedged item affected income statement £m**	**Income statement line item that includes reclassified amount**
Fair value hedges				
Interest rate				
Fixed rate issuance		**(2)**		
Cash flow hedges				
Interest rate				
Customer loans	**–**	**1**	**(4)**	**Interest income**
Central bank balances	**70**	**9**	**(19)**	**Interest income**

			Amounts reclassified from reserves to income statement as:	
The Group and the Bank – 31 December 2019	Gain (loss) recognised in other comprehensive income £m	Hedge ineffectiveness recognised in the income statement[1] £m	Hedged item affected income statement £m	Income statement line item that includes reclassified amount
Fair value hedges				
Interest rate				
Fixed rate issuance		(4)		
Cash flow hedges				
Interest rate				
Customer loans	23	–	(3)	Interest income
Central bank balances	46	4	(6)	Interest income

1 Hedge ineffectiveness is included in the income statement within net trading income.

There were no amounts reclassified from the cash flow hedging reserve in 2019 or 2020 for which hedge accounting had previously been used but for which the hedged future cash flows are no longer expected to occur.

Trading Portfolios

Exposures

The Group's trading activity is small relative to its peers, and it does not engage in any proprietary trading activities but rather seeks to meet the financial requirements of customers for foreign exchange, secondary credit market liquidity and interest rate products. These activities support customer flow and market making activities.

While the trading positions taken are generally small, any extreme moves in the main risk factors and other related risk factors could cause significant losses in the trading book depending on the positions at the time. The average 95 per cent 1-day trading VaR (Value at Risk; diversified across risk factors) was £0.8 million for 31 December 2020 and 2019. The main risk type areas are interest rate risk, foreign exchange risk and credit spread risk with individual VaR between £0.1 million and £0.8 million which peaked at £1.2 million during the year for interest rate risk.

Trading market risk measures are applied to all of the Group's regulatory trading books and they include daily VaR, sensitivity based measures, and stress testing calculations.

Measurement

The Group internally uses VaR as the primary risk measure for all trading book positions. The risk of loss measured by the VaR model is the minimum expected loss in earnings given the 95 per cent confidence over one day.

The market risk for the trading book continues to be low with respect to peers. This reflects the fact that the Group's trading operations are customer-centric and focused on hedging and managing client risks.

Although it is an important market standard measure of risk, VaR has limitations. One of them is the use of a limited historical data sample which influences the output by the implicit assumption that future market behaviour will not differ greatly from the historically observed period. Another known limitation is the use of defined holding periods which assumes that the risk can be liquidated or hedged within that holding period. Also calculating the VaR at the chosen confidence interval does not give enough information about potential losses which may occur if this level is exceeded. The Group fully recognises these limitations and supplements the use of VaR with a variety of other measurements which reflect the nature of the business activity. These include detailed sensitivity analysis, position reporting and a stress testing programme.

Trading book VaR (1-day 99 per cent) is compared daily against both hypothetical and actual profit and loss. The 1-day 99 per cent VaR charts for the Group can be found in Lloyds Banking Group's Pillar 3 Report.

Mitigation

The level of exposure is controlled by establishing and communicating the approved risk limits and controls through policies and procedures that define the responsibility and authority for risk taking. Market risk limits are clearly and consistently communicated to the business. Any new or emerging risks are brought within risk reporting and defined limits.

12 Derivative financial instruments (continued)

Monitoring
Trading risk appetite is monitored daily with 1-day 95 per cent VaR and stress testing limits. These limits are complemented with position level action triggers and profit and loss referrals. Risk and position limits are set and managed at both desk and overall trading book levels. VaR and Stress Test limits are reviewed annually and approved by the Board as part of the Group risk appetite framework.

Banking Activities
Interest rate risk
The Group's banking activities expose it to the risk of adverse movements in market rates or prices, predominantly interest rates, credit spread and exchange rates. The volatility of market rates or prices can be affected by both the transparency of prices and the amount of liquidity in the market for the relevant asset, liability or instrument.

The impact on Group net interest income to a +/- 25 bps movement in interest rates has an upside of £6.7 million and a downside of £0.2 million.

13 Financial assets at amortised cost

The Group	Gross Carrying Amount				Allowance for expected credit losses			
Year ended 31 December 2020	Stage 1 £m	Stage 2 £m	Stage 3 £m	Total £m	Stage 1 £m	Stage 2 £m	Stage 3 £m	Total £m
Loans and advances to banks								
At 1 January 2020	4,814	–	–	4,814	1	–	–	1
Exchange and other adjustments	75	–	–	75	–	–	–	–
Additions (repayments)	373	–	–	373	–	–	–	–
Transfer to Stage 2	–	–	–	–	–	–	–	–
Other items charged to the income statement	–	–	–	–	1	–	–	1
Charge to the income statement	–	–	–	–	1	–	–	1
Advances written off	–	–	–	–			–	–
Recoveries of advances written off in previous years	–	–	–	–			–	–
Discount unwind	–	–	–	–			–	–
At 31 December 2020	5,262	–	–	5,262	2	–	–	2
Allowance for impairment losses	(2)	–	–	(2)				
Net carrying amount	5,260	–	–	5,260				
Loans and advances to customers								
At 1 January 2020	20,028	29	293	20,350	7	2	77	86
Exchange and other adjustments	301	(74)	(222)	5	(1)	(1)	(8)	(10)
Acquisition of portfolios	–	–	–	–				
Transfer to Stage 1	3	(3)	–	–	2	(2)	–	–
Transfer to Stage 2	(339)	339	–	–	–	–	–	–
Transfer to Stage 3	(3)	(29)	32	–	–	–	–	–
Impact of transfers between stages	(339)	307	32	–	(2)	3	–	1
					–	1	–	1
Additions (repayments)	(1,908)	117	(3)	(1,794)	13	2	1	16
Other items charged/(credited) to the income statement	–	–	–	–	7	16	(6)	17
Charge/(credit) to the income statement	–	–	–	–	20	19	(5)	34
Advances written off	–	–	(61)	(61)			(61)	(61)
Recoveries of advances written off in previous years	–	–	–	–			–	–
Discount unwind	–	–	–	–			(1)	(1)
At 31 December 2020	18,082	379	39	18,500	26	20	2	48
Allowance for impairment losses	(26)	(20)	(2)	(48)				
Net carrying amount	18,056	359	37	18,452				
Debt securities								
At 1 January 2020	112	–	–	112	–	–	–	–
Exchange and other adjustments	(4)	–	–	(4)	–	–	–	–
Additions (repayments)	149	–	–	149	–	–	–	–
Financial assets that have been written during the year	–	–	–	–				
At 31 December 2020	257	–	–	257	–	–	–	–
Allowance for impairment losses	–	–	–	–				
Net carrying amount	257	–	–	257				
Due from fellow Lloyds Banking Group undertakings	1,118	–	–	1,118				
Net carrying amount	1,118	–	–	1,118				
Total financial assets at amortised cost	24,691	359	37	25,087				

During the year, a Stage 3 customer was restructured with £57 million of gross advances written off and a £57 million impairment provision utilised. The remaining gross advances balance of £222 million was transferred to a new debt securities financial asset classified at fair value through profit or loss.

13 Financial assets at amortised cost (continued)

Movements in allowance for expected credit losses in respect of undrawn balances were as follows:

The Group	Allowance for expected credit losses Stage 1 £m	Stage 2 £m	Stage 3 £m	Total £m
Undrawn balances				
At 1 January 2020	4	–	–	4
Exchange and other adjustments	(6)	(1)	–	(7)
Transfers to Stage 1	–	–	–	–
Transfers to Stage 2	(1)	1	–	–
Transfers to Stage 3	–	–	–	–
Impact of transfers between stages	–	12	–	12
	(1)	13	–	12
Other items charged to the income statement	23	1	–	24
Charge to the income statement	22	14	–	36
At 31 December 2020	20	13	–	33

The Group's total impairment allowances were as follows:

The Group	Allowance for expected credit losses Stage 1 £m	Stage 2 £m	Stage 3 £m	Total £m
In respect of:				
Loans and advances to banks	2	–	–	2
Loans and advances to customers	26	20	2	48
Debt securities	–	–	–	–
Due from fellow Lloyds Banking Group undertakings	–	–	–	–
Financial assets at amortised cost	28	20	2	50
Provisions in relation to loan commitments and financial guarantees	20	13	–	33
Total	48	33	2	83

13 Financial assets at amortised cost (continued)

The Group	Gross Carrying Amount				Allowance for expected credit losses			
Year ended 31 December 2019	Stage 1 £m	Stage 2 £m	Stage 3 £m	Total £m	Stage 1 £m	Stage 2 £m	Stage 3 £m	Total £m
Loans and advances to banks								
At 1 January 2019	2,584	–	–	2,584	1	–	–	1
Exchange and other adjustments	(95)	–	–	(95)	–	–	–	–
Additions (repayments)	2,325	–	–	2,325	–	–	–	–
Transfer to Stage 2	–	–	–	–	–	–	–	–
Other items charged to the income statement	–	–	–	–	–	–	–	–
Charge to the income statement	–	–	–	–	–	–	–	–
Advances written off	–	–	–	–			–	–
Recoveries of advances written off in previous years	–	–	–	–			–	–
Discount unwind	–	–	–	–			–	–
At 31 December 2019	4,814	–	–	4,814	1	–	–	1
Allowance for impairment losses	(1)	–	–	(1)				
Net carrying amount	4,813	–	–	4,813				
Loans and advances to customers								
At 1 January 2019	20,459	23	303	20,785	7	2	92	101
Exchange and other adjustments	(154)	–	(1)	(155)	1	–	(3)	(2)
Acquisition of portfolios	–	–	–	–				
Transfer to Stage 1	–	–	–	–	–	–	–	–
Transfer to Stage 2	(32)	32	–	–	–	–	–	–
Transfer to Stage 3	–	(4)	4	–	–	–	–	–
Impact of transfers between stages	(32)	28	4	–	–	–	–	–
					–	–	–	–
Additions (repayments)	(245)	(22)	(12)	(279)	–	1	(8)	(7)
Other items charged to the income statement	–	–	–	–	(1)	(1)	(3)	(5)
Charge to the income statement	–	–	–	–	(1)	–	(11)	(12)
Advances written off	–	–	(1)	(1)			(1)	(1)
Recoveries of advances written off in previous years	–	–	–	–			1	1
Discount unwind	–	–	–	–			(1)	(1)
At 31 December 2019	20,028	29	293	20,350	7	2	77	86
Allowance for impairment losses	(7)	(2)	(77)	(86)				
Net carrying amount	20,021	27	216	20,264				
Debt securities								
At 1 January 2019	132	–	–	132	–	–	–	–
Exchange and other adjustments	(4)	–	–	(4)	–	–	–	–
Additions (repayments)	(16)	–	–	(16)	–	–	–	–
Financial assets that have been written during the year	–	–	–	–			–	–
At 31 December 2019	112	–	–	112	–	–	–	–
Allowance for impairment losses	–	–	–	–				
Net carrying amount	112	–	–	112				
Due from fellow Lloyds Banking Group undertakings	710	–	–	710				
Net carrying amount	710	–	–	710				
Total financial assets at amortised cost	25,656	27	216	25,899				

13 Financial assets at amortised cost (continued)

Movements in allowance for expected credit losses in respect of undrawn balances were as follows:

	Allowance for expected credit losses			
The Group	Stage 1 £m	Stage 2 £m	Stage 3 £m	Total £m
Undrawn balances				
At 1 January 2019	3	–	–	3
Exchange and other adjustments	–	–	–	–
Transfers to Stage 1	–	–	–	–
Transfers to Stage 2	–	–	–	–
Transfers to Stage 3	–	–	–	–
Impact of transfers between stages	–	–	–	–
	–	–	–	–
Other items charged to the income statement	1	–	–	1
Charge to the income statement	1	–	–	1
At 31 December 2019	4	–	–	4

The Group's total impairment allowances were as follows:

	Allowance for expected credit losses			
The Group	Stage 1 £m	Stage 2 £m	Stage 3 £m	Total £m
In respect of:				
Loans and advances to banks	1	–	–	1
Loans and advances to customers	7	2	77	86
Debt securities	–	–	–	–
Due from fellow Lloyds Banking Group undertakings	–	–	–	–
Financial assets at amortised cost	8	2	77	87
Provisions in relation to loan commitments and financial guarantees	4	–	–	4
Total	12	2	77	91

13 Financial assets at amortised cost (continued)

The Bank	Gross Carrying Amount				Allowance for expected credit losses			
Year ended 31 December 2020	Stage 1 £m	Stage 2 £m	Stage 3 £m	Total £m	Stage 1 £m	Stage 2 £m	Stage 3 £m	Total £m
Loans and advances to banks								
At 1 January 2020	4,793	–	–	4,793	1	–	–	1
Exchange and other adjustments	75	–	–	75	–	–	–	–
Additions (repayments)	365	–	–	365	–	–	–	–
Transfer to Stage 2	–	–	–	–	–	–	–	–
Other items charged to the income statement	–	–	–	–	1	–	–	1
Charge to the income statement	–	–	–	–	1	–	–	1
Advances written off	–	–	–	–			–	–
Recoveries of advances written off in previous years	–	–	–	–			–	–
Discount unwind	–	–	–	–			–	–
At 31 December 2020	5,233	–	–	5,233	2	–	–	2
Allowance for impairment losses	(2)	–	–	(2)				
Net carrying amount	5,231	–	–	5,231				
Loans and advances to customers								
At 1 January 2020	19,759	19	293	20,071	6	2	77	85
Exchange and other adjustments	300	(75)	(222)	3	(1)	(1)	(8)	(10)
Acquisition of portfolios	–	–	–	–				
Transfer to Stage 1	1	(1)	–	–	2	(2)	–	–
Transfer to Stage 2	(331)	331	–	–	–	–	–	–
Transfer to Stage 3	(2)	(29)	31	–	–	–	–	–
Impact of transfers between stages	(332)	301	31	–	(2)	3	–	1
					–	1	–	1
Additions (repayments)	(1,894)	119	(3)	(1,778)	13	2	1	16
Other items charged/(credited) to the income statement	–	–	–	–	7	16	(7)	16
Charge/(credit) to the income statement	–	–	–	–	20	19	(6)	33
Advances written off	–	–	(60)	(60)			(60)	(60)
Recoveries of advances written off in previous years	–	–	–	–			–	–
Discount unwind	–	–	–	–			(1)	(1)
At 31 December 2020	17,833	364	39	18,236	25	20	2	47
Allowance for impairment losses	(25)	(20)	(2)	(47)				
Net carrying amount	17,808	344	37	18,189				
Debt securities								
At 1 January 2020	112	–	–	112	–	–	–	–
Exchange and other adjustments	(4)	–	–	(4)	–	–	–	–
Additions (repayments)	149	–	–	149	–	–	–	–
Financial assets that have been written during the year	–	–	–	–			–	–
At 31 December 2020	257	–	–	257	–	–	–	–
Allowance for impairment losses	–	–	–	–				
Net carrying amount	257	–	–	257				
Due from fellow Lloyds Banking Group undertakings	1,218	–	–	1,218				
Net carrying amount	1,218	–	–	1,218				
Total financial assets at amortised cost	24,514	344	37	24,895				

During the year, a Stage 3 customer was restructured with £57 million of gross advances written off and a £57 million impairment provision utilised. The remaining gross advances balance of £222 million was transferred to a new debt securities financial asset classified at fair value through profit or loss.

13 Financial assets at amortised cost (continued)

Movements in allowance for expected credit losses in respect of undrawn balances were as follows:

	Allowance for expected credit losses			
The Bank	**Stage 1 £m**	**Stage 2 £m**	**Stage 3 £m**	**Total £m**
Undrawn balances				
At 1 January 2020	4	–	–	4
Exchange and other adjustments	(6)	(1)	–	(7)
Transfers to Stage 1	–	–	–	–
Transfers to Stage 2	(1)	1	–	–
Transfers to Stage 3	–	–	–	–
Impact of transfers between stages	–	12	–	12
	(1)	13	–	12
Other items charged to the income statement	23	1	–	24
Charge to the income statement	22	14	–	36
At 31 December 2020	20	13	–	33

The Bank's total impairment allowances were as follows:

	Allowance for expected credit losses			
The Bank	**Stage 1 £m**	**Stage 2 £m**	**Stage 3 £m**	**Total £m**
In respect of:				
Loans and advances to banks	2	–	–	2
Loans and advances to customers	25	20	2	47
Debt securities	–	–	–	–
Due from fellow Lloyds Banking Group undertakings	–	–	–	–
Financial assets at amortised cost	27	20	2	49
Provisions in relation to loan commitments and financial guarantees	20	13	–	33
Total	47	33	2	82

13 Financial assets at amortised cost (continued)

The Bank	Gross Carrying Amount				Allowance for expected credit losses			
Year ended 31 December 2019	Stage 1 £m	Stage 2 £m	Stage 3 £m	Total £m	Stage 1 £m	Stage 2 £m	Stage 3 £m	Total £m
Loans and advances to banks								
At 1 January 2019	2,562	–	–	2,562	1	–	–	1
Exchange and other adjustments	(94)	–	–	(94)	–	–	–	–
Acquisitions	8	–	–	8	–	–	–	–
Additions (repayments)	2,317	–	–	2,317	–	–	–	–
Transfer to Stage 2	–	–	–	–	–	–	–	–
Other items charged to the income statement	–	–	–	–	–	–	–	–
Charge to the income statement	–	–	–	–	–	–	–	–
Advances written off	–	–	–	–			–	–
Recoveries of advances written off in previous years	–	–	–	–			–	–
Discount unwind	–	–	–	–			–	–
At 31 December 2019	4,793	–	–	4,793	1	–	–	1
Allowance for impairment losses	(1)	–	–	(1)				
Net carrying amount	4,792	–	–	4,792				
Loans and advances to customers								
At 1 January 2019	16,849	–	277	17,126	5	–	82	87
Exchange and other adjustments	(153)	–	–	(153)	–	–	(2)	(2)
Acquisition of portfolios	2,975	5	17	2,997	1	–	7	8
Transfer to Stage 1	–	–	–	–	–	–	–	–
Transfer to Stage 2	(31)	31	–	–	–	–	–	–
Transfer to Stage 3	1	–	(1)	–	–	–	–	–
Impact of transfers between stages	(30)	31	(1)	–	–	–	–	–
					–	–	–	–
Additions (repayments)	118	(17)	–	101	–	2	(5)	(3)
Other items charged to the income statement	–	–	–	–	–	–	(4)	(4)
Charge to the income statement	–	–	–	–	–	2	(9)	(7)
Advances written off	–	–	–	–			–	–
Recoveries of advances written off in previous years	–	–	–	–			–	–
Discount unwind	–	–	–	–			(1)	(1)
At 31 December 2019	19,759	19	293	20,071	6	2	77	85
Allowance for impairment losses	(6)	(2)	(77)	(85)				
Net carrying amount	19,753	17	216	19,986				
Debt securities								
At 1 January 2019	132	–	–	132	–	–	–	–
Exchange and other adjustments	(4)	–	–	(4)	–	–	–	–
Additions (repayments)	(16)	–	–	(16)	–	–	–	–
Financial assets that have been written during the year	–	–	–	–			–	–
At 31 December 2019	112	–	–	112	–	–	–	–
Allowance for impairment losses	–	–	–	–				
Net carrying amount	112	–	–	112				
Due from fellow Lloyds Banking Group undertakings	819	–	–	819				
Net carrying amount	819	–	–	819				
Total financial assets at amortised cost	25,476	17	216	25,709				

13 Financial assets at amortised cost (continued)

Movements in allowance for expected credit losses in respect of undrawn balances were as follows:

	Allowance for expected credit losses			
The Bank	Stage 1 £m	Stage 2 £m	Stage 3 £m	Total £m
Undrawn balances				
At 1 January 2019	3	–	–	3
Exchange and other adjustments	–	–	–	–
Transfers to Stage 1	–	–	–	–
Transfers to Stage 2	–	–	–	–
Transfers to Stage 3	–	–	–	–
Impact of transfers between stages	–	–	–	–
	–	–	–	–
Other items charged to the income statement	1	–	–	1
Charge to the income statement	1	–	–	1
At 31 December 2019	4	–	–	4

The Bank's total impairment allowances were as follows:

	Allowance for expected credit losses			
The Bank	Stage 1 £m	Stage 2 £m	Stage 3 £m	Total £m
In respect of:				
Loans and advances to banks	1	–	–	1
Loans and advances to customers	6	2	77	85
Debt securities	–	–	–	–
Due from fellow Lloyds Banking Group undertakings	–	–	–	–
Financial assets at amortised cost	7	2	77	86
Provisions in relation to loan commitments and financial guarantees	4	–	–	4
Total	11	2	77	90

Transfers of assets between stages are deemed to take place at the start of the year. All other movements in the value of the asset are deemed to take place within the Stage under which that asset is reported at the end of the year.

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

At 31 December 2020 £7,976 million of loans and advances to customers of the Group and £7,830 million of the Bank had a contractual residual maturity of greater than one year (2019: £9,465 million of the Group and £9,233 million of the Bank).

14 Finance lease receivables

The Group's finance lease receivables are classified as loans and advances to customers and accounted for at amortised cost. The balance is analysed as follow:

	The Group	
	2020 £m	2019 £m
Gross investment in finance leases, receivable:		
Not later than 1 year	**6**	6
Later than 1 year and not later than 2 years	**7**	7
Later than 2 years and not later than 3 years	**7**	7
Later than 3 years and not later than 4 years	**7**	7
Later than 4 years and not later than 5 years	**8**	7
Later than 5 years	**187**	188
	222	222
Unearned future finance income on finance leases	**(86)**	(85)
Rentals received in advance	**(2)**	(2)
Net investment in finance leases	**134**	135

The net investment in finance leases represents amounts recoverable as follows:

	The Group	
	2020 £m	2019 £m
Not later than 1 year	**(2)**	(1)
Later than 1 year and not later than 2 years	**1**	–
Later than 2 years and not later than 3 years	**1**	1
Later than 3 years and not later than 4 years	**2**	1
Later than 4 years and not later than 5 years	**2**	1
Later than 5 years	**130**	133
Net investment in finance leases	**134**	135

Equipment leased to customers under finance leases primarily relates to structured financing transactions in connection with infrastructure assets. There was no allowance for uncollectable finance lease receivables included in the allowance for impairment losses.

15 Financial assets at fair value through other comprehensive income

	The Group		The Bank	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Debt securities:				
Bank and building society certificates of deposit	–	97	–	97
Asset-backed securities:				
Other asset-backed securities	**113**	121	**113**	121
	113	218	**113**	218
Treasury and other bills	**36**	96	**36**	96
Total financial assets at fair value through other comprehensive income	**149**	314	**149**	314

At 31 December 2020 £115 million (2019: £121 million) of financial assets at fair value through other comprehensive income of the Group and the Bank had a contractual residual maturity of greater than one year.

16 Property, plant and equipment

	The Group				The Bank			
	Premises £m	**Equipment £m**	**Right-of-use asset[1] £m**	**Total £m**	**Premises £m**	**Equipment £m**	**Right-of-use asset[1] £m**	**Total £m**
Cost or valuation:								
At 1 January 2019	10	33	72	115	–	8	56	64
Acquisition of businesses	–	–	–	–	–	23	–	23
Additions	–	4	1	5	–	1	–	1
Disposals	–	(4)	(1)	(5)	–	(1)	–	(1)
At 31 December 2019	10	33	72	115	–	31	56	87
Exchange and other adjustments	**–**	**–**	**(2)**	**(2)**	**–**	**–**	**(2)**	**(2)**
Additions	**3**	**2**	**19**	**24**	**3**	**1**	**16**	**20**
Disposals	**(4)**	**(5)**	**(1)**	**(10)**	**–**	**(3)**	**–**	**(3)**
At 31 December 2020	**9**	**30**	**88**	**127**	**3**	**29**	**70**	**102**
Accumulated depreciation and impairment:								
At 1 January 2019	5	23	–	28	–	2	–	2
Acquisition of businesses	–	–	–	–	–	20	–	20
Charge for the year	2	5	12	19	–	2	9	11
Disposals	–	(4)	–	(4)	–	(1)	–	(1)
At 31 December 2019	7	24	12	43	–	23	9	32
Exchange and other adjustments	**–**	**1**	**(1)**	**–**	**–**	**–**	**(1)**	**(1)**
Charge for the year	**–**	**3**	**13**	**16**	**–**	**3**	**10**	**13**
Disposals	**(4)**	**(5)**	**(1)**	**(10)**	**–**	**(3)**	**–**	**(3)**
At 31 December 2020	**3**	**23**	**23**	**49**	**–**	**23**	**18**	**41**
Balance sheet amount at 31 December 2020	**6**	**7**	**65**	**78**	**3**	**6**	**52**	**61**
Balance sheet amount at 31 December 2019	3	9	60	72	–	8	47	55

1 Primarily premises.

17 Investment in subsidiary undertakings of the Bank

	2020 £m	2019 £m
At 1 January	**295**	908
Additions and capital injections	**–**	27
Disposals	**–**	–
Impairment	**(72)**	(640)
At 31 December	**223**	295

During the year ended 31 December 2020 the Bank wrote down the carrying value of its investments in certain subsidiaries, which followed a review of their financial position and anticipated future activities. Additionally, Lloyds Investment Fund Managers Limited was sold during the year as noted in the strategic report.

During the prior year, £27 million was further invested in Lloyds Bank Corporate Markets Wertpapierhandelsbank GmbH.

On 2nd December 2019, the business and the majority of the assets and liabilities of the Bank's subsidiary, Lloyds Bank International Limited ("LBIL"), were transferred to the Bank. This gave rise to the Bank acquiring net liabilities of £6.1 billion. The transfer was made by way of:-

- A transfer scheme pursuant to Section 3A of and Schedule 1A to the Financial Services Act 2008 approved by the High Court of Justice of the Isle of Man on 25 November 2019 in relation to the transfer of LBIL's Isle of Man branch to Bank's Isle of Man branch
- An application pursuant to Article 48D of and the Schedule to the Banking Business (Jersey) Law 1991 approved in the Royal Court of Jersey on 20 November 2019 in relation to the transfer of the business of LBIL's Jersey branch to Bank's Jersey branch
- A Business Transfer Agreement ("BTA") between LBIL and Bank relating to the transfer of the business of LBIL's Guernsey Branch, to the Guernsey branch of Bank's Guernsey Branch dated 29 November 2019
- A Global Transfer Deed dated 29 November 2019 between LBIL and Bank in addition to the Schemes and the Guernsey BTA in respect of certain specific assets

During the year ended 31 December 2019 the Bank wrote down the carrying value of its investments in certain subsidiaries, which followed a review of their financial position and anticipated future activities.

Certain subsidiary companies currently have insufficient distributable reserves to make dividend payments, however, there were no further significant restrictions on any of the Bank's subsidiaries in paying dividends or repaying loans and advances. All regulated banking subsidiaries are required to maintain capital at levels agreed with the regulators; this may impact those subsidiaries' ability to make distributions.

Details of the subsidiaries and related undertakings are given in note 40 and are incorporated by reference.

18 Other assets

	The Group		The Bank	
	2020 £m	2019 £m	2020 £m	2019 £m
Settlement balances	**997**	69	**997**	67
Other assets and prepayments	**28**	46	**22**	38
	1,025	115	**1,019**	105

19 Deferred taxation

The movement in the deferred tax asset is as follows:

	The Group		The Bank	
	2020 £m	2019 £m	2020 £m	2019 £m
Brought forward	**6**	6	**2**	4
Credit/(charge) for the year (see note 10)	**14**	11	**17**	1
Transfers from other group undertakings	**–**	–	**–**	–
	20	17	**19**	5
Amount (charged)/credited to equity				
– Cash flow hedges	**–**	(7)	**–**	1
– Fair value through other comprehensive income	**–**	(4)	**–**	(4)
– Movement on tax balances included within the Foreign Currency Translation Reserve	**(1)**	–	**(1)**	–
At 31 December	**19**	6	**18**	2

19 Deferred taxation (continued)

The movement in the deferred tax liability is as follows:

	The Group		The Bank	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Brought forward	**(18)**	–	**(16)**	–
Charge for the year (see note 10)	**–**	(10)	**–**	–
Transfers from other group undertakings	**–**	–	**–**	–
	(18)	(10)	**(16)**	–
Amount (charged)/credited to equity				
– Cash flow hedges	**(21)**	(11)	**(21)**	(19)
– Fair value through other comprehensive income	**1**	3	**1**	3
– Other	**–**	–	**1**	–
At 31 December	**(38)**	(18)	**(35)**	(16)

The deferred tax credit in the consolidated income statement comprises the following temporary differences:

	The Group		The Bank	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Accelerated capital allowances	**2**	2	**–**	–
Tax losses carried forward	**2**	(3)	**1**	(1)
IFRS9 impairments deductible in future	**(10)**	–	**(10)**	–
Other temporary differences	**(8)**	–	**(8)**	–
	(14)	(1)	**(17)**	(1)

The deferred tax asset comprises:

	The Group		The Bank	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Accelerated capital allowances	**–**	–	**–**	–
Tax losses carried forward	**2**	4	**1**	2
Subsidiary pension scheme	**–**	2	**–**	–
Cash flow hedges	**–**	–	**–**	–
IFRS9 impairments deductible in future	**10**	–	**10**	–
Other temporary differences	**7**	–	**7**	–
At 31 December	**19**	6	**18**	2

The deferred tax liability comprises:

	The Group		The Bank	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Accelerated capital allowances	**(14)**	(11)	**–**	–
Cash flow hedges	**(39)**	(18)	**(39)**	(18)
Other internal derivatives	**11**	7	**–**	–
Fair value through other comprehensive income	**4**	3	**4**	3
Other temporary differences	**–**	1	**–**	(1)
At 31 December	**(38)**	(18)	**(35)**	(16)

The Finance Act 2016 reduced the main rate of corporation tax to 17% with effect from 1 April 2020. Within the March 2020 Budget, the UK government stated its intention to maintain the corporation tax rate at 19% on 1 April 2020. That rate change was enacted under the Provisional Collection of Taxes Act 1968 on 17 March 2020.

On 3 March 2021, the UK Government announced its intention to increase the rate of corporation tax from 19% to 25% with effect from 1 April 2023. Had this change in corporation tax been enacted on 31 December 2020, the impact would have been to increase the Group's net deferred tax liabilities by approximately £9m. The UK Government also announced that in 2021 it will undertake a review of the surcharge on banking companies, its intention being to ensure that the combined rate of corporation tax and banking surcharge on bank profits does not increase substantially from its current level. The results of this review are expected to be announced later in 2021.

Deferred tax assets of approximately £4 million (2019: £nil) have not been recognised in respect of overseas tax losses and other temporary differences where it is currently not probable that there will be future profits against which they can be used.

20 Financial liabilities at fair value through profit or loss

The Group and the Bank	**2020 £m**	2019 £m
Trading liabilities:		
Liabilities in respect of securities sold under repurchase agreements	**14,997**	11,047
Other deposits	**3**	1
Short positions in securities	**815**	2,736
At 31 December	**15,815**	13,784

At 31 December 2020, the Group and the Bank had £823 million (2019: £2,630 million) of trading and other liabilities at fair value through profit or loss with a contractual residual maturity of greater than one year.

For the fair value of collateral pledged in respect of repurchase agreements see note 31.

21 Debt securities in issue

The Group and the Bank	**2020 £m**	2019 £m
Medium-term notes issued	**4,891**	2,208
Certificates of deposit issued	**4,405**	5,674
Commercial paper	**2,610**	957
Amounts due to fellow Group undertakings	**3,696**	3,590
At 31 December	**15,602**	12,429

At 31 December 2020 £7,107 million (2019: £2,578 million) of debt securities in issue of the Group and of the Bank had a contractual residual maturity of greater than one year.

22 Other liabilities

	The Group		The Bank	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Settlement balances	**876**	390	**875**	390
Lease liabilities (see below)	**71**	65	**55**	48
Other creditors and accruals	**98**	122	**90**	112
At 31 December	**1,045**	577	**1,020**	550

The maturity of the lease liabilities was as follows

	The Group		The Bank	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Not later than 1 year	**8**	3	**1**	–
Later than 1 year and not later than 2 years	**4**	2	**1**	–
Later than 2 years and not later than 3 years	**23**	16	**17**	14
Later than 3 years and not later than 4 years	**1**	2	**1**	1
Later than 4 years and not later than 5 years	**5**	2	**5**	1
Later than 5 years	**30**	40	**30**	32
At 31 December	**71**	65	**55**	48

23 Subordinated liabilities

The movement in subordinated liabilities during the year was as follows:

The Group and the Bank	Dated subordinated 2020 £m	Dated subordinated 2019 £m
At 1 January	**698**	725
Issued during the year	**–**	–
Repurchases and redemptions during the year	**–**	–
Foreign exchange movements	**(11)**	(27)
Other movements	**(1)**	–
At 31 December	**686**	698

24 Share capital

The Group and the Bank	2020 £m	2019 £m
Allotted, issued and fully paid		
120,050,000 (2019: 120,050,000) ordinary shares of £1 each	**120**	120

Share capital and control
There are no limitations on voting rights or restrictions on the transfer of shares in the Bank other than as set out in the articles of association, and certain restrictions which may from time to time be imposed by law and regulations (for example, insider trading laws).

Ordinary shares
The holders of ordinary shares, who held 100 per cent of the total ordinary share capital at 31 December 2020, are entitled to receive the Bank's report and accounts, attend, speak and vote at general meetings and appoint proxies to exercise voting rights. Holders of ordinary shares may also receive a dividend (subject to the provisions of the Bank's articles of association) and on a winding up may share in the assets of the Bank.

25 Other reserves

	The Group		The Bank	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Other reserves comprise:				
Revaluation reserve in respect of debt securities held at fair value through other comprehensive income	**(10)**	(9)	**(10)**	(9)
Cash flow hedging reserve	**105**	56	**105**	56
Foreign currency translation reserve	**(14)**	(15)	**(12)**	(16)
At 31 December	**81**	32	**83**	31

The revaluation reserve in respect of debt securities held at fair value through other comprehensive income represents the cumulative after tax unrealised change in the fair value of financial assets so classified since initial recognition.

The cash flow hedging reserve represents the cumulative after tax gains and losses on effective cash flow hedging instruments that will be reclassified to the income statement in the periods in which the hedged item affects profit or loss.

The foreign currency translation reserve represents the cumulative after-tax gains and losses on the translation of foreign operations and exchange differences arising on financial instruments designated as hedges of the Group's net investment in foreign operations.

25 Other reserves (continued)

Movements in other reserves were as follows:

	The Group		The Bank	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Revaluation reserve in respect of debt securities held at fair value through other comprehensive income				
At 1 January	**(9)**	(7)	**(9)**	(7)
Change in fair value	**(2)**	(1)	**(2)**	(1)
Transfers in	–	–	**–**	–
Deferred Tax	**1**	(1)	**1**	(1)
Current Tax	**–**	–	**–**	–
	(1)	(2)	**(1)**	(2)
Realised gains and losses transferred to other comprehensive income				
Disposals	**–**	–	**–**	–
Deferred Tax	**–**	–	**–**	–
Current Tax	**–**	–	**–**	–
	–	–	**–**	–
At 31 December	**(10)**	(9)	**(10)**	(9)

	The Group		The Bank	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Cash flow hedging reserve				
At 1 January	**56**	5	**56**	5
Change in fair value of hedging derivatives	**93**	78	**93**	78
Deferred Tax	**(27)**	(20)	**(27)**	(20)
	66	58	**66**	58
Income statement transfers	**(23)**	(9)	**(23)**	(9)
Deferred Tax	**6**	2	**6**	2
	(17)	(7)	**(17)**	(7)
At 31 December	**105**	56	**105**	56

	The Group		The Bank	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Foreign currency translation reserve				
At 1 January	**(15)**	(13)	**(16)**	(15)
Currency translation differences arising in the year	**1**	(2)	**4**	(1)
At 31 December	**(14)**	(15)	**(12)**	(16)

26 Retained profits

	The Group		The Bank	
	2020 £m	2019 £m	**2020 £m**	2019 £m
At 1 January	**3,342**	3,105	**3,442**	3,087
Profit/(Loss) for the year attributable to ordinary shareholders[1]	**4**	234	**(31)**	348
Dividends paid	**(700)**	–	**(700)**	–
Other adjustments	**–**	3	**–**	7
At 31 December	**2,646**	3,342	**2,711**	3,442

1 No income statement has been shown for the Bank, as permitted by Section 408 of the Companies Act 2006.

27 Other equity instruments

The Group and the Bank	**2020 £m**	2019 £m
At 1 January	**782**	782
Profit for the year attributable to other equity instruments	**40**	49
Distributions on other equity instruments	**(40)**	(49)
At 31 December	**782**	782

The Bank has in issue £782 million of Dollar and Euro Additional Tier 1 (AT1) securities to Lloyds Banking Group plc. The AT1 securities are floating rate Perpetual Subordinated Permanent Write-Down Securities with no fixed maturity or redemption date.

The principal terms of the AT1 securities are described below:

- The securities rank behind the claims against the Bank of unsubordinated creditors on a Winding-Up
- The fixed rate reset securities bear a fixed rate of interest until the first call date. After the initial call date, in the event that they are not redeemed, the fixed rate reset AT1 securities will bear interest at rates fixed periodically in advance. The floating rate AT1 securities will be reset quarterly both prior to and following the first call date
- Interest on the securities will be due and payable only at the sole discretion of the Bank and the Bank may at any time elect to cancel any Interest Payment (or any part thereof) which would otherwise be payable on any Interest Payment Date. There are also certain restrictions on the payment of interest as specified in the terms
- The securities are undated and are repayable, at the option of the Bank, in whole at the first call date, or at any Interest Payment date thereafter. In addition, the AT1 securities are repayable, at the option of the Bank, in whole for certain regulatory or tax reasons. Any repayments require the prior consent of the Prudential Regulation Authority
- The securities will be subject to a Permanent Write Down should the fully Loaded Common Equity Tier 1 ratio of the Bank fall below 7.0 per cent

28 Dividends on ordinary shares

The Group and the Bank	**2020 £m**	2019 £m
Dividends paid during the year were as follows:		
Interim dividends	**700**	–

The directors have proposed an interim dividend of £200 million to be paid in April 2021.

29 Related party transactions

Key management personnel
Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of an entity, the Group and Bank's key management personnel are the members of the Lloyds Bank Corporate Markets plc board.

The table below represents key management personnel emoluments.

	2020 £'000	2019 £'000
Salaries and other short term employee benefits	**2,299**	2,773
Post employment benefits	**43**	34
Total compensation	**2,342**	2,807

The amounts disclosed above relate wholly to directors of the Group.

29 Related party transactions (continued)

Balances and transactions with fellow Lloyds Banking Group undertakings

Balances and transactions between members of the Lloyds Bank Corporate Markets Group

In accordance with IFRS 10 *Consolidated financial statements*, transactions and balances between the Bank and its subsidiary undertakings, and between those subsidiary undertakings, have all been eliminated on consolidation and thus are not reported as related party transactions of the Group.

The Bank, as a result of its position as parent of a banking group, has a large number of transactions with various of its subsidiary undertakings; these are included on the balance sheet of the Bank as follows:

	2020 £m	2019 £m
Assets, included within:		
Derivative financial instruments	**61**	56
Financial assets at amortised cost: due from fellow Lloyds Bank Corporate Markets Group undertakings	**293**	388
	354	444
Liabilities, included within:		
Due to fellow Lloyds Bank Corporate Markets Group undertakings	**383**	506
	383	506

Due to the size and volume of transactions passing through these accounts, it is neither practical nor meaningful to disclose information on gross inflows and outflows. During 2020 the Bank earned interest income on the above asset balances of £3 million (2019: £9 million) and incurred interest expense on the above liability balances of £1 million (2019: £67 million).

Balances and transactions with Lloyds Banking Group plc and fellow subsidiaries of the Bank

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

	The Group		The Bank	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Assets, included within:				
Financial assets at amortised cost: due from fellow Lloyds Banking Group undertakings	**1,118**	710	**925**	431
Financial assets at fair value through profit or loss	**27**	40	**27**	40
Derivative financial instruments	**2,911**	2,734	**2,911**	2,734
	4,056	3,484	**3,863**	3,205
Liabilities, included within:				
Due to fellow Lloyds Banking Group undertakings	**3,283**	1,638	**3,276**	1,578
Financial liabilities at fair value through profit or loss	**–**	–	–	–
Derivative financial instruments	**3,788**	2,254	**3,788**	2,254
Debt securities in issue	**3,696**	3,590	**3,696**	3,590
Subordinated liabilities	**686**	698	**686**	698
	11,453	8,180	**11,446**	8,120
Other equity instruments				
Additional tier 1 instruments	**782**	782	**782**	782
	782	782	**782**	782

These balances include the Group's banking arrangements and, due to the size and volume of transactions passing through these accounts, it is neither practical nor meaningful to disclose information on gross inflows and outflows. During 2020 the Group earned £9 million and the Bank earned £9 million interest income on the above asset balances (2019: Group £45 million, Bank £9 million); the Group incurred £143 million and the Bank incurred £143 million interest expense on the above liability balances (2019: Group £201 million, Bank £200 million).

The Group earned £87 million and the Bank earned £84 million of Fee and Commission Income (2019: Group £92 million, Bank £88 million); the Group incurred £nil and the Bank incurred £nil of Fee and Commission Expense (2019: Group £18 million, Bank £18 million), both in respect of transactions with Lloyds Bank plc.

Management charges payable to Lloyds Bank plc of £186 million (2019: 205 million) have been incurred in the year see note 7 for further detail.

During the year, the Bank sold a portfolio of facilities (£53 million of assets and £1,425 million of commitments) to Lloyds Bank plc, as noted in the Strategic Report. No significant gain or loss arose.

30 Contingent liabilities, capital commitments and guarantees

Contingent liabilities	The Group 2020 £m	The Group 2019 £m	The Bank 2020 £m	The Bank 2019 £m
Acceptances and endorsements	**57**	57	**57**	57
Other:				
Other items serving as direct credit substitutes	**96**	86	**96**	86
Performance bonds and other transaction-related contingencies	**34**	180	**34**	180
	130	266	**130**	266
Total contingent liabilities	**187**	323	**187**	323

The contingent liabilities of the Group arise in the normal course of its banking business and it is not practicable to quantify their future financial effect.

Commitments and guarantees	The Group 2020 £m	The Group 2019 £m	The Bank 2020 £m	The Bank 2019 £m
Forward asset purchases and forward deposits placed	**3**	19	**3**	19
Undrawn formal standby facilities, credit line and other commitments to lend:				
Less than 1 year original maturity:				
Mortgage offers made	**52**	37	**52**	37
Other commitments and guarantees	**7,466**	7,319	**7,466**	7,319
	7,518	7,356	**7,518**	7,356
More than 1 year original maturity – 3rd party	**7,014**	9,347	**7,014**	9,287
Total commitments and guarantees	**14,535**	16,722	**14,535**	16,662

Of the amounts shown above in respect of undrawn formal standby facilities, credit lines and other commitments to lend £14,416 million for the Group (2019: £16,589 million) and £14,416 million for the Bank were irrevocable (2019: £16,528 million).

There were no contracted capital commitments at the Balance sheet date.

31 Financial instruments

(1) Measurement basis of financial assets and liabilities

The accounting policies in note 2 describe how different classes of financial instruments are measured, and how income and expenses, including fair value gains and losses, are recognised. The following tables analyse the carrying amounts of the financial assets and liabilities by category and by balance sheet heading.

The Group	Derivatives designated as hedging instruments £m	Mandatorily held at fair value through profit or loss: Held for trading £m	Mandatorily held at fair value through profit or loss: Other £m	At fair value through other comprehensive income £m	Held at amortised cost £m	Total £m
At 31 December 2020						
Financial assets						
Cash and balances at central banks	–	–	–	–	23,369	23,369
Items in the course of collection from banks	–	–	–	–	–	–
Financial assets at fair value through profit or loss	–	20,262	664	–	–	20,926
Derivative financial instruments	6	21,751	–	–	–	21,757
Loans and advances to banks	–	–	–	–	5,260	5,260
Loans and advances to customers	–	–	–	–	18,452	18,452
Debt securities	–	–	–	–	257	257
Due from fellow Lloyds Banking Group undertakings	–	–	–	–	1,118	1,118
Financial assets at amortised cost	–	–	–	–	25,087	25,087
Financial assets at fair value through other comprehensive income	–	–	–	149	–	149
Total financial assets	6	42,013	664	149	48,456	91,288
Financial liabilities						
Deposits from banks	–	–	–	–	5,601	5,601
Customer deposits	–	–	–	–	25,497	25,497
Due to fellow Lloyds Banking Group undertakings	–	–	–	–	3,283	3,283
Financial liabilities at fair value through profit or loss	–	15,815	–	–	–	15,815
Derivative financial instruments	3	21,230	–	–	–	21,233
Debt securities in issue	–	–	–	–	15,602	15,602
Subordinated liabilities	–	–	–	–	686	686
Total financial liabilities	3	37,045	–	–	50,669	87,717

31 Financial instruments (continued)

The Group	Derivatives designated as hedging instruments £m	Mandatorily held at fair value through profit or loss: Held for trading £m	Mandatorily held at fair value through profit or loss: Other £m	At fair value through other comprehensive income £m	Held at amortised cost £m	Total £m
At 31 December 2019						
Financial assets						
Cash and balances at central banks	–	–	–	–	16,250	16,250
Items in the course of collection from banks	–	–	–	–	21	21
Financial assets at fair value through profit or loss	–	17,732	414	–	–	18,146
Derivative financial instruments	15	18,821	–	–	–	18,836
Loans and advances to banks	–	–	–	–	4,813	4,813
Loans and advances to customers	–	–	–	–	20,264	20,264
Debt securities	–	–	–	–	112	112
Due from fellow Lloyds Banking Group undertakings	–	–	–	–	710	710
Financial assets at amortised cost	–	–	–	–	25,899	25,899
Financial assets at fair value through other comprehensive income	–	–	–	314	–	314
Total financial assets	15	36,553	414	314	42,170	79,466
Financial liabilities						
Deposits from banks	–	–	–	–	3,970	3,970
Customer deposits	–	–	–	–	24,479	24,479
Due to fellow Lloyds Banking Group undertakings	–	–	–	–	1,638	1,638
Financial liabilities at fair value through profit or loss	–	13,784	–	–	–	13,784
Derivative financial instruments	6	17,756	–	–	–	17,762
Debt securities in issue	–	–	–	–	12,429	12,429
Subordinated liabilities	–	–	–	–	698	698
Total financial liabilities	6	31,540	–	–	43,214	74,760

31 Financial instruments (continued)

The Bank	Derivatives designated as hedging instruments £m	Mandatorily held at fair value through profit or loss: Held for trading £m	Mandatorily held at fair value through profit or loss: Other £m	At fair value through other comprehensive income £m	Held at amortised cost £m	Total £m
At 31 December 2020						
Financial assets						
Cash and balances at central banks	–	–	–	–	23,369	23,369
Items in the course of collection from banks	–	–	–	–	–	–
Financial assets at fair value through profit or loss	–	20,262	579	–	–	20,841
Derivative financial instruments	6	21,812	–	–	–	21,818
Loans and advances to banks	–	–	–	–	5,231	5,231
Loans and advances to customers	–	–	–	–	18,189	18,189
Debt securities	–	–	–	–	257	257
Due from fellow Lloyds Banking Group undertakings	–	–	–	–	1,218	1,218
Financial assets at amortised cost	–	–	–	–	24,895	24,895
Financial assets at fair value through other comprehensive income	–	–	–	149	–	149
Total financial assets	6	42,074	579	149	48,264	91,072
Financial liabilities						
Deposits from banks	–	–	–	–	5,601	5,601
Customer deposits	–	–	–	–	25,061	25,061
Due to fellow Lloyds Banking Group undertakings	–	–	–	–	3,659	3,659
Financial liabilities at fair value through profit or loss	–	15,815	–	–	–	15,815
Derivative financial instruments	3	21,230	–	–	–	21,233
Debt securities in issue	–	–	–	–	15,602	15,602
Subordinated liabilities	–	–	–	–	686	686
Total financial liabilities	3	37,045	–	–	50,609	87,657

31 Financial instruments (continued)

The Bank	Derivatives designated as hedging instruments £m	Mandatorily held at fair value through profit or loss: Held for trading £m	Mandatorily held at fair value through profit or loss: Other £m	At fair value through other comprehensive income £m	Held at amortised cost £m	Total £m
At 31 December 2019						
Financial assets						
Cash and balances at central banks	–	–	–	–	16,250	16,250
Items in the course of collection from banks	–	–	–	–	21	21
Financial assets at fair value through profit or loss	–	17,732	327	–	–	18,059
Derivative financial instruments	15	18,877	–	–	–	18,892
Loans and advances to banks	–	–	–	–	4,792	4,792
Loans and advances to customers	–	–	–	–	19,986	19,986
Debt securities	–	–	–	–	112	112
Due from fellow Lloyds Banking Group undertakings	–	–	–	–	819	819
Financial assets at amortised cost	–	–	–	–	25,709	25,709
Financial assets at fair value through other comprehensive income	–	–	–	314	–	314
Total financial assets	15	36,609	327	314	41,980	79,245
Financial liabilities						
Deposits from banks	–	–	–	–	3,970	3,970
Customer deposits	–	–	–	–	24,010	24,010
Due to fellow Lloyds Banking Group undertakings	–	–	–	–	2,084	2,084
Financial liabilities at fair value through profit or loss	–	13,784	–	–	–	13,784
Derivative financial instruments	6	17,756	–	–	–	17,762
Debt securities in issue	–	–	–	–	12,429	12,429
Subordinated liabilities	–	–	–	–	698	698
Total financial liabilities	6	31,540	–	–	43,191	74,737

31 Financial instruments (continued)

(2) Fair value measurement

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. It is a measure at a specific date and may be significantly different from the amount which will actually be paid or received on maturity or settlement date.

Wherever possible, fair values have been calculated using unadjusted quoted market prices in active markets for identical instruments held by the Group. Where quoted market prices are not available, or are unreliable because of poor liquidity, fair values have been determined using valuation techniques which, to the extent possible, use market observable inputs, but in some cases use non-market observable inputs. Valuation techniques used include discounted cash flow analysis and pricing models and, where appropriate, comparison to instruments with characteristics similar to those of the instruments held by the Group. The Group measures valuation adjustments for its derivative exposures on the same basis as the derivatives are managed.

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

Because a variety of estimation techniques are employed and significant estimates made, comparisons of fair values between financial institutions may not be meaningful. Readers of these financial statements are thus advised to use caution when using this data to evaluate the Group’s financial position.

Fair value information is not provided for items that are not financial instruments or for other assets and liabilities which are not carried at fair value in the Group’s consolidated balance sheet. These items include intangible assets, such as the value of the Group’s branch network, the long-term relationships with depositors and credit card relationships; premises and equipment; and shareholder's equity. These items are material and accordingly the Group believes that the fair value information presented does not represent the underlying value of the Group.

Valuation control framework

The key elements of the control framework for the valuation of financial instruments include model validation, product implementation review and independent price verification. These functions are carried out by appropriately skilled risk and finance teams, independent of the business area responsible for the products.

Model validation covers both qualitative and quantitative elements relating to new models. In respect of new products, a product implementation review is conducted pre-and post-trading. Pre-trade testing ensures that the new model is integrated into the Group’s systems and that the profit and loss and risk reporting are consistent throughout the trade life cycle. Post-trade testing examines the explanatory power of the implemented model, actively monitoring model parameters and comparing in-house pricing to external sources. Independent price verification procedures cover financial instruments carried at fair value. The frequency of the review is matched to the availability of independent data, monthly being the minimum. Valuation differences in breach of established thresholds are escalated to senior management. The results from independent pricing and valuation reserves are reviewed monthly by senior management.

Formal committees, consisting of senior risk, finance and business management, meet at least quarterly to discuss and approve valuations in more judgemental areas, in particular for unquoted equities, structured credit, over-the-counter options and the Credit Valuation Adjustment (CVA) reserve.

Valuation of financial assets and liabilities

Assets and liabilities carried at fair value or for which fair values are disclosed have been classified into three levels according to the quality and reliability of information used to determine the fair values.

Level 1

Level 1 fair value measurements are those derived from unadjusted quoted prices in active markets for identical assets or liabilities. Products classified as level 1 predominantly comprise equity shares, treasury bills and other government securities.

Level 2

Level 2 valuations are those where quoted market prices are not available, for example where the instrument is traded in a market that is not considered to be active or valuation techniques are used to determine fair value and where these techniques use inputs that are based significantly on observable market data. Examples of such financial instruments include most over-the-counter derivatives, financial institution issued securities, certificates of deposit and certain asset-backed securities.

Level 3

Level 3 portfolios are those where at least one input which could have a significant effect on the instrument’s valuation is not based on observable market data. Certain of the Group’s asset-backed securities and derivatives, principally where there is no trading activity in such securities, are classified as level 3.

Transfers out of the level 3 portfolio arise when inputs that could have a significant impact on the instrument’s valuation become market observable after previously having been non-market observable. In the case of asset-backed securities this can arise if more than one consistent independent source of data becomes available. Conversely transfers into the portfolio arise when consistent sources of data cease to be available.

31 Financial instruments (continued)

(3) Financial assets and liabilities carried at fair value

(A) Financial assets, excluding derivatives

Valuation hierarchy

At 31 December 2020, the Group's financial assets carried at fair value, excluding derivatives, totalled £21,075 million (2019: £18,460 million). The table below analyses these financial assets by balance sheet classification, asset type and valuation methodology (level 1, 2 or 3, as described on page 75). The fair value measurement approach is recurring in nature. There were no significant transfers between level 1 and 2 during the year.

The Group	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
As at 31 December 2020				
Financial assets at fair value through profit or loss				
Loans and advances to customers	–	12,775	344	13,119
Loans and advances to banks	–	229	–	229
Debt securities:				
Government securities	6,983	–	–	6,983
Bank and building society certificates of deposit	–	66	–	66
Asset-backed securities:				
Mortgage-backed securities	–	7	–	7
Other asset-backed securities	–	4	–	4
Corporate and other debt securities	–	273	223	496
	6,983	350	223	7,556
Treasury and other bills	19	–	–	19
Equity shares	–	–	3	3
Total financial assets at fair value through profit or loss	7,002	13,354	570	20,926
Financial assets at fair value through other comprehensive income				
Debt securities:				
Bank and building society certificates of deposit	–	–	–	–
Asset-backed securities:				
Other asset-backed securities	–	–	113	113
	–	–	113	113
Treasury and other bills	36	–	–	36
Total financial assets at fair value through other comprehensive income	36	–	113	149
Total financial assets carried at fair value, excluding derivatives	7,038	13,354	683	21,075

31 Financial instruments (continued)

The Group	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
As at 31 December 2019				
Financial assets at fair value through profit or loss				
Loans and advances to customers	–	10,422	326	10,748
Loans and advances to banks	–	513	–	513
Debt securities:				
Government securities	6,501	–	–	6,501
Bank and building society certificates of deposit	–	68	–	68
Asset-backed securities:				
Mortgage-backed securities	–	6	–	6
Other asset-backed securities	–	17	–	17
Corporate and other debt securities	–	274	–	274
	6,501	365	–	6,866
Treasury and other bills	19	–	–	19
Equity shares	–	–	–	–
Total financial assets at fair value through profit or loss	6,520	11,300	326	18,146
Financial assets at fair value through other comprehensive income				
Debt securities:				
Bank and building society certificates of deposit	–	97	–	97
Asset-backed securities:				
Other asset-backed securities	–	–	121	121
	–	97	121	218
Treasury and other bills	96	–	–	96
Total financial assets at fair value through other comprehensive income	96	97	121	314
Total financial assets carried at fair value, excluding derivatives	6,616	11,397	447	18,460

31 Financial instruments (continued)

The Bank	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
As at 31 December 2020				
Financial assets at fair value through profit or loss				
Loans and advances to customers	–	12,775	344	13,119
Loans and advances to banks	–	229	–	229
Debt securities:				
Government securities	6,983	–	–	6,983
Bank and building society certificates of deposit	–	–	–	–
Asset-backed securities:				
Mortgage-backed securities	–	7	–	7
Other asset-backed securities	–	4	–	4
Corporate and other debt securities	–	273	223	496
	6,983	284	223	7,490
Treasury and other bills	–	–	–	–
Equity shares	–	–	3	3
Total financial assets at fair value through profit or loss	6,983	13,288	570	20,841
Financial assets at fair value through other comprehensive income				
Debt securities:				
Bank and building society certificates of deposit	–	–	–	–
Asset-backed securities:				
Other asset-backed securities	–	–	113	113
	–	–	113	113
Treasury and other bills	36	–	–	36
Total financial assets at fair value through other comprehensive income	36	–	113	149
Total financial assets carried at fair value, excluding derivatives	7,019	13,288	683	20,990

31 Financial instruments (continued)

The Bank	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
As at 31 December 2019				
Financial assets at fair value through profit or loss				
Loans and advances to customers	–	10,422	326	10,748
Loans and advances to banks	–	513	–	513
Debt securities:				
Government securities	6,501	–	–	6,501
Bank and building society certificates of deposit	–	–	–	–
Asset-backed securities:				
Mortgage-backed securities	–	6	–	6
Other asset-backed securities	–	17	–	17
Corporate and other debt securities	–	274	–	274
	6,501	297	–	6,798
Equity shares	–	–	–	–
Treasury and other bills	–	–	–	–
Total financial assets at fair value through profit or loss	6,501	11,232	326	18,059
Financial assets at fair value through other comprehensive income				
Debt securities:				
Bank and building society certificates of deposit	–	97	–	97
Asset-backed securities:				
Other asset-backed securities	–	–	121	121
	–	97	121	218
Treasury and other bills	96	–	–	96
Total financial assets at fair value through other comprehensive income	96	97	121	314
Total financial assets carried at fair value, excluding derivatives	6,597	11,329	447	18,373

Movements in level 3 portfolio
The table below analyses movements in level 3 financial assets, excluding derivatives, carried at fair value:

	2020			2019		
The Group and the Bank	**Financial assets at fair value through profit or loss £m**	**At fair value through other comprehensive income £m**	**Total level 3 assets carried at fair value, excluding derivatives £m**	Financial assets at fair value through profit or loss £m	At fair value through other comprehensive income £m	Total level 3 assets carried at fair value, excluding derivatives £m
Opening balance	**326**	**121**	**447**	3	194	197
Exchange and other adjustments	**–**	**4**	**4**	–	(7)	(7)
Gains recognised in the income statement within other income	**3**	**–**	**3**	–	–	–
(Losses) gains recognised in other comprehensive income within the revaluation reserves in respect of financial assets at fair value through other comprehensive income	**–**	**–**	**–**	–	1	1
Purchases	**410**	**–**	**410**	633	–	633
Sales	**(169)**	**(12)**	**(181)**	(310)	(86)	(396)
Transfers into the level 3 portfolio	**–**	**–**	**–**	–	19	19
At 31 December	**570**	**113**	**683**	326	121	447
Gains recognised in the income statement, within other income, relating to the change in fair value of those assets held at 31 December	**–**	**6**	**6**	–	7	7

31 Financial instruments (continued)

Valuation methodology for financial assets, excluding derivatives

Loans and advances to customers and banks

These assets are principally reverse repurchase agreements. The fair value of these assets is determined using discounted cash flow techniques. The discount rates are derived from observable repo curves specific to the type of security purchased under the reverse repurchase agreement.

Debt securities

Debt securities measured at fair value and classified as level 2 are valued by discounting expected cash flows using an observable credit spread applicable to the particular instrument.

Where there is limited trading activity in debt securities, the Group uses valuation models, consensus pricing information from third party pricing services and broker or lead manager quotes to determine an appropriate valuation. Debt securities are classified as level 3 if there is a significant valuation input that cannot be corroborated through market sources or where there are materially inconsistent values for an input. Asset classes classified as level 3 mainly comprise certain collateralised loan obligations and collateralised debt obligations.

Equity investments

Unlisted equity is valued using techniques in accordance with the Group's valuation policy and International Private Equity and Venture Capital Guidelines.

Equity securities measured at fair value and classified as level 2 are valued by discounting expected cash flows using an observable credit spread applicable to the particular instrument.

Where there is limited trading activity in equity securities, the Group uses valuation models, consensus pricing information from third party pricing services and broker or lead manager quotes to determine an appropriate valuation.

(B) Financial liabilities, excluding derivatives

Valuation hierarchy

At 31 December 2020, the Group's financial liabilities carried at fair value, excluding derivatives, totalled £15,815 million (2019: £13,784 million). The table below analyses these financial liabilities by balance sheet classification, liability type and valuation methodology (level 1, 2 or 3, as described on page 75). The fair value measurement approach is recurring in nature. There were no significant transfers between level 1 and 2 during the year.

The Group and the Bank	**Level 1 £m**	**Level 2 £m**	**Level 3 £m**	**Total £m**
As at 31 December 2020				
Financial liabilities at fair value through profit or loss				
Liabilities designated at fair value through profit or loss	**–**	**–**	**–**	**–**
Trading liabilities:				
Liabilities in respect of securities sold under repurchase agreements	**–**	**14,997**	**–**	**14,997**
Short positions in securities	**777**	**38**	**–**	**815**
Other deposits	**–**	**3**	**–**	**3**
Total trading liabilities	**777**	**15,038**	**–**	**15,815**
Total financial liabilities carried at fair value, excluding derivatives	**777**	**15,038**	**–**	**15,815**

The Group and the Bank	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
As at 31 December 2019				
Financial liabilities at fair value through profit or loss				
Liabilities designated at fair value through profit or loss	–	–	–	–
Trading liabilities:				
Liabilities in respect of securities sold under repurchase agreements	–	11,047	–	11,047
Short positions in securities	2,708	28	–	2,736
Other deposits	–	1	–	1
Total trading liabilities	2,708	11,076	–	13,784
Total financial liabilities carried at fair value, excluding derivatives	2,708	11,076	–	13,784

Movements in level 3 portfolio

There have been no movements in level 3 financial liabilities, excluding derivatives, carried at fair value during the year.

Valuation methodology for financial liabilities, excluding derivatives

Trading liabilities in respect of securities sold under repurchase agreements

The fair value of these liabilities is determined using discounted cash flow techniques. The discount rates are derived from observable repo curves specific to the type of security sold under the repurchase agreement.

31 Financial instruments (continued)

(C) Derivatives

All the Group's derivative assets and liabilities are carried at fair value. At 31 December 2020 such assets totalled £21,757 million for the Group and £21,818 million for the Bank (2019: £18,836 million for the Group and £18,892 million for the Bank) and liabilities totalled £21,233 million for the Group and £21,233 million for the Bank (2019: £17,762 million for the Group and £17,762 million for the Bank). The table below analyses these derivative balances by valuation methodology (level 1, 2 or 3, as described on page 75). The fair value measurement approach is recurring in nature. There were no significant transfers between level 1 and level 2 during the year.

	2020				2019			
The Group	**Level 1 £m**	**Level 2 £m**	**Level 3 £m**	**Total £m**	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Derivative assets	**1**	**20,808**	**948**	**21,757**	5	18,046	785	18,836
Derivative liabilities	**9**	**19,973**	**1,251**	**21,233**	18	16,674	1,070	17,762

	2020				2019			
The Bank	**Level 1 £m**	**Level 2 £m**	**Level 3 £m**	**Total £m**	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Derivative assets	**1**	**20,869**	**948**	**21,818**	5	18,102	785	18,892
Derivative liabilities	**9**	**19,973**	**1,251**	**21,233**	18	16,674	1,070	17,762

Where the Group's derivative assets and liabilities are not traded on an exchange, they are valued using valuation techniques, including discounted cash flow and options pricing models, as appropriate. The types of derivatives classified as level 2 and the valuation techniques used include:

- Interest rate swaps which are valued using discounted cash flow models; the most significant inputs into those models are interest rate yield curves which are developed from publicly quoted rates
- Foreign exchange derivatives that do not contain options which are priced using rates available from publicly quoted sources
- Credit derivatives which are valued using standard models with observable inputs, except for the items classified as level 3, which are valued using publicly available yield and credit default swap (CDS) curves
- Less complex interest rate and foreign exchange option products which are valued using volatility surfaces developed from publicly available interest rate cap, interest rate swaption and other option volatilities; option volatility skew information is derived from a market standard consensus pricing service. For more complex option products, the Group calibrates its models using observable at-the-money data; where necessary, the Group adjusts for out-of-the-money positions using a market standard consensus pricing service

Complex interest rate and foreign exchange products where inputs to the valuation are significant and unobservable are classified as level 3.

Where credit protection, usually in the form of credit default swaps, has been purchased or written on asset-backed securities, the security is referred to as a negative basis asset-backed security and the resulting derivative assets or liabilities have been classified as either level 2 or level 3 according to the classification of the underlying asset-backed security.

Certain unobservable inputs used to calculate CVA, FVA, and own credit adjustments, are not significant in determining the classification of the derivative and debt instruments. Consequently, these inputs do not form part of the level 3 sensitivities presented.

Movements in level 3 portfolio

The table below analyses movements in level 3 derivative assets and liabilities carried at fair value.

	2020		2019	
The Group and the Bank	**Derivative assets £m**	**Derivative liabilities £m**	Derivative assets £m	Derivative liabilities £m
At 1 January	**785**	**(1,070)**	922	(707)
Losses (Gains) recognised in the income statement within other income	**89**	**(102)**	81	(75)
Purchases	**61**	**(6)**	4	(4)
(Sales) redemptions	**(85)**	**75**	(19)	–
Exchange and other adjustments	**15**	**(17)**	(25)	4
Transfers into the level 3 portfolio	**83**	**(131)**	336	(616)
Transfers out of the level 3 portfolio	**–**	**–**	(514)	328
At 31 December	**948**	**(1,251)**	785	(1,070)
Gains (Losses) in the income statement, within other income, relating to the change in fair value of those assets or liabilities at 31 December	**(97)**	**131**	13	(18)

31 Financial instruments (continued)

Derivative valuation adjustments
Derivative financial instruments which are carried in the balance sheet at fair value are adjusted where appropriate to reflect credit risk, market liquidity and other risks.

(i) Uncollateralised derivative valuation adjustments, excluding monoline counterparties
The following table summarises the movement on this valuation adjustment account for the Group during 2019 and 2020.

Uncollateralised derivative valuation adjustments	2020 £m	2019 £m
At 1 January	195	310
Transfers out	(19)	(3)
Income statement charge/(credit)	53	(112)
At 31 December	**229**	195

Represented by:	2020 £m	2019 £m
Credit Valuation Adjustment (CVA)	185	142
Debit Valuation Adjustment (DVA)	(34)	(34)
Funding Valuation Adjustment	78	87
	229	195

Credit and Debit Valuation Adjustments (CVA and DVA) are applied to the Group's over-the-counter derivative exposures with counterparties that are not subject to standard collateral arrangements (CSAs). These adjustments reflect the level of interest rates, foreign exchange rates, expectations of counterparty creditworthiness and the Group's own credit spread respectively.

A CVA is taken where the Group has a positive future uncollateralised exposure (asset). A DVA is taken where the Group has a negative future uncollateralised exposure (liability). These adjustments reflect interest rates and expectations of counterparty creditworthiness and the Group's own credit spread respectively.

The CVA is sensitive to:

– the current size of the mark-to-market position on the uncollateralised asset
– expectations of future market volatility of the underlying asset
– expectations of counterparty creditworthiness

Market Credit Default Swap (CDS) spreads are used to develop the probability of default for quoted counterparties. For unquoted counterparties, internal credit ratings and market sector CDS curves and recovery rates are used. The Loss Given Default (LGD) is based on market recovery rates and internal credit assessments.

The combination of a one notch deterioration in the credit rating of derivative counterparties and a ten per cent increase in LGD increases the CVA by £38 million. Current market value is used to estimate the projected exposure for products not supported by the model, which are principally complex interest rate options that are traded in very low volumes. For these, the CVA is calculated on an add-on basis (in total contributing £nil of the overall CVA balance at 31 December 2020).

The DVA is sensitive to:

– the current size of the mark-to-market position on the uncollateralised liability
– expectations of future market volatility of the underlying liability
– the Group's own implied CDS spread

A one per cent rise in the CDS spread would lead to an increase in the DVA of £82 million to £116 million.

The risk exposures that are used for the CVA and DVA calculations are strongly influenced by interest rates and foreign exchange rates. Due to the nature of the Group's business and client hedging needs, CVA/DVA exposures and valuation adjustments tend to fall when interest rates rise. A one per cent rise in interest rates would lead to a £31 million fall in the overall valuation adjustment to £120 million. The CVA model used by the Group does not assume any correlation between the level of interest rates and default rates.

The Group has also recognised a Funding Valuation Adjustment to adjust for the net cost of funding uncollateralised derivative positions. This adjustment is calculated on the expected future exposure discounted at a suitable cost of funds. A ten basis points increase in the cost of funds will increase the funding valuation adjustment by approximately £13 million.

(ii) Market liquidity
The Group includes mid to bid-offer valuation adjustments against the expected cost of closing out the net market risk in the Group's trading positions within a timeframe that is consistent with historical trading activity and spreads that the trading desks have accessed historically during the ordinary course of business in normal market conditions.

At 31 December 2020, the Group's derivative trading business held mid to bid-offer valuation adjustments of £56 million (2019: £58 million).

31 Financial instruments (continued)

(D) Sensitivity of level 3 valuations

The Group and the Bank			**At 31 December 2020**			At 31 December 2019		
				Effect of reasonably possible alternative assumptions[2]			Effect of reasonably possible alternative assumptions[2]	
	Valuation technique(s)	**Significant unobservable inputs[1]**	**Carrying value £m**	**Favourable changes £m**	**Unfavourable changes £m**	Carrying value £m	Favourable changes £m	Unfavourable changes £m
Financial Assets at fair value through profit or loss:								
Debt Securities	Discounted Cash Flow	Credit Spreads (Discount Factor) and Inflation Volatility	**223**	**–**	**(7)**	–	–	–
Loans and advances to customers	Comparable Pricing	Spread	**344**	**4**	**(4)**	326	3	(3)
Equity investments	Discounted Cash Flow	Credit Spreads (Discount Factor) and Inflation Volatility	**3**	**10**	**(3)**	–	–	–
			570	**14**	**(14)**	326	3	(3)
Financial Assets at fair value through other comprehensive income								
Asset-backed securities	Comparable Pricing	Price	**96**	**2**	**(2)**	103	2	(2)
	Comparable Pricing	Spread	**17**	**1**	**(1)**	18	–	–
			113	**3**	**(3)**	121	2	(2)
Derivative financial assets								
Interest rate derivatives	Option pricing model	Inflation Volatility	**436**	**5**	**(3)**	330	3	(3)
	Option pricing model	Interest Rate Volatility	**512**	**2**	**(1)**	455	–	(1)
			948	**7**	**(4)**	785	3	(4)
Level 3 financial assets carried at fair value			**1,631**	**24**	**(21)**	1,232	8	(9)
Derivative financial liabilities								
Interest rate derivatives	Option pricing model	Illiquid Long Dated Repo Rate	**(2)**	**–**	**–**	–	–	–
	Option pricing model	Inflation Volatility	**(324)**	**2**	**(3)**	(260)	–	–
	Option pricing model	Interest Rate Volatility	**(925)**	**1**	**(2)**	(810)	–	–
			(1,251)	**3**	**(5)**	(1,070)	–	–
Level 3 financial liabilities carried at fair value			**(1,251)**	**3**	**(5)**	(1,070)	–	–

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

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

Unobservable inputs

Significant unobservable inputs affecting the valuation of debt securities and derivatives are as follows:

- Interest rates and inflation rates are referenced in some derivatives where the payoff that the holder of the derivative receives depends on the behaviour of those underlying references through time
- Credit spreads represent the premium above the benchmark reference instrument required to compensate for lower credit quality; higher spreads lead to a lower fair value
- Volatility parameters represent key attributes of option behaviour; higher volatilities typically denote a wider range of possible outcomes

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.

Debt securities

Reasonably possible alternative assumptions have been determined in respect of the Group's structured credit investment by flexing credit spreads.

Derivatives

Reasonably possible alternative assumptions have been determined in respect of swaptions in the Group's derivative portfolios which are priced using industry standard option pricing models. Such models require interest rate volatilities which may be unobservable at longer maturities. To derive reasonably possible alternative valuations these volatilities have been flexed within a range of 13 per cent to 128 per cent (2019: 14 per cent to 115 per cent).

31 Financial instruments (continued)

(4) Financial assets and liabilities carried at amortised cost

(A) Financial assets

Valuation hierarchy

The table below analyses the fair values of the financial assets of the Group which are carried at amortised cost by valuation methodology (level 1, 2 or 3, as described on page 75). Financial assets carried at amortised cost are mainly classified as level 3 due to significant unobservable inputs used in the valuation models. Where inputs are observable, debt securities are classified as level 1 or 2.

			Valuation hierarchy		
The Group	**Carrying value £m**	**Fair value £m**	**Level 1 £m**	**Level 2 £m**	**Level 3 £m**
As at 31 December 2020					
Loans and advances to customers	**18,452**	**18,524**	**–**	**4,196**	**14,328**
Loans and advances to banks	**5,260**	**5,260**	**–**	**1,660**	**3,600**
Debt securities	**257**	**257**	**–**	**257**	**–**
Due from fellow Lloyds Banking Group undertakings	**1,118**	**1,118**	**–**	**–**	**1,118**
Reverse repos included in above amounts:					
Loans and advances to customers	**4,196**	**4,196**	**–**	**4,196**	**–**
Loans and advances to banks	**1,660**	**1,660**	**–**	**1,660**	**–**
As at 31 December 2019					
Loans and advances to customers	20,264	20,418	–	2,976	17,442
Loans and advances to banks	4,813	4,815	–	1,148	3,667
Debt securities	112	112	–	112	–
Due from fellow Lloyds Banking Group undertakings	710	710	–	–	710
Reverse repos included in above amounts:					
Loans and advances to customers	2,976	2,976	–	2,976	–
Loans and advances to banks	1,148	1,148	–	1,148	–

			Valuation hierarchy		
The Bank	**Carrying value £m**	**Fair value £m**	**Level 1 £m**	**Level 2 £m**	**Level 3 £m**
As at 31 December 2020					
Loans and advances to customers	**18,189**	**18,261**	**–**	**4,196**	**14,065**
Loans and advances to banks	**5,231**	**5,231**	**–**	**1,660**	**3,571**
Debt securities	**257**	**257**	**–**	**257**	**–**
Due from fellow Lloyds Banking Group undertakings	**1,218**	**1,218**	**–**	**–**	**1,218**
Reverse repos included in above amounts:					
Loans and advances to customers	**4,196**	**4,196**	**–**	**4,196**	**–**
Loans and advances to banks	**1,660**	**1,660**	**–**	**1,660**	**–**
As at 31 December 2019					
Loans and advances to customers	19,986	20,139	–	2,976	17,163
Loans and advances to banks	4,792	4,792	–	1,148	3,644
Debt securities	112	112	–	112	–
Due from fellow Lloyds Banking Group undertakings	819	819	–	–	819
Reverse repos included in above amounts:					
Loans and advances to customers	2,976	2,976	–	2,976	–
Loans and advances to banks	1,148	1,148	–	1,148	–

Valuation methodology

Loans and advances to customers

The Group provides loans and advances to commercial, corporate and personal customers at both fixed and variable rates. Due to their short term nature, the carrying value of the variable rate loans and those relating to lease financing is estimated to be their fair value.

31 Financial instruments (continued)

To determine the fair value of loans and advances to customers, loans are segregated into portfolios of similar characteristics. A number of techniques are used to estimate the fair value of fixed rate lending; these take account of expected credit losses based on historic trends, prevailing market interest rates and expected future cash flows. For retail exposures, fair value is usually estimated by discounting anticipated cash flows (including interest at contractual rates) at market rates for similar loans offered by the Group and other financial institutions. Certain loans secured on residential properties are made at a fixed rate for a limited period, typically two to five years, after which the loans revert to the relevant variable rate. The fair value of such loans is estimated by reference to the market rates for similar loans of maturity equal to the remaining fixed interest rate period. The fair value of commercial loans is estimated by discounting anticipated cash flows at a rate which reflects the effects of interest rate changes, adjusted for changes in credit risk.

Loans and advances to banks
The carrying value of short dated loans and advances to banks is estimated to be their fair value. The fair value of loans and advances to banks is estimated by discounting the anticipated cash flows at a market discount rate adjusted for the credit spread of the obligor or, where not observable, the credit spread of borrowers of similar credit quality.

Debt securities
The fair values of debt securities are determined predominantly from lead manager quotes and, where these are not available, by alternative techniques including reference to credit spreads on similar assets with the same obligor, market standard consensus pricing services, broker quotes and other research data.

Reverse repurchase agreements
The carrying amount is considered a reasonable approximation of fair value given the short-term nature of these instruments.

(B) Financial liabilities

Valuation hierarchy
The table below analyses fair values of the financial liabilities of the Group which are carried at amortised cost by valuation methodology (level 1, 2 or 3, as described on page 75).

			Valuation hierarchy		
The Group	**Carrying value £m**	**Fair value £m**	**Level 1 £m**	**Level 2 £m**	**Level 3 £m**
As at 31 December 2020					
Deposits from banks	**5,601**	**5,603**	**–**	**5,603**	**–**
Customer deposits	**25,497**	**25,596**	**–**	**25,596**	**–**
Due to fellow Lloyds Banking Group undertakings	**3,283**	**3,283**	**–**	**3,283**	**–**
Debt securities in issue	**15,602**	**15,849**	**–**	**15,849**	**–**
Subordinated liabilities	**686**	**686**	**–**	**686**	**–**
Repos included in above amounts:					
Deposits from banks	**–**	**–**	**–**	**–**	**–**
Customer deposits	**–**	**–**	**–**	**–**	**–**
Due to fellow Lloyds Banking Group undertakings	**–**	**–**	**–**	**–**	**–**
As at 31 December 2019					
Deposits from banks	3,970	3,965	–	3,965	–
Customer deposits	24,479	24,504	–	24,504	–
Due to fellow Lloyds Banking Group undertakings	1,638	1,638	–	1,638	–
Debt securities in issue	12,429	12,329	–	12,329	–
Subordinated liabilities	698	698	–	698	–
Repos included in above amounts:					
Deposits from banks	–	–	–	–	–
Customer deposits	–	–	–	–	–
Due to fellow Lloyds Banking Group undertakings	–	–	–	–	–

31 Financial instruments (continued)

The Bank	Carrying value £m	Fair value £m	Valuation hierarchy Level 1 £m	Level 2 £m	Level 3 £m
As at 31 December 2020					
Deposits from banks	**5,601**	**5,603**	**–**	**5,603**	**–**
Customer deposits	**25,061**	**25,160**	**–**	**25,160**	**–**
Due to fellow Lloyds Banking Group undertakings	**3,659**	**3,659**	**–**	**3,659**	**–**
Debt securities in issue	**15,602**	**15,849**	**–**	**12,152**	**–**
Subordinated liabilities	**686**	**686**	**–**	**686**	**–**
Repos included in above amounts:					
Deposits from banks	**–**	**–**	**–**	**–**	**–**
Customer deposits	**–**	**–**	**–**	**–**	**–**
Due to fellow Lloyds Banking Group undertakings	**–**	**–**	**–**	**–**	**–**
As at 31 December 2019					
Deposits from banks	3,970	3,965	–	3,965	–
Customer deposits	24,010	24,035	–	24,035	–
Due to fellow Lloyds Banking Group undertakings	2,084	2,084	–	2,084	–
Debt securities in issue	12,429	12,329	–	12,329	–
Subordinated liabilities	698	698	–	698	–
Repos included in above amounts:					
Deposits from banks	–	–	–	–	–
Customer deposits	–	–	–	–	–
Due to fellow Lloyds Banking Group undertakings	–	–	–	–	–

Valuation methodology

Deposits from banks and customer deposits

The fair value of bank and customer deposits repayable on demand is estimated to be equal to their carrying value.

The fair value for all other deposits is estimated using discounted cash flows applying either market rates, where applicable, or current rates for deposits of similar remaining maturities.

Debt securities in issue

The fair value of short-term debt securities in issue is approximately equal to their carrying value. Fair value for other debt securities is calculated based on quoted market prices where available. Where quoted market prices are not available, fair value is estimated using discounted cash flow techniques at a rate which reflects market rates of interest and the Group's own credit spread.

Subordinated liabilities

The fair value of subordinated liabilities is determined by reference to quoted market prices where available or by reference to quoted market prices of similar instruments. Subordinated liabilities are classified as level 2, since the inputs used to determine their fair value are largely observable.

Repurchase agreements

The carrying amount is deemed a reasonable approximation of fair value given the short-term nature of these instruments.

(5) Reclassifications of financial assets

There have been no reclassifications of financial assets in 2019 or 2020.

32 Business combinations

During the prior year, the Bank acquired a business from one of its subsidiaries.

The acquired assets and liabilities were accounted for using predecessor accounting (see note 2) and as the consideration paid was equal to the book value no goodwill or discount arose on acquisition. Total consideration was paid as cash.

The Bank did not dispose of any operations of the acquiree as part of the business combination.

33 Offsetting of financial assets and liabilities

The following information relates to financial assets and liabilities which have been offset in the balance sheet and those which have not been offset but for which the Group has enforceable master netting agreements or collateral arrangements in place with counterparties.

				Related amounts where set off in the balance sheet not permitted[3]		
At 31 December 2020	Gross amounts of assets and liabilities[1] £m	Amounts offset in the balance sheet[2] £m	Net amounts presented in the balance sheet £m	Cash collateral received/ pledged £m	Non-cash collateral received/ pledged £m	Potential net amounts if offset of related amounts permitted £m
Financial assets						
Financial assets at fair value through profit or loss:						
Excluding reverse repos	7,931	–	7,931	–	(2,565)	5,366
Reverse repos	27,934	(14,939)	12,995	–	(12,995)	–
	35,865	(14,939)	20,926	–	(15,560)	5,366
Derivative financial instruments	21,757	–	21,757	(4,809)	(12,887)	4,061
Loans and advances to banks:						
Excluding reverse repos	3,600	–	3,600	(2,065)	–	1,535
Reverse repos	1,660	–	1,660	–	(1,660)	–
	5,260	–	5,260	(2,065)	(1,660)	1,535
Loans and advances to customers:						
Excluding reverse repos	14,256	–	14,256	(1,801)	–	12,455
Reverse repos	4,196	–	4,196	–	(4,196)	–
	18,452	–	18,452	(1,801)	(4,196)	12,455
Debt securities	257	–	257	–	–	257
Financial assets at fair value through other comprehensive income	149	–	149	–	–	149
Financial liabilities						
Deposits from banks:						
Excluding repos	5,601	–	5,601	(3,460)	–	2,141
Repos	–	–	–	–	–	–
	5,601	–	5,601	(3,460)	–	2,141
Customer deposits:						
Excluding repos	25,497	–	25,497	(1,349)	–	24,148
Repos	–	–	–	–	–	–
	25,497	–	25,497	(1,349)	–	24,148
Financial liabilities at fair value through profit or loss:						
Excluding repos	818	–	818	–	–	818
Repos	29,936	(14,939)	14,997	–	(14,997)	–
	30,754	(14,939)	15,815	–	(14,997)	818
Derivative financial instruments	21,233	–	21,233	(3,865)	(15,066)	2,302

33 Offsetting of financial assets and liabilities (continued)

At 31 December 2019	Gross amounts of assets and liabilities[1] £m	Amounts offset in the balance sheet[2] £m	Net amounts presented in the balance sheet £m	Related amounts where set off in the balance sheet not permitted[3]: Cash collateral received/ pledged £m	Related amounts where set off in the balance sheet not permitted[3]: Non-cash collateral received/ pledged £m	Potential net amounts if offset of related amounts permitted £m
Financial assets						
Financial assets at fair value through profit or loss:						
Excluding reverse repos	7,211	–	7,211	–	(1,876)	5,335
Reverse repos	23,938	(13,003)	10,935	–	(10,935)	–
	31,149	(13,003)	18,146	–	(12,811)	5,335
Derivative financial instruments	18,836	–	18,836	(4,483)	(10,003)	4,350
Loans and advances to banks:						
Excluding reverse repos	3,665	–	3,665	(1,800)	–	1,865
Reverse repos	1,148	–	1,148	–	(1,148)	–
	4,813	–	4,813	(1,800)	(1,148)	1,865
Loans and advances to customers:						
Excluding reverse repos	17,288	–	17,288	(1,498)	–	15,790
Reverse repos	2,976	–	2,976	–	(2,976)	–
	20,264	–	20,264	(1,498)	(2,976)	15,790
Debt securities	112	–	112	–	–	112
Financial assets at fair value through other comprehensive income	314	–	314	–	–	314
Financial liabilities						
Deposits from banks:						
Excluding repos	3,970	–	3,970	(2,571)	–	1,399
Repos	–	–	–	–	–	–
	3,970	–	3,970	(2,571)	–	1,399
Customer deposits:						
Excluding repos	24,479	–	24,479	(1,912)	–	22,567
Repos	–	–	–	–	–	–
	24,479	–	24,479	(1,912)	–	22,567
Financial liabilities at fair value through profit or loss:						
Excluding repos	2,737	–	2,737	–	–	2,737
Repos	24,050	(13,003)	11,047	–	(11,047)	–
	26,787	(13,003)	13,784	–	(11,047)	2,737
Derivative financial instruments	17,762	–	17,762	(3,298)	(11,582)	2,882

1 After impairment allowance.

2 The amounts set off in the balance sheet as shown above represent derivatives and repurchase agreements with central clearing houses which meet the criteria for offsetting under IAS 32.

3 The Group enters into derivatives and repurchase and reverse repurchase agreements with various counterparties which are governed by industry standard master netting agreements. The Group holds and provides cash and securities collateral in respective of derivative transactions covered by these agreements. The right to set off balances under these master netting agreements or to set off cash and securities collateral only arises in the event of non-payment or default and, as a result, these arrangements do not qualify for offsetting under IAS 32.

The effects of over-collateralisation have not been taken into account in the above tables.

34 Financial risk management

Financial instruments are fundamental to the Group's activities and, as a consequence, the risks associated with financial instruments represent a significant component of the risks faced by the Group.

The primary risks affecting the Group through its use of financial instruments are: credit risk; market risk, which includes interest rate, foreign exchange and credit spread risks; and liquidity risk. Information about the Group's management of these risks is given below.

(1) Credit risk

The Group's credit risk exposure arises in respect of the instruments below. Credit risk appetite is set at Board level and is described and reported through a suite of metrics devised from a combination of accounting and credit portfolio performance measures, which include the use of various credit risk rating systems as inputs and measure the credit risk of loans and advances to customers and banks at a counterparty level using three components: (i) the probability of default by the counterparty on its contractual obligations; (ii) the current exposures to the counterparty and their likely future development, from which the Group derives the exposure at default; and (iii) the likely loss ratio on the defaulted obligations, the loss given default. The Group uses a range of approaches to mitigate credit risk, including internal control policies, obtaining collateral and security, using master netting agreements and other credit risk transfers, such as asset sales and credit derivative based transactions.

A. Maximum credit exposure

The maximum credit risk exposure of the Group and the Bank in the event of other parties failing to perform their obligations is detailed below. No account is taken of any collateral held and the maximum exposure to loss is considered to be the balance sheet carrying amount or, for non-derivative off-balance sheet transactions and financial guarantees, their contractual nominal amounts.

	2020			2019		
The Group	**Maximum exposure £m**	**Offset[2] £m**	**Net exposure £m**	Maximum exposure £m	Offset[2] £m	Net exposure £m
Loans and advances to banks, net[1]	**5,260**	**–**	**5,260**	4,813	–	4,813
Loans and advances to customers, net[1]	**18,452**	**–**	**18,452**	20,264	–	20,264
Debt securities, net[1]	**257**	**–**	**257**	112	–	112
	23,969	**–**	**23,969**	25,189	–	25,189
Financial assets at fair value through other comprehensive income	**149**	**–**	**149**	314	–	314
Financial assets at fair value through profit or loss:						
Loans and advances	**13,348**	**–**	**13,348**	11,261	–	11,261
Debt securities, treasury and other bills[3]	**7,575**	**–**	**7,575**	6,885	–	6,885
	20,923	**–**	**20,923**	18,146	–	18,146
Derivative assets	**21,757**	**(10,055)**	**11,702**	18,836	(8,683)	10,153
Off-balance sheet items:						
Acceptances and endorsements	**57**	**–**	**57**	57	–	57
Other items serving as direct credit substitutes	**96**	**–**	**96**	86	–	86
Performance bonds and other transaction-related contingencies	**34**	**–**	**34**	180	–	180
Irrevocable commitments and guarantees	**14,416**	**–**	**14,416**	16,589	–	16,589
	14,603	**–**	**14,603**	16,912	–	16,912
	81,401	**(10,055)**	**71,346**	79,397	(8,683)	70,714

34 Financial risk management (continued)

The Bank	2020 Maximum exposure £m	2020 Offset[2] £m	2020 Net exposure £m	2019 Maximum exposure £m	2019 Offset[2] £m	2019 Net exposure £m
Loans and advances to banks, net[1]	**5,231**	**–**	**5,231**	4,792	–	4,792
Loans and advances to customers, net[1]	**18,189**	**–**	**18,189**	19,986	–	19,986
Debt securities, net[1]	**257**	**–**	**257**	112	–	112
	23,677	**–**	**23,677**	24,890	–	24,890
Financial assets at fair value through other comprehensive income	**149**	**–**	**149**	314	–	314
Financial assets at fair value through profit or loss:						
Loans and advances	**13,348**	**–**	**13,348**	11,261	–	11,261
Debt securities, treasury and other bills[3]	**7,490**	**–**	**7,490**	6,798	–	6,798
	20,838	**–**	**20,838**	18,059	–	18,059
Derivative assets	**21,818**	**(10,055)**	**11,763**	18,892	(8,683)	10,209
Off-balance sheet items:						
Acceptances and endorsements	**57**	**–**	**57**	57	–	57
Other items serving as direct credit substitutes	**96**	**–**	**96**	86	–	86
Performance bonds and other transaction-related contingencies	**34**	**–**	**34**	180	–	180
Irrevocable commitments and guarantees	**14,416**	**–**	**14,416**	16,528	–	16,528
	14,603	**–**	**14,603**	16,851	–	16,851
	81,085	**(10,055)**	**71,030**	79,006	(8,683)	70,323

1 Amounts shown net of related impairment allowances.

2 Offset items comprise deposit amounts available for offset, and amounts available for offset under master netting arrangements, that do not meet the criteria under IAS 32 to enable loans and advances and derivative assets respectively to be presented net of these balances in the financial statements.

3 Excluding equity shares.

34 Financial risk management (continued)

B. Concentrations of exposure

The Group's management of concentration risk includes single name, industry sector and country limits as well as controls over the Group's overall exposure to certain products.

At 31 December 2020 the most significant concentration of exposure was in Financial, business and other services (comprising 81 per cent of total loans and advances to customers).

Loans and advances to customers

	The Group		The Bank	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Agriculture, forestry and fishing	**1**	1	**1**	1
Energy and water supply	**38**	9	**38**	9
Manufacturing	**502**	1,224	**502**	1,224
Construction	**50**	96	**50**	96
Transport, distribution and hotels	**112**	359	**112**	359
Postal and telecommunications	**404**	243	**404**	243
Property companies	**984**	877	**984**	877
Financial, business and other services	**15,008**	16,396	**15,008**	16,396
Personal:				
Mortgages	**1,120**	845	**1,120**	845
Other	**69**	107	**17**	21
Lease financing	**134**	135	**–**	–
Hire purchase	**78**	58	**–**	–
Total loans and advances to customers before allowance for impairment losses	**18,500**	20,350	**18,236**	20,071
Allowance for impairment losses (note 13)	**(48)**	(86)	**(47)**	(85)
Total loans and advances to customers	**18,452**	20,264	**18,189**	19,986

C. Credit quality of assets

Loans and advances

The analysis of lending has been prepared with the business segment in which the exposure is recorded reflected in the ratings system applied. The internal credit ratings systems used by the Group for commercial business reflects the characteristics of these exposures and the way that they are managed internally; these credit ratings are set out below. All probabilities of default (PDs) include forward-looking information and are based on 12 month values, with the exception of credit impaired.

	Corporate	
	Grade	IFRS 9 PD%
Good quality	**1-10**	0.00-0.50
Satisfactory quality	**11-14**	0.51-3.00
Lower quality	**15-18**	3.01-20.00
Below standard	**19**	20.01-99.99
Credit impaired	**20-23**	100

34 Financial risk management (continued)

The Group Gross carrying amount	2020 Loans and advances to banks £m	2020 Loans and advances to customers £m	2019 Loans and advances to banks £m	2019 Loans and advances to customers £m
Stage 1				
Good quality	**5,211**	**17,273**	4,814	19,611
Satisfactory quality	**51**	**800**	–	414
Lower quality	**–**	**9**	–	3
Below standard, but not credit-impaired	**–**	**–**	–	–
	5,262	**18,082**	4,814	20,028
Stage 2				
Good quality	**–**	**13**	–	9
Satisfactory quality	**–**	**311**	–	5
Lower quality	**–**	**39**	–	15
Below standard, but not credit-impaired	**–**	**16**	–	–
	–	**379**	–	29
Stage 3				
Credit-impaired	**–**	**39**	–	293
Purchased or originated credit-impaired				
Credit-impaired	**–**	**–**	–	–
Total	**5,262**	**18,500**	4,814	20,350

The Group Loan commitments and financial guarantees	2020 Loans and advances to customers £m	2019 Loans and advances to customers £m
Stage 1		
Good quality	**13,203**	16,599
Satisfactory quality	**510**	122
Lower quality	**–**	–
Below standard, but not credit-impaired	**–**	–
	13,713	16,721
Stage 2		
Good quality	**–**	–
Satisfactory quality	**798**	–
Lower quality	**24**	1
Below standard, but not credit-impaired	**–**	–
	822	1
Stage 3		
Credit-impaired	**–**	–
Purchased or originated credit-impaired		
Credit-impaired	**–**	–
Total	**14,535**	16,722

34 Financial risk management (continued)

The Bank **Gross carrying amount**	**2020** **Loans and advances to banks** **£m**	**2020** **Loans and advances to customers** **£m**	2019 Loans and advances to banks £m	2019 Loans and advances to customers £m
Stage 1				
Good quality	**5,182**	**17,158**	4,788	19,342
Satisfactory quality	**51**	**666**	–	414
Lower quality	**–**	**9**	–	3
Below standard, but not credit-impaired	**–**	**–**	5	–
	5,233	**17,833**	4,793	19,759
Stage 2				
Good quality	**–**	**2**	–	–
Satisfactory quality	**–**	**308**	–	4
Lower quality	**–**	**39**	–	15
Below standard, but not credit-impaired	**–**	**15**	–	–
	–	**364**	–	19
Stage 3				
Credit-impaired	**–**	**39**	–	293
Purchased or originated credit-impaired				
Credit-impaired	**–**	**–**	–	–
Total	**5,233**	**18,236**	4,793	20,071

The Bank **Loan commitments and financial guarantees**	**2020** **Loans and advances to customers** **£m**	2019 Loans and advances to customers £m
Stage 1		
Good quality	**13,203**	16,539
Satisfactory quality	**510**	122
Lower quality	**–**	–
Below standard, but not credit-impaired	**–**	–
	13,713	16,661
Stage 2		
Good quality	**–**	–
Satisfactory quality	**798**	–
Lower quality	**24**	1
Below standard, but not credit-impaired	**–**	–
	822	1
Stage 3		
Credit-impaired	**–**	–
Purchased or originated credit-impaired		
Credit-impaired	**–**	–
Total	**14,535**	16,662

34 Financial risk management (continued)

Debt securities held at amortised cost

An analysis by credit rating of debt securities held at amortised cost is provided below:

	2020			2019		
The Group and the Bank	**Investment grade[1] £m**	**Other £m**	**Total £m**	Investment grade[1] £m	Other £m	Total £m
Asset-backed securities:						
Mortgage-backed securities	–	–	–	74	–	74
Other asset-backed securities	–	–	–	2	–	2
	–	–	–	76	–	76
Corporate and other debt securities	**257**	–	**257**	36	–	36
Gross exposure	**257**	–	**257**	112	–	112
Allowance for impairment losses	–	–	–	–	–	–
Total debt securities held at amortised cost	**257**	–	**257**	112	–	112

1 Credit ratings equal to or better than 'BBB'.

Financial assets at fair value through other comprehensive income

An analysis of financial assets at fair value through other comprehensive income is included in note 15. The credit quality of financial assets at fair value through other comprehensive income is set out below:

	2020			2019		
The Group and the Bank	**Investment grade[1] £m**	**Other £m**	**Total £m**	Investment grade[1] £m	Other £m	Total £m
Debt securities						
Bank and building society certificates of deposit	–	–	–	97	–	97
Asset-backed securities:						
Mortgage-backed securities	–	–	–	–	–	–
Other asset-backed securities	**113**	–	**113**	121	–	121
	113	–	**113**	121	–	121
Corporate and other debt securities	–	–	–	–	–	–
Total debt securities	**113**	–	**113**	218	–	218
Treasury and other bills	**36**	–	**36**	96	–	96
Total financial assets at fair value through other comprehensive income	**149**	–	**149**	314	–	314

1 Credit ratings equal to or better than 'BBB'.

34 Financial risk management (continued)

Debt securities, treasury and other bills held at fair value through profit or loss
An analysis of financial assets at fair value through profit or loss is included in note 11. The credit quality of debt securities, treasury and other bills held at fair value through profit or loss is set out below.

	2020			2019		
The Group	**Investment grade[1] £m**	**Other[2] £m**	**Total £m**	Investment grade[1] £m	Other[2] £m	Total £m
Trading assets						
Government securities	**6,983**	**–**	**6,983**	6,501	–	6,501
Asset-backed securities:						
Mortgage-backed securities	**4**	**3**	**7**	1	5	6
Other asset-backed securities	**–**	**4**	**4**	14	3	17
	4	**7**	**11**	15	8	23
Corporate and other debt securities	**225**	**21**	**246**	232	1	233
Total held as trading assets	**7,212**	**28**	**7,240**	6,748	9	6,757
Other assets mandatorily at fair value through profit or loss						
Bank and building society certificates of deposit	**66**	**–**	**66**	68	–	68
Corporate and other debt securities	**–**	**223**	**223**	1	–	1
Total debt securities mandatorily at fair value through profit or loss	**66**	**223**	**289**	69	–	69
Treasury and other bills	**19**	**–**	**19**	19	–	19
Total other assets mandatorily at fair value through profit or loss	**85**	**223**	**308**	88	–	88
	7,297	**251**	**7,548**	6,836	9	6,845
Due from fellow Lloyds Banking Group undertakings: Corporate and other debt securities	**27**	**–**	**27**	40	–	40
Total held at fair value through profit or loss	**7,324**	**251**	**7,575**	6,876	9	6,885

1 Credit ratings equal to or better than 'BBB'.

2 Other comprises sub-investment grade £nil (2019: £1 million) and not rated £251 million (2019: £8 million).

34 Financial risk management (continued)

The Bank	2020 Investment grade[1] £m	2020 Other[2] £m	2020 Total £m	2019 Investment grade[1] £m	2019 Other[2] £m	2019 Total £m
Trading assets						
Government securities	**6,983**	**–**	**6,983**	6,501	–	6,501
Asset-backed securities:						
Mortgage-backed securities	**4**	**3**	**7**	1	5	6
Other asset-backed securities	**–**	**4**	**4**	14	3	17
	4	**7**	**11**	15	8	23
Corporate and other debt securities	**225**	**21**	**246**	232	1	233
Total held as trading assets	**7,212**	**28**	**7,240**	6,748	9	6,757
Other assets mandatorily at fair value through profit or loss						
Corporate and other debt securities	**–**	**223**	**223**	1	–	1
Total debt securities mandatorily at fair value through profit or loss	**–**	**223**	**223**	1	–	1
Treasury and other bills	**–**	**–**	**–**	–	–	–
Total other assets mandatorily at fair value through profit or loss	**–**	**223**	**223**	1	–	1
	7,212	**251**	**7,463**	6,749	9	6,758
Due from fellow Lloyds Banking Group undertakings: Corporate and other debt securities	**27**	**–**	**27**	40	–	40
Total held at fair value through profit or loss	**7,239**	**251**	**7,490**	6,789	9	6,798

1 Credit ratings equal to or better than 'BBB'.

2 Other comprises sub-investment grade £nil (2019: £1 million) and not rated £251 million (2019: £8 million).

Derivative assets
An analysis of derivative assets is given in note 12.

The Group and the Bank reduces exposure to credit risk by using master netting agreements and by obtaining collateral in the form of cash or highly liquid securities. In respect of the net credit risk relating to derivative assets of £11,702 million for the Group and £11,763 million for the Bank (2019: £10,153 million for the Group and £10,209 million for the Bank), cash collateral of £4,809 million (2019: £4,483 million) for the Group was held and a further £303 million (2019: £153 million) for the Group was due from OECD banks.

The Group	2020 Investment grade[1] £m	2020 Other[2] £m	2020 Total £m	2019 Investment grade[1] £m	2019 Other[2] £m	2019 Total £m
Trading and other	**17,912**	**928**	**18,840**	15,256	831	16,087
Hedging	**6**	**–**	**6**	15	–	15
	17,918	**928**	**18,846**	15,271	831	16,102
Due from fellow Lloyds Banking Group undertakings			**2,911**			2,734
Total derivative financial instruments			**21,757**			18,836

1 Credit ratings equal to or better than 'BBB'.

2 Other comprises sub-investment grade £530 million (2019: £602 million) and not rated £398 million (2019: £229 million).

34 Financial risk management (continued)

The Bank	2020 Investment grade[1] £m	2020 Other[2] £m	2020 Total £m	2019 Investment grade[1] £m	2019 Other[2] £m	2019 Total £m
Trading and other	**17,912**	**928**	**18,840**	15,256	831	16,087
Hedging	**6**	**–**	**6**	15	–	15
	17,918	**928**	**18,846**	15,271	831	16,102
Due from fellow Lloyds Banking Group undertakings			**2,972**			2,790
Total derivative financial instruments			**21,818**			18,892

1 Credit ratings equal to or better than 'BBB'.

2 Other comprises sub-investment grade £530 million (2019: £602 million) and not rated £398 million (2019: £229 million).

Financial guarantees and irrevocable loan commitments

Financial guarantees represent undertakings that the Group will meet a customer's obligation to third parties if the customer fails to do so. Commitments to extend credit represent unused portions of authorisations to extend credit in the form of loans, guarantees or letters of credit. The Group is theoretically exposed to loss in an amount equal to the total guarantees or unused commitments, however, the likely amount of loss is expected to be significantly less; most commitments to extend credit are contingent upon customers maintaining specific credit standards.

D. Collateral held as security for financial assets

The Group holds collateral against loans and advances and irrevocable loan commitments; qualitative and, where appropriate, quantitative information is provided in respect of this collateral below. Collateral held as security for financial assets at fair value through profit or loss and for derivative assets is also shown below.

The Group holds collateral in respect of loans and advances to banks and customers as set out below. The Group does not hold collateral against debt securities, comprising asset-backed securities and corporate and other debt securities, which are classified as financial assets held at amortised cost.

Loans and advances to banks

There were reverse repurchase agreements which are accounted for as collateralised loans within loans and advances to banks with a carrying value of £1,660 million for the Group and the Bank (2019: £1,148 million for the Group and the Bank), against which the Group and the Bank held collateral with a fair value of £1,642 million (2019: £1,128 million for the Group and the Bank).

These transactions were generally conducted under terms that are usual and customary for standard secured lending activities.

Loans and advances to customers

Commercial lending

Reverse repurchase transactions

At 31 December 2020 there were reverse repurchase agreements which were accounted for as collateralised loans with a carrying value of £4,196 million for the Group and the Bank (2019: £2,976 million for the Group and the Bank) against which the Group and the Bank held collateral with a fair value of £4,126 million (2019: £2,583 million for the Group and the Bank) all of which the Group was able to repledge. No collateral in the form of cash was provided in respect of reverse repurchase agreements to the Group or the Bank in 2020 and 2019. These transactions were generally conducted under terms that are usual and customary for standard secured lending

Stage 3 secured lending

At 31 December 2020, stage 3 secured commercial lending amounted to £nil, net of an impairment allowance of £1 million for the Group and the Bank (2019: impaired secured commercial lending amounted to £216 million, net of an impairment allowance of £77 million for the Group and the Bank). The fair value of the collateral held in respect of stage 3 secured commercial lending was £nil (2019: £nil).

Financial assets at fair value through profit or loss (excluding equity shares)

Included in financial assets at fair value through profit or loss are reverse repurchase agreements treated as collateralised loans with a carrying value of £12,995 million for the Group and the Bank (2019: £10,935 million). Collateral is held with a fair value of £13,199 million for the Group and the Bank, all of which the Group is able to repledge (2019: £10,733 million for the Group and the Bank). At 31 December 2020, £9,665 million had been repledged (2019: £8,627 million).

In addition, securities held as collateral in the form of stock borrowed amounted to £22,923 million (2019: £8,154 million) for the Group and the Bank. Of this amount, £21,631 million (2019: £7,616 million) has been resold or repledged as collateral for the Group and Bank's own transactions.

These transactions were generally conducted under terms that are usual and customary for standard secured lending activities.

Derivatives assets, after offsetting of amounts under master netting arrangements

The Group reduces exposure to credit risk by using master netting agreements and by obtaining collateral in the form of cash or highly liquid securities. In respect of the net derivative assets after offsetting of amounts under master netting agreements of £11,702 million for the Group (2019: £10,153 million) and £11,763 million for the Bank (2019: £10,209 million), cash collateral of £4,809 million (2019: £4,483 million) for the Group and the Bank was held.

Irrevocable loan commitments and other credit-related contingencies

At 31 December 2020, the Group held irrevocable loan commitments and other credit-related contingencies of £14,603 million (2019: £16,912 million) and the Bank held irrevocable loan commitments and other credit-related contingencies of £14,603 million (2019: £16,851 million).

E. Collateral pledged as security

The Group pledges assets primarily for repurchase agreements and securities lending transactions which are generally conducted under terms that are usual and customary for standard securitised borrowing contracts.

34 Financial risk management (continued)

Repurchase transactions

Deposits from banks

Included in deposits from banks are balances arising from repurchase transactions of £nil for the Group and the Bank (2019: £nil for the Group and the Bank); the fair value of the collateral provided under these agreements at 31 December 2020 was £nil for the Group and the Bank (2019: £nil for the Group and the Bank).

Customer deposits

Included in customer deposits are balances arising from repurchase transactions of £nil for the Group and the Bank (2019: £nil for the Group and the Bank); the fair value of the collateral provided under these agreements at 31 December 2020 was £nil for the Group and the Bank (2019: £nil for the Group and Bank).

Trading and other financial liabilities at fair value through profit or loss

The fair value of collateral pledged in respect of repurchase transactions, accounted for as secured borrowing, where the secured party is permitted by contract or custom to repledge was £12,608 million for the Group and the Bank (2019: £8,324 for the Group and the Bank).

Securities lending transactions

The following on balance sheet financial assets have been lent to counterparties under securities lending transactions:

The Group and the Bank	2020 £m	2019 £m
Financial assets at fair value through profit or loss	**3,724**	3,348
Financial assets at fair value through other comprehensive income	**–**	253
Total	**3,724**	3,601

(2) Market risk

Interest rate risk

Interest rate risk arises from the different repricing characteristics of the assets and liabilities. Liabilities are either insensitive to interest rate movements, for example interest free or very low interest customer deposits, or are sensitive to interest rate changes but bear rates which may be varied at the Group's discretion and that for competitive reasons generally reflect changes in the Bank of England's base rate. The rates on the remaining deposits are contractually fixed for their term to maturity.

Many banking assets are sensitive to interest rate movements; there is a large volume of managed rate assets such as variable rate mortgages which may be considered as a natural offset to the interest rate risk arising from the managed rate liabilities. However, a significant proportion of the Group's lending assets, for example some personal loans and mortgages, bear interest rates which are contractually fixed.

The Group's risk management policy is to optimise reward whilst managing its market risk exposures within the risk appetite defined by the Board. The largest residual risk exposure arises from balances that are deemed to be insensitive to changes in market rates and is managed through the Group's structural hedge. The structural hedge consists of longer-term fixed rate assets or interest rate swaps and the amount and duration of the hedging activity is reviewed regularly by the Group Asset and Liability Committee.

The Group and the Bank establish hedge accounting relationships for interest rate risk using cash flow hedges and fair value hedges. The Group and the Bank are exposed to cash flow interest rate risk on its variable rate loans and deposits together with its floating rate subordinated debt. The derivatives used to manage the structural hedge may be designated into cash flow hedges to manage income statement volatility. The economic items related to the structural hedge, for example current accounts, are not eligible hedged items under IAS 39 for inclusion into accounting hedge relationships. The Group and the Bank are exposed to fair value interest rate risk on its fixed rate customer loans, its fixed rate customer deposits and the majority of its subordinated debt, and to cash flow interest rate risk on its variable rate loans and deposits together with its floating rate subordinated debt. The Group and the Bank apply netting between similar risks before applying hedge accounting.

Hedge ineffectiveness arises during the management of interest rate risk due to residual unhedged risk. Sources of ineffectiveness, which the Group may decide to not fully mitigate, can include basis differences, timing differences and notional amount differences. The effectiveness of accounting hedge relationships is assessed between the hedging derivatives and the documented hedged item, which can differ to the underlying economically hedged item.

At 31 December 2020 the aggregate notional principal of interest rate swaps designated as fair value hedges was £7,700 million for the Group and Bank (2019: £4,126 million for the Group and Bank) with a net fair value asset of £1 million (2019: £2 million). There were gains recognised on the hedging instruments of £121 million for the Group and Bank (2019: £143 million for the Group and Bank). There were losses on the hedged items attributable to the hedged risk of £123 million for the Group and Bank (2019: £147 million for the Group and Bank). The gains and losses relating to the fair value hedges are recorded in net trading income.

In addition the Group has cash flow hedges which are primarily used to hedge the variability in the cost of funding within the commercial business. The notional principal of the interest rate swaps designated as cash flow hedges at 31 December 2020 was £9,750 million for the Group and Bank (2019: £10,844 million for the Group and Bank) with a net fair value asset of £2 million (2019: £7 million). Ineffectiveness recognised in the income statement that arises from cash flow hedges was a gain of £10 million for the Group and Bank (2019: £4 million for the Group and Bank).

34 Financial risk management (continued)

Interest Rate Benchmark Reform
For the purpose of determining whether:

- a forecast transaction is highly probable;
- hedged future cash flows are expected to occur;
- a hedge is expected to be highly effective in achieving offsetting changes in fair value or cash flows attributable to the hedged risk; and
- an accounting hedging relationship should be discontinued because of a failure of the retrospective effectiveness test

the Group assumes that the interest rate benchmark on which the hedged risk or the cash flows of the hedged item or hedging instrument are based is not altered by uncertainties resulting from the proposed interest rate benchmark reform. In addition, for a fair value hedge of a non-contractually specified benchmark portion of interest rate risk, the Group assess only at inception of the hedge relationship and not on an ongoing basis that the risk is separately identifiable and hedge effectiveness can be measured.

The Group's most significant hedge accounting relationships are exposed to the following interest rate benchmarks: Sterling LIBOR, US Dollar LIBOR and EURIBOR.

At 31 December 2020, the Group expects that EURIBOR will continue to exist as a benchmark rate for the foreseeable future and, as a result, does not anticipate changing the hedged risk of financial assets and liabilities dependent on EURIBOR to a different benchmark. Accordingly, at 31 December 2020, the Group does not consider its fair value or cash flow hedges of the EURIBOR benchmark interest rate to be directly affected by interest rate benchmark reform.

The notional value of hedged items that the Group has designated into cash flow hedge relationships that are directly affected by the interest rate benchmark reform is £2,136 million (2019: £2,428 million), of which £1,403 million (2019: £1,971 million) relates to Sterling LIBOR and £733 million (2019: £457 million) relates to US Dollar LIBOR. These are principally loans and advances to customers.

The interest rate benchmark reforms also affect liabilities designated in fair value hedges with a notional of £3,167million (2019: £4,010 million), of which £1,100 million (2019: £500 million) is in respect of Sterling LIBOR and £2,067million (2019: £984 million) relates to US Dollar LIBOR. These fair value hedges principally relate to debt securities in issue. There are no fair value hedges of assets affected.

At 31 December 2020, the notional amount of the hedging instruments in hedging relationships to which these amendments apply was £12,342million (2019: £14,970 million), of which £1,100 million (2019: £500 million) relates to Sterling LIBOR fair value hedges and £8,433 million (2019: £9,522million) relates to Sterling LIBOR cash flow hedges.

The Group is managing the process to transition to alternative benchmark rates under the Lloyds Banking Group-wide IBOR Transition Programme. This programme has developed an implementation plan for new products and a transition plan for legacy products. The programme also encompasses the associated impacts on systems, processes, accounting and reporting and includes dealing with the impact on hedge accounting relationships of the transition to alternative reference rates.

Foreign exchange risk
The corporate and retail businesses incur foreign exchange risk in the course of providing services to their customers. All nonstructural foreign exchange exposures in the non-trading book are transferred to the trading area where they are monitored and controlled. These risks reside in the authorised trading centres who are allocated exposure limits. The limits are monitored daily by the local centres and reported to the central market and liquidity risk function in London. The Group also manages foreign exchange risk via cash flow hedge accounting, utilising currency swaps.

Risk arises from the Group's investments in its overseas operations. The Group's structural foreign currency exposure is represented by the net asset value of the foreign currency equity and subordinated debt investments in its subsidiaries and branches. Gains or losses on structural foreign currency exposures are taken to reserves.

The Group's main overseas operations are in the USA, Europe and Singapore. Details of the Group's structural foreign currency exposures, after net investment hedges, are as follows:

	2020		2019	
The Group and the Bank	**US Dollar £m**	**Other non-sterling £m**	US Dollar £m	Other non-sterling £m
Exposure	**74**	**–**	101	–

Credit spread risk
Credit spread risk arises primarily from (i) the Markets business; (ii) the Credit Valuation Adjustment (CVA) and Debt Valuation Adjustment (DVA) sensitivity to credit spreads; (iii) fair value positions in the banking book; and (iv) debt securities holdings in the liquid asset portfolio in management of liquidity. Credit spread risks are measured primarily through scenario analysis and Value at Risk (VaR) measures, which are reported within the Board risk appetite framework on a monthly basis. Supplementary measures such as sensitivity and exposure limits are also applied where they provide greater insight into risk positions. The frequency of reporting supplementary risk measures varies from daily to monthly.

(3) Liquidity risk
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. Liquidity risk is managed through a series of measures, tests and reports that are primarily based on contractual maturity. The Group carries out weekly stress testing of its liquidity position against a range of scenarios, including those prescribed by the PRA. The Group's liquidity risk appetite is also calibrated against a number of stressed liquidity metrics.

34 Financial risk management (continued)

The tables below analyse financial instrument liabilities of the Group and the Bank on an undiscounted future cash flow basis according to contractual maturity, into relevant maturity groupings based on the remaining period at the balance sheet date; balances with no fixed maturity are included in the over 5 years category. Certain balances, included in the table below on the basis of their residual maturity, are repayable on demand upon payment of a penalty.

The Group	**Up to 1 month £m**	**1-3 months £m**	**3-12 months £m**	**1-5 years £m**	**Over 5 years £m**	**Total £m**
31 December 2020						
Deposits from banks	**251**	**864**	**478**	**4,011**	**–**	**5,604**
Customer deposits	**15,258**	**3,788**	**3,021**	**2,507**	**933**	**25,507**
Financial liabilities at fair value through profit or loss	**3,829**	**7,033**	**4,828**	**458**	**402**	**16,550**
Debt securities in issue	**1,288**	**1,395**	**5,715**	**5,436**	**2,420**	**16,254**
Other liabilities (lease liabilities)	**–**	**2**	**8**	**36**	**30**	**76**
Subordinated liabilities	**–**	**–**	**–**	**551**	**135**	**686**
Total non-derivative financial labilities	**20,626**	**13,082**	**14,050**	**12,999**	**3,920**	**64,677**
Derivative financial liabilities:						
Gross settled derivatives – outflows	**40,793**	**31,915**	**28,034**	**34,784**	**11,653**	**147,179**
Gross settled derivatives – inflows	**(39,055)**	**(30,204)**	**(26,965)**	**(34,107)**	**(12,017)**	**(142,348)**
Gross settled derivatives – net flows	**1,738**	**1,711**	**1,069**	**677**	**(364)**	**4,831**
Net settled derivative liabilities	**11,437**	**–**	**–**	**–**	**–**	**11,437**
Total derivative financial labilities	**13,175**	**1,711**	**1,069**	**677**	**(364)**	**16,268**

The Group	Up to 1 month £m	1-3 months £m	3-12 months £m	1-5 years £m	Over 5 years £m	Total £m
31 December 2019						
Deposits from banks	294	261	514	2,924	–	3,993
Customer deposits	17,531	2,993	2,466	1,392	117	24,499
Financial liabilities at fair value through profit or loss	4,310	5,473	1,959	1,383	1,440	14,565
Debt securities in issue	1,534	2,174	6,084	3,487	–	13,279
Other liabilities (lease liabilities)	–	1	3	33	56	93
Subordinated liabilities	–	–	–	–	698	698
Total non-derivative financial labilities	23,669	10,902	11,026	9,219	2,311	57,127
Derivative financial liabilities:						
Gross settled derivatives – outflows	40,708	41,312	23,168	9,926	3,198	118,312
Gross settled derivatives – inflows	(39,944)	(40,313)	(22,196)	(8,791)	(2,783)	(114,027)
Gross settled derivatives – net flows	764	999	972	1,135	415	4,285
Net settled derivative liabilities	8,965	–	–	–	–	8,965
Total derivative financial labilities	9,729	999	972	1,135	415	13,250

34 Financial risk management (continued)

The Bank	**Up to 1 month £m**	**1-3 months £m**	**3-12 months £m**	**1-5 years £m**	**Over 5 years £m**	**Total £m**
31 December 2020						
Deposits from banks	**251**	**864**	**478**	**4,011**	**–**	**5,604**
Customer deposits	**14,844**	**3,778**	**3,010**	**2,506**	**933**	**25,071**
Financial liabilities at fair value through profit or loss	**3,829**	**7,033**	**4,828**	**458**	**402**	**16,550**
Debt securities in issue	**1,288**	**1,395**	**5,715**	**5,436**	**2,420**	**16,254**
Other liabilities (lease liabilities)	**–**	**1**	**6**	**27**	**22**	**56**
Subordinated liabilities	**–**	**–**	**–**	**551**	**135**	**686**
Total non-derivative financial labilities	**20,212**	**13,071**	**14,037**	**12,989**	**3,912**	**64,221**
Derivative financial liabilities:						
Gross settled derivatives – outflows	**40,793**	**31,915**	**28,034**	**34,784**	**11,653**	**147,179**
Gross settled derivatives – inflows	**(39,055)**	**(30,204)**	**(26,965)**	**(34,107)**	**(12,017)**	**(142,348)**
Gross settled derivatives – net flows	**1,738**	**1,711**	**1,069**	**677**	**(364)**	**4,831**
Net settled derivative liabilities	**11,437**	**–**	**–**	**–**	**–**	**11,437**
Total derivative financial labilities	**13,175**	**1,711**	**1,069**	**677**	**(364)**	**16,268**

The Bank	Up to 1 month £m	1-3 months £m	3-12 months £m	1-5 years £m	Over 5 years £m	Total £m
31 December 2019						
Deposits from banks	294	261	514	2,924	–	3,993
Customer deposits	17,102	2,984	2,437	1,390	117	24,030
Financial liabilities at fair value through profit or loss	4,310	5,473	1,959	1,383	1,440	14,565
Debt securities in issue	1,534	2,174	6,084	3,487	–	13,279
Other liabilities (lease liabilities)	–	–	1	23	46	70
Subordinated liabilities	–	–	–	–	698	698
Total non-derivative financial labilities	23,240	10,892	10,995	9,207	2,301	56,635
Derivative financial liabilities:						
Gross settled derivatives – outflows	40,708	41,312	23,168	9,926	3,198	118,312
Gross settled derivatives – inflows	(39,944)	(40,313)	(22,196)	(8,791)	(2,783)	(114,027)
Gross settled derivatives – net flows	764	999	972	1,135	415	4,285
Net settled derivative liabilities	8,965	–	–	–	–	8,965
Total derivative financial labilities	9,729	999	972	1,135	415	13,250

34 Financial risk management (continued)

The following tables set out the amounts and residual maturities of off balance sheet contingent liabilities, capital commitments and guarantees.

The Group	Up to 1 month £m	1-3 months £m	3-12 months £m	1-5 years £m	Over 5 years £m	Total £m
31 December 2020						
Acceptances and endorsements	**54**	**3**	**–**	**–**	**–**	**57**
Other contingent liabilities	**28**	**84**	**13**	**5**	**–**	**130**
Total contingent liabilities	**82**	**87**	**13**	**5**	**–**	**187**
Lending commitments and guarantees	**1,876**	**655**	**4,987**	**6,764**	**250**	**14,532**
Other commitments	**–**	**–**	**2**	**1**	**–**	**3**
Total commitments and guarantees	**1,876**	**655**	**4,989**	**6,765**	**250**	**14,535**
Total contingents, commitments and guarantees	**1,958**	**742**	**5,002**	**6,770**	**250**	**14,722**
31 December 2019						
Acceptances and endorsements	16	17	24	–	–	57
Other contingent liabilities	96	27	15	128	–	266
Total contingent liabilities	112	44	39	128	–	323
Lending commitments and guarantees	1,744	754	4,858	9,067	280	16,703
Other commitments	–	1	17	1	–	19
Total commitments and guarantees	1,744	755	4,875	9,068	280	16,722
Total contingents, commitments and guarantees	1,856	799	4,914	9,196	280	17,045

The Bank	Up to 1 month £m	1-3 months £m	3-12 months £m	1-5 years £m	Over 5 years £m	Total £m
31 December 2020						
Acceptances and endorsements	**54**	**3**	**–**	**–**	**–**	**57**
Other contingent liabilities	**28**	**84**	**13**	**5**	**–**	**130**
Total contingent liabilities	**82**	**87**	**13**	**5**	**–**	**187**
Lending commitments and guarantees	**1,876**	**655**	**4,987**	**6,764**	**250**	**14,532**
Other commitments	**–**	**–**	**2**	**1**	**–**	**3**
Total commitments and guarantees	**1,876**	**655**	**4,989**	**6,765**	**250**	**14,535**
Total contingents, commitments and guarantees	**1,958**	**742**	**5,002**	**6,770**	**250**	**14,722**
31 December 2019						
Acceptances and endorsements	16	17	24	–	–	57
Other contingent liabilities	96	27	15	128	–	266
Total contingent liabilities	112	44	39	128	–	323
Lending commitments and guarantees	1,744	754	4,858	9,007	280	16,643
Other commitments	–	1	17	1	–	19
Total commitments and guarantees	1,744	755	4,875	9,008	280	16,662
Total contingents, commitments and guarantees	1,856	799	4,914	9,136	280	16,985

35 Capital disclosures

Capital management

Capital is actively managed on an ongoing basis covering the Bank and its regulated subsidiaries. Regulatory capital ratios are a key factor in budgeting and planning processes with updates on forecast and stressed ratios reviewed by the Group Asset and Liability Committee and the Board. Target capital levels take account of regulatory requirements, capacity for growth and to cover uncertainties. Capital policies and procedures are subject to independent oversight.

The Bank measures both its capital requirements and the amount of capital resources it holds to meet those requirements through applying the regulatory framework defined by the Capital Requirements Directive and Regulation (CRD IV), as amended by revisions to the Capital Requirements Directive implemented in December 2020 (CRD V) and by those provisions of the revised Capital Requirements Regulation (CRR II) that came into force in June 2019 and December 2020. The requirements are implemented in the UK by the Prudential Regulation Authority (PRA) and supplemented through additional regulation under the PRA Rulebook.

The UK left the EU on 31 January 2020 but remained subject to changes to EU capital regulation until the end of the transition period on 31 December 2020. Under temporary transitional powers (TTP) granted to the PRA, EU capital rules that existed on 31 December 2020 will continue to generally apply until 31 March 2022. This is subject to revision following any significant changes introduced by UK regulators, including changes which implement the remaining parts of CRR II that are not yet in force.

35 Capital disclosures (continued)

The minimum amount of total capital, under Pillar 1 of the regulatory framework, is set at 8 per cent of total risk-weighted assets. At least 4.5 per cent of risk-weighted assets are required to be covered by common equity tier 1 (CET1) capital and at least 6 per cent of risk-weighted assets are required to be covered by tier 1 capital. These minimum Pillar 1 requirements are supplemented by additional minimum requirements under Pillar 2A of the regulatory framework, the aggregate of which is referred to as the Total Capital Requirement (TCR).

Under Pillar 2A, additional requirements are set through the issuance of a bank specific Individual Capital Requirement (ICR), which adjusts the Pillar 1 minimum requirement for those risks not covered or not fully covered under Pillar 1. A key input into the PRA's ICR process is a bank's own assessment of the amount of capital it needs, a process known as the Internal Capital Adequacy Assessment Process (ICAAP).

A range of additional bank specific regulatory capital buffers apply under CRD IV, which are required to be met with CET1 capital. These include a capital conservation buffer (2.5 per cent of risk-weighted assets) and a time-varying countercyclical capital buffer (0.01 per cent of risk-weighted assets as at 31 December 2020)

The Bank applies the full extent of the IFRS 9 transitional arrangements for capital as set out under CRR Article 473a (as amended via the CRR 'Quick Fix' revisions published in June 2020). Specifically, the Bank has opted to apply both paragraphs 2 and 4 of CRR Article 473a (static and dynamic relief) and in addition to apply a 100 per cent risk weight to the consequential Standardised credit risk exposure add-back as permitted under paragraph 7a of the revisions.

As at 31 December 2020, dynamic relief under the transitional arrangements amounted to £34 million (31 December 2019: £3 million) through CET1 capital.

Regulatory capital development

The regulatory framework within which the Bank operates continues to be developed at a global level through the Financial Stability Board (FSB) and Basel Committee on Banking Supervision (BCBS) and within the UK by the PRA and through directions from the Financial Policy Committee (FPC). The Bank continues to monitor these developments very closely, analysing the potential capital impacts to ensure that, through organic capital generation and management actions the Bank and its regulated subsidiaries continue to maintain a strong capital position that exceeds both minimum regulatory requirements and the Bank's risk appetite and is consistent with market expectations.

Capital resources

Regulatory capital is divided into tiers depending on the degree of permanency and loss absorbency exhibited.

- Common equity tier 1 capital represents the strongest form of capital consisting of shareholders' equity after a number of regulatory adjustments and deductions are applied. These include adjustments for IFRS 9 transitional arrangements, the elimination of the cash flow hedging reserve, the prudent valuation adjustment, the debit valuation adjustment and the accrual for foreseeable dividends
- Fully qualifying additional tier 1 (AT1) capital comprises non-cumulative perpetual securities containing specific provisions to write down the security should the CET1 ratio fall to a defined trigger limit
- Tier 2 (T2) capital comprises certain other subordinated debt securities that do not qualify as AT1. They must have an original term of at least 5 years, cannot normally be redeemed within their first 5 years and are phased out as T2 regulatory capital in the final 5 years before maturity.

The Bank's capital resources are summarised as follows:

	2020 £m	2019 £m
Common equity tier 1 capital	**2,462**	2,381
Additional tier 1 capital	**757**	757
Tier 2 capital	**526**	547
Total capital	**3,745**	3,685

36 Notes to the Cash flow statement

a Change in operating assets

	The Group		The Bank	
	2020 £m	2019[1] £m	**2020 £m**	2019[1] £m
Change in financial assets held at amortised cost	**1,335**	(30)	**1,320**	(2,170)
Changes in amounts due to fellow Lloyds Banking Group undertakings	**(408)**	5,883	**(399)**	4,304
Change in derivative financial instruments and financial assets at fair value	**(5,451)**	(3,772)	**(5,455)**	(3,763)
Change in other operating assets	**(938)**	325	**(942)**	327
Change in operating assets	**(5,462)**	2,406	**(5,476)**	(1,302)

1 Restated, see note 1.

36 Notes to the Cash flow statement (continued)

b Change in operating liabilities

	The Group		The Bank	
	2020 £m	2019[1] £m	**2020 £m**	2019[1] £m
Change in deposits from banks	**1,634**	794	**1,634**	795
Change in customer deposits	**1,069**	(2,329)	**1,102**	(1,003)
Changes in amounts due to fellow Lloyds Banking Group undertakings	**1,645**	(156)	**1,575**	(4,610)
Change in derivative financial instruments and financial liabilities at fair value	**5,502**	3,027	**5,502**	3,028
Change in debt securities in issue	**3,289**	(353)	**3,288**	(353)
Change in other operating liabilities	**470**	79	**473**	40
Change in operating liabilities[2]	**13,609**	1,062	**13,574**	(2,103)

1 Restated, see note 1.

2 Includes £6 million (2019: £65 million) for the Group and £7 million (2019: £48 million) for the Bank in respect of lease liabilities.

c Non-cash and other items

	The Group		The Bank	
	2020 £m	2019[1] £m	**2020 £m**	2019[1] £m
Depreciation and amortisation	**16**	19	**13**	11
Dividends received from subsidiary undertakings	**–**	–	**(57)**	(811)
Impairment of subsidiary undertaking	**–**	–	**72**	640
Foreign exchange element on balance sheet[2]	**86**	139	**83**	134
Other non-cash items	**1**	–	**–**	3
Non-cash and other items	**103**	158	**111**	(23)

1 Restated, see note 1.

2 When considering the movement on each line of the balance sheet, the impact of foreign exchange rate movements is removed in order to show the underlying cash impact.

d Analysis of cash and cash equivalents as shown in the balance sheet

	The Group		The Bank	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Cash and balances with central banks	**23,369**	16,250	**23,369**	16,250
Less: mandatory reserve deposits[1]	**(160)**	(111)	**(160)**	(111)
	23,209	16,139	**23,209**	16,139
Loans and advances to banks	**5,260**	4,813	**5,231**	4,792
Less: amounts with a maturity of three months or more	**(2,099)**	(1,858)	**(2,099)**	(1,858)
	3,161	2,955	**3,132**	2,934
Total cash and cash equivalents	**26,370**	19,094	**26,341**	19,073

1 Mandatory reserve deposits are held with local central banks in accordance with statutory requirements; these deposits are not available to finance the Group's day-to-day operations.

37 Events since the balance sheet date

There are no events since the balance sheet date to disclose.

38 Future accounting developments

The following pronouncements are not applicable for the year ending 31 December 2020 and have not been applied in preparing these financial statements.

With the exception of certain minor amendments, as at 11 March 2021 these pronouncements have been endorsed for use in the United Kingdom.

Interest Rate Benchmark Reform

The IASB's Phase 2 amendments in response to issues arising from the replacement of interest rate benchmarks in a number of jurisdictions are effective for annual periods beginning on or after 1 January 2021.

Under these amendments, an immediate gain or loss is not recognised in the income statement where the contractual cash flows of a financial asset or financial liability are amended as a direct consequence of the rate reform and the revised contractual terms are economically equivalent to the previous terms. In addition, hedge accounting is continued for relationships that are directly affected by the reform.

These amendments are not expected to have a significant impact on the Group.

Minor amendments to other accounting standards

The IASB has issued a number of minor amendments to IFRSs effective 1 January 2021 and in later years (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.

39 Ultimate parent undertaking and controlling party

Lloyds Bank Corporate Markets plc and its subsidiaries form a leading UK-based financial services group, whose businesses provide a wide range of banking and financial services in the UK and overseas.

Lloyds Bank Corporate Markets plc's immediate parent undertaking and ultimate parent undertaking and controlling party is Lloyds Banking Group plc which is incorporated in Scotland. Copies of the consolidated annual report and accounts of Lloyds Banking Group plc may be obtained from Lloyds Banking Group's head office at 25 Gresham Street, London EC2V 7HN or downloaded via www.lloydsbankinggroup.com.

40 Subsidiaries and related undertakings

In compliance with Section 409 of the Companies Act 2006, the following comprises a list of all related undertakings of the Bank, as at 31 December 2020. The list includes each undertaking's registered office and the percentage of the class(es) of shares held by the Group. All shares held are ordinary shares unless indicated otherwise in the notes.

The Bank directly or indirectly holds 100 per cent of the share class and a majority of voting rights in the following undertakings.

Subsidiary undertakings	Bank interest	Registered Address
Black Horse Offshore Limited	100.00%	11-12 Esplanade, St Helier, Jersey JE4 8ZU
Lloyds America Securities Corporation	100.00%[a]	1095 Avenue of the Americas, 34th Floor, New York, NY 10036, United States
Lloyds Bank (International Services) Limited	100.00%	11-12 Esplanade, St Helier, Jersey JE2 3QA
Lloyds Bank Corporate Asset Finance (No.1) Limited	100.00%	25 Gresham Street, London EC2V 7HN
Lloyds Bank Corporate Markets Wertpapierhandelsbank GmbH	100.00%	Thurn-Und, Frankfurt Am Main, 60313, Germany
Lloyds Bank International Limited	100.00%	11-12 Esplanade, St Helier, Jersey JE2 3QA
Lloyds Corporate Services (Jersey) Limited	100.00%	11-12 Esplanade, St Helier, Jersey JE2 3QA
Lloyds Holdings (Jersey) Limited	100.00%	11-12 Esplanade, St Helier, Jersey JE2 3QA
Lloyds Nominees (Guernsey) Limited	100.00%	Sarnia House, Le Truchot, St. Peter Port, Guernsey, GY1 4EF
Lloyds Securities Inc.	100.00%[b]	1095 Avenue of the Americas, 34th Floor, New York, NY 10036, United States
Nominees (Jersey) Limited	100.00%	11-12 Esplanade, St Helier, Jersey JE2 3QA

Notes

a. 10,000 US$ No par value

b. 10 US$ 0.1% common