Lloyds Bank plc

Q3 2017 Interim Management Statement

25 October 2017

BASIS OF PRESENTATION

This release covers the results of Lloyds Bank plc (the Bank) together with its subsidiaries (the Group) for the nine months ended 30 September 2017.

Unless otherwise stated, income statement commentaries throughout this document compare the nine months ended 30 September 2017 to the nine months ended 30 September 2016, and the balance sheet analysis compares the Group balance sheet as at 30 September 2017 to the Group balance sheet as at 31 December 2016.

FORWARD LOOKING STATEMENTS

This document contains certain forward looking statements with respect to the business, strategy and plans of Lloyds Bank Group and its current goals and expectations relating to its future financial condition and performance. Statements that are not historical facts, including statements about Lloyds Bank Group's or its directors' and/or management's beliefs and expectations, are forward looking 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 the plans, objectives, expectations, estimates and intentions expressed in such forward looking statements made by the Lloyds Bank 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 (including low or negative rates), exchange rates, stock markets and currencies; the ability to access sufficient sources of capital, liquidity and funding when required; changes to the Lloyds Bank Group's or Lloyds Banking Group plc's credit ratings; the ability to derive cost savings and other benefits including, but without limitation as a result of any acquisitions, disposals and other strategic transactions; changing customer behaviour including consumer spending, saving and borrowing habits; changes to borrower or counterparty credit quality; instability in the global financial markets, including Eurozone instability, instability as a result of the exit by the UK from the European Union (EU) 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; 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 and other disasters, adverse weather and similar contingencies outside the Lloyds Bank Group's or Lloyds Banking Group plc's control; inadequate or failed internal or external processes or systems; acts of war, other acts of hostility, terrorist acts and responses to those acts, geopolitical, pandemic or other such events; changes in laws, regulations, accounting standards or taxation, including as a result of the exit by the UK from the EU, or a further possible referendum on Scottish independence; changes to regulatory capital or liquidity requirements and similar contingencies outside the Lloyds Bank Group's or Lloyds Banking Group plc's control; the policies, decisions and actions of governmental or regulatory authorities or courts in the UK, the EU, the US or elsewhere including the implementation and interpretation of key legislation and regulation together with any resulting impact on the future structure of the Lloyds Bank Group; the ability to attract and retain senior management and other employees; actions or omissions by the Lloyds Bank Group's directors, management or employees including industrial action; changes to the Lloyds Bank Group's post-retirement defined benefit scheme obligations; the extent of any future impairment charges or write-downs caused by, but not limited to, depressed asset valuations, market disruptions and illiquid markets; the value and effectiveness of any credit protection purchased by the Lloyds Bank 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 together with examples of forward looking statements. 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 Lloyds Bank Group expressly disclaims any obligation or undertaking to release publicly any updates or revisions to any forward looking statements. 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.

REVIEW

As a result of the requirements of the ring-fencing regulations, the Bank expects to sell its subsidiary, Scottish Widows Group Limited, to its ultimate holding company during 2018. This is only an internal reorganisation within the Lloyds Banking Group, but due to the significance of the Scottish Widows entities they have been classified as discontinued operations for the purposes of the Bank's consolidated statutory reporting.

Continuing operations

During the nine months to 30 September 2017, the Group recorded a profit before tax from its continuing operations of £4,342 million compared with a profit before tax in the nine months to 30 September 2016 of £1,332 million. The results have been affected by a number of one-off items. In the nine months to 30 September 2016 the Group had incurred a loss of £993 million on transactions related to Lloyds Banking Group's tender offers and redemptions in respect of its Enhanced Capital Notes which completed in March 2016 and a loss of £1,026 million which arose pursuant to a restructuring of the Bank's capital instruments in June 2016. In the nine months to 30 September 2017 the Group has incurred conduct charges of £1,211 million in its continuing businesses compared to £1,553 million in the nine months to 30 September 2016. Excluding these items from both periods, the Group recorded a profit before tax of £5,553 million in the nine months to 30 September 2017, an increase of £649 million, or 13 per cent, from £4,904 million in the nine months to 30 September 2016.

Total income increased by £2,635 million, or 25 per cent, to £13,117 million in the nine months to 30 September 2017 compared with £10,482 million in the nine months to 30 September 2016, comprising a £1,879 million increase in other income and a £756 million increase in net interest income.

Net interest income was £9,130 million in the nine months to 30 September 2017; an increase of £756 million, or 9 per cent, compared to £8,374 million in the nine months to 30 September 2016. Average interest-earning assets fell, reflecting lower balances in run-off, global corporates and closed mortgage books, but the net interest margin improved driven by lower deposit and wholesale funding costs which more than offset continued pressure on asset margins.

Other income was £1,879 million higher at £3,987 million in the nine months to 30 September 2017 compared to £2,108 million in the nine months to 30 September 2016. Net fee and commission income was £2 million lower at £1,388 million compared to £1,390 million in the nine months to 30 September 2016. Net trading income increased by £62 million, or 9 per cent, to £779 million in the nine months to 30 September 2017 compared to £717 million in the nine months to 30 September 2016; in part due to a net release of £50 million in relation to the net derivative valuation adjustment compared to a charge of £42 million in the nine months to 30 September 2016. Other operating income was £1,819 million higher at £1,820 million in the nine months to 30 September 2017 compared to £1 million in the nine months to 30 September 2016. Other operating income in the nine months to 30 September 2016 included the losses on capital transactions totalling £2,019 million detailed above but this impact is partly offset by a £194 million reduction in gains on sale of available-for-sale financial assets. Losses of £15 million on liability management actions in the nine months to 30 September 2017 compared to gains of £133 million in the nine months to 30 September 2016.

Operating expenses decreased by £283 million, or 3 per cent, to £8,321 million in the nine months to 30 September 2017 compared with £8,604 million in the nine months to 30 September 2016. A provision of £1,211 million was made in respect of conduct issues in the nine months to 30 September 2017 compared to a charge of £1,553 million in the same period in 2016. The charge in 2017 includes £700 million in respect of PPI; claim levels increased as expected in the third quarter following the FCA advertising campaign, reaching about 16,000 per week and have now reduced to about 11,000 per week, above the Group's assumed run-rate of about 9,000 per week. Other conduct provisions of £511 million cover a number of items including packaged bank accounts and arrears handling. Following a review of the Group's arrears handling activities, the Group has put in place a number of actions to improve further its handling of customers in these areas and the Group is reimbursing mortgage arrears fees. The Group is also currently undertaking a review of the HBOS Reading fraud and is in the process of paying compensation to the victims of the fraud for economic losses, ex-gratia payments and awards for distress and inconvenience. A provision of £100 million was taken and reflects the estimated compensation costs for HBOS Reading.

REVIEW (continued)

Excluding all conduct charges from both years, operating expenses were £59 million higher at £7,110 million in the nine months to 30 September 2017 compared to £7,051 million in the nine months to 30 September 2016. Staff costs were £92 million, or 3 per cent, lower at £3,358 million in the nine months to 30 September 2017 compared with £3,450 million in the nine months to 30 September 2016; annual pay rises have been offset by the impact of headcount reductions resulting from the Group's rationalisation programmes and there has been a reduction in severance costs. Premises and equipment costs were £56 million or 11 per cent, higher at £560 million in the nine months to 30 September 2017 compared with £504 million in the nine months to 30 September 2016, in part due to lower profits on sale of tangible assets. Other expenses were £132 million, or 10 per cent, higher at £1,515 million in the nine months to 30 September 2017 compared to £1,383 million in the nine months to 30 September 2016. Depreciation and amortisation costs were £37 million, or 2 per cent, lower at £1,677 million in the nine months to 30 September 2017 compared to £1,714 million in the nine months to 30 September 2016, as higher depreciation on operating lease assets due to increased balances has been offset by reduced charges on intangible assets following certain intangibles related to the acquisition of HBOS in 2009 becoming fully amortised.

Impairment losses decreased by £92 million, or 17 per cent, to £454 million in the nine months to 30 September 2017 compared with £546 million in the nine months to 30 September 2016; with the decrease being due to a charge of £6 million in the nine months to 30 September 2017, compared to £146 million in the nine months to 30 September 2016, in respect of the impairment of available-for-sale financial assets. Impairment losses in respect of loans and advances to customers were £40 million, or 10 per cent, higher at £454 million in the nine months to 30 September 2017 compared with £414 million in the nine months to 30 September 2016; however the charge in 2017 includes £63 million from the consolidation of MBNA, excluding which the charge is £23 million lower. The UK housing market has been resilient and overall credit performance in the mortgage book remains stable. The Motor Finance book benefits from conservative residual values and prudent provisioning with stable credit performance. The credit card book continued to perform strongly, with reductions in persistent debt, and benefiting from a conservative risk appetite. The MBNA portfolio is performing in line with both the Group's expectations and the existing credit card book.

In the nine months to 30 September 2017, the Group recorded a tax charge in respect of its continuing operations of £1,304 million compared to a charge of £703 million in the nine months to 30 September 2016, representing an effective tax rate of 30 per cent, compared to the standard UK corporation tax rate of 19.25 per cent, principally as a result of the banking surcharge and restrictions on the deductibility of conduct provisions.

Discontinued operations

During the nine months to 30 September 2017, the Group recorded a profit before tax from discontinued operations of £613 million compared with a profit before tax in the nine months to 30 September 2016 of £451 million.

Total income decreased by £9,192 million, or 44 per cent, to £11,876 million in the nine months to 30 September 2017 compared with £21,068 million in the nine months to 30 September 2016, comprising a £10,102 million decrease in other income and a £910 million improvement in net interest income.

Net interest income was an expense of £829 million in the nine months to 30 September 2017; an improvement of £910 million compared to an expense of £1,739 million in the nine months to 30 September 2016. There was a decrease of £778 million in the nine months to 30 September 2017 in the amounts payable to unit holders in those Open-Ended Investment Companies (OEICs) included in the consolidated results of the Group, reflecting relative levels of investment returns on the assets held by the OEICs. After adjusting for these amounts payable to unitholders, net interest income was £132 million higher.

REVIEW (continued)

Other income was £10,102 million lower at £12,705 million in the nine months to 30 September 2017 compared to £22,807 million in the nine months to 30 September 2016. Net fee and commission income was £16 million or 12 per cent, lower at a deficit of £148 million compared to a deficit of £132 million in the nine months to 30 September 2016. Net trading income decreased by £9,327 million, or 59 per cent, to £6,447 million in the nine months to 30 September 2017 compared to £15,774 million in the nine months to 30 September 2016; with reduced gains on debt securities and equity investments in line with market performance. Insurance premium income was £413 million, or 6 per cent, lower at £6,009 million in the nine months to 30 September 2017 compared with £6,422 million in the same period in 2016; there was a decrease of £325 million in life insurance premiums, with lower levels of bulk annuity income only partly offset by increases in corporate pension products, and a decrease of £88 million in general insurance premiums following the run-down of closed products. Other operating income was £346 million lower at £397 million in the nine months to 30 September 2017 compared to £743 million in the nine months to 30 September 2016.

Insurance claims expense was £9,307 million lower at £10,535 million in the nine months to 30 September 2017 compared to £19,842 million in the nine months to 30 September 2016. The insurance claims expense in respect of life and pensions business was £9,287 million lower at £10,281 million in the nine months to 30 September 2017 compared to £19,568 million in the nine months to 30 September 2016; this decrease reflects a similar reduction in net trading income. Insurance claims in respect of general insurance business were £20 million, or 7 per cent, lower at £254 million in the nine months to 30 September 2017 compared to £274 million in the same period in 2016.

Operating expenses decreased by £47 million, or 6 per cent to £728 million in the nine months to 30 September 2017 compared with £775 million in the nine months to 30 September 2016.

Balance sheet and capital

Total assets were £6,195 million lower at £824,732 million at 30 September 2017 compared to £830,927 million at 31 December 2016. Loans and advances to customers were £10,739 million higher at £462,021 million at 30 September 2017 compared to £451,282 million at 31 December 2016; the addition of £8,003 million of lending following the acquisition of MBNA and a £5,841 million increase in reverse repurchase agreement balances together with the impact of the reacquisition of a portfolio of mortgages from TSB and growth in Consumer Finance and SME lending have more than offset reductions in the larger corporate sector, as the Group focuses on optimising capital and returns, and in closed mortgage books.

Total liabilities were £6,823 million, or 1 per cent, lower at £773,853 million at 30 September 2017 compared to £780,676 million at 31 December 2016. Deposits from banks were £12,063 million, or 77 per cent, higher at £27,753 million at 30 September 2017 compared to £15,690 million at 31 December 2016 as a result of an increase of £14,184 million in repurchase agreements, used as a favourable form of funding. Customer deposits were £1,512 million lower at £413,948 million compared to £415,460 million at 31 December 2016 as a £1,760 million reduction in repurchase agreement balances and reductions in non-relationship deposit balances were more than offset by strong inflows from Commercial clients. Debt securities in issue were £10,696 million, or 14 per cent, lower at £64,037 million at 30 September 2017 compared to £74,733 million at 31 December 2016 following maturities of some tranches of securitisation notes and covered bonds. Other liabilities were £4,182 million, or 33 per cent, higher at £16,935 million at 30 September 2017 compared to £12,753 million at 31 December 2016.

At the end of September the credit rating for Lloyds Bank plc was upgraded by one notch to Aa3 by Moody's. This reflected improvements in asset risk and capital levels combined with an expectation of improving profitability as conduct charges decrease.

Total equity was £628 million higher at £50,879 million at 30 September 2017 compared to £50,251 million at 31 December 2016; as retained profits have been partly offset by dividend payments and negative movements in the Group's cash flow hedging reserve.

REVIEW (continued)

The Group's common equity tier 1 capital ratio increased to 15.5 per cent at 30 September 2017 from 15.1 per cent at 31 December 2016, largely driven by retained profit for the period, net of dividends paid and accrued, and movements in reserves and other items, offset by an increase in the deduction for goodwill and other intangible assets following the acquisition of MBNA. The tier 1 capital ratio increased to 18.0 per cent from 17.7 per cent at 31 December 2016. The total capital ratio remained flat at 21.2 per cent. Risk-weighted assets increased by £1,544 million, or 1 per cent, to £217,727 million at 30 September 2017, compared to £216,183 million at 31 December 2016.

Capital resources (transitional)	At 30 Sept 2017 £ million	At 31 Dec 2016 £ million
Common equity tier 1		
Shareholders' equity per balance sheet	**46,889**	46,289
Deconsolidation adjustments[1]	**999**	911
Other adjustments	**(2,373)**	(3,795)
Deductions from common equity tier 1	**(11,705)**	(10,861)
Common equity tier 1 capital	**33,810**	32,544
Additional tier 1 instruments	**6,583**	7,061
Deductions from tier 1	**(1,261)**	(1,329)
Total tier 1 capital	**39,132**	38,276
Tier 2 instruments and eligible provisions	**8,296**	9,106
Deductions from tier 2	**(1,361)**	(1,571)
Total capital resources	**46,067**	45,811
Risk-weighted assets		
Credit risk	**168,948**	166,621
Counterparty credit risk	**6,449**	8,419
Contributions to the default fund of a central counterparty	**530**	340
Credit valuation adjustment risk	**762**	864
Operational risk	**26,222**	25,292
Market risk	**3,439**	3,147
Threshold risk-weighted assets	**11,377**	11,500
Total risk-weighted assets	**217,727**	216,183
Ratios		
Common equity tier 1 capital ratio	**15.5%**	15.1%
Tier 1 capital ratio	**18.0%**	17.7%
Total capital ratio	**21.2%**	21.2%

[1] Deconsolidation adjustments relate to the deconsolidation of certain Group entities for regulatory capital purposes, being primarily the Group's Insurance business.

STATUTORY CONSOLIDATED INCOME STATEMENT (UNAUDITED)

	Nine months to 30 Sept 2017 £ million	Nine months to 30 Sept 2016 £ million
Interest and similar income	**11,790**	12,681
Interest and similar expense	**(2,660)**	(4,307)
Net interest income	**9,130**	8,374
Fee and commission income	**2,153**	2,113
Fee and commission expense	**(765)**	(723)
Net fee and commission income	**1,388**	1,390
Net trading income	**779**	717
Other operating income	**1,820**	1
Other income	**3,987**	2,108
Total income	**13,117**	10,482
Regulatory provisions	**(1,211)**	(1,553)
Other operating expenses	**(7,110)**	(7,051)
Total operating expenses	**(8,321)**	(8,604)
Trading surplus	**4,796**	1,878
Impairment	**(454)**	(546)
Profit before tax – continuing operations	**4,342**	1,332
Taxation	**(1,304)**	(703)
Profit after tax – continuing operations	**3,038**	629
Profit after tax – discontinued operations	**521**	320
Profit for the period	**3,559**	949
Profit attributable to ordinary shareholders	**3,295**	824
Profit attributable to other equity holders[1]	**205**	49
Profit attributable to equity holders	**3,500**	873
Profit attributable to non-controlling interests	**59**	76
Profit for the period	**3,559**	949

[1] The profit after tax attributable to other equity holders of £205 million (nine months to 30 September 2016: £49 million) is offset in reserves by a tax credit attributable to ordinary shareholders of £55 million (nine months to 30 September 2016: £14 million).

STATUTORY BALANCE SHEET (UNAUDITED)

	At 30 Sept 2017 £ million	At 31 Dec 2016 £ million
Assets		
Cash and balances at central banks	**49,771**	47,452
Trading and other financial assets at fair value through profit or loss	**48,735**	51,198
Derivative financial instruments	**25,582**	33,859
Loans and receivables:		
Loans and advances to banks	**5,559**	5,583
Loans and advances to customers	**462,021**	451,282
Debt securities	**3,703**	3,397
Due from fellow Lloyds Banking Group undertakings	**7,082**	5,624
	478,365	465,886
Available-for-sale financial assets	**47,127**	56,524
Assets of held-for-sale disposal group	**151,423**	158,194
Other assets	**23,729**	17,814
Total assets	**824,732**	830,927
Liabilities		
Deposits from banks	**27,753**	15,690
Customer deposits	**413,948**	415,460
Deposits from fellow Lloyds Banking Group undertakings	**11,093**	5,444
Trading and other financial liabilities at fair value through profit or loss	**54,715**	54,504
Derivative financial instruments	**26,414**	33,896
Debt securities in issue	**64,037**	74,733
Subordinated liabilities	**14,996**	17,258
Liabilities of held-for-sale disposal group	**143,962**	150,938
Other liabilities	**16,935**	12,753
Total liabilities	**773,853**	780,676
Shareholders' equity	**46,889**	46,289
Other equity interests	**3,217**	3,217
Non-controlling interests	**773**	745
Total equity	**50,879**	50,251
Total equity and liabilities	**824,732**	830,927

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The statement can also be found on the Group's website – www.lloydsbankinggroup.com

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