LLOYDS BANKING GROUP PLC – Q3 2018 INTERIM MANAGEMENT STATEMENT PRESENTATION

Thursday 25 October 2018

George Culmer, Chief Financial Officer

Good morning everyone and thanks for joining today's call. I have a couple of slides on our results and strategic progress, with some more detail in the appendices. We will then have just under an hour for Q&A and we have also arranged a follow up session next week.

I'll cover first the financial performance for the nine months on slide 1. The Group continues to deliver strong and sustainable financial performance. Statutory profit after tax of £3.7 billion is up 18 per cent on prior year with underlying profit up 5 per cent, and 11 per cent reduction in below the line charges and an improved effective tax rate of 26 per cent.

Net income for the nine months is up 2 per cent at £13.4 billion, with net interest income up 5 per cent, supported by a stable margin of 2.93 with slightly higher average interest earning assets.

Other income is in line with last year after excluding the sale of Vocalink, driven by a strong Q3, which was 4 per cent up on a year ago, and a strong 9 month performance from Insurance, led by new business growth. Operating lease depreciation is also down 5 per cent, due mainly to accelerated write-offs in 2017.

Operating costs are also down on prior year for both the quarter and year to date, with a 4 per cent reduction in BAU costs for the 9 months, more than offsetting higher investment spend. Remediation costs are down 30 per cent year on year and our market leading cost:income ratio has again improved to 47.5 per cent, down 2.5 percentage points.

Credit quality remains strong and we continue to see no deterioration across the portfolio. The gross asset quality ratio of 28 basis points is in line with previous years, and new to arrears remain stable in both mortgages and cards.

The net asset quality ratio has increased to 22 basis points due entirely to the expected lower write backs and releases, and we continue to expect the full year AQR to be below 25.

In terms of growth, we are delivering targeted lending growth in SME, Mid-markets and motor finance, with Group loans and advances at £445 billion, up £2.3 billion in the quarter. We also continue to optimise our funding, with target growth in Retail and Commercial current accounts, which are up £7.5 billion in 2018.

Returns also continue to increase. The underlying return on tangible equity was up 1.4 points at 16.2 per cent, while the statutory return was 13 per cent, up 2.5 percentage points.

Capital also remains strong with an increase of 41 basis points in the quarter, comprising an underlying movement of 49 points offset by 11 for pensions and 5 from market movements. Capital build is now 162 basis points for the year to date, and we are on track to meet our full year guidance of around 200 with Q4 benefits from the final Insurance dividend but also impacted by further pension contributions and the bank levy.

TNAV at 51.3 pence per share is up 0.3 in the quarter, before the 1.07p impact of paying the interim dividend.

And we completed our £1 billion buyback in August and have now returned more than £3.2 billion to shareholders in 2018, the equivalent of over 4.5 pence per share.

Finally, we are reaffirming our financial targets for 2018, including the margin of around 2.93 per cent and, as I've mentioned, asset quality ratio below 25 basis points, and capital build of around 200 basis points. And we are also reaffirming our longer-term guidance as well.

I will now turn briefly to the progress we have made in delivering the Group's strategy. As we set out in February, we are building on the strong progress of recent years to further digitise the Group, maximise its capabilities, deliver a leading customer experience and transform our ways of working.

We have made a strong start, having already invested around £600 million out of our target of more than £3 billion over the next 3 years.

In terms of Digitising the Group, our investment in robotics has driven significant process improvements, with around 600,000 colleague hours saved to date, while our Private Cloud solution is now operational and delivering a more efficient, scalable and flexible infrastructure.

On developing a Leading Customer Experience, we have transformed branch account opening journeys for current accounts, savings, loans and credit cards, reducing average account opening times from over 50 minutes to around half an hour.

And within the next month we will be launching our integrated, API-only solution for Open Banking.

Within Maximising Capabilities, one of our key goals is to develop the Group's Financial Planning & Retirement proposition. And our FP&R business is now delivering real growth with sales of workplace pensions, retirement accounts and protection up between 30 and 40 per cent on prior year, while growth in assets under administration is ahead of plan, up more than £11 billion so far this year, driven by organic flows and the acquisition of Zurich's UK workplace pensions and savings business.

At the same time, we have rolled out our single customer view, enabling more than 3 million customers to see their banking and insurance products in one place for the first time, and this will rise to around 4 million customers by year end.

You will also have seen that on Tuesday we announced an agreement with Schroder's. This unique combination of two of the UK's strongest financial services businesses and brands creates a market-leading wealth proposition for affluent customers, and addresses the growing gap in the advice market through a personalised, advice-led financial planning proposition. We have an ambitious medium-term strategy and aim for the JV to be a top 3 UK financial planning business within 5 years.

We are also taking a stake in Cazenove's UK private client business, which allows our high net worth clients to benefit from its leading wealth management proposition.

This agreement is an important step in building our customer propositions and our FP&R proposals and the growth from this initiative is in addition to our existing £50 billion of assets under administration target.

So, there is much going on. We have made a strong start to the latest strategic plan. We are delivering strong and sustainable financial results and we face the future with confidence and reaffirm our financial targets.

That's all I was going to say up front and we will now turn to Q&A.

End of presentation

Question and Answer Session

Question 1: Raul Sinha, JP MORGAN
Morning George. I hope you are not calling the top of the cycle with your retirement, but I have two questions.

George Culmer
I'm not going just yet.

Raul Sinha
Just two quick ones really. The first one is, I was hoping you could provide us with any more colour on the other income performance this quarter which is up 4 per cent?

And the second question was just your broader thoughts on the mortgage market. I am really interested in what are the marginal returns do you think the market is operating at, at current spin levels? Thanks.

Answer: George Culmer
Okay, as far as the answer to the latter it's what capital we put behind it, but we can come to that. So yes the OOI was up sort of 4 per cent quarter on quarter Q3 versus Q3 so that was about £70 million or so I think within that. In terms of things like the usual suspects, gilts, where we continue to be a seller of gilts. I think we had about £68 million or so in the Q3 versus about £55 million in the equivalent quarter, so a slight contribution there quarter on quarter. I think gilts by the way in Q4 will be at a slightly lower level as we move forward into Q4. A big contributor was LDC you will have seen some of the stuff around NEC sale etc. So NEC were about £60 million up quarter on quarter. And then relatively flat in terms of the other businesses. Across the 9 months though I should call out and I said it in the Presentation, whilst insurance, which tends to be slightly lumpy through the quarters, was relatively flat Q3 on Q3 – for the 9 months we have seen a strong performance and great growth in new business which I pulled out, which is up, the sales are up sort of 40-50 per cent. So it is a tremendous performance in line with what we are talking about.

In terms of Q3 versus Q3, relatively stable across the main core businesses in terms of Retail, Commercial and Insurance as I said in the three months bit. You have got things like LDC contribution coming through in Q3.

In terms of mortgage markets, look it is kind of more of the same. And as you know and you have been monitoring it, having things got a little better in terms of pricing first part of the year, certainly got slightly tougher post summer. Sort of encouraged with what you hear others talk about, it would be good to see that reflected in action. In terms of returns people will talk about some pretty chunky returns in terms of mortgage front book prices, but that all depends on what capital you put behind them as I was saying. And I think if you look at sort of leverage type ratio capital which is where we will obviously go in terms of things like ring fencing and we are talking about doubling the amount of capital to have to put behind it. I think you get back to just sort of scraping into the sort of double digit, that type of return.

Raul Sinha
Okay, thanks very much.

Question 2: Chris Manners, BARCLAYS
Good morning George. So just two questions if I may. The first one was about the benefit of the rate hike and how much came in Q3 versus how much we should expect in Q4. I guess we had the rate hike in August you then notify your customers before you put up their SVR. So just maybe a bit of colour on the phasing of when that benefit comes through and how that has benefited you in the quarter we have just had?

And then the second question was on the loan growth. Your Q on Q loan growth obviously flagged in the statement, £2.3 billion, that is pretty encouraging. Could you maybe share with us a little bit of colour about where you think the loan growth is, is it going to continue at that pace and if that loan growth is actually going to translate into earning asset growth because obviously that is something that we are all watching. Thanks.

Answer: George Culmer
Hi Chris, So yeah, I will deal with the second one first. Again and some of these will be familiar things to you, but we continue to target the usual suspects and continue to be important to the SMEs which is up in the quarter, Mid Markets will be up and would continue to expect in the unsecured we will probably track market type growth with the sort of 3 per cent going forward. We talk about, again I think open book mortgages are dead flat I think in terms of the Q3 position versus start of the year, but I would still expect to close the year marginally up and I would still expect some marginal growth as we move forward.

So all that, you know going the other way, I have got a bit of run up book down, but some of the big ones have gone out there and you have seen the Irish book actually come out of the RWAs because cash came in for that during Q3 as we expected so that has now gone. So I would place all those pieces together to give you some upward momentum in RWAs as we move forward as we put those pieces together.

The benefit of the rate hike, we are not going to see a huge number. I think I called out 25 basis points sensitivity at full year, about 12 months seems to be about £100 million, I think Q2, because we have invested some funds it is probably slightly under that now. So that is about £80 million and that is a sort of 12 month number. So quarter on quarter it gives you the sort of indication of the type of impact which isn't a big number.

You are right, in terms things like liability prices and savings prices, we continue to put a small amount through and we continue to benefit from our continued management of funds. If I look at for example, even after the rate hike came through, if I look at my total cost of my savings book, I think for Q3 it is round about sort of 48 basis points which is pretty much the same as it was in Q2 and that is the other side of the rate hike. So you can see sort of what we have done and what we haven't done in terms of passing that through. And on the other side obviously we pushed that through in terms of asset prices. So I won't give you a number, but you won't see a material impact in the quarter on quarter for 25 basis points, it takes further for it to work through. And as you know it is more around things like 5 year swaps flow through into structural hedge and then through into the results.

Chris Manners
Okay, thank you very much.

<u>Question 3: Jason Napier, UBS</u>
Good morning George and congratulations on the retirement. So three questions if I could. Two simple ones and then one on the Schroders Agreement. First of all on costs. The trajectory is pretty strong into the third quarter. I just wanted to check whether there was anything to call out in terms of lumpiness of forward investment plans or whether that is sustainable or indeed a base from which you might improve?

Secondly just to confirm on the impairment line. There have been no changes to IFRS 9 assumptions and as things stand your assumption set is in line with consensus expectations. Is there anything to call out in terms of timing and when those things are revisited and so on?

Lastly, at a kind of practical level I appreciate the JV will be set up and become operational next year, but I am just trying to picture what the, how it will work from a customer standpoint, referrals, branding and kind of service model for the mass affluent model? Thank you.

Answer: George Culmer
Okay. Hi Jason. So in terms of cost, there is nothing particular to call out. Again you see that we are marginally down year to date and marginally down in Q3. We are actually sticking by our guidance to be below 8 by 2020. And the low cost:income ratio in the low 40s. Q4 you obviously have this bank levy come through which is always a couple of hundred million in Q4 but as you know that is a year after year impact. But no, I don't see anything funny in terms of how we got here or go forward and we have got very much commitment to continue to lower that cost:income ratio. And what you see is the continuation of that which we have been doing which is investing in technology, our structured approach to driving down these costs. A real industrialised process within the Group. And just to continue a massive focus upon this. So it is a base on which we will move forward and it is a base on which we will continue to reduce that cost number. So I don't think there is anything exceptional that I will call out and you know about the bank levy anyway.

On IFRS 9, no material changes. As you know in terms of a process perspective, you each quarter look at your, the economic scenarios. And we refresh our outlook as we move through each quarter which we have done this year as part, sorry this quarter, as part of the process. The impact of refresh is nothing has deviated from the mean and you have a small impact in the tens of millions so it is a very minor movement. But we continue to look out. Our house view is again we think there will be a withdrawal agreement. What we have seen in the economy, it is continued robustness, we call out in terms of no signs of deterioration etc., which you would have seen. We are still in the 1½ per cent in terms of GDP. You will have seen the record levels of employment and the low levels of unemployment. You've seen wage growth outstripping inflation etc. So refuelling the consumer purse if you like. So we continue to see a very resilient economy which we have called out for the last couple of years. And that is what we see as we move forward.

Finally on the Schroders bit, look we are massively excited by this and our ability to work with them and have a holistic offering to our customer base. And as we go forward, what we essentially see it in three groupings. There is, we are building with our own FP&R, a sort of digitised execution only capacity, but we are building in-house. So very much a sort of mass market type offering as I say digitised, non-advice. You have then got within the joint venture this personalised, advice-led capability which we think this is an attractive part of the market, it is growing for all the reasons you know, demographics, the switch from DB to DC etc., pensions freedom and the consequence of some of the change in regulations. This is underserved and we see a big price here. We have got about £13 billion of assets which we will move over. We will also transfer over our 300 or so advisers into this.

But we think the bringing together of the Schroder's investment expertise, platform technology with our digital capability, our franchise base and both our brands into this, gives an offering that is hugely exciting. The way it would work is in terms of, you will have, the ongoing referrals from our franchise, our sort of 25-30 million customer base, and the ability to refer into this JV and then the provision of high quality advice with high quality product within that joint venture. And then over to the far right hand side, we have also got this 20 per cent, 19.9 per cent stake in Cazenove which for the high net worth individuals, it will give them access to us. So from our perspective it gives you joined up across the waterfront for execution only, for the appropriate market place, an advice-led proposition for the affluent and then access to this high net worth.

And in working with Schroder we are massively excited in terms of similar views of culture, similar views of ambition and we have talked about wanting to be a top 3 within 5 years. Already about number 4 or 5 at the £13 billion. To get to that top 3, I think we would have to be at the sort of £25 billion type size for assets under administration. We see that as a very viable target. Organic, we would be open to inorganic through this JV as well in terms of getting there. But as I say, we have big ambitions for this and we have massive excitement about the opportunity.

Jason Napier
Thank you.

<u>Question 4: Rohith Chandra-Rajan, BAML</u>
Morning George. I wonder if I could just come back on your comments earlier on the mortgage market if you don't mind given the prices we have seen. Based on what you said about your consideration of returns, I was wondering what you can do in terms of positioning the mortgage book and if there are any particular parts of the market that you are finding more attractive at the moment? So that is sort of on the asset side.

And are there any additional levers you can pull on the liability side to the ones you have already talked about? You know should these trends continue in order to try and defend the margin over the next few years? So that was the first one.

The second one, hopefully quite a quick one, just in terms of tangible book evolution in the 4th quarter. I wondered if there was anything apart from retained earnings obviously that you would call out like the additional pension contributions for example that we should think about? Thanks.

Answer: George Culmer
Okay, I will deal with the second one first. TNAV. Well contributions aren't, they don't flow into TNAV, they impact sort of capital in terms of they are a use of cash flow. But from TNAV it is the movement in the pension schemes for valuation and that is driven by market movement. And in that you would have seen for example in Q3 we had a negative which was the sort of further tightening of credit spreads. Now credit spreads are phenomenally tight at the moment and we have over the years de-risked the pension scheme significantly and you have seen that in terms of how it has responded to market movements and in terms of how the surplus has moved versus some of our peers. So I think we have done and perhaps I would say this, a good job in de-risking, but we remain exposed to credit spreads and there is a, for every single basis point it is about £65 million. And I think, you can take your view on what happens to credit spreads at the moment, but given the tightness of them we have seen the impact of that tightness in Q3. It was more likely they will go out than come in further and if they were to go out that would be a benefit to net assets in terms of how that flowed through in terms of discounting those pension liabilities. So it is not about contributions. Contributions are much more around capital position and you have seen from our CET1 walk, that there was about 11 basis points of capital deduction in Q3 from our expected pension contribution, which will be repeated. That is our sort of £400 million part deficit payment that we will be making in Q3 and Q4. But on TNAV, I have talked too long about pensions and credit. Anything else, I mean what swap rates will do to, sort of what rates will do to cash flow hedge, and this is where the trade-off is, I would rather rates would go up. But the immediate impact of rates going up is it depresses the cash flow hedge which flows through TNAV, but I would rather take rising than any other. But anything else in Q4, I don't think there is anything else particularly in Q4.

Going to your first and the mortgage market, look we are not going to give out of all our sort of state secrets, but in terms of managing it, as we have bored you numerous times before, we have the great advantage of managing things centrally. And everything that we do is co-ordinated. And everything that we do is deliberate and it is tied up. So you know you saw us move into sort of 5 year new business mortgage origination earlier and gave us a 20 or 30 basis point spread. I think most recent pricing I have seen, others have moved that way and that has been eroded. So we have got to look at what the next thing is we are going to do in terms of just finding that point where you are not cannibalising your existing book and you are looking for points of leverage within the system. So that is on the new business.

On the retention, retention has been the big sort of success story and where most people transfer out of our SVRs etc; they will transfer into one of our products which is attractive for us. So we will continue to work hard on that. There is nothing though I am going to tell you on specific tangible things because I wouldn't or shouldn't do all those things. But on the liability side, again it is more of the same. You have seen for example the success in terms of continuing to generate current accounts that I talked about, retail and commercial being up something like £7.5 billion in the year. You have seen our structural hedge grow from about 171 and I think it is now, what is now £175 billion at the end of Q3 and I would expect that to be higher still at the end of the year. It doesn't track automatically between what happens in current accounts in the quarter to what happens in the structural hedge. You always get a sort of delay in terms of making sure the accounts come in, you understand they are eligible etc. etc. So I would continue to see us build those current accounts and deploy them within the structural hedge.

In terms of management, again it is the same thing in terms of looking across the book. So trade-offs between commercial versus retail and within retail in terms of the tactical and relationship etc. etc. And going back to some of the things I threw out the answer to, Raul or Chris, in continuing to manage the rates on the book on offer. And you have seen from the pre-rate increase to post-rate increase actually the cost of my savings book hasn't moved very much and continues to look at opportunities to margin widening and we would assume a 25 basis point hike each year and that will continue to be opportunity for us.

So look it stays tough, we continue to do things. We will continue to do things, but we remain confident in our ability to manage that margin, to manage that spread across the business, utilising the various levers that are under our command.

Rohith Chandra-Rajan
Thank you very much for that.

Question 5: Joseph Dickerson, JEFFERIES
Hi, good morning George, thanks for taking the question. Just a quick question on the capital return ambitions. On my arithmetic if you have accrued a one-third, two-third interim versus full year dividend, and you generate the type of capital you expect and certainly we expect you to generate in Q4, what was generated in Q3. If I pay you down to a 14 per cent common equity Tier 1 ratio, I get around a £2 billion excess. Could you just discuss the appetite to distribute that number down to that level if you agree with the maths and if there are any hindrances to that? I know that there seemed to be a newspaper article over the weekend about a £2 billion buyback which seems to have taken tie with that arithmetic, but I just wanted to see what your ambitions were around excess capital return? Many thanks.

Answer: George Culmer
Hi Joseph. Yeah there is nothing wrong with the math in simple speak, yeah 200 basis points is £4.5 billion in pounds terms and if you were to put into p, it is about 6p type stuff. So that is the basic maths and you see I am currently paying out for the ordinary was just a bit over 3p. So that is the maths. What I would also say, the affirmation of two things. One in terms of confidence around capital generation. You have seen that in the 162, you have seen that in 41. And we are confident of delivering the 200 basis points for the full year. We are also confident in terms of our capital position and our capital requirement. So we have got the 13 plus 1, in terms of management buffer. So those pieces together say that I will come to the end of the year and that 200 basis points will be over and above that which I need to meet my capital requirement. So therefore are eligible for distribution. What I will say and I would stress, the Board will make its determination early next year, it will make that in that, we have updated our plan; we have seen various stress tests etc. come through and the Board will decide at that point. But as you know, the current board position is that we will look to distribute any surplus that we have and at the moment we have a requirement of 14, and as you have said, we have a capital position that will take us significantly in excess of that. So there has been reaffirmed confidence in capital contribution, continued confidence in requirement and absolutely no change in terms of how the Board will look at our capital position and surplus usage when we come to that time in early January/February of next year.

Joseph Dickerson
Thanks

Question 6: Fahed Kunwar, REDBURN
Hi morning. Just a couple of questions. On the deposit cost, for clarification, the 48 basis points you called out, is that including current accounts as well? I guess what I am asking is are the funding costs still falling quarter on quarter if you incorporate the current account growth into that overall funding cost that you guys look at? I know it's flat, just wondered what you paid for deposits? That is question one.

Question two was just following up on Joe's point actually on the capital returns. You are confident on capital requirement. I assume that confidence is also taking into account any potential IFRS 9 impacts on a PRA buffer on PRA stress tests?

And also you talked about inorganic growth potentially to supplement the Schroders JV. Would you think about kind of holding some capital above 14 per cent so that just if that inorganic acquisition potential is there, you have a bit of a buffer to kind of fall back on? Or do you think that actually staying at 14 per cent is enough to do that for any kind of inorganic acquisition? Thanks.

Answer: George Culmer
Okay, hi there. So two things. In terms of cost of liabilities, yes. If you look at the overall retail liabilities, then the cost have fallen marginally. So it was sort of 38-39 basis points I think in Q2 including current accounts. So across the whole of the retail stack and that has dropped to sort of 36-37 in terms of as at Q3. So you continue to see a reduction in those overall costs of liabilities as we move through that. And that is just within the retail accounts and does not take any account of movement of funds between the retail and the commercial book.

So to answer your question, bringing in the current accounts etc. and the growth we are seeing, yes you can see a continued reduction in those costs to funds.

In terms of the capital requirements, yes IFRS 9, we have got the stress tests coming up. We have got the EBA, obviously got PRA and as we all know IFRS 9 for the first time, which we all know, the wonders of perfect foresight etc. which will introduce some pretty significant volatility into the results. As we also all know the regulators quite rightly don't want to see any additional capital requirements flowing through the system because of IFRS 9, they have been very clear of that and they have been talking about ways that might effect that either through changes in the required hurdle etc. So in the early years as you know, we have got the transitional arrangements which essentially deal with the IFRS 9 through year 1, but then take us off. What we were looking for is that permanent solution because it is absolutely right and I agree entirely with the regulator in terms of the accounting shouldn't interfere with the capital requirement and it is trying to find the longer term solution to that which I am sure we will get to that place. So I expect to see IFRS9 will make this look pretty ugly, but as I said, we need to look through in terms of the capital position post the IFRS 9.

And then look on inorganic. This applies across the Group. You know we are open to opportunities across the Group. You saw that last year in things like Zurich. So things that are better to buy rather than build, we are open to that. This isn't signalling any big deals, it is just signalling that we are open and we are flexible and we have the capabilities and we have the capital. It is nothing of a consequence or a size that requires me to concentrate hard about what do I do with my capital position. Within the JV, look, no, to your question again. I make that comment only because we are going to, there is big ambition for this joint venture. As I say we have the target of being top three within the next five years. As I say growing from 13 into 25. Let's see what happens. All I am saying is we are going in there with a very open view as to how we might make that. But there is nothing that concerns me in terms of how that might impact my capital management over the short or even the medium term. You know the scale is not going to impact that in any way.

Further question
Great. Can I particularly ask one follow-up on the current account point. Obviously you have this structural hedge that you think will need to grow over the strategic period. If I look at your total current accounts, the percentage of deposits, it is sitting at about 30-35. Where do you think that can get to, let's say kind of rates stay pretty low or they raise to 1.25 over the period. Do you think that can increase? Is that the missing point around funding costs and how they continue to fall and you can keep your margins stable?

Answer:
No I am not going to give you a number, which might frustrate you. When you look back, if you look at our sort of our total deposits, our Group funding. We have been pretty stable around the £422 billion, £420 billion over the last few years. But if I look at the current account, that is the retail and the commercial banks. If I go back to something like 2014, they were only about £70 billion out of that £423 billion. It is now £108 billion out of that £423 billion. So there has been a massive shift as we have deliberately managed composition of those liabilities. Now I am not going to say it is going to grow by that again and I won't put a number on. And as you sort of say it is or infer, there is a rate dependency on this and again we would prefer a rising rate environment. But look, this year, the structural hedge, I think we came in I think round about 165 or something. Like I said, we have now grown to 171 at the half year, 175; I think we will pick up again. So I won't give a number, but our strategy continues to focus on the current accounts.

Fahed Kunwar
Thank you very much.

<u>Question 7: Edward Firth, KBW</u>
Morning. Just two quick questions. One was on costs again. Could you just update us on how much you have capitalised over the quarter, if anything at all?

And secondly, in terms of the restructuring costs, I guess they are now running at about 10 per cent of your cost base. Is that a sort of number we should see for the rest of the year or is there something? I mean it seemed quite big in Q3 so would we expect that down in Q4? That was the cost question. Do you want the other one as well now?

George Culmer
Go on then.

Further question
And I guess the second question was just about the Citizens Advice. They have obviously made a special complaint about the mortgage pricing, and a number of other markets. I guess we would expect the Competition Authorities to respond shortly. But you have got to imagine that there is going to be some sort of investigation. Would you expect to have to respond to that in any way during the process or would you just leave things as they are and wait and see when that comes out?

Answer: George Culmer
Okay, to deal with the first bit. On the restructuring. So I think as we came into this year I talked about almost a full year view, I talked about below the line ring-fencing would be £200-300 million, property about 0.1, MBNA/Zurich 0.1-2. And then we didn't give a number for severance, but I think at the start of year, but we talked about it being likely to be about 0.2 of a billion. I would still stick by those and probably ring-fencing would be about 0.3, property 0.1, MBNA/Zurich 0.1 whatever and severance around about 0.2 for the full year. In Q3 and that £200 million, you have kind of seen 0.1 across all of those so there is about £50 million for MBNA/Zurich, about £40 million for additional severance, about £50 million for property and £50 million or so for ring-fencing. So that is kind of where we are. If I go forwards to answer your question. MBNA and Zurich falls away, ring-fencing by definition will fall away. There is a bit of a tail of cost in next year, but nowhere near like what you have seen. So ring-fencing kind of falls away. The property has a finite period. You know redundancy will be what we think it needs to be in terms of as we continue to automate within the business. But you know a number of those that you see this year have a finite life period to them.

In terms of the BAU type costs, again as I think we sort of say in the Presentation, we're down marginally period on period, but within that the BAU costs. I mean in all this the strategies are, I invest in technology and I drive down BAU costs and what you see is a shift between kind of normal BAU into things like revex and depreciation type costs. So my BAU costs, I think as I said in the Presentation are down about 4 per cent, I think they are about £4.5 billion or something like that, £4.4 billion. With the revex and depreciation about a billion and a half. So you see about a 4 per cent reduction in BAU and about a 10 per cent uplift in investment associated. There has been no change in our capitalisation rates which I think were round about 60 per cent and I think this was disclosed at the half year. And that is something that has remained constant and I wouldn't see a reason why it would change. So those would be the numbers there.

Further question
Just to make sure I got all the numbers right. In terms of adding up your 0.3s and your 0.1s etc. on restructuring, it is about £700 million for the year then?

Answer
If that's what I said, there or thereabouts yes.

Further question
And in terms of the capitalisation rate. I think you capitalised about £400 million in the first half. So it sounds like about £200 million a quarter, have I got those numbers right?

Answer
As I say, they will be there or thereabouts. If I am materially wrong we will give you a buzz.

And then, on CMA, slightly woollier, I have bombarded you with numbers. I would expect to participate, you know these things come around. You know we have done an awful lot over the years in terms of enhancing our customer propositions whether that is combining savings accounts, whether it is the work we did on overdrafts, whether it is the work we do on insurance in terms of general insurance in terms of front book/back book. So we have made an awful amount of progress and made real tangible steps over the last few years in terms of enhancing and already improving our proposition. And part of that is absolutely transparent disclosures and ongoing communications with customers. So we have done an awful lot of that stuff. I can't comment in terms of what our involvement will be as we go forward. I would expect to be involved.

Further question
But given their look is obviously or seems to be focused on the front book/back book spreads and I guess they are looking across a number of markets, not just banking. Is that something, I mean clearly in other industries people have been pre-emptive to try and effectively try and head them off at the pass and come up with something reasonable before we get there. Is that the sort of way you look at this or is this more something where you just stick where it is, you are happy with the pricing?

Answer
I am not going to do anything knee-jerk because they have come out. So if that was the basis, I am not going to do anything today because they have written their report yesterday. What I am saying is we have done an awful lot of over the last few years in terms of transparencies, disclosures, aggregation of products. Already movement on differentials between front book and back book. So there is an awful lot we have done over the past few years which takes us in this direction anyway. But there is absolutely nothing I will be doing today from a product perspective in anticipation of what I think they might be saying.

Edward Firth
Sure. Okay, thanks a lot.

<u>Question 8: Guy Stebbings, EXANE BNP</u>
Morning. Two questions from me. First on UK motor finance. Pace of growth remains very strong. It looks like accelerating in the third quarter yet you see headlines on markets starting to slow and I am presuming we are starting to reach a point where you would expect maturities to pick up given the timing of your growth in the book. So could you give some colour around outlook there that would be very helpful?

And the second question was just on PPI if you can give us an update on what you are seeing for PPI claims given the comments regarding the pick-up in volumes and the latest campaign and with more being done direct rather than through claims management companies? And what impact the fee cap is having there?

Answer: George Culmer
Okay so PPI, the facts. First up we are at 13,000, we have obviously made no addition to the provision this quarter. As you know I think we came in around about I think it was 11,000 and then we moved to 12,000 and then up to 13,000. Most recent experience in terms of the reactives is that we've probably seen around about 11-12,000. So inside our expectations in terms of weekly run-rate. That has moved into another FCA campaign which is a few weeks through. And again as its predecessors what you get is very immediate reaction to that. So the sort of 11-12,000 which is a sort of undisturbed level we have seen, goes up to about a 14,000 type number. It then comes down again pretty quickly. So it is incredibly correlated with the ad spend. So it shoots up to the sort of 13-14,000 but then it comes back. The fee capping, yet to see strong impact in terms of, we are seeing a bit of a mix in terms of additional direct complaints coming through. But we are yet to see a massive discernible impact from the fee cap in things. There is no doubt about that. But we will still wait and see. But as I said the good news is the time bar is in place, we have got about a billion and a half unspent in terms of the provision and that will sort of cover me, expect it not just to cover me, not just the 11 months through to the end of August, which will get some tail in terms in dealing with those complaints so probably a couple of months thereafter. So let's assume it is 13 months, so that is about £120 million spend. The first few months of this year were slightly higher than that, round about £150 billion and that was because I was doing some Plevin outbound mailings and things like that so I expect it to come down to that. So at the moment as I say, it is inside, we have seen the pick-up but that was to be expected. The FCA have actually combined two, there were going to be four marketing and we have now had three I think. So there is one left to go prior to the end. So that is where we expect it to be.

The UK Motor Finance in terms of our growth, we are starting moving to period where you get the increased redemptions within the Black Horse book and I would expect our growth to come back down into mid-ish single digits expectations of growth. The market remains pretty robust. As you know the main thing people focus on is on residual value exposures. We have actually seen second hand car sales pick up and what you get in terms of flows, it is also basic supply and demand. But actually the focus on the drop off in new business, new car sales and yes what actually that means is that acts as a boost to second car values, second hand prices. And we have seen actually a pickup in second hand car prices as we have moved through the year, that is both petrol and diesel and we still are selling at auction cars at several hundred pounds, vans more than that. So we are still seeing relatively robust. But I would expect our growth to come back into the mid-single digits.

Guy Stebbings
Okay, thanks.

<u>Question 9: Chris Cant, AUTONOMOUS</u>
Good morning, thanks for taking my questions and congratulations on the retirement. Can I just ask you to give us an update on the SVR book and give a few stats in terms of book size and pace of attrition as that would be helpful?

And secondly on mortgage pricing, obviously you are confident still on your NIM trend out to 2020. But some of your peers are sounding rather more downbeat. How much further would mortgage pricing need to tighten for you to see it as a threat to your broadly stable NIM guidance?

Answer: George Culmer
A slightly open ended question. Okay, on the SVR bit, first up what you are seeing is kind of, I won't say it is no news, but it is remarkably stable. So you are still within that 13 per cent type attrition rate that we are seeing across the piece. So that, so for the Halifax book I think it was about 13.5 per cent in terms of Q3 on Q3. And so it has been sort of moving around at that rate and again the rest of the book is remarkably stable and we gave you the stats and the composition of the book at the half year. So we are seeing nothing, no major change in the themes or the trends there.

To the mortgage bit. Look, this is a tough market and you have to manage it accordingly. And so I am going to sort of frustratingly not give you numbers, but it is hard unless you are managing both sides as we go on about endlessly. And unless you are managing the interactions between the front and back book and looking at the you know combinations of risk profile in terms of franchise protection etc. You know it does require work and it does require effort. If I just go out there and follow one side of the balance sheet and try to stick to a market share type target, then I will see the consequence in my NIM and I will see the consequence in my short term.

So it is a bit like going back to the earlier questions, we have worked enormously hard on developing propositions that don't cannibalise the five year. We have worked enormously hard on retention and pushing up potentially. So we are up to 70-80 per cent in terms of retention which I forget the precise number of a few years ago, but it was nowhere near as high as that. And then to sort of bore you with this stuff, as we talk about it, we work incredibly hard on the liability side. So it is tough and that toughness is reflected in our sub-market growth rates which you see, we have been shrinking the book. We held it last year, we are looking for slight growth, but it is reflected in our whole strategy to the market. So I am not going to tell you that another 20 basis points or whatever jeopardises this or whatever. Sorry, it just means we work harder in terms of seeking off-sets and trying to manage this thing.

Further question
If I could ask it in a slightly different way then and I appreciate you don't want to give a specific number. But if one of the levers you are pulling to manage that is sub-market rates of growth, and from your comments on an earlier question, it sounds like you are viewing, as one of your large peers has recently, some of the pricing in the market is irrational in terms of just scraping into double digit returns if you allocate capital properly. Do you think you can deliver growth in interest earning assets and deliver your stable margin guidance given pricing where it is over the next couple of years? Could you give a sense of delivering growth with stable margin, is that holistic with pricing where it stands today?

Answer
Yes, we believe it is. So as you know Chris, when you look at the composition of the balance sheet. When mortgages were coming down, everything else has to work to a factor of ten to sort of offset that. If I can hold my mortgage book then growth through the other areas that we've talked to you endlessly about, the SMEs, the Mids, the unsecured etc. enable me to move the assets forward and I would stick to our stable guidance in terms of the NIM.

So again, going back to my earlier comments and I am not looking for sympathy here, you have to work at this and you have to manage it and you have to control every piece of the book, both sides of the balance sheet and try and effect this. Because those are tough markets but if I can hold my mortgage position, the targeted growth in the other areas of the book should move those assets forward.

Chris Cant
Thank you.

<u>Question 10: Martin Leitgeb, GOLDMAN SACHS</u>
Good morning. Could I have two or three on the liability side and you made reference to some of the earlier questions with regard to your ability here not to pass on the benefit of the rate hike in full and keep some further scope for optimisation. What do you see in terms of competition currently within the deposit market in the UK and I think previously some time ago we had a discussion of shifting some of the retail and focusing more on the commercial side of deposits there being an attractive pricing differential. Do you still see this pricing differential at this stage?

And my second question would be just on the stress test from the Bank of England obviously in a few weeks' time. I was just wondering if you could share what your thoughts are going into this stress test? From an external perspective it seems the amount of stress being applied it is broadly similar to last year's exercise, but obviously the methodology in terms of IFRS 9 and the application of that stress is likely to be much earlier compared to before. I was just wondering if you could share what your thoughts were on this stress testing and what you expect the stress test could be potentially tougher for Lloyds this year? Thank you.

Answer: George Culmer
Okay. So if I see the question around the overall competitiveness of the liability market which it continues to be not as competitive on the asset side. And the ability to shave rates etc. across the book, you would see that evidenced in the numbers that I have spoken to you about. So I am not saying it isn't competitive and it is nowhere near the intensity that exists on certainly parts of the asset side of the balance sheet. So that has been the case and I would say that generally that remains the case across the piece. And so there is no doubt about that. And there is still the opportunity in terms of moving between commercial and retail and opportunities there as long as they are the right type of commercial deposits.

Stress tests, you are right, essentially it is a re-run of last year and with IFRS 9 thrown in, I think as I answered in an earlier question, I think headline with IFRS 9 and perfect foresight, you could get some big movements. What is important isn't the P&L noise, but the interaction through, with capital base and the imposition of the transitionals and then hopefully a longer-term more permanent solution in terms of either adjusting hurdle rates or whatever in terms of dealing with IFRS 9. But I think both, I mean EBA, as you know, EBA in terms of construction and the artificiality and the constraints around and asset cures and things like that, always produce some interesting outcomes. But PRA in particular, same stress. We are a year further on though. So I would say that things like we are a year closer to obviously time-bar in terms of conduct. We have also, well things like pension schemes in better position, they are in a surplus position which is positive as well. And we have also continued to de-risk the balance sheet. So you are seeing things like for example the sale of our Irish mortgage business which is a benefit. And you have just got the general seasoning of the book as well. But I still think you know post IFRS 9, post perfect foresight, you are going to see some relatively ugly numbers across the piece. But what is important is how the PRA deals with and protects the capital position.

Martin Leitgeb
Thank you very much.

Question 11: James Invine, SOC GEN
Good morning. I have just got one on your non-banking net interest income please. I note this has been running low single digit million negative kind of on average over the past few quarters. You don't know a sustainable level? I am just asking because consensus has got that picking up to pretty much a negative £100 million in 2019. Thanks.

Answer: George Culmer
I can't think anything odd in terms of quarterly numbers. You have only got one question and I don't think we are going to answer it very well. I don't think there is anything dramatic in this quarter's non-banking net interest income. So we will have a look, sorry James, we will have a look and come back to you. But I am not aware of any change in trends or anything like that. So I will come back to you.

James Invine
Fine. Thank you.

End of Q&A