Q1 2022 FREQUENTLY ASKED INVESTOR QUESTIONS

How was the Group's financial performance in Q1?

- The Group delivered solid financial performance, with strong income growth and capital build. Statutory profit after tax was £1,204 million (three months to 31 March 2021: £1,397 million), reflecting higher total income, net of insurance claims and an impairment charge for the period (compared to a net credit in the first quarter of 2021).
- Net income of £4,112 million was up 12 per cent on the first three months of 2021, with increased net interest income and other income, and a reduction in the charge for operating lease depreciation. Underlying net interest income of £2,945 million was up 10 per cent driven by average interest-earning banking asset growth, deposit growth and a stronger banking net interest margin of 2.68 per cent (three months to 31 March 2021: 2.49 per cent). The net interest margin benefitted from the UK Bank Rate increases, deposit growth, structural hedge earnings from a rising rate environment and continued capital base optimisation, offsetting headwinds from mortgage book growth and pricing.
- Average interest-earning banking assets were up 2 per cent compared to the first three months of 2021 at £448.0 billion, driven by continued growth in the open mortgage book, but slightly lower compared to the fourth quarter of 2021, due to lower average lending within the Commercial Banking portfolio.
- The Group's cost:income ratio was 52.3 per cent compared to 57.6 per cent in the first three months of 2021. Total costs of £2,150 million were 2 per cent higher than in the first three months of 2021 reflecting stable business-as-usual costs and planned incremental strategic investment.
- Asset quality remains strong with new to arrears remaining very benign and below pre-pandemic levels, resulting in an asset quality ratio for the quarter of 0.16 per cent. Underlying impairment was a net charge of £177 million, compared to a net credit of £360 million in the first three months of 2021, reflecting a low incurred charge and limited impact from revised economic outlook, including higher inflation offset by stronger HPI and lower unemployment.
- Return on tangible equity was 10.8 per cent. Although lower than 13.8 per cent in 2021, last year included the benefit of £2.2 billion of one off items. Earnings per share were 1.5 pence (2021: 1.8 pence).
- The Group's balance sheet reflects continued franchise growth. Loans and advances to customers were up £3.2 billion at £451.8 billion, driven by continued growth in the open mortgage book of £1.7 billion and increases in Corporate and Institutional lending of £2.9 billion, partially offset by continued reductions in the closed mortgage book. Customer deposits have increased by £4.8 billion since the end of 2021, with continued inflows to the Group's trusted brands.
- Strong capital build of 50 basis points allowed for significant accelerated pension contributions, comprising the full 2022 fixed contributions, as well as around half of the variable element. The Group's CET1 capital ratio at 31 March 2022 was 14.2 per cent.

For more on our full year results, please see our Q1 2022 News Release.

How do you expect the Group to perform going forward?

- Given the solid financial performance in the first quarter of 2022 and based on current business performance expectations and macroeconomic assumptions, the Group is enhancing its guidance for 2022 for banking net interest margin and return on tangible equity, with all other guidance as announced with our full year results:
  - Banking net interest margin now expected to be above 270 basis points *(enhanced)*
  - Operating costs of c.£8.8 billion on the new reporting basis *(as announced in February)*
  - Asset quality ratio expected to be c.20 basis points *(as announced in February)*
  - Return on tangible equity now expected to be greater than 11 per cent *(enhanced)*
  - Risk-weighted assets at the end of 2022 to be c.£210 billion *(as announced in February)*
- Based on the Group's new strategy, our 2024 and 2026 guidance reflects focus on our growth potential, improved efficiency and realising the capabilities of our people, technology and data *(as announced in February)*:
  - Return on tangible equity in excess of 10 per cent by 2024 and in excess of 12 per cent by 2026, as the full benefits of our investment are realised
  - Additional revenues of c.£0.7 billion by 2024 and more than double that of c.£1.5 billion by 2026
  - Business-as-usual costs flat in 2024 versus 2021, while costs increase only to finance new investment, enabling a cost:income ratio of less than 50 per cent by 2026
  - Asset quality ratio to be less than 30 basis points over 2022 to 2024
  - Capital generation of around 150 basis points per annum over 2022 to 2024, improving to 175 to 200 basis points by 2026. We are committed to returning excess capital to shareholders and expect to pay down to our target capital ratio by 2024

How are you progressing against your strategic goals in 2022 so far?

- In February, we announced our ambitious new strategy, aiming to transform our business, generating a stronger growth trajectory and enabling the Group to deliver higher, more sustainable returns and capital generation.
- In March we announced a new business structure, aligned to the new strategy and have started work on the strategic initiatives which will drive revenue growth and diversification, strengthen our cost and capital efficiency, as well as maximise the potential of our people, technology and data.

What is your exposure to the war in Ukraine?

- The Group's operations are predominantly UK-based with no direct credit exposure to Russia or Ukraine.
- The Group does have credit exposure to businesses that are impacted, either directly or indirectly, by higher energy costs or commodity prices, or potential disruption within their supply chains. Such activity is monitored through prudent risk management.
- The Group continues to monitor and analyse carefully key internal and external indicators for signs of contagion risk and any second or third order risks that may arise from the war in Ukraine above and beyond those captured in the macroeconomic outlook. Investigations so far have not revealed any significant risks, although the Group remains vigilant and proactive risk mitigation is undertaken as appropriate to ensure that it supports clients, including those in financial difficulty, whilst protecting its portfolios.
- Uncertainties persist around the macroeconomic environment and its impact on consumers, although given our clear UK-focus, low risk business model and strategy, the Group is likely to be less impacted than many of our peers.

How are your customers managing with the current energy price and cost of living pressures in the UK?

- Our prudent approach to lending means the vast majority of our customers hold a level of income and affordability which should allow them to absorb the risks. To date, we are not seeing any worrying or unexpected signs from our customers in aggregate and the impact of overall of rising inflation has been benign.
- Over the course of the pandemic some customers and businesses have seen their savings rise or financial position get stronger with our customer deposits up £69.4 billion to £481.1 billion since December 2019.
- We are monitoring the situation and have engaged in a proactive outreach, contacting at risk customers in the period.
- We have a comprehensive package of communications, nudges and online tools to provide support to customers in need, enabled by the strength of our data capability to ensure we contact those who need it in a timely fashion and focus on those that need our support most.
- From late-April we plan to contact the c.72,000 customers identified as in the greatest need. We anticipate the tranche of c.72,000 customers will take around 12 weeks to contact. When completed, we'll have a rolling target cohort of 50,000 customers for outbound calling, assessed as being most in need of support at that time.
- We will continue to stay in contact with our customers through financial health checks; and encourage people to get advice early, talk to us, and seek independent debt advice.

What are you doing to address the deficit in your pension fund?

- The Group has agreed a plan with the Trustees of its final salary pension schemes to return the schemes to a fully-funded position. These plans include additional payments of £800 million a year, plus a 30 per cent share of whatever amount the Group returns to shareholders (up to a maximum total contribution of £2 billion per year). This is in addition to the Group's regular monthly payments.
- The schemes are required to have valuations every 3 years. The most recent valuation (December 2019) identified a shortfall of c.£7.3 billion. At December 2020, an interim valuation update showed the deficit had reduced to £6.0 billion and we have subsequently paid c.£1 billion into the schemes during 2021, and a further £1.3 billion in 2022 so far being the full £800 million annual fixed deficit contribution, plus around half of the expected variable contributions relating to our year end planned distributions. The deficit is therefore much lower than at the last revaluation.

What is your dividend policy?

- The Group has a progressive and sustainable ordinary dividend policy, whilst maintaining the flexibility to return surplus capital through buybacks or special dividends.

What is a share buyback and how might I benefit?

- A share buyback (also known as a share repurchase) is a form of returning surplus capital held by a company to shareholders involving the purchase by a company of its own shares.
- The effect of a buyback is to reduce the total number of shares in issue. It is expected that shareholders who retain their shares in the company will benefit from the share buyback programme as they will own an increased proportion of the total shares in the company and should therefore see an increase in the dividend per share going forward given the reduced number of shares in issue.

How is the buyback programme progressing?

- As at 31 March 2022 we have bought £0.5 billion of shares, with a weighted average price per share of 46.6 pence.

How can I participate in the share buyback programme?

- The share buyback programme does not work by buying individual investors' shares, regardless of whether they are large or small holders. The buyback operates through the bank's brokers buying shares on the open market, as any investor can do every day. Once the brokers have bought the shares in the market, they transfer them to the Group treasury function, who then cancel those shares.
- If an investor wished to sell their shares, the appropriate way to do so would be on the open market, in the normal way.

Can you give an update on your ambitions to support the transition to a low carbon economy?

- We continue to make progress towards our climate ambitions and in working with our customers, government and the market to support the UK's transition. For example we have:
  - In February 2022, published new ambitions for three of our highest emitting sectors: motor (Retail), oil and gas and thermal coal, which complement our ambition for the power sector
  - Scottish Widows' investment in the Climate Transition World Equity Fund (co-created with BlackRock) reached more than £5 billion (YE 2021)
  - Joined Powering Past Coal Alliance, confirming our commitment to a full exit from thermal coal by 2030
  - Funded one in ten new electric cars on the road today
  - Completed our first three net zero carbon operations branches
  - Remained Carbon Trust Standard certification holders for carbon reduction for the twelfth consecutive year
  - Published our inaugural 2021 Climate Report containing our disclosures aligned to the Task Force on Climate-related Financial Disclosures (TCFD) recommendations
  - Joined the Net Zero Banking Alliance (NZBA) as one of its founding members in April 2021.
- Our new Group strategy includes a number of stakeholder outcomes that will help finance the transition of our customers for green mortgages, electric vehicle financing, sustainable finance for businesses and investments in climate aware investment strategies through Scottish Widows.
- To continue to drive progress, we have also included specific measures aligned to our environmental sustainability ambitions in our senior executive performance measures in our Group Balanced Scorecard.

Can you comment on how your interest rate sensitivity has been calculated and how it will impact the Group? Why does your sensitivity differ so much to your peers?

- Our sensitivity analysis shows an illustrative c.£175 million additional NII from a 25bps rate increase in Y1, assuming a simple 50 per cent pass through on deposits and 100 per cent pass-through on assets.
- LBG's illustrative disclosure is to an instantaneous parallel shift in interest rate curves.
- The net interest income impact from the shift is driven by structural hedge maturity reinvestment and benefit on certain deposit balances. The actual impact will also depend on the prevailing regulatory and competitive environment at the time. This sensitivity is illustrative and does not reflect new business margin implications and/or pricing actions, other than as outlined. In reality, we'd also be taking management actions, not reflected in our analysis.
- The following assumptions have been applied: (i) illustrative pass-through assumption of 50 per cent on administered deposits (those in which the Group can manage the deposit rate); (ii) a static balance sheet (31 March 2022), (iii) no impact on fixed rate mortgages i.e. maturing business reinvested at same margins. Hence does not capture any adverse impacts on mortgage pricing / NB margins if increased swap rates are not fully passed on to customer rates.

How are you addressing the competitive threat posed by the rise of fintechs and challenger banks?

- While competitive threats are real, we remain able to compete effectively in the market, including against fintechs and challenger banks, utilising our strong customer franchise, broad product suite, and profitable businesses with positive cash flow which allows sustained, through-the-cycle investments to improve our customer proposition.
- We are in a strong position to compete effectively in the market, not least through a leading digital business, underpinned by our robust UK focused franchise and multi-brand model.
- Neobanks often don't have product breadth or all channel capability, which limits appeal given all start-ups have to spend significant money to acquire customers, whereas we already have 18.3 million digital customers. Our challenge is to create the digital capability to offer the same easy, convenient and personalized experiences. We already have the skills to do this and can replicate success in these new areas.