LLOYDS BANKING GROUP PLC – 2024 HALF YEAR RESULTS – PRESENTATION TRANSCRIPT
(amended in places to improve readability only)

Thursday 25 July 2024 – 9.30am

LBG:
Charlie Nunn, Group Chief Executive
William Chalmers, Chief Financial Officer

CHARLIE NUNN, GROUP CHIEF EXECUTIVE
Good morning everyone and thank you for joining our 2024 half year results presentation.

As usual, I will start by providing a short overview of the Group's financial and strategic performance. William will then run through the financials in detail. Following a brief summary, we will have plenty of time to take your questions.

Let me begin on slide 3

SLIDE 3 – CONSISTENT STRATEGIC DELIVERY, ROBUST FINANCIAL PERFORMANCE

I am pleased to say that we are continuing to make strong progress on delivering in line with our purpose, driving positive outcomes for customers, colleagues, and shareholders. I will cover this in more detail on the following pages, but to start I would like to highlight the following three key messages:

Firstly, we are now half-way through our five-year strategic transformation. We remain on track to deliver our interim 2024 targeted outcomes, delivering meaningful change for our customers and creating value for the Group.

Secondly, we have delivered a robust financial performance in the first half, in line with the expectations we laid out at the full year. This is driving strong capital generation and enabling consistent growth in shareholder distributions.

And finally, we are reaffirming our guidance for 2024 and remain confident of delivering higher, more sustainable returns in 2026.

Turning now to our purpose on slide 4

SLIDE 4 – DELIVERING ON PURPOSE DRIVEN GROWTH STRATEGY FOR ALL STAKEHOLDERS

Delivering in line with our clear, longstanding purpose of Helping Britain Prosper ensures that we drive outcomes that benefit all stakeholders.

During the first half we have continued to provide extensive support to our customers to help them meet their lifecycle financial needs, such as supporting their savings goals through our strong ISA propositions. Our 19 per cent share of Cash ISA flows has enabled an additional £6 billion of tax-free savings for our customers. We also helped more than 50,000 small businesses and charities start a new banking relationship with us.

We remain focused on contributing to an inclusive society and supporting the transition to a low carbon economy, with these also representing new opportunities for growth. Since the beginning of 2022 we have provided around £38 billion of sustainable financing.

Looking ahead, we welcome the emphasis that has been placed on sustainable economic growth by the new Government. Businesses like ours have a vital role to play in working in partnership with the Government to address national priorities and help communities across the UK prosper. We are well positioned in this regard and believe we can make a meaningful contribution across key focus areas such as sustainable infrastructure, housing, and financial planning.

On slide 5, I will provide a brief overview of our financial performance.

SLIDE 5 – ROBUST FINANCIAL PERFORMANCE, IN LINE WITH EXPECTATIONS

Our robust financial performance in the second quarter and across the first half was consistent with our expectations and guidance. Our Q2 NIM has remained resilient, whilst we continue to deliver strong momentum in Other Income, with our strategic initiatives supporting this growth. Net income was lower reflecting an increase in operating lease depreciation, an area that William will cover in more detail shortly.

Elsewhere on the P&L, costs are tracking in line with guidance and asset quality remains strong. We have also grown the balance sheet in the quarter, with broad-based lending growth of £5 billion excluding a Q2 securitisation, whilst deposits were up £6 billion, with growth in both Retail and Commercial Banking.

Our Return on Tangible Equity was 13.5 per cent for the first half. This translates into strong capital generation of 87 basis points, with 47 basis points in Q2.

In line with our intention to deliver attractive shareholder distributions, we have today announced a 15 per cent increase in the interim ordinary dividend to 1.06 pence per share.

Our financial performance is supported by our strategic progress as we realise the benefits of our investment. I will provide an update on this over the coming slides, starting with slide 6.

SLIDE 6 – BUILDING MOMENTUM IN STRATEGIC INITIATIVES

We are now halfway through our five-year strategic transformation and nearing the end of the first phase. Through our investor seminars we have provided you with increased detail on our plans and progress across our main business areas.

To reiterate, the key messages from those sessions were:

- We are building upon our strong foundations, including our significant scale, digital leadership, and broad offering.

- We have increased investment in the business, with circa £3 billion incremental investment out to 2024.

- We are building momentum across our businesses, delivering growth in priority areas, whilst investing in our enablers to improve operating leverage and enhance capabilities.

- And finally, we remain on track to meet our financial targets for both 2024 and 2026.

To bring this to life, on slide 7 I will provide some examples of our progress in the first half.

SLIDE 7 – DELIVERING GROWTH

We are addressing a variety of growth opportunities, meeting more of our customers' needs, focusing on high-value segments, and leveraging the unique breadth of the Group's businesses.

Building upon our existing scale, we are focused on deepening relationships right across the Group. We are extending our digital leadership position, with new features and propositions that increase engagement. For example, we launched Invest Wise, a new mobile-first investment proposition for 18–25 year-olds which has supported a doubling of customers in this segment.

Additionally, we are delivering strong growth in our CIB Markets business, deepening our share of wallet and diversifying revenues, with CIB Other Income up 30 per cent compared to the first half of 2021.

Our strategy is also focused on building our offering with high value customer groups that have a greater number of needs. The development of our Mass Affluent proposition is a key example of this. We have scaled the number of customers with access to Lloyds Bank 360 10-times since launch, with early benefits such as higher investment portfolio sizes for these customers. We would expect these benefits to grow as we scale further, with a larger addressable customer base.

Finally, we are better connecting our businesses to address our customers' financial needs. This includes increasing the penetration of our IP&I products within our Consumer and Commercial franchises. For example, we have seen a marked improvement in Protection take-up rates and have reclaimed the #1 share in new Home Insurance policies.

Importantly, these outcomes are translating into financial benefits. We remain on track to deliver circa £0.7 billion of additional revenues from strategic initiatives by the end of the year, with this growing to £1.5 billion per annum by 2026.

Let me now cover our enablers on slide 8.

SLIDE 8 – INVESTING IN ENABLERS TO DRIVE OPERATING LEVERAGE

Complementary to our growth focus, we are investing in our enablers to enhance our capabilities and drive operating leverage.

By digitising end-to-end and modernising our technology estate, we are increasing efficiency benefits as we scale. For example, we have now digitised around 45 per cent of servicing journeys within BCB. By digitising the journey to change a business address for example, we have reduced unit costs in this area by 60 per cent.

We are also transforming our physical footprint. Our new Leeds offices are the most energy efficient in the region, and later this year we will be moving to our new head office in London as we improve and consolidate our estate. Since the end of 2021 we have reduced our office footprint by more than 20 per cent.

These activities have contributed to the delivery of circa £0.9 billion of gross cost savings to date, leaving us on track to deliver circa £1.2 billion by the end of the year.

At the same time, we continue to demonstrate discipline with regards to capital efficiency, growing in capital-lite areas and undertaking securitisation activities. We have now realised around £15 billion of RWA savings from optimisation since the end of 2021.

Finally, our people remain critical to our future success, and we are taking action to build capability in key areas. For example, we have recruited another 1,500 technology and data specialists in the first half, taking the total to more than 4,000 over the past two and a half years.

Turning now to slide 9, where I will close with our financial outlook.

SLIDE 9 – STRONG FINANCIAL DELIVERY

As you have heard, we are making strong strategic progress in all areas and are on track to deliver our targeted outcomes.

We are also on track to deliver our interim 2024 financial targets and remain confident in the outlook for 2026 - this includes a Return on Tangible Equity of greater than 15 per cent and capital generation in excess of 200 basis points. These higher, more sustainable returns and capital generation represent a highly attractive proposition for shareholders.

Thanks for listening, I will now hand over to William for the financials.

WILLIAM CHALMERS, CHIEF FINANCIAL OFFICER
Thank you, Charlie. Good morning everyone and thanks again for joining. Let me start with an overview of the financials on slide 11

SLIDE 11 – ROBUST FINANCIAL PERFORMANCE

As you heard, Lloyds Banking Group delivered a robust financial performance in H1 and in Q2. Statutory profit after tax for the first half was £2.4 billion, with return on tangible equity at 13.5 per cent.

In H1, net income of £8.4 billion was down 9 per cent year on year. This was built upon a resilient banking net interest margin of 2.94 per cent, including a Q2 net interest margin of 2.93 per cent, 2 basis points lower than in Q1.

Operating costs of £4.7 billion were up 7 per cent year on year, in line with our expectations. Excluding the impact of the sector-wide Bank of England levy in Q1, H1 operating costs were up 4 per cent on the prior year. We continue to see strong asset quality. The H1 impairment charge of £101 million equates to an asset quality ratio of 5 basis points. Excluding MES benefits totalling £324 million, the asset quality ratio was a still low 19 basis points.

After the impact of shareholder distributions, TNAV per share is now 49.6 pence, down 1.2 pence in H1, given distributions and rate developments.

Our performance resulted in strong capital generation of 87 basis points in the first half, after the impact of regulatory headwinds. This supports our 15 per cent increase in the interim dividend.

I will now turn to slide 12 to look at the customer franchise.

SLIDE 12 – GROWTH ACROSS LENDING AND DEPOSITS

Our business grew in the first six months of the year, across the lending and deposit franchise. Group lending balances of £452 billion were up £3.9 billion, or 1 per cent in Q2. This is led by growth across the Retail business. In the mortgage book, balances were up £3.2 billion in Q2 excluding the £0.9 billion legacy mortgage securitisation, or £2.3 billion after that transaction. Higher mortgage balances reflect the increase in application volumes observed at the start of the year, as we mentioned at Q1.

Elsewhere in the Retail business, we saw continued growth across cards, motor finance and unsecured loans. Commercial lending balances were also up slightly in Q2, by £0.3 billion. Within this, we saw modest growth in Corporate and Institutional, partly offset by net repayments in Small and Medium businesses, including £0.4 billion of Government backed lending balances.

Let's look at the liability franchise. It's also been a good performance in deposits which now stand at £475 billion, up £5.5 billion, or 1 per cent in Q2.

We saw growth of £3.6 billion in Retail, with Savings accounts up £5 billion, driven by inflows to limited withdrawal and fixed term products in a successful ISA season. Current accounts were £1.4 billion lower in the quarter, given the reversal of the bank holiday timing impact we saw at the end of Q1. This is probably a touch better than our expectations, driven by salary increases and lower spend.

Commercial deposits were also up in Q2, by £1.9 billion. In particular, we saw some stabilisation of non-interest bearing accounts and growth in targeted sectors within Small and Medium businesses. Alongside deposit developments, we continue to see steady liability growth in Insurance, Pensions and Investments with circa £2.7 billion of net new money in H1.

Turning to net interest income on slide 13

SLIDE 13 – RESILIENT NET INTEREST INCOME PERFORMANCE

The Group delivered a resilient performance in net interest income in the first six months of the year.

Net Interest Income of £3.2 billion in Q2 was down 1 per cent quarter on quarter. Alongside, AIEAs of £449 billion were stable on Q1, driven by the weighting of customer lending growth towards the end of the quarter.

As mentioned, the Q2 Net Interest Margin of 293 basis points was down 2 basis points on the first quarter, resulting in a first half Net Interest Margin of 294 basis points. This gentle decline in the margin through the first half is consistent with our expectations, as we outlined previously.

The H1 non-banking NII charge of £229 million was driven by increased funding costs in the current rate environment, and strategic growth in the Group's non-banking businesses. The charge is tracking in line with the indication we gave previously for the full year, of between £450 and £500 million.

Looking ahead, we continue to expect AIEAs for 2024 to be greater than £450 billion, driven by current lending activity and expected further lending growth in the second half of the year.

We also continue to expect the Net Interest Margin to be in excess of 290 basis points for 2024. Indeed, our confidence in this guidance is further reinforced by the performance in H1.

Within the margin, mortgage refinancing and deposit churn developments continue to evolve in line with our expectations. Forecasted Bank Base Rate cuts will add to the deposit headwind in the second half. However, the structural hedge refinancing will also play a greater role as we progress through the year, helping offset these pressures. Putting all this together, as we said at year end and at Q1, we continue to expect the Net Interest Margin to be on a positive trajectory before the end of the year.

Looking at the mortgage portfolio on slide 14

SLIDE 14 – GROWTH IN MORTGAGES

The mortgage book now stands at £307 billion. This is up £1.6 billion in H1 and up £3.2 billion in Q2, excluding the £0.9 billion legacy portfolio securitisation.

In Q2, completion margins increased to around 70 basis points, albeit maturities in the book were around 110 basis points. As I said, the impact of the mortgage book refinancing on the Group's margin is playing out more or less in line with our expectations.

As Charlie mentioned, a key element of our strategy is to increase connectivity between businesses, meeting more of our customers' financial needs. As an example of this, we have now enhanced the integration of our protection insurance offering into the mortgage journey. This drove a 3 percentage point increase in protection take-up in H1, albeit this is still below where we think it should be. The financial benefits gained by partnering across divisions reinforce the attractiveness of new mortgage lending from a strategic and an economic value perspective.

Looking ahead, we expect the mortgage book to continue to grow through the remainder of this year.

Let me now look at the other lending books on slide 15

SLIDE 15 – SOLID PERFORMANCE IN OTHER LENDING PORTFOLIOS

Consumer balances are performing well. Credit cards, Loans and Motor were collectively up £2.7 billion in the first half of the year, including £1.4 billion in Q2.

We continue to see credit card spend recovering, with balances up £0.5 billion in H1. Likewise, loan balances grew by £1.3 billion, partly driven by lower repayments following a securitisation in Q4 last year. Meanwhile, Motor Finance was also up £0.9 billion.

In Commercial, lending was down £0.5 billion in the first half. Within this, Corporate and Institutional lending was up £1 billion, including growth in strategic areas such as Working Capital and Securitised Products. In Small and Medium Businesses, balances were down £1.5 billion, with slow customer demand continuing to impact performance, alongside £0.8 billion of government backed lending repayments.

Moving on to deposits on slide 16.

SLIDE 16 – GROWING CUSTOMER DEPOSIT FRANCHISE

Our deposit franchise grew strongly in the first half of the year. Total deposits are up by £3.3 billion or 1 per cent to £475 billion.

Within this, Retail deposits were up £4.9 billion. Continued growth in savings balances more than offset expected current account reductions.

Retail Savings balances were up £6.7 billion in H1, supported by net new money inflows and strong retention activity. Two points stand out. First, as Charlie mentioned, we had a strong ISA season, attracting significant cash ISA savings from new and existing customers in the half. Second, our limited withdrawal product continues to see strong demand, enabling us to retain a high proportion of rate sensitive money within our own savings proposition. Current account balances reduced in the half by £1.0 billion. Outflows were driven by seasonal tax payments and movement to savings products, partly offset by wage inflation.

Commercial deposits decreased by £1.6 billion in H1. Within this, Small and Medium Business balances increased due to growth in targeted sectors, particularly in Q2. Non-interest bearing balances meanwhile showed early signs of stabilisation. Elsewhere, outflows in Corporate and Institutional balances reflected the Group managing deposits for value.

As you are aware, the performance of our deposit franchise supports the structural hedge, which I will now update on.

SLIDE 17 - CONTINUING TAILWIND FROM THE STRUCTURAL HEDGE

Our structural hedge is a significant tailwind to income. The hedge notional currently stands at £242 billion, down £5 billion in H1, including £2 billion in Q2. This is in line with our expectations for a modest notional reduction during 2024, linked to deposit churn trends.

In H1, we saw gross hedge income of £1.9 billion, £0.3 billion higher than last year. The average earnings rate on the hedge is now circa 1.6 per cent, with the reinvestment rate continuing to be significantly higher than this. The weighted average life of the hedge remains stable at around 3 and a half years.

Market rates over H1 have been slightly stronger than our expectations at the start of the year. Accordingly, looking ahead we now expect the growth in 2024 hedge income to be slightly higher than the £0.7 billion we mentioned in February.

Moving onto other income on slide 18.

SLIDE 18 - BUILDING MOMENTUM IN OTHER INCOME

We continue to build momentum in other income across the franchise and linked to the successful execution of our strategic initiatives.

Other income of £1.4 billion in Q2 was 9 per cent higher than Q2 last year, with H1 up 8 per cent year on year. Pleasingly, this increase is driven by growth across all of our business divisions.

Within Retail, we saw a growing contribution from our motor business driven by an increased fleet size, and alongside we saw quarter-on-quarter growth in banking fee activity. In Commercial, the team drove a strong H1 performance in our Markets business, with growth supported by strategic investment as well as higher client activity.

Insurance, Pensions and Investments delivered increased income within General Insurance as well as Workplace Pensions.

Looking forward, we continue to expect strategic initiatives across our business to drive further growth in other income.

Turning to operating lease depreciation. The H1 charge of £679 million included £396 million in Q2. The increased depreciation in Q2 incorporates a circa £100 million additional charge. This is caused by the half yearly fleet revaluation exercise recognising used car price developments, particularly in electric vehicles. These are a material part of our leasing business.

Looking forward, this charge will revert to something slightly higher than the Q1 run rate, because of the revised depreciation schedules alongside business growth.

Taking a step back, today's charge comes after a period of significant net benefits from used car price movements. Overall, we continue to see this business as an attractive and profitable growth opportunity.

Moving on to costs on slide 19

SLIDE 19 - CONTINUED DISCIPLINE ON COSTS

We remain on track to deliver our cost guidance in 2024. Operating costs of £2.3 billion in Q2 were stable on the prior quarter, excluding the circa £0.1 billion Bank of England levy in Q1.

H1 operating costs were £4.7 billion, up 7 per cent on the prior year, or up 4 per cent excluding the levy. Costs include expected elevated and front loaded severance charges, taken to facilitate cost efficiencies. Excluding the levy and the component of severance in excess of last year, costs were up 2 per cent, with inflationary pressures partially mitigated by continued cost efficiency. The cost-to-income ratio was 57 per cent, or 56 per cent excluding remediation.

The Group continues to maintain strong cost discipline in the context of inflationary pressures and strategic investment. As Charlie mentioned earlier, we remain on track to deliver £1.2 billion of gross cost savings this year. Excluding the Bank of England levy, costs will be up in total by 7 per cent over the three years from 2022 to 2024, in the context of what was much higher CPI growth during the same period.

As said, we continue to expect operating costs of circa £9.4 billion in 2024, including the £0.1 billion Bank of England levy. The remediation charge was £95 million in H1. This is substantially in relation to pre-existing programmes. There have been no further charges relating to the FCA investigation into historical motor finance commission arrangements.

Let me move to asset quality on slide 20

SLIDE 20 - STRONG ASSET QUALITY

Asset quality remains very strong. Credit quality continued to improve in the quarter, with either stable or reduced new to arrears seen across our portfolios. This reflects the resilience of our prime customer base and our prudent approach to risk.

Strong credit performance, alongside MES adjustments, resulted in a low Q2 impairment charge of £44 million, equivalent to an asset quality ratio of 5 basis points.

On a pre-MES basis, the asset quality ratio was a still low 16 basis points in the quarter. This benefited from a modest underlying charge, as well as the release of inflationary judgements in Retail, given the strong portfolio performance despite the environment. The £132 million MES release in Q2 was primarily driven by a revised approach to our severe downside scenario. This now incorporates the more evenly balanced risks of supply side and demand side shocks, with attendant CPI and bank base rate impacts.

Our stock of ECLs on the balance sheet is now £3.8 billion. This remains circa £500 million above our base case, and like-for-like, higher than pre pandemic levels, driving strong coverage across the portfolio.

We feel confident on asset quality. Considering the strength of the portfolio and performance year to date, in the context of an improved economic outlook, we now expect the asset quality ratio to be less than 20 basis points for 2024.

Let me briefly update on our latest economic assumptions.

SLIDE 21 - UPDATED MACROECONOMIC OUTLOOK

We've made modest changes to our forecast since Q1. We now forecast GDP to be slightly stronger than our previous expectations, with 0.8 per cent growth in 2024.

Given sticky pay rises and inflation we now assume two rather than three base rate cuts in 2024, starting in the third quarter. This higher rate environment leads us to expect unemployment to rise a little earlier, peaking at 4.9 per cent in 2025. Our assumptions for house prices meanwhile are broadly unchanged.

Let me now move onto slide 22 and address the below the line items and TNAV

SLIDE 22 - ROBUST RETURN ON TANGIBLE EQUITY

The return on tangible equity of 13.5 per cent in H1 represents a robust performance. Looking ahead to the full year, we continue to expect the ROTE for 2024 to be circa 13 per cent.

Restructuring costs remain low at £15 million for the first half. The volatility and other impact of £158 million in H1 was essentially driven by negative insurance volatility given the increase in long term rates. The charge also includes the usual fair value unwind.

Tangible net assets per share at 49.6 pence were down 1.2 pence in H1, 1.6 pence in Q2. The decrease was driven by shareholder distributions, including the full year ordinary dividend payment in April, and also by movements in the rate curve impacting the cash flow hedge reserve in Q1. As usual at this time, TNAV is also temporarily suppressed by an accrual for the share buyback over the H1 closed period, with no corresponding share count reduction. This 0.9 pence per share accrual impact will mechanically reverse in Q3.

Looking ahead, we continue to expect TNAV per share to grow this year and indeed over the medium term, from lending growth, buybacks and the unwind of headwinds. Inevitably, the growth trajectory may be influenced in the short term by rate volatility, just as we saw in the first quarter of this year.

Turning now to capital generation on slide 23

SLIDE 23 - STRONG CAPITAL GENERATION

We have delivered strong capital generation in the first half. In H1, RWAs were up £2.9 billion, ending at £222 billion. Lending growth was offset by securitisation and other capital optimisation activities. In quarter RWA developments were further impacted by the reversal of the temporary increase in market risk RWAs related to hedging, that we mentioned at Q1. We continue to expect Risk Weighted Assets to be between £220 and £225 billion at the end of the year. This is led by expected lending growth in H2, with continued active balance sheet management to offset regulatory pressures. Capital generation of 87 basis points in the first half was, as said, a strong result.

In this context we continue to expect Full Year 2024 capital generation to be circa 175 basis points. This represents a healthy level of capital generation, from a robust business performance.

The closing CET1 ratio of 14.1 per cent is after 48 basis points of ordinary dividend accrual. This is inclusive of the announced interim dividend increase of 15 per cent.

I'll now move on to talk further on capital distributions on slide 24.

SLIDE 24 - GROWING DISTRIBUTIONS, WITH INCREASED INTERIM DIVIDEND

The Group's strong capital generation and CET1 position continues to support growth in shareholder distributions.

Today the Board announces an increased interim dividend of 1.06 pence per share, 15 per cent growth on last year. As usual, we will consider further capital distributions at year end.

Both the interim and final dividend per share have grown consistently over our strategic plan. The 2024 interim dividend per share announced today is around 60 per cent higher than in 2021. This strong distribution growth is consistent with our guidance for a progressive and sustainable dividend.

Alongside this growth, we have undertaken consecutive and significant share buyback programmes. These have reduced the Group's share count by around 12 per cent since the end of 2021, supporting growth in value for our shareholders.

We remain committed to growth in distributions and returning excess capital to shareholders, alongside delivery of our strategy for the benefit of all stakeholders.

I will now move onto slide 25 to wrap up the financials.

SLIDE 25 - DELIVERING IN LINE WITH EXPECTATIONS

In sum, the Group is delivering in line with expectations. As Charlie said, our strategy is progressing well towards our ambition of generating higher, more sustainable returns for shareholders. As part of this, we saw a robust financial performance over the first 6 months of the year, with solid profitability, strong capital generation and an increased interim dividend.

Looking forward, we reaffirm our 2024 guidance, as set out in full on the slide, and remain confident in our 2026 commitments. We remain very well-positioned for the future.

That concludes my comments for this morning. Thank you for listening. I will now hand back to Charlie for closing remarks.

SLIDE 27 - CONSISTENT STRATEGIC DELIVERY, ROBUST FINANCIAL PERFORMANCE

Thank you, William. So to summarise, the Group has once again delivered in line with the expectations we laid out, increasing our track record of consistent delivery.

We have continued to deliver in line with our purpose of Helping Britain Prosper and see further opportunities to drive sustainable economic growth. We are continuing to execute against our strategic plans and are on track to deliver our interim 2024 outcomes.

Our financial performance remains robust, with strong capital generation supporting increasing shareholder distributions. We have today reaffirmed our guidance for 2024, and remain confident in the outlook of delivering higher, more sustainable returns and capital generation in 2026.

Thank you for listening, that concludes our presentation. We are now very happy to take your questions.

QUESTION AND ANSWER SESSION

Question 1 – Jason Napier, UBS

Good morning. Thank you for taking my questions. Two on net interest margin, please, if I could. The walk on margins on a quarter-on-quarter basis, just focusing first on the four basis point headwind from mortgages, I wonder whether you could talk a little bit about the spreads that you achieved in the second quarter, the pipeline for the third quarter, and how that looks. The persistence of the headwind is a particular focus for investors. How long do you think that headwind will continue?

Then secondly, the support in this quarter from funding capital and other, it looks to me like that's mostly about the Bank of England levy change, but if you could talk about whether we should consider that to be a plus or minus or neither in future periods, that would be most helpful. Thanks very much.

William Chalmers

Thanks, Jason. I'll perhaps take those two questions, maybe that Charlie wants to add a little on the mortgage point in particular. On the mortgage question first of all in relation to NIM, as you say, we've seen a bit of a headwind during the course of quarter two in relation to mortgages - four basis points. That's very consistent with what we saw in quarter one. To your look-forward point, Jason, it's consistent with what we would expect to see for the remainder of this year. That's playing out very much in line with expectations.

What's going on behind that, as commented on in my comments, I think perhaps in Charlie's too, we've seen completion margins of around 70 basis points in the course of quarter two. That's up a touch versus quarter one, which I think was more like 65. That's good to see, but it's a gradual and obviously relatively modest progression, but it's progress nonetheless. That is, however, as you know, in the context of maturing mortgages coming off the balance sheet, around 110 basis points, and it's that combination that leads that four-basis-points headwind in quarter two. As I say, I expect that pattern to be pretty consistent for the remainder of this year.

As we go forward on that, today's not the day, obviously, to be making guidance or giving guidance for 2025, but as we go forward, and consistent with the comments that we've made before, we expect that headwind to temper slightly during the course of 2025 and then get effectively eliminated during the first half of 2026, at which point we are taking on new mortgages at much the same rate as they're coming off. So it's that type of development looking forward, Jason, which hopefully is helpful to your question.

In terms of the second question there, funding capital and other on the margin, as you say, we've had about a three-basis-point benefit from that. What's underneath that number is basically three things. You mentioned Bank of England levy, which is quite right. That is certainly a feature of that. Alongside of that, we've seen some spread compression, which is helpful, and we've also seen lower quantities of wholesale issuance than we might otherwise have had, partly because of the deposit strength that we've seen on the balance sheet. Those things are coming together to help steer the margin in the context of our 293 basis points for Q2, 294 basis points for the half as a whole.

Looking forward, Jason, on that particular point, I would expect that to continue to be a bit of a tailwind going forward. It'll ebb and flow a little bit, but overall, that bank levy benefit will continue to contribute through the course of the year, and likewise may be a bit of benefit from wholesale in the context of strong deposits. Charlie, I don't know whether you want to talk a little bit about mortgage volumes.

Charlie Nunn

Thanks, William. Just on the mortgage market more broadly, I think probably everyone will know, we saw a strong Q1 actually in terms of customers coming back and origination around mortgage volume. That was linked to obviously the lower swap curve that we saw in January and February, and I think the good thing from our perspective is our strategy about being focused on our segments that we are the leader, and maintaining and growing market share in those segments played out well, and it played out at margins, as William said, that we're very much in line or slightly better than our guidance.

Volumes in Q2 slightly dropped as the swap curves moved up, but has stayed healthy. We'll have to see how the second half develops. Probably along with the rest of the market, we're not expecting huge volatility in the swap curves and therefore pricing. It remains a competitive market, but what we are pleased about is we are competing well within the segments we've seen, and we've actually gained a bit of share in the first half, so let's see how the second half goes, but it's a good start to the year, and obviously those balances will be supportive of our AIEAs in the second half and hopefully into 2025 and 2026. Thanks, Jason.

Question 2 – Aman Rakkar, Barclays

Good morning, Charlie. Good morning, William. I had a follow-on question on the net interest margin. So, you're talking about a bit more mortgage margin pressure in the coming quarters that are similar run rate to Q2, so there's quite a lot of heavy lifting that needs to be done by the deposit side of NIM here. I guess could you break out your expectations of the deposit margin sequentially from here, and in particular the structural hedge? Do you think we're at a level now where the structural hedge is stabilized? Should we expect that to be a pretty meaningful pickup from here? I guess that's coming in the broader context of NIM, which to me, I think you are pointing to a weaker NIM profile in H2 than consensus is modeling.

I guess I'll attach a second question to that, is if it's right to think of NIM down in Q3 and then some pickup in Q4, but one that probably may not approximate consensus. Is there any chance you can comment on those points, please? Thank you.

William Chalmers

Thanks, Aman. I'll take those question on the margin generally and the direction going forward. The guidance for the margin remains consistent with what we said at the beginning of the year and then again at Q1. So, hopefully that's helpful in the sense that it's consistent over the course of the year. What's going on behind that, as I mentioned in my comments earlier on, actually the developments in half one that we have seen have given us, I suppose, or rather underlined our confidence in that guidance as we stand today. It continues to be greater than 290 for the full year - underlining 'greater than' - and it continues to be turning towards a positive inflection point before the end of the year.

Behind that, what is going on is the principal headwinds and tailwinds that we've discussed before, which is to say that we see the mortgage headwind developing in the way that I've just described, pretty consistent the remainder of this year. We see the deposit churn evolving but actually slowing in the second half of the year, and there's some early signs of that happening, Aman, that we have discussed in the context of Q2.

We expect to see that churn continue, and the rates environment will be natural to expect people to continue to put money into things like fixed-term accounts, likewise limited withdrawal, but nonetheless that pattern we expect to slow in the second half, and as I said, some early signs of that in Q2. Alongside of that in deposits, that pressure is going to be slightly augmented by the bank base rate reductions that we expect to see, which in turn, as you know, will lead to certain lags before we're able to pass those on to depositors in whatever shape or form we choose to pass them on. That's the picture of the deposit headwind, which evolves in the pattern described.

At the same time, we commented earlier on the 'funding capital and other' tailwind, which is helpful, but actually much more important in the second half is the structural hedge, and the structural hedge comes back in a significant way in the context of the second half to offset a number of those headwinds that I just described a second ago.

I'm not sure I would totally buy into the profile that you've described in terms of the overall performance of the margin. We feel, as I say, very comfortable in the overall guidance for credit in 290, and likewise the guidance that we expect the margin to turn before the end of the year. In that context, I think it's also reasonable to expect the net interest income to turn in advance of the margin turning.

As we see it today, based upon the guidance that we have given you in respect to net interest margin, in respect of non-banking net interest income, of respect to the AIEAs, we expect modest progress in H2 NII over H1. It gives you a bit of context, if you like, for the way in which you might view not just the margin, but also the net interest income picture as a whole.

Aman Rakkar:

That's excellent. Thank you so much. Appreciate it.

Question 3 – Benjamin Toms, RBC

Good morning, both. Thank you for taking my questions. The first one's on that structural hedge, and just to help with our modelling, can you just provide some color onto what extent you've pre-hedged your '24, '25 and '26 swap maturities? Swap curves have been a bit all over the place, so to the extent that you have pre-hedged, when did you do the bulk of that pre-hedging? Or to put it another way, how does the rate that you've locked in at compare to swap rates today?

Then secondly, on securitization, in May you performed an SRT securitization. Some of your peers are utilizing this method more than you are, relative to the size of their loan books. Could you talk a bit around your ambitions around

further securitizations, whether they're traditional or SRT, and maybe put some color around the economics on this type of transaction from a ROTE and capital perspective? Thank you.

William Chalmers
Thanks, Ben. Again, perhaps I'll go through those two questions. In relation to the structural hedge, consistent with the pattern that we described at Q1 and perhaps also in February, we have, as you know, a structural hedge, which is right now £242 billion invested. That's come off a touch since quarter one, by about £2 billion. That's pretty much tracking in line with our expectations for this year, which is to say that we expect a modest notional reduction, probably not unlike what we saw last year, which is about £8 billion. It may be the deposit performance that we've seen this year actually helps us out a little bit in that respect, but let's see how the rest of the year fares.

As we look forward, to your question, Ben, we do obviously try to ensure that the hedge is both a source of shareholder value but also stability in our earnings, which in turn means that we do look to lock in the hedge in a way that's not hugely different to what you would expect out of a three-and-a-half-year average life and the kind of lock-in associated with that as you roll it forward. So specifically what I mean by that, it means that within 2024, we are very largely locked in, as you would expect. We've only got six more months, or in fact five more months of the year, to run, so you would expect us to be largely locked in for 2024. When we look forward into 2025, we're about four-fifths locked in. If you were to extrapolate the hedge over the course of its seven-year total life, three-and-a-half-year wage average life, that's about what you would expect. And then in 2026 we're probably around two thirds locked in. Again, if you extrapolate the hedge over, its total life of roughly seven years, weighted average life of three and a half years, pretty much what you would expect. So that gives you a sense as to our hedge position, Ben, as we roll forward. In terms of timing, I'm not going to address precisely your timing question, but I think it is safe to say that when we see the curve look advantageous, if you like, relative to our long-term expectations, then we will incrementally take steps forward on that basis. I wouldn't take that too far though, Ben, because if you look at our hedge, it is more like a conventional hedge that you would expect to roll forward in a pretty conventional way than anything else. But occasionally when rates are looking very favourable, then yes, we'll deploy a touch more than we would do in other less favourable circumstances.

In respect of the SRTs and the like, Ben, as you know, optimization is a part of our balance sheet management strategy that we seek to pursue in a very net present value positive way for shareholders. There are a range of tools available at our disposal in respect to that optimization. Some of them are simply around making sure that we are efficient in our interpretations of how risk weighted assets should sit on the balance sheet. Some of them are around management with counterparties, for example, netting of collateral. Some of them, to your question, involve transactions, and to your particular point, yes, we do deploy SRTs. You'll see SRTs are being deployed in respect of our commercial business, including in respect of our commercial real estate business in particular, and so we do take advantage of SRTs.

Likewise, we also take advantage of retail securitizations, particularly in the mortgage book. We did both the mortgage book actually and personal loans last year. The question that we ask ourselves every time we do an SRT or for that matter of retail securitization is: 'Is this structure, is this transaction net present value positive?' And if it is, then we see it as a useful source or shareholder value added. It is also, by the way, a useful source of risk management, of course, on the balance sheet. Talked about SRTs in the context of CRE just a second ago, but also over the course of quarter two, we securitized about £900 million of Bank of Scotland self-certified mortgages.

That combined with a transaction that we did in securitization space last year, similarly, part of it relating to the legacy book has saved us about £200 million in expected loss, and therefore helped us in terms of the ECL management of the business going forward. So we are effectively risk managing in the context of some of these transactions as well as obviously managing risk weight asset base that we seek to adhere to and target, as you know, for our year-end. Thanks, Ben.

Question 4 – Edward Firth, KBW
Morning, everybody, and thanks so much for taking my question. I had two questions actually on a slightly different topic. Just coming back to Charlie's comments about growth and the labour imperative or the labour government's imperative for growth, because if I look at your full year 2026 targets, a 15 per cent plus return target on a 13 per cent core tier one, if you're going to generate 200 basis points of capital, that doesn't suggest there's much spare there for growth, in fact that's virtually close to nothing. So I'm just trying to think how important, how much do you have to gear up your growth to actually get the economy going, and I'm particularly thinking of the commercial book that's now been falling reasonably consistently for some time, and I'm just not clear in my own mind how the economy can really pick up if you as one of the biggest players can continue to decline that loan book. That was my first question. I've got another slightly different question. Should I give it to you now or wait till after that one?

Charlie Nunn
Yes, give them both at once and I'll take the first one in a second, but please go with the second.

Edward Firth
Okay, great. And the other one is a completely different topic. When I look at the regulatory papers that are coming out at the moment from the FSB and everybody else, there seems to be about one a week on artificial intelligence and the potential in the banking sector for huge efficiencies and huge transformations in the way you do your business. And I'm just welcoming your thoughts on where you are at Lloyds in your thinking. Is this potentially going to be a big game changer like digital banking was, perhaps, 20 years ago? Should we be thinking about a lot of costs potentially to implement that, and where are the big pluses and minuses from that sort of initiative? Thanks very much.

Charlie Nunn
Great. Thanks, Ed. And thanks for giving me a question as well today, this is great. On the first one around growth and the imperative or the focus that the Labour government put around growth. I think the starting point is, you've seen our forecast and the basis of our plan as we assume the GDP this year, although we upgraded it slightly as only 0.8 per cent growth and then we start heading towards 1.4, 1.7 per cent growth in 2025, 2026. That's not in line with the Labour government's objective of getting to 2.5 per cent, so we have laid out a growth plan, we think is realistic based on the current government policy and the current fiscal policy. We'll have to see what plays out in terms of the Labour government policies and whether that changes that trajectory. We think there is an opportunity, by the way, for a government to take a more proactive stance around blocking the supply side and encouraging investment in the UK that could enable that. It's not going to be in the first 6 or 12 months. It makes a difference obviously, but we do think there's an opportunity to beat that, but obviously our forecast is based on what we can see today.

In terms of our own growth and then balance sheet, I think about it in a couple of ways. The first thing is our baseline does have some core growth in AIEAs. We haven't given you specific guidance obviously beyond 2024, but I think what you've seen this quarter around the kind of growth we can achieve when markets are returning to more stability is a good example of the trust we have in the Lloyds Banking Group business and the broad-based growth we can achieve. That was both across our CIB businesses and then our whole consumer businesses. So we do have that growth built in, and that is even with the capital return and the ROE that we're expecting in 2026. If growth were to be faster, it does depend on where it comes from. And of course, as you know, when you talk about a lot of the investment and infrastructure growth the UK needs, it's going to be in some of that longer-term capital, and it's going to be in areas like the energy transition, building out housing infrastructure, etc. Some of that can be bank-based lending, but we have some of the leading structurers and especially ESG structuring teams in the UK focused on those sectors where most of the investment needs to go. And often we do that through obviously debt financing, debt capital markets. We're a leading structure on behalf of insurance companies.

You've just seen the announcement this week around Oaktree, we are a source or a destination for private credit companies to come and say, "How can you help us use your expertise to originate assets?" And so we see that as a really exciting area both for our CIB business, but also the right way to think about supporting some of this growth because it needs long-term patient capital with the right cost of equity and the right liquidity profile underpinning that. And the great news is that we start as the leader in the UK on many of those sectors, and we already have strong relationships. So I think if that's where the growth comes, it doesn't have to be just bank balance sheet-based. In fact, I think if it were just bank balance sheet-based, we wouldn't get the right return profiles for those sectors and for those industries. So that's a really important part of this.

I suppose the third thing, and William, you might have covered this, but if we see our ability to grow our core retail and SME franchises is faster than is in our plan, they are accretive businesses and we'll always look to take economically positive growth for our shareholders if we can see it because we know that builds long-term sustainable returns. And if we see that coming, we'll just give you guidance as we go through this period.

Maybe your second point and, you all know me by now, I feel like I'm about to start a two-hour lecture on AI because I'm very passionate about this topic. Maybe just a couple of thoughts. Look, the first thing is we're already a leader in the context of financial services. We have over 800 AI models. Most of them aren't generative AI, but they are AI models that we are using to make better decisions, optimize the efficiency of the way we manage the bank today, to manage risk better. And we've been doing that for a long of time, and in the last two and a half years in the period of this strategy, William and I have been making sure we're now investing in and leapfrogging into some of the data and technology capabilities that really will enable us to use AI at the next level.

So, we're already a leader and it's already driving significant impact for shareholders, as I say, across things like risk management, efficiency, our ability to meet needs, and we definitely see that as part of the next two or three years, and that is part of the investment we've been making unless you want me to go into about specific technologies. Generative AI is an additional opportunity for better services to customers, better risk management, better efficiency in terms of how we serve customers. We're already piloting those and we've had some good case studies and impact around bringing generative AI tools to support our colleagues, and make better decisions faster and more efficiently. And we're seeing some good lift in different areas, customer servicing, our encoding team, and we definitely think that provides additional opportunities over the next few years. The one thing I'd say is I think like all technologies, I've been 32 years doing this since the early '90s, and I've from day one being totally disrupting and building better efficiency around banking and financial services from day one, started on the trading floors in the 1990s.

All of these adoption curves don't happen overnight. It's going to take a few years for this to really be used, generative AI that is, on top of the existing AI tools. And I do think it provides an exciting opportunity for the industry over the 3-5 year time period. And I think what you should be looking for and what I can give you confidence about is we're already a leader in AI and we're already leading on how we deploy the new tools to get the best outcomes for the shareholders over the medium term. So we definitely see it as an opportunity. I think it's going to probably be more about 2026 plus that it really starts to make a difference, but just have the confidence we're already working on it.

Edward Firth
And so just to come back very quickly, do you see it as something that can provide a source of competitive advantage, or is it something where it's just going to be good for the industry as a whole in terms of credit risk management and cost?

Charlie Nunn
So I've seen some of the comments from some of the US CEOs around this who say, if you are not using this service, you are no longer relevant to your customers. Look, I have always believed the way we use technology will be a source of competitive advantage and that's why for example, our digital capabilities and the differentiated position we have on customer engagement and use of digital and data is already differentiating. Just to give you one tangible thing, why do I think we are doing better than other high street banks around our core deposit and our relationship banking? I think it's because of our digital engagement services and relevance to our services, so I think it is differentiating. How we use generated AI directly with customers' needs a bit of development because there are risks about it, and obviously the regulatory context is going to have to develop for how you use it.

So I think the initial application of it will be around efficiency, making better risk decisions, which are guided by people and some enhancement around customer service. I think in that 3 to 5 year time period it could start to really improve how you serve customers and differentiate the service and therefore gain more market share if you like, for the businesses that are winners in that segment. And we are obviously going to be thinking that way and are piloting things in that context. So short term, probably more about support for doing what we do to stay better, managing risk better and being more efficient. But I do think there's this medium-term piece, and maybe we've just done our 4 seminars, as we think about what we do next, we should just highlight some of those examples, I think, around guided online advice in the wealth space, it's a really good example. So maybe we'll bring that back in one of the next set of seminars that we haven't yet committed to, and I'm looking at my team with a smile. Thank you.

Edward Firth
Perfect. Thanks very much.

Question 5 – Joseph Dickerson, Jefferies
Hi, thank you, just back to the 'on the ground', another question just on the margin outlook, I guess. One thing that's really stood out is that if you look at your retail unsecured, the car, the motor finance, you've grown those three segments on the balance sheet by £2.7 billion, and they're currently at a 550 basis points margin. You've had a neutral hedge impact in Q2 following the maturity yield issues that you flagged at Q1, but this looks like it's going to turn, and you've highlighted on slide 17 that the contribution this year is going to be a little more than £700 million, plus you've got some funding benefits. So I guess, if you're relatively consistent on the mortgage headwind and what's happening on deposits, is there any reason why the Q2 NIM won't be the lowest for the year? Thank you.

William Chalmers
Thanks for the question, Joe. Just to comment on one or two of those component parts that you've been through there, perhaps, starting off before that with the overall reiteration really of the guidance for greater than 290 basis points for the full year and indeed the turn before the year end to a positive trajectory, I'll come back to that in just a second. You mentioned there consumer finance as the first of your component parts, and effectively what we've seen within consumer finance is a couple of things going on. One is decent growth in balances. You'll have seen it's circa half a billion for the course of quarter two for card business or personal loans business and so forth, and those are in relatively high margin parts of the book, so that is net beneficial. At the same time, if you look at an over a temporal period, the margins have come in a little bit for one or two of those areas, and that's

mainly because funding costs have been going up and we haven't passed on all of those funding costs to customers, so a little bit of margin compression there.

But as we look forward, that is easing up a little bit. That as a source of pressure is easing up a little bit on the margin going forward. So consumer finance is playing its part in short in the margin as we look forward. The second, the structural hedge, as you say, we were in abeyance really for quarter two. We flagged it at quarter one, that quarter two contributions from the hedge would not be terribly much. That's simply a function of the impact of maturities within the hedge and the yield that the maturing hedges come off at, as well as any pre-hedging that we might've put on to manage duration and the yield of those, so that combination is what's led to the hedge being pretty static in Q2. But as I mentioned earlier on, our expectation is that the hedge picks up significantly in the second half and goes, as I say, considerable way to offsetting the headwinds that I mentioned in respect of deposits and in respect of mortgages. So overall the structural hedge makes a much more significant contribution in the second half of this year.

You asked about timing in terms of the turn of the margin, Joe. I'd make two comments really. One is to revert to the earlier points where I went through the headwinds and the tailwinds as we see them for the second half of this year. I shan't repeat that. The second is clearly you can see based upon the flattening of the Q1 into the Q2 margin that we are getting very close to the turn, which precise day of the week the turn happens on is going to be a function of customer behaviour, it's going to be a function of rates, it's going to be a function of competitive pricing and the like, but we have complete confidence as said in greater than 290 basis points, and indeed the turn before the year-end.

And again, in that context, I'll just repeat the earlier point that I made, which is, in this context, it's reasonable to expect net interest income to turn before the margin, and that's based upon all the guidance that you have out there as to net interest margin as to AIEAs, as the non-banking net interest income. We would expect that modest progress in H2 NII. So the margin is going to turn. We are not calling the precise day of the week in which it happens right now because of the uncertainties that I mentioned just a second ago, Joe. But it is going to turn, and alongside of that, in fact in advance of that, we expect NII to turn.

Joseph Dickerson
Thanks, William. Can I just confirm the full year guidance is still using a 4.5 per cent base rate?

William Chalmers
The full year guidance is expecting two cuts in base rate this year, which takes it down to 4.75 per cent, not 4.5 per cent.

Joseph Dickerson
4.75 per cent. Okay, great. Thank you.

Question 6 – Guy Stebbings, Exane BNP
Morning. Thanks for taking the questions. The first one was on asset quality, and really thinking about the impairment charge in the medium term. We can sense this sat around 30 basis points figure you've talked to historically. You've improved the guidance this year to sub 20 basis points. I recognize that change in part reflects the more one-off changes during the first half, but then even excluding those model changes we're still running below 20 basis points in terms of experience, and that comes at a time in households and corporates have faced some pressures. So I'm just interested if your view on medium term cost of risk is, perhaps, lower than 30 base points given the experience of the last 18 months or so in particular.

And then a couple of brief ones on NIM. On the hedge, could you talk about maturities between Q3 and Q4 given they are quite significant on NIM dynamics? And related to Jason's earlier question on mortgage rates, could you tell us what the average back book spread is now on the mortgage book? Thank you.

William Chalmers
Yeah, thanks Guy. A couple of different questions there. First of all, asset quality, second of all, the hedge, and then third of all, the back book mortgage spread. So I'll cover each of those in turn. Taking a step back, as said, the impairment experience for Q2 and also for H1 has been extremely benign. Specifically within that, the Q2 impairment charge £44 million as you know five basis points. The H1 impairment charge £101 million, also coincidentally five basis points. What's going on within that? Two things. One is the observed charge has been extremely low. The observed charge, as you know, relates to the customers going through default process, customers having difficulties. We are seeing those at extremely low levels. That is augmented by a very benign write-off picture, very few write-offs, very few flows to default, and indeed improving new to arrears pictures within most of our portfolios in Q2, so that's a very benign observed charge.

That is augmented still within the observed charge of £176 million in Q2 by the withdrawal or release of some inflationary judgments. Why did we do that? It is because the inflation happened, but the defaults that we thought might be associated with that inflation did not happen, i.e. the credit quality of the customers was more resilient than we had expected, therefore, the inflationary judgment has been withdrawn.

The second component of the impairment charge in Q2 was MES revisions, and the MES revisions gave us a credit of £132 million in Q2. That was principally because of a modest change in the way in which we model the severe scenario. The severe scenario within our IFRS 9 provisioning is still pretty severe. You'll see it in the context of our economic assumptions, and it produces a circa £7 billion ECL associated with it. But what we have done is, in recognition of the evolving economic environment around us, is we now have a blended demand shock and supply shock in the context of our severe modelling. What does that mean? It means that a supply shock, which has been associated with very high inflation and very high interest rates, is balanced in our severe scenario with a demand shock, which is associated with the contra of that, i.e. low inflation and low interest rates, and it is that modelling change which is fed into our MES in Q2. And as I say, it is conditioned upon the evolving environment as we see it in terms of the outside world.

So stepping back for a moment, Guy, on your first question, asset quality continues to be very benign Q1 going into Q2. Now as we look forward, two points, one is I'm not going to give guidance on 2025, but the second is we would expect, as you can tell from our AQR revision, to be below 20 basis points for the full year. And if you look at the underlying charges that we've seen within the first half, going back to my observed charge earlier on, we've seen a observed charge of around 25 basis points averaged over the first half as a whole. That is not a bad signpost to what you might expect to see in the context of the second half of this year, and in turn helps inform our less than 20 basis points AQR guidance for 2024 as a whole. How that then progresses into 2025 as said, I'm not going to give guidance in 2025, but you can see that the underlying performance of the portfolio has been pretty robust, and at the moment at least we're not seeing any sign that is about to change.

Second question Guy, in terms of the Q3, Q4 structural hedge movements in the maturities and so forth in respect of that, I'll just give you some guidance for the second half of the year in respect of the structural hedge, which is that we're expecting about £20 billion of maturities. That obviously ticks up, it's more like £40 billion of maturities in the context of 2025, but it's £20 billion for the remainder of this year. The slight word of caution that I would apply that, Guy, as you interpret that, bear in mind that the maturities will be coming off, and indeed the refinancing is going on at various different yields at any given moment. So there's some numbers behind that, that are required to build a full picture. But I think bearing in mind my earlier comments, if you consider those, we do expect the structural hedge to play a much more significant part in development of the margin, Q3 and Q4, and that's the right context to look at that £20 billion of maturities in.

Final question, Guy, in respect to the mortgages, as said earlier on, we've seen maturity yields on those mortgages are rolling off the balance sheet at 110 basis points. I know that's not exactly your question. Your question is about the yield on the back book. The yield on the back book as we stand today is around 1 per cent. It's going to be about that on a go-forward basis, and so hopefully that gives you the answer that you need in respect to the back book.

Guy Stebbings
That's all very helpful. Can I just check on that last one? Would that be ex-SVR or including SVR? The 1 per cent?

William Chalmers
That number that I've given you is the total book of mortgages, Guy, so it's 1 per cent for the £307 billion of mortgages that we have based on where we are today. The SVR is obviously going to be marginally higher than that. I don't think we disclose the SVR yield, but you can see it in the context of our publications and public information.

Charlie Nunn
And William, as you said earlier, the mortgage headwind, we think as we get towards 2026, the front book, back book frankly becomes no longer a headwind to us, and that guidance helps the back book, front book pricing assumption. Thanks, Guy.

Guy Stebbings
Thank you.

Question 7 – Andrew Coombs, Citi

Good morning. Thanks for taking my questions. I just wanted to push you a little bit on the full-year guidance, I guess firstly with respect to NIM, and second, average interest earning assets. So on the NIM, just to follow up on Joe's point earlier, you talk about mortgage and deposit trends being as expected, you've seen good growth in motor and card.

The structural hedge is now expected to contribute more than £700 million, before, it was around £700 million, and you're only assuming two cuts now rather than three. So that all sounds quite positive, and yet your full-year guidance is unchanged on NIM. So what's the offsetting negative?

And similarly, on average interest earning assets, you're at £449 billion. Your guidance is for greater than £450 billion for the full year. You've just done five billion Q-on-Q for securitization, with very strong volume growth in mortgages. Even if that does slow in Q3, Q4, why the caution on the greater than £450 billion? Why has that been reiterated? Thank you.

William Chalmers
Thanks, Andrew. I'll perhaps take each of those and then Charlie may wish to add, particularly in respect to AIEAs. In respect of net interest margin, your question is effectively why are we not increasing guidance today?

Let me just put a bit of context around that. The guidance today, as said, is greater than 290 basis points, right? I've just underlined that point. Greater than 290 basis points. We feel very comfortable. In fact, per my comment earlier on in my script, we feel more confident now around that guidance than we did at the start of the year, so we're feeling very comfortable with that. And again, greater than 290 basis points. We also continue to feel very comfortable with the guidance around the turn of the margin before year-end. We're just not calling out precisely which day of the week it is going to happen on.

So why is that, to your question Andrew. When we look at the year as a whole as it's developed so far, we've clearly seen some things turn out pretty much as we expected. The macro more or less as we expected, the direction of deposit churn more or less as we expected, refinancing in mortgages, again, more or less as we expected. We've also, to your question, Andrew, have seen some developments that are more positive, more constructive than we had expected. We talked a bit about PCA balances being a little bit better than expected in my comments earlier on. We talked about the rate environment that was in your question being a bit higher than expected. And likewise, we've had the bank levy change.

At the same time, we've consistently pointed out, including in Q1, there are one or two developments that have been more balanced, frankly. So BCB, non-interest-bearing current accounts, for example, there's been a touch more of a headwind than we had expected. To a degree, in the rate environment that we've seen, augmented by the prompts and customer attention that we paid, the SVR book in the mortgage business has come off perhaps a little bit more than we had expected. Not huge, but perhaps a little bit more than expected.

So those are the balancing factors, Andrew, in response to your question, but overall, where does that lead us? That leads us to feel, as said, very comfortable, in fact very confident, with greater than 290 basis points as the margin guidance. Very confident in the point that I made earlier on is that we expect to see progress in H2 NII over H1 NII, and very confident in the development of the margin on a positive trajectory before the end of the year. And we'll call out precisely when as we see the third quarter develop, and obviously come back to you accordingly.

Your second question, AIEAs, Andrew, we feel very comfortable, actually, with our guidance of greater than £450 billion for AIEAs. Why do we feel comfortable with that? Look at the lending developments over the course of quarter two. We've had lending developments of £3.9 billion, adding back to securitization, it's over £4 billion of lending, predominantly backend loaded. So if you look at our £449.4 billion, I think it is, AIEAs in Q2, those are not really being influenced by the lending that we saw in Q2, but of course, Q3 and Q4 will be. That's one reason.

The second reason is we've seen not just those lending developments in Q2, but we expect to see continued positive lending developments in Q3 and Q4, and that'll be across the business. It'll be across the retail business, obviously mortgages, but also the unsecured books, likewise motor. It will also be across good parts of the commercial business.

And so in that context, Andrew, our AEIAs view is very firmly in £450 billion. Again, consistent with the guidance we've been giving all year. You don't see it so much in the AIEA numbers of Q2. You should expect to see it in Q3 and Q4. Charlie, anything else you'd want to add on the lending?

Charlie Nunn
Well just on lending, and actually, on SME deposits, I think the other thing you can imagine we are very focused on is just understanding our market shares and where the customers are choosing to bank with us on SME cash flows and deposits. What you've seen in the industry, as you know, is they've been smaller than we all expected, and in that context, we've actually grown our market share of SME deposits.

But it is a good indication of we can't get everything right in terms of our projections, even when the market is smaller than we think, you can trust us to be really focused on whether customers are choosing us and whether we're competing well. And that's also true in mortgages.

I think just stepping back on both of these, and I understand, I think the question is really why didn't you take a positive upgrade on both of these? Our guidance, we're very comfortable with. The greater-than is important in this context and just talking at a macro level here of I think a couple of basis points and a couple of billion, on numbers which we've given really quite clear guidance on.

So, as William said, we're comfortable with the guidance. I'm going to say very focused with William and the team on winning the trust of our customers in these businesses. We know there can be quite significant swings in the market, and the volumes in the market. And from my perspective, it's good that we can stay committed to our guidance that we gave at the start of the year. Thanks, Andrew.

Andrew Coombs
Very clear message. Thank you.

Question 8 – Chris Cant, Autonomous
Good morning, both. Thanks for taking my questions. I had one on NII, please, and then one on operating lease depreciation. On NII, and obviously discussed very extensively this morning, I guess cutting to the chase, you've indicated modest half-on-half growth. I think the current consensus is looking for about 3 per cent half-on-half growth. Is that consistent with your view of what modest means in your own sort of lexicon, as it were?

And then on operating lease depreciation, obviously this has been a source of ongoing misses for several quarters now. Just keen to get a bit more insight into actually the underlying dynamics here, so could you give us a bit more visibility on the composition of the current fleet? How much of the fleet is electric vehicles versus ICE, and what's the sort of sensitivity you would encourage us to think about in terms of potential further residual value provisions? So I think it's about 10 per cent move in the first half. So if it's 100 million, if there's a further 10 per cent fall, we should assume another top-up? Or is that too simplistic? Thank you.

William Chalmers
Thanks, Chris. I'll take both of those two questions and hopefully address your queries. First of all, in respect to NII, you repeated my words, obviously, a modest tick-up in NII in the second half over the first. Progress, in that respect. I'm not going to comment on consensus numbers, so I won't answer your question directly in that respect. But hopefully, what we've given you in the context of the AIEA, that interest margin, and indeed, non-banking net interest income guidance, which is pretty comprehensive, gives you enough to work from.

Operating lease depreciation, Chris, it's an entirely fair question. When we look at operating lease depreciation, it might be worth just stepping back for a moment and saying what do we do in the car finance area. First of all, as you know, car finance is an absolutely integral part of the UK economy. Circa 85 per cent of customers use car finance when they buy new cars, that means there is a significant market which is going to grow as we look forward.

We participate in that car finance business in two respects. One is a leasing business and one is a financing business. The financing business, first of all, as you know, trades under the Black Horse name. It's a conventional financing business. Income comes in through net interest income. Any impairments go through the impairments line.

The leasing business, which is Lex Auto, number one, and Tusker, number two, the income comes in through the other operating income line, and the charge, if you like, or the depreciation comes through the operating lease depreciation line. When we execute on the leasing business, we have, as you know, the obligation to take the vehicle back at the end of the term, which means that we then set aside a residual value expectation against that vehicle and depreciate the automobile against that residual value expectation. If the residual value expectation changes, so does our depreciation schedule.

What that means is in times of used car strength, we will actually get some benefit from that, and that has been the experience. As you know, since 2020, we've been significant net beneficiaries from strength in used car prices, which in turn has come through the P&L to the benefit of shareholders.

From time to time, we also see car price weakness, and over the last six months, we've seen weakness in particular in electric vehicles. And so that causes us to revise down the residual values, to revise up the additional appreciation, and accordingly, take an adjustment of the type that we saw in quarter two.

Now, a couple of points to follow on with there, Chris. In terms of the implications of that operating depreciation going forward, the combination of fleet growth within the business, plus the revised additional depreciation schedules that I just mentioned, are going to mean that operating lease depreciation in quarter 3 and quarter 4 is going to be a touch above £300 million.

Why is it going to be above that? As I said, it's those two factors that I just mentioned. And as you look forward, you should expect the business growth to contribute to that number growing over time. But that's what you would expect in the context of other income growth that comes with that. As you would expect, we'd hope for that business to grow, it serves an important part of our strategy, and likewise, charge in operating lease depreciation will grow as other operating income grows. That's one point.

Second point, you asked about sensitivity, the residual value exposure within the business, across the Black Horse business, and across Lex Auto, and across Tusker, in total, and we disclosed this number, residual value is around £10 and a half billion, £10.4 billion, to be precise. The operating lease part or component of that residual value is £4.7 billion. That's relating to Tusker and it's relating to Lex.

Now, within the operating lease business, partly because a lot of it is company-linked, that is a more electric vehicle heavy part of the business. So to give you some idea, just 50 per cent of the RV exposure within Lex and Tusker is electric vehicle linked.

To come to your question, what kind of sensitivity do we have or exposure do we have for those electric vehicle prices going forward? The schedules for operating lease depreciation that I mentioned just a second ago, i.e., the touch above £300 million or Q3 and beyond, they incorporate a further circa 7 per cent reduction fall in electric vehicle prices over the course of 2024, and then a further 2 to 3 per cent fall over the course of 2025.

The internal combustion engine equivalent of that is around 2 to 3 per cent for 2024 and a further 2 to 3 per cent for 2025. So you can see, in terms of the indications that we're giving for operating lease depreciation in Q3 and beyond, we are taking into account some further buffer for expected electric vehicle price reductions during that time.

Final point Chris, which I would emphasize, is we are now seeing the operating costs of an internal combustion engine and an electric vehicle engine, basically come into equilibrium. In fact, it might even be cheaper to operate an electric vehicle today than it is to operate an internal combustion engine. That in turn should lead to some stability in prices. Let's see. I'm not forecasting it as such, but let's see. It should be an ingredient, if you like, for stability of prices.

In that context, because of the residual value exposure within the leasing business, we are also exposed to the upside of that business. Now, if we see it, that will obviously be of net benefit to shareholders. Again, I'm not forecasting it. It's not in our additional depreciation expectations, Chris, but it has happened before. It happened in the period between 2020 - 2023. So I just want to land on that or rather end on that point, if you'd like. This exposure goes both ways.

Charlie Nunn
William, I'm not going to jump in too much on that, but just one thought, Chris. William and I are highly aware that the volatility in this line isn't something that the shareholders have appreciated, so we are taking actions at the moment, we're not going to give you specifics today on ways we can mitigate that volatility going forward. So we'll come forward back with some of the things we've done, but we are aware that the volatility isn't really what you want to see, and we're going to make sure we can see if there's any ways of mitigating that going forward. But the returns on this business are good. Thanks, Chris.

Chris Cant
That was very helpful. Thank you.

William Chalmers
Thanks, Chris.

Question 9 – Amit Goel, Mediobanca
Hi. Thank you, and thanks for taking my question. So really just one clarification on NIM. I appreciate you don't want to say exactly when you expect it to turn, but just wanted to get a sense, making sure I understand it correctly. So would you expect the Q4 NIM in aggregate to be better than the Q3 NIM? Or are we saying that you'd expect the exit rate at some point in this year to pick up?

And then secondly, just to follow on, on the operating lease depreciation, the market's a bit different now, but just curious if you were to use depreciation curves from back in 2000, how different it looks now and what kind of order of impact could there be? Thank you.

William Chalmers
Thank you, Amit. Why don't I take those questions? And maybe Charlie wants to add before finishing up. In respect of your net interest margin question, as your question implies, and hopefully as my comments have implied through the course of the session this morning, in short, we would expect the net interest margin to be better in Q4 than Q3. That is not predicting anything about the Q2 to Q3 shape, which I've obviously given you commentary on during the course of this call.

But by its very nature, the evolution of the deposit churn picture, the evolution of the structural hedge picture, to a degree at least, the evolution of the mortgage picture, although I'd said that that will be stable through the course of the second half, and I'd repeat that, but that combination naturally leads to the strengthening of the margin over the course of this year. So that's that question, Amit.

The second question on operating lease depreciation, the depreciation curve has naturally changed since previous years. The one point that I would make there, is that there's a couple of things going on in our business. One is used car prices. We talked a bit about that. Two is the evolution of car prices themselves. Car prices are up around 50 per cent over the course of the last five years or so, so naturally, for any given size of fleet, you're going to get a higher operating lease depreciation charge.

And then the third component is obviously the growth of our fleet itself. This, as said earlier on, is a growth driver for the business, and we expect it to continue to be so, and that's a factor that leads into the operating lease depreciation charge.

But at the same time, Amit, there are two points to bear in mind there. One is that is a contributor, that business is a contributor, to the significant growth that we have seen in other operating income, half-on-half, other operating income as a whole, up 8 per cent quarter-on-quarter, year-on-year, that is, up 9 per cent. So that's a significant driver of other operating income growth alongside businesses elsewhere in retail, businesses in commercial, businesses in IP&I.

And the final point, Amit, is just to underline the point that Charlie made, the automobile finance business is a very attractive, profitable and growing business. Charlie, anything you wanted to add?

Charlie Nunn
Well, just a couple of things, because I'd love to talk about the business a bit more. As you said, William, the great thing here is we're operating at the kind of 17 per cent market share, so we just have a very, very extensive set of data across the whole industry, both on new cars and second hand car prices.

And when you look at the way about how has the depreciation curves changed since 2000? As William said at the aggregate level, we've seen a significant increase in the second hand car prices, especially in ICE vehicles. It actually differs quite significantly by vehicle, and so we have a really distinctive competitive advantage around understanding around individual vehicles, depreciation schedules, what customers do and don't want. And then every time we set prices for our operating leases, we can learn of what's happened in the previous weeks, quarters, and months.

So that's why it's hard for us to give you sensitivity, as Chris asked, because if we learn that a specific vehicle type is depreciating faster, we'll actually price the operating lease to incorporate that expectation. And we have the best leadership team in the market making those kinds of judgements and assessments, which is why you should confidence around the ability for us to manage this risk going forward.

William Chalmers
Thank you, Amit. I think we are through with the call today. I'd just like to say thank you to everybody for taking the to join. Your interest is much appreciated, and we wish you a good summer.

END

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 Banking Group plc together with its subsidiaries (the Group) and its current goals and expectations. Statements that are not historical or current facts, including statements about the Group's or its directors' and/or management's beliefs and expectations, are forward-looking statements. 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