LLOYDS BANKING GROUP PLC– 2025 FULL YEAR RESULTS – SELLSIDE ROUNDTABLE TRANSCRIPT
(amended in places to improve readability only)

Tuesday 3 February – 4.00pm

LBG:
William Chalmers, Chief Financial Officer

William Chalmers:
Thank you, operator, and thank you to everybody for joining this afternoon. You have all participated in and listened to our full year results in respect of 2025, we were trying to put forward four main messages.

First of all, 2025's strategic delivery and sustainable strength in financial performance. Second, strength of capital returns, and indeed you'll have seen our 15% increase in the dividend. Alongside of that, the buyback of £1.75 billion together amounting to £3.9 billion capital returns for 2025. Third, 2026 guidance, clear, consistent, and upgraded. And finally, fourth, our beyond 2026 commitment to continued income growth, enhanced operating leverage, and improving and sustainable returns. So I thought I'd put those forward as just the four main points that we were trying to convey in our results last Thursday. And at this point, happy to open up and address any questions or topics that might come out of that. So back to you operator for questions perhaps.

Question 1 – Ben Caven-Roberts, Goldman Sachs:
Afternoon, thanks very much for the presentation and taking the questions. So two from me, please, first on asset quality and then second on return on tangible equity. So first on asset quality and the guidance of roughly 25 basis points for 2026. Could you just run through the puts and takes within that and then any key variables you're monitoring therein?

And secondly, on the ROTE upgrade, could you just frame how you thought about that process for upgrading guidance for 2026 and whether there was something which is now trending better than your prior planning assumptions, or if it's effectively more a function of the fact we're now in 2026 and is therefore a narrower band of potential outcomes on certain key variables, such as the path of interest rates, inflation, motor, etc. Thank you very much.

William Chalmers:
Yeah. Thank you, Ben. Thanks for those questions. In respect of each of them in turn, first of all, asset quality, maybe just to take a moment and reflect briefly upon '25 performance and then go into '26. Within the context of 2025, as you know, full year impairment there, £795 million. That's 17 basis points or ex the MES charge, 15 basis points. I think the important thing to realise in the context of that overall performance for the full year is that we had, in that year, some benefits from model calibrations, which essentially means that the event happened, but the loss didn't, is the best way of putting it. Alongside of that, we had some model refinements, which essentially just means replacing what were previously PMAs with models, and then we get the improved, if you like, or refined outcome, I suppose. And then on top of that, we had one or two releases like, for example, bounce back loans, which previously we did not think were going to be eligible for government repayment for one procedural reason or another. And in fact, they were good and so we were reimbursed as we should have been, but the issues, if you like, were not there.

So you add all of those things together, plus one further element, which was a debt sale, which we saw in, I think it was Q4, strip all of those out and we get to an observed run rate of more like 23, 24 basis points, thereabouts, just below the 25 basis point mark. Now within that, we are also seeing the development of things like new to arrears, which are very stable, very low, in some cases improving, but at least we're seeing stability pretty much in all cases. And that goes for the secured book, it goes for the unsecured book, it goes for the motor book absent VTs, as it were. And when we look at the commercial side, we're seeing a very similar and benign pattern.

So again, abstracting for those model refinements, calibrations, debt sales, bounce back loans and so forth, we are seeing a run rate charge of just below 25 basis points. We do expect that to tick up a little bit in the course of '26, and that is for reasons of commercial's not going to be zero forever, if you like, absent the fibre.

And therefore, we are expecting the run rate in '26 to be more or less similar to the run rate that we saw in '25 maybe ticked up a basis point or two. That's really what's behind it.

Alongside of that, and perhaps the most important point to make, Ben, is that we are underpinning that judgement with our macroeconomic assumptions. So we look at our GDP expectations, 1.2% up, as you know. We look at our unemployment assumptions, 5.3% peak over the course of the year. Importantly, we think that's being driven by increased participation in labour force and weak hiring as opposed to redundancies per se. And then alongside of that, we look at things like HPI inflation, which it rounds 2%, but underneath that, it's about 1.6% positive for '26.

These are the inputs to that AQR judgement of c.25 basis points, Ben, over the course of the year, but it rests upon more or less continuity and those macro assumptions that I just mentioned. On your second point around, or second question rather, around ROTE, as you say, '26 ROTE guidance increased to greater than 16%. I think first and foremost, what is there is an increased level of confidence about our ability to deliver what we have said that we would always deliver. And you're seeing therefore an increased level of concreteness, if you like, in our overall numbers. Beyond that, you're seeing probably some marginal improvement versus what we might have expected on that AQR line that I touched upon just a second ago, c.25 basis points is probably a touch better than what we might have previously expected.

Alongside of that, we're seeing strengthening achievements in our strategic initiatives, and you'll see there, we put guidance forward of around £2 billion in terms of the strategic initiatives delivery. Previously, we talked about greater than £1.5 billion. So you're seeing some income improvements off the back of that. And it's that combination that is in turn leading to the numerator of the ROTE improving, if you like. What is perhaps worthwhile pointing out is that we do expect equity to build over the course of the year in conjunction with the business building off the back of RWA builds. This ROTE improvement to greater than 16% is not because we are assuming equity goes down, for example, off two buybacks, that is not what is driving it. It would have been the same guidance absent that point. It is being driven primarily by the numerator factors alongside increased confidence as mentioned.

Ben, final point that I'll make there, which you may ask, or if not, it may come up later on in the discussion, is that why has that not led then to increased capital guidance? And what we've done, as you know, is label the capital guidance as in excess of 200 basis points. So there is some marginal positive coming back through there, but the relationship is not strictly one-to-one. That is to say the ROTE reflects the factors that I've just mentioned. At the same time through lending activities, for example, RWAs get driven up off the back of that, a little bit of a modest shift in RWA density and CB and so forth. And so our capital guidance, it perhaps nudges up a little bit off the back of this ROTE enhancement, but to be clear, it's not one for one.

Ben Caven-Roberts:
Very helpful, thank you.

William Chalmers:
Thanks, Ben.

Question 2 – Andrew Coombs, Citi:
Good afternoon. I'll start with a couple. I may come back around for a third later if there's time, but just a couple of numbers questions. Firstly, on the hedge contribution, thank you for the incremental guidance on 2027, the extra £1 billion. You've also reaffirmed the £1.5 billion for 2026. I was hoping you might just be able to provide a bit more detail on what your working assumptions are to get to that £1.5 billion in '26 and £1 billion in 2027. What are you now assuming for notional growth? What are you assuming for the amount of maturities in each year? And perhaps you could touch on the maturing versus the reinvestment yield that you're assuming as well. So that would be the first question.

Second question on the deposit book. On the £213 billion of retail savings, I think you said that the mix shift between instant access and time had slowed and stabilised, but perhaps you could just give us the split. I think you previously talked about a quarter being time, and then a similar question on the commercial book of that £171 billion, what's the split between current account savings and time? Thank you.

William Chalmers:
Thanks, Andrew. I'll go some way towards addressing your questions, perhaps not all the way, given that we don't disclose all of that information, but I'll certainly do my best. First of all, in respect of the structural hedge, as you know, just tracking back briefly to '25 again, we've got a £244 billion notional in the hedge. Over the course of '25 as a whole, we saw a 2.3% yield off the back of that structural hedge, which in turn allowed us to increase the structural hedge income to £5.5 billion, £1.3 billion increase on '24. That was a touch above what we previously expected off the back of effectively a slightly better rates picture than we had previously expected, and therefore an opportunity to somewhat improve. And then when we see '26, we obviously roll that benefit forward and expect to see a further £1.5 billion on top of that £5.5 billion to get to a '26 income of £7 billion, and then a further £1 billion in '27, as we discussed on Thursday.

The working assumption that we have there in respect of notional growth for '26 is really very modest. So I won't put a precise number on it, but if I say low single digits, then you get the idea as to what we mean in that context. There is a little bit more in the context of '27, but not a great deal more. So in each year, '26 is really very modest. '27, it's a slight notch up from that, but not terribly much. What that then allows us to produce off the back of the refinancing and the maturity yield is a yield in '27, and you'll be able to do the arithmetic obviously on this of about 3.2% in '27. We then see market rates, depends on the day of the week you ask obviously, but market rates anywhere between 3.6-3.8%, and that hedge contribution then continues to grow over the course of '28 and beyond, as we discussed on Thursday.

We haven't put a precise number in terms of the level of maturities. Typically, we talk about £35 billion odd in an average year. That's again, the arithmetic of an average duration of 7-7.5 years off the back of £244 billion in notional. That's just the arithmetic, as it were. But I would just be a bit cautious in terms of using that number for the reasons that you mention, which is the yield on which that stuff is maturing and the yield at which we're able to reinvest varies quite a bit simply because the different hedges were put on at different times. And alongside of that, in order to manage concentration risk in the hedge, we have to a degree at least, not terribly much, but to a degree at least, diluted concentration risk by virtue of effectively pre-hedging certain parts of the year. It's not a big deal, but it does make it slightly harder to judge exactly what the numbers will be from the outside.

That in turn, Andrew, is why we try to give these headline numbers for what we expect the yield on the hedge to be this year, next, and so forth. We've always said, and I think it's still true to say that this hedge is more like a caterpillar than anything else, and therefore you're going to be able to get to the rough increase in yield simply by treating it that way, but the initial guidance is intended just to get you a little bit more resistance. In respect to the deposits, the deposits performance in '25, as you know, decent performance over the course of the year, roughly £14 billion of increase. Within that, we saw retail going up by a number, about £5.5 billion I think it was, commercial deposits going up by about £8.5 billion.

You asked about the split within that overall balance, Andrew, in your question earlier on, we haven't really split out the fixed book, the, what we call limited withdrawal book, the instant access book and the PCA book, but you'll be able to see the PCA numbers in our disclosures. And then if we look at that, for the sake of clarity, we're looking at the fixed book being around 25-30% of savings typically in that zone. We're looking at the rest of the book being limited withdrawal and instant access, so that gives you some sense. And then secondarily, on your question around what is the interest bearing and non-interest bearing within commercial, we won't split out the term and other forms of deposit account within commercial, but to give you some idea, the non-interest bearing element in commercial, it's about 20-25% typically of the commercial balances, last year or so, more like 20% thereabouts of the commercial balances.

Andrew Coombs:
That's really helpful, thank you for all the detail.

William Chalmers:
Thanks, Andrew.

Question 3 – Guy Stebbings, Exane BNP:
Hi William, thanks for hosting the call. The first question was on mortgage spreads. Sorry to get into the minutia of basis points and that sort of thing, but you talked about 1 basis point decline each quarter through '25 and then still holding around 70 basis points.

Just want to check, is that on a like-for-like mortgage or is there any benefit in there for mix? I'm mindful the average LTV did drift up a little bit through the year, so I'm just wondering if that helps at all in terms of offsetting some of the competitive pressures when we're thinking about what an exact like-for-like mortgage spread has done through the course of the last 12 months or so.

And then the second question was on capital. You've given the £6-8 billion guide for Basel 3.1. Can I just check firstly, you're still not expecting any impact from the Basel output floor once that's fully incorporated, and then secondly, how do we think about Pillar 2A movements off the back of that? I'm conscious that £6-8 billion will be a net number and there'll be some puts and takes within that. And the regulators clearly talk to some benefits for where you're seeing an uptick in RWAs, you should get a Pillar 2A reduction, but I'm not sure the inverse is true. So maybe you could just help us walk us through how to think about Pillar 2 evolution from here. Thanks.

William Chalmers:
Thanks for the question, Guy. In respect to mortgage spreads, first of all, it is true to say that you've seen maybe a percentage point or two in respect of LTV, but that is just a function of the lending strategy of the bank. So typically, as you know, we've had a decent share within the first time buyer market. That is part of our franchise. We see it as an important assistance first and foremost for our customers, obviously, but it is also about partnering, if you like, with the customer through their lifetime and addressing various parts of their financial needs. So that's more a strategic choice than a financial pricing one.

Having said that, as you know, slightly higher LTV products will generally speaking have a slightly higher margin attached to them, but we've always been at the lower risk end of the overall mortgage portfolio. And so if you look at our new to arrears within mortgages, for example, 18 basis points is the latest read, and that continues to come down, particularly in new lending, that is to say setting aside some of the heritage lending from the HBOS era. So it is very low risk. Again, LTV is around 45%, inching up ever so slightly, maybe a percentage point or thereabouts off the back of, again, primarily strategic considerations.

I do think, though, that your 70 basis points, it's worth just, in a sense, repeating what I said last Thursday, which is that 70 basis points completion margin has been edging down by a basis point or two pretty much every quarter. And so as we go into the first, and indeed, ultimately, I'm sure the Q2 of this year, we'll probably continue to see the same. That is certainly our core assumption, we expect to see the same. At some point, therefore, it's going to be less c.70 basis points, it'll be c.65 basis points. That's just the direction of travel right now. Of course, that might improve, it might turn a little bit better, and I'll come back to that in just a moment.

We do look at that margin in two respects. One is we look at the overall product relationship that we have with the customer. I mentioned protection take up rates of c.20% when we spoke on Thursday. Alongside of that, we look at the Group margin as a whole, which as you know, was 306 for the year. We expect a material step up in the course of the margin. Exit rate of 310 in Q4, we expect a material step up in the course of 2026 in that margin as a whole, and that's very much the way in which we look at it. With the proviso that business being written at around a 70 basis point mark is still satisfying the cost of equity objectives that we have.

The point that I've made though, Guy, which hopefully also addresses your question, is at the moment we are seeing slightly better product transfer margins than we are new business margins. We have, and I think a lot of other banks probably say the same actually, we have quite a load of basically product transfers in the pipeline this year as the five year mortgages start to redeem and they transfer into new products alongside obviously the two-year mortgages. So there's quite a chunk of product transfer activity going on in our book this year. At the moment, that product transfer margin is better than new business margin. So I think the key dependency this year is to see how that evolves, because that is where a lot of activity is going on.

The second point I'd make, Guy, alongside of that, is that as I mentioned on Thursday, our new business assumptions for mortgages are down on what they were last year. That is to say we see a smaller net lending market in totality than we did in 2025. Now, that might change. And certainly some of the early indicators in January, without being too bullish about it, are probably a touch better than we have previously expected. Things like the house price data out this morning, some of the moving data in January. I don't want to overstate that, Guy, but it's perhaps a touch better. And of course, that volume factor would make a difference in respect to new business margins.

So overall, continued competitive conditions within mortgages, for sure. We are not assuming a recovery. At the moment, there is a bit of a mix effect in favour of product transfers, which is where we expect quite a lot of the activity is going to take place. There are some signs that the new business market might be strengthening a little. Let's see.

Guy, secondly, on your Basel 3.1 question, and I'll address it and just let me know if for whatever reason it doesn't actually hit the mark in respect to the question, but when we look at Basel 3.1, first of all, as you know, we're seeing, as we put it on Thursday, £6-8 billion in expected benefits. That is primarily a function of the move from foundation IRB, or rather the progress, if you like, that is being made in respect to foundation IRB.

Within that, we've got a couple of headwinds and a couple of tailwinds. The tailwinds are things like CVA movements. The headwinds are things like operational, standardised operational risk, which is getting more heavily loaded in the context of Basel 3.1. We do expect in respect of some of the Basel 3.1 headwinds, that we will see some compensatory Pillar 2A adjustments for those. The best example is the SME scaler, where effectively you're getting that SME scaler taken off of RWAs, therefore RWAs go up. You are then getting that compensated for by a Pillar 2A adjustment, which as you will know, is helpful, but doesn't totally swap the CET1 hit that you're taking, i.e. 56% of the CET1 impact from that scaler removal is made up for by the Pillar 2A relief.

So the sum of all of that is of that £6-8 billion, probably around £5ish billion or so is coming from that FIRB move or the combination of FIRB moves that I mentioned, and then probably another £1-2 billion or thereabouts from the retail improvements, which are less affected by the Pillar 2A moves that you highlighted. Guy, just to pause there, does that address your question or did I miss a piece?

Guy Stebbings:
No, no, I think you've covered everything there, that's really helpful. Thank you.

William Chalmers:
There was a point, actually just thinking back, Guy, there was a point on the floors and whether or not we get impacted by the floors. And maybe just to pick up on that, the short answer is the floors that are in there as a percentage of standardised do not hit us as we go through this Basel3.1 implementation period out to 2030. And that is simply because the types, things like the CRDIV rebalancing of RWAs and secured, for example, have now lifted our risk weightings above the minimum requirements that are otherwise implied by floors. And so as a result, you're not seeing that have an impact.

Having said that, we do expect some impact in the 2029-2030 period, i.e. those two years, pretty modest, but some impact from the re-weightings around equity investments. And of course, that will impact our LDC business, that will impact, depending upon size, possibly our Lloyds Living business.

And so '29 and '30, you will see somewhere around £2 billion, something like that, of RWA potential impact from that in those two years, depending upon the growth in those businesses. So while we don't get impacted by output floors, we do get impacted a little bit, i.e. of the order of a couple of billion in 2029, in 2030, by the re-weightings within equity, depending upon how fast LDC and Lloyds Living might grow.

Guy Stebbings:
Very helpful, thank you very much.

William Chalmers:
Thanks, Guy.

Question 4 – Chris Cant, Autonomous:
Hi, yeah, thanks for taking the questions, always useful, these sessions. I guess nice segue into asking you about some of the commentary you gave last week on the Group's centre and equity investments business. You talked about some reasonably strong growth expected for things like Lloyds Living and I think you mentioned a 15% growth number, but obviously there's quite a bit of stuff in central and equity investments.

Thinking back a couple of years during one of these sessions, you helpfully unpacked that for us in terms of the negative, kind of structural running negative from the MTNs and how we should think about some of the other parts. Just wondering if you could give us a refresh on that. So what are the netting items within that other income line during '25? And then we have a better starting point for thinking about what growth might look like on a net basis.

And then the other question was just on cost of risk. I guess just to round out this commentary around the 25 basis points for '26, how should we think about through the cycle cost of risk for the balance sheet as you see it today? Just interested in your take. Thank you.

William Chalmers:
Thanks for those questions, Chris. First of all, in respect to central items, the intention was to increase the disclosure on this item because we wanted to really help people understand the component parts in that, and in particular, help understand the benefits, if you like, of the investments that we're making in respect to some of the LBGI businesses. Alongside of that, Chris, as you highlighted, just help them understand what's going on in respect to the internal funding charges, which is the other part of central items.

So maybe just to take a moment just to explain what is in central items, and I appreciate that this is probably a bit of a recap for many people, so bear with me. Within central items, essentially, there's two components. One is effectively internal recharging after transfer pricing, number one. And number two is LBGI equity investments. And what we did on Thursday is to split those two components out.

Taking a step back, the central items disclosure that we added, as you will be aware, has an NII component and an OOI component. The NII component is basically two things. One is, as I say, the internal recharging, the internal funding costs, if you like, after transfer pricing, from things like AT1s and the cost of MTNs, number one. And then the NII is also the cost of funding the LBGI businesses. So that's the NII component.

The OOI component is very largely LBGI, i.e. the investments businesses, LDC, Lloyds Living, Housing Growth Partnership, those businesses, plus it is also the cost of the structured MTNs, which are recognised as fair value and therefore accounted for through the OOI line. And that is because they've got derivatives attached to them. So that's the OOI, largely LBGI, and then the cost of the structured MTNs, as said.

When you look at what happened in respect to '25, NII declines, and there are two things going on there. One is the internal recharging costs for both MTNs and AT1 is falling as rates decline and balances are lower. And the second is that the cost of funding LBGI businesses rises, increases because those businesses get bigger. And therefore NII, i.e. the positive, if you like, declines to £479 million, as you'll see in our disclosures.

The second thing that goes on is that OOI increases, and it increases by quite a meaningful chunk, as you can see. And again, there are two things that are going on in there, both in the same direction. One is the cost of that MTN funding instrument is falling as rates fall. It is linked to rates. And two is the LBGI, i.e. the investments OOI, is growing as those businesses grow. And so that's what's going on in OOI. And as you know, it increases substantially by £91 million to £228 million over the course of '25.

Now, if you look forward, the question is, how should you think about that? And I think the simplest way to think about that is to say that when you look at '26 as an example, it's reasonable to expect a similar, and take these words in a broad sense, but a similar percentage increase in NII and OOI in '26 to what you saw in '25. And why is that? It's because the same patterns basically are repeating themselves in '26 as we saw in '25. That is to say, underlying favourability in OOI driven both by MTN costs coming down as rates decline, plus most importantly, the continued growth in LBGI, which as you said, Chris, is up 15% in '25, and we would expect growth to be basically similar, if not better, in '26 from those businesses.

So I think the easy, forgive the term, guide to give you for how to look at it in '26 is to say those same patterns repeat themselves as they did in '25. Therefore, the percentage changes are not going to be terribly different. I might just pause there, Chris, just to make sure that is addressing your questions on central, but hopefully that gives you some background.

Chris Cant:
That's helpful, thank you.

William Chalmers:
Thanks, Chris. Through the cycle cost of risk. Well, let me just take a step back. As you know, historically, we have looked at through the cycle cost of risk for the business at around the 30 basis point mark. The recent history of the business has actually been favourable versus that for some years now. And I think that is a function of, as we said on Thursday, effectively a prime portfolio together with a stable, if unspectacular, macroeconomic backdrop. And that has combined to produce pretty healthy customer behaviours, which in turn have led to very favourable and consistently favourable AQR ratios. I mentioned underlying of, let's say, 23-24 basis points in '25 last year, with a repetition of around that c.25 basis points in '26.

I think when we look through the cycle charge, there's a couple of things going on. One is assuming that macro holds in much the same way as we would expect it to, that is overall lending some strength to the AQR output. Alongside of that, we are seeing certainly in many of our books, the continued de-risking, for want of a better term, as to our positions. So for example, in the beginning of this year, we dealt with the fibre issues that we had. We then had a write back in respect of one or two of those in the course of the second part of this year. Likewise, the CRE portfolio is now sub £10 billion and has been pretty carefully risk managed over the period of time.

There isn't much going on within the commercial book that is changing that overall pattern. Within the retail book, we are looking at whether or not there are ways in which we can serve customer propositions, which just kind of inch out a little bit from the risk that we have historically taken. So for example, you'll be familiar with our advanced credit card proposition, which is deliberately designed to introduce people to credit card borrowing. And off the back of that, you will see a basis point or two going the other way within retail. And it's a very deliberate strategic pattern, and it's built off the back of oftentimes customer relationships which stem from things like personal current account relationships and the like, but it is a desire to make use of our overall group risk appetite. It's not about stretching our appetite, it's about making use of the risk appetite that we actually have on the books right now, it is consistent with our board risk appetite metrics. And so, that goes slightly the other way.

I think overall what that means, Chris, is that our expectations for '26 are as we've described. To the extent that we would see a through-the-cycle charge, assuming that relatively, as I say, steady but unspectacular macroeconomic backdrop, then I think you're looking at 25 basis points, plus maybe a basis point or two, as we seek to fill out our risk appetite at the consumer level in particular, and as we seek to contain the corporate level at something that's not terribly different from where we are today. So I think it's a long-winded way of saying, Chris, that it's probably a nudge above 25 basis points as we strategically grow into our risk appetite.

Chris Cant:
Thank you.

William Chalmers:
Thanks Chris.

Question 5 – Aman Rakkar, Barclays:
Hi William, hopefully you can hear me.

William Chalmers:
Yeah, we can, Aman, thanks.

Aman Rakkar:
Yeah. I want to ask around interest rate sensitivity. I think you've nudged slightly higher versus the HY position in terms of the impact of a 25 basis point rate cut, just interested in what the driver is of that slightly increased rate sensitivity.

And I wanted to ask around, I think you're forecasting two rate cuts in '26, and the kind of pass-through assumption that you're making on these two rate cuts from here, is the illustrative 50% pass-through, as per the disclosure, I think it's at a similar level that you've been operating at, is that the right kind of baseline assumption that sits behind that?
I do note that just on some of your savings products, your headline rate is now quite low, so it seems like you might actually struggle to fully execute on that basis on some of your product lines.

And then, second question was around costs, maybe picking up some of the discussion from last week really, just around the 1% cost growth that you're guiding for this year, the sub £9.9 billion, which I guess ex-Schroders' personal wealth is even better than that, just the sustainability of that level of cost growth. You point to positive jaws in coming years. That feels well underwritten because of the income tailwinds. But can you continue this level of cost growth beyond '26? Thank you so much.

William Chalmers:
Thanks, Aman, for those questions. Just dealing with each of them in turn. Rate sensitivity, first of all, we've put rate sensitivity, I think it is c.£125 million in terms of the year one impact of a 25 basis point parallel reduction in interest rates. It's interesting, actually, that sensitivity is slightly greater where it was versus the HY. It is slightly less, I think, versus where it was at the FY. And there's two different things going on there. In respect of the HY, it is because the buffer at the FY is higher than it was at the HY. And so, as a result, when rates come down, that buffer gets hit harder when it's larger, meaning that at the end of year, when our buffers were larger, which is partly what led us to increase the weighted average life of the hedge, of course, we get hit harder, and as a result, the sensitivity goes up to £125 million, whereas I think it was something like £100 million as of the HY.

Versus the FY, it has come down, and essentially, what's going on there is largely the work that has been going on around repricing lags within the retail area. As you know, we've had repricing lags, which are dictated by the regulations surrounding the particular deposit books, whether it's PSR or whether it's BCOBS. We have started to shift those deposit books so that we can effectively pass on interest rate changes more quickly, and therefore the effect of a reduction in bank base rates is less because we're able to pass on, we're able to move quicker in terms of the deposit books. And overall, it's the effect of that that has benefited us versus our year-end '24 disclosures as to interest rate sensitivity.

It is worth saying, Aman, while we're on this topic, that that £125 million, as you know, is basically looking at it from a fairly single-minded perspective, which is to say this is the impact on the hedge, the buffers and so forth. It doesn't take any account, or rather it assumes stability in other aspects of the book margin. So it assumes stability in asset margins, for example. It doesn't make any assumption about reduced churn that you might get in the context of falling rates. And so, we think that, actually, if you add together the more holistic picture, and assess things like asset margin offsets or possibly less churn, and indeed take account of possibly increased activity levels in the general economy off the back of bank base rate reductions, that the true sensitivity is probably a fair bit less than that £125 million. But that £125 million nonetheless is an objective way of looking at it, taking into account the factors that I just mentioned. But bear in mind that it doesn't take into account those other points that I've made, whether it's churn, whether it's asset repricing, whether it's activity levels and so forth.

The second question in terms of pass-through, I think this is largely a question of timing, Aman, that is to say, so far at least, we have probably passed through a touch over 50% of the bank base rate reductions that we have seen. Having said that, we have assumptions over the course of the year, based upon the next couple of bank base rates that we see, that we will pass on slightly less of those. And so, I think the way to look at it is what is the pass-on rate over the course of the cycle rather than what is the pass-on rate at any particular point in time. And therefore, I think some of the moves that we have made to date in respect of pass-on will be different to some of the moves that we'll be making later on in the year in respect to pass-on.

And what that does is it essentially allows us to calibrate when we're in the market and when we're not in the market, which is a calibration that takes account of clearly customer value, but also the funding needs of the business, what is now, as you know, a 97% loan-to-deposit ratio, and also relative costs of funds vis-a-vis things like wholesale funding and the like. So we're trying to look at this in the round, the pass-on decisions at any given point in time are essentially a reflection of where we think the balance of the business is and when we want to be in the market and when we don't want to be in the market. But as I said, look at it in the round over the course of the cycle rather than look at it so much at any particular point in time, because the conclusions, if you like, will change.

The final question, in respect of costs, it's a good question. The 1%, or c.1%, cost increase that we see in '26, let me talk about that a little. I think the first point is to say, where did we get to in '25? And the headline number, as you know, in '25, is that costs were up 3%. But actually, if you exclude the bump-up in severance costs that we saw in '25, the underlying number beneath that is more like 2.4%, and if you exclude severance costs bump-up plus Lloyds Wealth, then the underlying number is more like 2.3%. So a headline number of 3% is actually more like 2.3% when you take account of those two factors. As a result, the growth in costs in '25 is lower than you might first think based upon that headline.

The second point is, and this is what you're getting at, clearly, when we look at '26, we're expecting cost increases to go to sub £9.9 billion. I'll come back to that in just a second. And as you say, that's about a 1% cost increase over the course of the year. But actually, if you strip out a combination of Lloyds Wealth and also the acquisition of Curve, which has some costs associated with it, albeit we haven't put a number on it, you strip those two elements out and the cost increase over '26 is actually markedly lower than that 1%.

Now, what is going on there, a couple of things. One is the benefit of lower inflation. That is benefiting us in terms of lower pay settlements with our colleagues. It's benefiting us in terms of lower price increases that we expect from third party providers. That's block one. Block two is the full run rate of our BAU reductions, if you like, which are things like organisational design, things like matrix management, third party contracts, these types of things. We're getting the full run rate benefit of measures that we have taken in '25, loaded into '26, clearly that's an ongoing exercise. The third point is a lot of our strategic investments, if you count the technology ones as part of that, let's say c.50% plus are oriented towards cost-saving activities. And not surprisingly, those strategic investments which are now coming to their culmination for their strategic cycle are achieving the full benefits of that in respect of '26. And so, it's the cumulative effect of those and the full year benefits of those strategic investments that we're seeing benefit the cost base in '26. So that's the third factor.

And then, the final factor is, as you would expect at this stage in the cycle, for all of our various different projects, we have spent a fair bit of the money to establish those projects, whether it's things like operational resilience in the COO area or whether it's building out the mass affluent proposition. They are starting to plateau, and as a result, we have a slight reduction in cash investment, which in turn is probably giving us about a £100 million tailwind in respect of costs in 2026, and that £100 million tailwind is simply a reflection of our overall investment portfolio and the expected patterns of that cash investment over the period of the strategic cycle.

So Aman, it's a combination of those four or five factors. I think a couple of points I'll make on top of that. One is, when we look beyond '26, we committed on Thursday to continued income growth, to improvements in operating leverage, which translates as improvements in cost-to-income ratio, and to improving and sustainable returns for the business. And as we look forward, what we're not going to do is to, if you like, shy away from what is justifiable, as long as it's value-added investment in the business. Now is not the time to do that. The sector's in a massive state of change, as you know. And we will be investing in the BAU and we will be investing in customer propositions and operational resilience and the like. And so, that is built into the expectation going forward, and we'll talk more about that clearly in July. So that's point number one.

Point number two is just going back to '26 momentarily, we've committed to sub £9.9 billion costs for 2026. That is what we see as consistent with the opportunity set that we have in front of us right now, which in turn is consistent with delivering on the guidance that we've given you, whether that is net interest income, whether that is cost:income ratio, ROTE and so forth. As you'll notice from our presentation, we put that sub £9.9 billion in parentheses, because that's what is consistent with achieving all of our guidance. If we see the market take off in a benign way and present us with more value-added opportunities, then I hope that you would support us, and we would expect to invest into those opportunities in order to improve the outcomes for shareholders, top-line growth, ultimately ROTE.

Now, that is an if statement. It is not more than that. We are sub £9.9 billion, and based upon everything I know right now, that is what we're going to deliver. We are certainly going to deliver the cost:income ratio of sub-50%, that is an absolute commitment. Based upon all of our plans, and as I say, opportunity set as we see them today, that is consistent with sub £9.9 billion. But as I say, if we see opportunities to improve shareholder returns off the back of the available opportunity set, then we're going to look at them. So I hope that gives you some context and guidance, Aman, in terms of the way in which we're thinking about it.

Aman Rakkar:
Yeah, that's really good. Thank you so much, I really appreciate it.

William Chalmers:
Thanks, Aman.

Question 6 – Jonathan Pierce, Jefferies:
Hi, William, thanks for doing this. A couple of questions, please. The intangible line went up £550 million in the second half of the year. Can you give us a sense as to how much of that was from the software intangible versus Curve versus Schroders Personal Wealth, please, that'd be the first question.

The second one on the hedge, in terms of where you're actually reinvesting on the curve, obviously the weighted average life is 3.75 years now and increasing, so one assumes you're putting quite a lot of stuff on at 7-10 years, not just five years. So which part of the curve should we be looking at when we're thinking about those reinvestment rates? Because obviously, there is a not-insignificant premium at the 7-10 year part of the curve versus the five year. And maybe you can just tell us what you've assumed for the reinvestment rate this year and next year. I'm assuming it's consistent with your average base rate assumptions, so around about 3.5% or something. That would be useful, thank you.

William Chalmers:
Thanks Jonathan, for both of those two questions. Maybe just to take them in turn. Intangibles, first of all, as you know, that's about £8.2 billion *[note for reader clarity: this is quoted net of deferred tax of £366 million. Gross of this it is £8.6bn, in line with the number quoted in the FY25 results announcement]*. Of that £8.2 billion, about £3 billion or so is goodwill, which you'll be familiar with the sources of that *[note for reader clarity: goodwill increased by c.£260 million in 2025]*. It *[the other intangibles, net of deferred tax]* did *[also]* increase, like you say, about £130 million in 2025. The vast majority of it *[the movements in intangibles]* was to do with the Lloyds Wealth acquisition. None of it, I think, would be to do with Curve, simply because we haven't actually done the Curve acquisition so far, so it's not on our books. So that jump that you're seeing in 2025 in terms of intangibles or rather the goodwill would be associated with Lloyds Wealth.

And then, you're seeing £4.5 billion of basically capitalised software within our overall intangibles, Jonathan, and that is growing off the back of the investments that we're making. In particular, one of the shifts that we have been doing as a group is to steadily enhance our own internal capabilities, which in turn means that we are building more capabilities than we used to, in turn building up the capitalised software asset, which as much as we might like it to be, unfortunately, is not included within our capital base, it's a deduction from capital. So there's two things going on there. The goodwill coming off the Lloyds Wealth acquisition, number one, the increase in capitalised software that we're seeing off the back of the investments, driven by basically a strategic choice to build rather than buy, in significant part, for our infrastructure requirements and needs.

What that does tend to lead to, Jonathan, within that context, is a little bit of an increase in terms of the intangible as a proportion of capitalised assets. And there's a third element going on there, which is to say not only are we building into the infrastructure of the business, but we're also, as you know, starting to economise on things like head office space. I think we've reduced head office space by about 45% since 2021. Likewise, we've announced some branch closures. These are in pursuit clearly of trying to ensure that we still serve our customers properly, but we have announced some branch closures. And so the tangibles as proportion of capitalised assets comes off as part of that. So there's a bit of, if you like, give in the context of what we are building, there's a bit of take in the context of head office and other tangible assets coming off the balance sheet as we economise on head office space and indeed close some branches.

In respect of the structural hedge, second question, I think the way in which we look at it is, as I said earlier on, first and foremost, a rolling caterpillar type approach to the replacement of the structural hedge. And therefore, when I look at it, when I look at the curve, I look first and foremost at the curve that is basically replicating the structural hedge weighted average life. And typically I look at the three years, the five years, the 3-5 years is the spread that I'm looking at. At the same time, you will find some long-dated hedges within the overall book that we have. And so your point around longer dated hedges in respect of, is there any exposure to 7-10 years? Yes, there is. It's pretty modest, it's pretty small, but there is a little bit of that in there, which is intended to balance out some of the behavioural lives of the assets against which we're hedging. In particular, current accounts are a good example of having a weighted average life, which is significantly beyond the average for the hedge.

I think the overall expectation, when we look at the plan versus the market, you'll be familiar overall with our base rate expectations for this year, but also then tilting up a little bit in 2028 where we expect there to be a 25 basis point add-on for what it's worth. Our swap rates are not terribly different to that. Well, they're not tracking exactly Jonathan, but they're not terribly different to what you're seeing in respect of our bank base rate assumptions on a projected basis. And of course, market expectations can differ from that. And so you will see a bit of a difference at times from the market rates versus what we're assuming in the swaps. And at the moment, I think our assumptions in the swaps are probably a touch inside of, i.e., below market rates.

Jonathan Pierce:
Okay, thanks for that. Sorry, can I just come back briefly on both of those because I think intangibles in 2025 went from just under £8.2 billion to almost £8.6 billion. Having gone down a bit in the first half, so I must have missed something, there's quite a big increase in intangible in the second half of last year, which I can't quite source. And sorry, on the hedge as well, the weighted average life of 3.75 years, if it's a static, notional, and rolling in a caterpillar type nature, you must be reinvesting everything at sort of 7.5 years on average. So why would we be looking more at sort of 3-5 year swap rates rather than something a bit longer than that, please?

William Chalmers:
In respect of the movement in intangibles, as said, I think it is very much oriented around the SPW acquisition, both goodwill and any intangibles movement. So I'll look at it just to make sure that I'm not missing anything, but that is, I think, the bulk of the movement allied to some of the investments that I made earlier on. I'm just trying to think on the intangibles movement if there's anything much more than that. The investments in terms of the cash profile would've been adding to intangibles over the course of the year, for sure. We've got the SPW acquisition. I don't think it's anything much more than that, Jonathan, but I'll come back to you if there is anything that occurs to me post the call.

Jonathan Pierce:
Okay, thanks.

William Chalmers:
In respect to the structural hedge, when we look at the weighted average life of the hedge, I guess we're looking at the entire spectrum really of what is in the hedge. It is generally the case that the behavioural lives of much of what is in the hedge significantly exceed the 3.75 years that we have within it. I guess what that means, I think, in translation, is that the hedge is oriented towards a relatively conservative approach, but you'll see that there is the overall approach that we would adopt is to not exactly mimic, but to basically build the hedge around the weighted average life assumption. And in a way, I guess that's testified to by the fact that this is indeed the weighted average life of the hedge. There are undoubtedly features of that £244 billion, the equity is the best example, but equally the PCA deposits balances are another example of behavioural lives that significantly exceed the weighted average life.

We are effectively, I suppose, for reasons of prudence, as much as anything else, putting in a hedge that is much shorter than that on a stylised basis and coming in with 3.75 years. If we see deposit balances change their behaviour, there is an argument for us to go out beyond that. We've typically not gone beyond the kind of 3-4 year corridor, at least not recently. As you know, when curves were totally flat, we actually went down below that, for obvious reasons. But we've stuck within the overall 3-4 year corridor for that reason. Not to say that there aren't hedges in there that exceed that, overall though, we take the stance that I just mentioned.

Jonathan Pierce:
Okay, thanks, William.

William Chalmers:
Thanks, Jonathan.

Question 7 – Alvaro Serrano, Morgan Stanley:
Hi, thanks for taking my questions. William, thanks for your comments around the equity investments division and kind of a rough expectation of what growth could look like in '26. Any chance you can give a similar commentary or colour around the retail other income because we don't have the same level of disclosure, I guess that's more for the strategic update, but any colour would be useful for this year.

And then a follow-up on the mortgage spread. Obviously completion margins are, you've quoted 70 basis points, but a touch below several quarters now, which looking at the front book and that we can see in the market made me think that you could easily sort of come down to 60 basis points, or even below during 2026. But I got the impression that your comments earlier today in the call were a bit more constructive when you were talking about refinancing, so have I misunderstood? Can you sort of maybe comment if I've misunderstood or you got too negative or you're a bit more constructive based on the activity year to date? Thank you.

William Chalmers:
Thanks, Alvaro. Just dealing with each of those in turn. The retail OOI, as you know, looking back at '25, up 12% over the course of the full year, we don't disclose this figure on a quarterly basis particularly, but to give you some idea, up around 10% year-on-year in Q4. What's driving those? It's a combination of things, but in some, transportation is clearly playing a significant role. The right way to look at transportation, of course, is partly to look at the op lease depreciation. I'll come back to that in just a second. But then alongside of that, benefits from the overall cards portfolio, we saw particular benefits from PCA products, basically value added products alongside of that, some benefits from debit spend. And then alongside of that, some benefits from cards interchange all within retail.

I do think it's fair to say that of the growth, a decent chunk of it is coming from transport. As you know, the right way to look at that is to take account, I suppose, of the op lease depreciation that we saw during the year. One point that's worth making there is that when we look at op lease depreciation for '26, we are expecting that to slow down a little bit over the course of '26. And the reason for that is because the additional depreciation that was previously loaded into '25 numbers off the back of the RV, or rather electric vehicle price corrections that we've seen historically, starts to drop out as we go into '26. And therefore you see growth within the transport OOI line that exceeds growth within op lease depreciation, at least for '26, and then '27 and beyond, we'll see.

But that is a bit of a benefit that you see within the overall retail performance on a net basis for OOI. On a top line basis, again, transportation, value added PCAs, card interchange, debit card spend, these things are driving retail. What would we expect to see for '26 as a whole? I think it would be somewhere between what we saw in Q4 that I mentioned a second ago. If things go well, it might be up at '25 type levels, but that type of level we'd expect to see replicating itself.

Second, in respect of mortgages, when we look at the overall mortgage spreads right now, you're right, we are seeing some fairly competitive offers out there in the market. I do think, as I mentioned earlier on, there is this discrepancy between product transfer margins and new business margins, number one. Number two, we are targeting different parts of the market that we think are attractive from a return perspective. And therefore, I think our overall spread wouldn't necessarily fit perfectly with what you see in terms of external indicators. When we go forward, our core assumption is that this doesn't recover in any particular way over the course of the year. It may be that we see a little bit of pressure getting exerted on mortgages above and beyond what we expect. We'll see. I mean, I think if you do, you've got to look at the margin in around still, because I suspect you'll see that pressure being eased up, if you like, or offset in respect of other parts of the business, whether that's on the liability side or other consumer product pricing. That's usually what happens.

So I think Alvaro, in short, we're seeing c.70 basis points in Q4. We're seeing that, as I mentioned earlier on, experience a basis point or two of erosion. We're seeing that continue into Q1. And then over the course of this year, we're not expecting any particular recovery in terms of basis points within mortgages. I do think as said earlier, this product transfer versus new business discrepancy is going to be important. And of course, alongside, we'll be doing our best to build the overall relationship with the customer to ensure that the depth of relationship statistics that we're aiming for as a strategic outcome are maintained, if not built.

Alvaro Serrano:
Thanks William.

William Chalmers:
Thanks Alvaro.

William Chalmers:
Well, I think just to say thank you very much indeed for taking the time to join the call this afternoon. Hopefully it's been helpful in terms of understanding the numbers. We'll look forward to maintaining the dialogue and indeed building the dialogue with you over the course of the coming weeks. So thanks very much indeed for taking the time.

FORWARD-LOOKING STATEMENTS

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