LLOYDS BANKING GROUP PLC – Q3 2013 INTERIM MANAGEMENT STATEMENT

TUESDAY 29 OCTOBER 2013

António Horta-Osório, Group Chief Executive

Good morning everyone, and thank you for joining us for our 2013 third quarter results presentation. I am joined here today by our Group Finance Director, George Culmer, who will shortly present the financial results in detail.

So turning to slide 1, for those of you following the website presentation. We continue to make significant progress in the delivery of our strategic plan as we create a lower risk, highly efficient UK retail and commercial bank, focused on our customers' needs, and on supporting the UK economic recovery.

We are lending more to SMEs and to larger corporates, and in the last quarter returned our core mortgage net lending to growth. As a result, the Group's core loan book is now growing in all divisions, with net lending increasing another £2 billion in the quarter and having increased by £5 billion year-to-date in a falling market for corporate loans.

The third quarter was also a significant one with our launch of a new bank, TSB, the first time this has been done through a spin-off in the UK, bringing a fresh new competitor to the high street, and we also launched the rebranded, revitalised Lloyds Bank, building on its history of almost 250 years of serving the people and businesses of Britain.

We are focusing relentlessly on meeting the needs of our customers, who are at the heart of our strategy, by investing in the products and services they require. As a result, we have seen a further reduction in customer complaints of 20 per cent compared to last year, or 50 per cent compared to 2011. Complaints per 1,000 accounts are now around a third of the average level of the main UK banks and we continue to see a strong performance in customer service metrics, with Net Promoter Scores increasing by 13 per cent in the first nine months of the year.

We also further reshaped our business, increasing our focus on our core UK business through further capital accretive non-core reductions, and sales of international businesses including Australia. We are now ahead of our twice revised plan, and have effectively met our target for non-core disposals and country exits 15 months ahead of schedule and I will come back to this shortly.

We continued to strengthen our balance sheet and capital position, despite a further charge for legacy PPI business in the third quarter, and have now commenced discussions with our regulators on the timetable and conditions for dividend payments.

Turning now to an overview of our financial performance on slide 2.

We have delivered significant improvements in profitability and returns, driven by progress on all lines of the income statement.

The increase in income was supported by core loan growth, and by the substantial expansion in margin, primarily driven by improved deposit margins, as you will hear from George.

At the same time, costs continued to reduce as we further simplified the business, and impairments fell sharply as we continued to de-risk the balance sheet.

As a result, profit increased both in the Group and in our core business, with Group underlying profit increasing to £4.4 billion and core profit by 20 per cent to £5.5 billion. We delivered a statutory profit of £1.7 billion, despite legacy charges and losses on capital accretive non-core asset sales, as you will hear from George.

And with this improved profitability, together with a reduction in non-core RWAs, the Group return on risk-weighted assets more than doubled to 2.01 per cent, while the core return has now reached 3.17 per cent.

Turning to the balance sheet on slide 3. We have taken significant steps this year to further strengthen and de-risk the balance sheet.

We continued to strengthen our funding position, with further growth in customer deposits matching our core loan growth, resulting in our core loan to deposit ratio remaining at 100 per cent, and the Group ratio reducing by a further 3 percentage points to 114 per cent.

Our wholesale funding is now around half of what it was at June 2011 at £151 billion and our money market funding is now £31 billion which is less than a third of the level at that time.

Simultaneously, we made excellent progress on non-core reductions in a capital accretive way. We have achieved our revised year end targets and are now targeting a further reduction to around £66 billion of non-core assets, and around £26 billion of non-retail non-core assets by the end of 2013 and to around £15 billion by the end of 2014. This means the non-retail assets will represent only 3 per cent of our Group's balance sheet by the end of this year and less than 2 per cent by the end of 2014.

In line with our UK-focused strategy, we have also reduced our international presence, most recently selling our remaining Australian operations. As a result, we are now in nine countries, having exited or announced the exit from 21 countries and achieving our target to be operating in 10 countries or fewer by the end of 2014, down from 30 two years ago. This means our UK assets now represents 95 per cent of Group assets. Therefore this key element of our June 2011 strategy of refocusing of the Bank on its core UK Retail and Commercial business has now been delivered 15 months ahead of schedule.

We also further increased our fully loaded core tier 1 capital ratio to 9.9 per cent, an improvement of 1.8 per cent in the first nine months of the year, and remain on track to deliver our guidance for a fully loaded ratio of above 10 per cent by the year end.

Turning now to slide 4, and looking in more detail at the dynamics of core loan growth.

The support we are giving to our customers and the UK economy has been evident in the growth of our core loan book this year. We have grown core loans and advances by £5 billion, or around 1 per cent, against a market that has fallen by 1 per cent, or around £14 billion.

We have now committed over £28 billion to our UK customers through the Funding for Lending scheme, and have continued to support UK manufacturing by committing over £1 billion of lending in the last 12 months, again ahead of our target.

For SMEs, which are a key driver of employment and economic growth, we have supported nearly 100,000 start ups this year, and have also continued to grow lending strongly to these customers, with an accelerated net growth of 5 per cent in the last 12 months, which compares to a market that has declined by 3 per cent.

For our retail customers, as we show on slide 5, we returned our core loan book to growth in the third quarter, as targeted one year ago, and after reaching a 100 per cent core loan to deposit ratio in March of this year. We expect to continue to grow our core mortgage book into 2014.

We are continuing to focus on key areas which support the housing market and the UK economy, particularly first time buyers. Here, we have already exceeded our £6.5 billion gross lending target for 2013, with £6.7 billion of lending to the end of September. In October we also reached our full year end target of helping over 60,000 customers buy their first home.

After the quarter end, the Government launched the second stage of the Help to Buy scheme. We were one of the first participants to launch a range of products, under our Halifax brand, making mortgages accessible to those with small deposits, but who are able to afford the monthly payments.

We expect the scheme to help to increase the liquidity in the UK housing market and increase the volume of mortgages available, while offering support to the wider UK economy through increased activity in the construction sector, one of the main drivers of employment in this country.

We have already seen significant interest in Help to Buy mortgages from our customers in just the first few weeks of the scheme, with enquiries running at a very high level and applications growing strongly week after week.

And with that, let me now hand the call over to George for a more detailed look at our financial performance.

George Culmer, Group Finance Director

Thank you António and good morning everyone. Beginning with the P&L on slide 6. As you've heard, we've continued to make substantial progress with our strategy and this is reflected in the Group's financial performance in the first nine months.

The Group's underlying profitability has more than doubled on prior year to £4.4 billion, with profits in our core business increasing by 20 per cent to £5.5 billion and losses from the non-core more than halved to £1.1 billion.

Underlying income grew 1 per cent to £14 billion and within this, net interest income was up 2 per cent, reflecting core loan growth and improved margin, while other income was broadly stable despite non-core reductions and the subdued external environment.

Costs were down by 6% or £427 million, mainly driven by Simplification, and the impairment charge was nearly £2 billion lower at £2.5 billion.

Statutory profit was up £2.3 billion to £1.7 billion, mainly driven by the increase in underlying profit. Looking at the movement between underlying and statutory profit in more detail. Slide 7 sets out the key items, starting with asset sales where losses on disposals totalled £637 million. These included approximately £330 million from Heidelberger Leben, which we announced in August, and £256 million from the sale of our Spanish retail operations in Q2. Our disposal programme remains capital accretive, generating approximately £2 billion in the year to date.

Gains on government bond sales were £786 million, while volatile items of £39 million were significantly better than last year, mostly driven by positive insurance volatility of £637 million due mostly to rising equity markets.

On Simplification, we expensed £608 million in the first nine months. This brings costs to date to £1.5 billion, with over £2 billion expected to be directly expensed through the income statement, out of an estimated total cost of approximately £2.3 billion.

On Verde, we are making good progress towards an IPO in mid 2014. TSB is now operating as a stand-alone business within the Group and the nine month spend of £586 million brings the total costs to date to just under £1.4 billion.

On legacy, we have taken a further PPI provision of £750 million in the third quarter, bringing the total in the first nine months of the year to £1.25 billion. I will cover this in more detail shortly.

The movement in other statutory items primarily reflects, as at the half year, a charge of £104 million relating to revisions in pension benefits, which compares with a £250 million pension gain recognised in the previous year.

Finally, the year-to-date tax charge is £1.4 billion. This is significantly higher than the UK tax rate, primarily due to the write-down of deferred tax assets, with £503 million from reduction in the UK corporate tax rates and £355 million from the exit from Australian operations.

Turning now to slide 8 and underlying income. Core income grew 5 per cent in the nine months to £13.5 billion, or up 2 per cent excluding St. James's Place with income in the third quarter of £4.4 billion up 4 per cent compared to Q3 2012.

This growth has been driven by net interest income, which was up 5 per cent in the nine months and on the second quarter, due to both margin expansion and loan growth. Other operating income remains challenging, and is down 2 per cent year to date excluding St. James's Place, reflecting the subdued external environment and a general trend towards net interest income.

With the deposit margin continuing to expand and the further reduction in non-core assets, the Group margin rose to 2.17 per cent in the third quarter, giving 2.06 in the nine months compared to 2.01 at the half year. Given this progression, we now expect a full-year 2013 margin of 2.11, with further margin widening in Q4 and a more stable profile in 2014.

Slide 9 shows the movement in greater detail. As you can see, the trends we highlighted at the half year have continued, with a widening deposit margin as a result of lower rates and the ongoing maturity of more expensive fixed term deposits, and this has more than offset asset margin pressures.

The margin impact from the sale of Government securities remains in line with expectations at 8 basis points.

And we maintained the beneficial impact of the repositioned structural hedge into Q3, resulting in a drag of only 1 basis point, compared to the expected 6 at the beginning of the year.

Moving now to costs on slide 10. As mentioned, costs were down 6 per cent, net of inflation and the ongoing investment in our core franchise. This reduction was again primarily driven by Simplification, where we have now achieved annual run-rate savings of £1.3 billion out of our end-2014 target of £1.9 billion. For the 2013 full year we continue to target costs of £9.6 billion and this includes the expected FSCS and bank levy charges that we will incur in Q4.

Turning to slide 11 and impairments. On impairments we've seen another further substantial reduction in the P&L charge and a significantly improved AQR, reflecting, once again, the benefits of non-core reductions and robust credit quality in the core book.

Core impairments of £1.2 billion are down £120 million due mainly to strong underlying performance across our Retail portfolios, while non-core impairments were £1.3 billion, compared with over £3 billion last year, with reductions in Commercial Banking and International.

The Group AQR was 63 basis points for the year to date, and 51 basis points in the third quarter, with improvements in both core and non-core.

In terms of impaired loans and coverage, the quality of the Group's loan portfolio continues to improve and impaired loans now stand at 7.2 per cent, a reduction of half a percent since the half year, while coverage levels have been maintained at 51 per cent.

Moving now to slide 12 and legacy issues. On PPI, complaint volumes have continued to fall in the third quarter although at a slower pace than projected. Average monthly complaint volumes fell 8 per cent in Q3, with a weekly average of approximately 11,000 compared to around 12,500 in Q2.

Costs were also higher than projected. This was driven by the acceleration of cases with the Financial Ombudsman Service, higher than projected reactive volumes, as well as an increased scope of proactive mailings combined with higher response rates.

As a result of the incremental volumes and costs, we are increasing our forward projections and raising the provision by £750 million, which brings the total amount provided for PPI to £8 billion, of which £1.7 billion relates to administration costs. £1.7 billion remained unutilised as at the end of the quarter.

Turning to the non-core portfolio on slide 13. We continue to make excellent progress in reducing our non-core assets in a capital accretive manner. As you've already heard, with the disposal of our Australian operations and German insurance business, we've reached our 2013 year end target of £70 billion.

We've also continued to see the reduction in risk outstrip the fall in assets, with non-core RWAs down 39%, well ahead of the 29% fall in assets.

We now expect the portfolio to be around £66 billion at year end, and within this we expect the non-retail non-core to be around £26 billion and to fall to around £15 billion by the end of 2014.

And finally to slide 14 and our progress on capital. As you know, the regulatory framework for capital continues to evolve and we are currently awaiting the finalisation of CP5/13 and the implementation of CRD IV in the UK.

What matters most is that we continue to strengthen our capital position, and as you've already heard today our pro forma fully loaded CRD IV core tier 1 ratio now stands at 9.9 per cent, representing a 1.8 percentage point increase since the start of the year and 0.3 percentage points in Q3. This has been achieved after charging the additional legacy costs and adverse pension fund valuation movements, with these more than offset by strong capital generation in the core business and from our capital accretive non-core reductions.

I continue to expect our fully loaded ratio to be above 10 per cent at the end of this year. On a current rules basis, our ratio now stands at 13.5 per cent, which gives us the seventh strongest capital ratio of the top 50 global banks.

That concludes my review of the financials and I would now like to hand back over to António.

António Horta-Osório, Group Chief Executive

Thank you George. Before we move to Q&A, let me close this morning's presentation by drawing together our forward looking guidance, which I will follow with a brief summary of our performance so far in 2013.

As you can see on slide 15, our accelerated progress on our strategic plan has driven the need to enhance our guidance in a number of areas so far this year.

Today, we are upgrading our Group margin guidance for 2013 to 2.11 per cent.

On non-core assets, we are now expecting the total portfolio to be reduced to around £66 billion by the end of the year within which the non-retail assets are expected to be around £26 billion and then further reduced to around £15 billion by the end of 2014, less than 2 per cent of our balance sheet.

The Group's fully loaded core tier 1 ratio has continued to increase and we expect it to be over 10 per cent by the end of the year.

Meanwhile, our drive to create a customer focused and more efficient bank is reflected in our expectation of continued core lending growth and for costs to end the year at around £9.6 billion.

Moving to slide 16 and to summarise our progress. We have continued to execute strongly on our strategy. The investments we are making in our core franchise to improve our products and services are increasingly benefiting our customers, while supporting the economic recovery.

At the same time, we have made rapid progress in strengthening, de-risking and simplifying the business, creating a strongly capitalised, low cost, lower risk business, which should deserve one of the lowest costs of equity in the sector over time.

We have returned our core lending to growth, with the loan book now growing in all divisions.

We are already the most efficient of the main UK banks and will continue to drive our cost/income ratio down, building a sustainable competitive advantage in the UK retail market. This has resulted in a substantial improvement in profitability and returns, both in the core business, and in the Group as a whole, a trend which we expect to continue.

We therefore remain confident in delivering our strategic plan, which in turn will enable us to deliver strong, stable and sustainable returns to our shareholders over time.

We are proud that the improvement in our performance and the progress we have made on our strategy has enabled the UK government to begin the process of returning Lloyds Banking Group to full private ownership, and getting taxpayers' money back at a profit.

And we have now commenced discussions with our regulators on the timetable and conditions for dividend payments.

Thank you, this concludes our presentation, and I would now like to take any questions you may have.

End of presentation

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TUESDAY 29 October 2013

Question and Answer Session

Question 1: Chris Manners, Morgan Stanley
Good morning António, good morning George. So two questions if I may. Firstly was on the Help to Buy Scheme. Obviously you are indicating you're seeing good demand so far. It looked like the pricing for some of the products from yourselves and RBS were maybe a little bit higher than people originally anticipated and that may reduce, sort of, back book SVR cannibalisation. I just thought I would ask about how much volume improvement you think you are going to get in the mortgage market from the Help to Buy Scheme and also that impact on the margin dynamic?

And the second one was you alluded to CP5/13 and just trying to work out where you think you can run the steady state capital ratio because I guess Pillar 2A coming in, it looks like it could be quite capital consumptive considering, you know, I guess pension volatility is a reasonably big number for you and given you're 25 per cent of the UK banking system, presumably your domestic SIFI buffer could actually be quite substantial, just maybe some thoughts around those. Thank you.

Answer: António Horta-Osório
Okay Chris, I will answer the Help to Buy question and then George will answer the capital one. In terms of the Help to Buy. This is quite interesting because I mean I have just as an analogue, I have been on my monthly branch visits last month, where I was in the North of England and as we expected, and we have said when the scheme was launched, there is a very, very strong interest through the Halifax brand where we launched the scheme first as you know. Lots of interest from customers and also non customers, mostly from first time buyers, some from movers, but mostly first time buyers. People that can clearly meet their monthly payments, but don't have access to a significant deposit to put up front. And we see applications increasing very strongly week after week. We are three weeks down the road so it is too early to tell you about numbers. But my expectation as I have said before is that it will be quite significant and we will increase significantly I think the rates of mortgage growth in the next few quarters which as per last Bank of England numbers were around 0.7-0.8 per cent. I think we will see growth increasing significantly based on this and on the increase of confidence that this is also instilling in the market.

In terms of specifics of what you ask, our impression is the following. First in terms of pricing. I think it was logical that the price would have to be higher than 75 or 80 per cent LTVs because with higher risks you have higher prices. This is normal. And you have to take into consideration that we pay a commercial price for the guarantee of the Government. Therefore as I have already said at Q2, we were not expecting and are not expecting a significant cannibalisation from the introduction of the scheme. What we are expecting as I have said also at Q2 results is that there will be significant uplift in volumes. At a 75 or around LTV, adjusted LTV, with healthy margins at that level and therefore you can expect higher volumes at healthy margins. And I think, as I thought at the end of Q2, that the cannibalisation in part two will be small and will be much more offset by what I just told you.

So we are quite positive on the scheme. Early indications are quite positive and I will update you in more depth at the year end results.

Answer: George Culmer
Hi Chris, on CP5/13, as you know, when the paper came out August time, consultation was open until October 2nd. We are waiting, I think we are expecting to get, sort of, the PRA's response and finalisation probably I think about December time. Regarding the constituents, there are a number of items we think are genuinely open for consultation as you say. Some of the Pillar 2A stuff, 56 per cent or the 100 per cent. You have probably seen some of the responses go back. Just the overall treatment of pensions and whether that should be covered with gone concern capital or going concern type capital. From our perspective I can't give you a precise number mainly because the rules are you know, still to be written. I do think we are in a good position in a sort of absolute sense when you look at our capital ratios and our capital trajectory. I also think we are in a good position in a relative sense when you look at our risk composition and you look where we stand from a capital basis versus our peers. In terms of managing some of those risks, again we continue to

take action. Again coming back to pensions, and we will see where the treatments come out, but we have spent a lot of time or the Bank has spent a lot of time prior to my arrival in the last year and a half as well in terms of looking how we can match that and take risk out. And we have been active in that and will continue to be so.

So I can't, and I can't answer, you know, your question precisely and tell you where we expect to come out, but I do think we stand in good stead and we are in a good position to respond to what the PRA comes out with and I do think that their deliberations and the way they are heading suits the type of bank that we are constructing with that lower risk and the more certain profile. So I can't give you a precise number, we await feedback, but I am feeling good about where we stand.

Chris
Thanks very much, that's encouraging.

Question 2: Tom Rayner, Exane BNP Paribas
Good morning António, good morning George. A couple please. Just the first on the margin. I think your four year guidance points us to a Q4 margin of around 224, that is up around 30 basis points over the 12 month period, I am just wondering why George was guiding to stable margins into 2014? I was just trying to get a sense whether that is a deliberate decision to maybe add volume rather than generate further margin expansion, whether the competition is hotting up? Have you factored in any interest rate assumptions into that guidance? Could you add a bit of colour to that please and I have a second question on costs if that is okay?

Answer: George Culmer
Hi Tom, it's George here. Yes, as I said in the presentation, we expect it to be more stable. And you are right in the math, you come out in Q4 in terms of the sort of 220, you know, 223, that type of stuff, that is the sort of number. We will give formal, I think, guidance as part of our full-year results. At the moment that is just an indicative look at them, but we will give formal guidance in 2014 as part of our full-year. So we'll firm up on it then. But it is just about the trends we are seeing, so in terms of what has driven the margin forward in 2013 has predominantly been the liability repricing. But we are still seeing a bit of that, particularly again as I mentioned in the presentation in terms of the fixed term book which tends to reprice. And so we are still getting the benefit come through from that. A bit of mortgage headwinds although, you should note that the answer to that António gave a couple of moments ago in terms of overall margins and Help to Buy impact. But it is predominantly you will see a coming to the end of in terms of the liability pricing. And if we do end up with that level which I expect us to and that 220-223 type range, which is going to be where we set out to be in terms of our long-term strategic margin guidance. What then happens within the grouping and you are seeing this now in terms of Q3 again in terms of the core business returning to growth, it is sort of, this moves on to be about volumes and driving up NII, so I have now got the margin into the zone where I want it to be and it is now about fixing the focus to drive it to actually drive in those core volumes forward and you have seen all segments of the bank return to growth in Q3 with the mortgage book coming back. And going forward as we move into 2014 is the focus I think will be much more about driving forward net interest income if you like rather than just the focus on net interest margin.

Further question
Is there another angle there that if you do more volume there will be other associated revenues maybe from insurance sales etc, is that part of the thinking?

Answer: George Culmer
Well it certainly helps. There is no doubt, you know, and as you say, again the things we have talked about, it is a slightly tougher world in OOI and there is no doubt the more connections, the more relationships, as a sort of lead time indicator in terms of OOI potential is there, but it is a lead, pretty much a sort of lead indicator on that.

Answer: António Horta-Osório
And Tom to add a bit of colour within the segments so you that you have it clear. Our intention is, as we have always said, that we would start growing our mortgage book in net terms in Q3 after having reached the 100 per cent core loan to deposit ratio in Quarter 2 which we actually did exactly at the end of March. So this started to grow, the book started to grow in Q3 and you will continue to see it growing. But we want to grow our mortgage book as a whole in line with the market, with special emphasis as I have referred to Chris on first time buyers because we think that is a key segment

and because, as you just asked, we think those are the more loyal customers that drive a bigger share of wallet because they also need the insurance for the first time, you know home insurance, life insurance, current accounts. So those are the customers that have the most number of products per customer because they are buying their house for the first time. But as a whole our intention is to grow our mortgage book in net terms in line with the markets. Okay.

On the contrary on SMEs as we have been doing now for three years and on mid-corporates as we have been doing since the beginning of the year, we intend to continue growing our market share which was on SMEs, around 19 per cent three years ago when we now estimate to be around 21 per cent, so we have room. If you consider that post TSB we have 25 per cent of the UK retail market in terms of current accounts, mortgages and savings. In SMEs we can continue to grow from 21 to 25 we have a lot of room. And also as George mentioned, a lot in OOI as we develop transaction banking in the commercial bank. And we continue to increase, which has been done very well, our capital markets activities in terms of debt issuance and provision of swaps in terms of foreign exchange risk and in terms of interest rate risk. So that is going quite well.

And in terms of mid corporates, where we have around 20 per cent of the market, we also want to grow and potentially continue towards the 25 per cent level as well. So you can expect us in summary, to grow with the markets in mortgages with the special emphasis on first time buyers. And to continue to grow in SMEs as for the last three years and in mid corporates from the beginning of the year, to continue to grow those two segments on a sustainable basis in spite of having the markets falling between 3 and 4 per cent on those two segments year on year as per the BoE numbers.

Further question

And just on costs, the full year guidance £9.6 billion is not changed. Am I right, is there, have you absorbed more sort of one-off type costs such as a higher bank levy and maybe some of the deposit compensation scheme in there therefore the underlying is a little bit better or was that very much part of the original guidance? Because I am trying to get a sense of what you might now tell us 2014 could look like obviously ex-TSB costs, what you think the number should or cost income if not the actual number?

Answer: George Culmer

Yeah, the £9.6 billion as you have said, we have been a constant with that I think since about Q1 we first put that out there. Yeah within Q4 the bank levy will be whatever it is £230-240 million. Might be a bit north of that. FSCS will be in that number as well. No I don't, I haven't seen a huge shift in the underlying trends. So I don't think I would revise my one-offs if you like. So I am not seeing a shift between one-offs and underlying. So I think actually the outlook or the composition of that £9.6 billion hasn't changed materially certainly since the half year, Tom.

Further question

And any sort of steer on what is going into 2014 on the cost side. We have talked £9.15 billion I think before?

Answer: George Culmer

Yeah I mean that stays and that includes a Verde element within that. So, I think that, as I say, we are not giving guidance for 2014 today, but that remains out there.

Question 3: Raul Sinha, JP Morgan

Morning António, morning George. Can I have two please? Firstly on your asset quality outlook. Given that you are near the bottom end of your normalised range at 51 basis points already. Is there anything we should be aware about that is not helping you take the asset quality ratio lower going forward? Is there anything that we should be aware about pointing in the other direction or should we just continue to see that go lower going forward?

And then I have got a second one on PPI if I can?

Answer: António Horta-Osório

Okay, let me answer yours first on AQR Raul. I think that is a fair question. As George said on other matters, I mean we are not revising other aspects of our guidance today, so we will wait for the year end. But what's happening in terms of colour to let you know what is happening is the following. So as we have commented every quarter since the beginning of the year, we continue to see the UK's economic recovery where if you remember, we were always quite firm in saying that it would be the economy would progressively recover. But we also said it would be long and difficult. We have seen since the beginning of the year an increase in both the breadth and intensity of the economic recovery. So I do think that now GDP expectations, sorry GDP outcome at the end of the year in my opinion will be very close to the high end of expectations. So I do expect GDP to grow around 1.5 per cent this year. And more next year towards the 2.5 per cent. So we are seeing, because when you asked in the beginning of the year I said the expectations were between half and one per cent and I was more on the upper side. So I now believe it will be close to 1.5 per cent.

And to go to the colour on your question. When we look segment by segment, we see apart from a substantial reduction in non-core as George referred, on the core book which is the critical one in terms of trend going forward, we see not only the same trends that we saw at Quarter 2, but we saw an improvement in those trends which I believe reinforces this idea I am telling you that the economic recovery is taking steam. And now we have all segments in our core book, so mortgages, which were flat and now are slightly down, UPL has continued to go down, SMEs, mid corporates all segments are either stable or going down which is very reassuring from an asset quality perspective. And I think we have already said that we don't see a difference in terms of the yearly trend going forward. But this is not the moment for us to review AQR guidance for next year.

Further question

I suspect the question really is if your economic outlook is correct and which is clearly consensus as well, then shouldn't we be at a point where you are starting to see some write-backs in portfolios where you have taken big charges? Is that something that is starting to crop up in parts of your portfolio yet?

Answer: António Horta-Osório

No I wouldn't say so Raul, what I would say is that exactly, as the economic recovery will continue to improve, I think you have to separate the analysis of us in two parts. On the non-core bank which we now basically completed the main pillar of our June 2011 strategic review of the refocusing. So we are now in nine countries and we will be at year end at £26 billion. So we have now at £30 billion of non-core, non-retail assets which is less than 5 per cent of our banking balance sheet. So that is basically not significant any more. We will continue as we said to provide you granular information on these portfolios going forward. But after the end of the year they do not deserve, if you want, the non-core reporting because they are quite small. So we have finished that refocusing in terms of UK focus and non-core exits. And on those you can expect that a better UK economic recovery will lead to a continued good progress on those as we have been doing. We have been selling much more than we had thought would have been possible in a capital accretive way, which is the difficult part, because it is very easy to sell but it is much more difficult to sell when you generate significant amounts of capital at the same time. And as George referred to you, we have already generated to the nine month, £2 billion of capital in the non-core reductions which was more than the total of last year, £1.6 billion during last year. So on those ones you can expect a continued good performance as I told you by the end of next year there will be no more than £15 billion. So less than 2 per cent of the balance sheet.

And on the core book, which is the trend going forward I think you can expect lower AQR than in the past and I think we have said already at Q2 that while the strategic review we had said 50 to 60 basis points for the Group as a whole in the medium term with the core around 50, I think we have already said, as per track record so far that the core bank will be below that. But we will prepare next year the new strategic plan and we will announce the revised metrics and guidance at the end of next year as we announce the new '15-'17 plan. And we don't want to revise it now. But the trends are clear and more than clear as you ask, they are robust because they are across all core segments and they are accelerating as the economic recovery gets more steam.

Further question

Just a second one I had, probably, maybe for George, is on Slide 12, on the PPI data that you very helpfully show us. There is this one point of concern George I had on that. I mean that slide the top one shows you complaint volumes are down 48 per cent since Q4 2012, but over the same period your average PPI costs are broadly flat even when you

exclude the one-off costs. And I suspect some of that is the acceleration of the cases pending at the Ombudsman, but my understanding was quite low. So I wonder if you can give us some comfort around why the sort of quarterly run-rate at £600 million you know wouldn't continue at these levels even though you are seeing complaint volumes go down?

Answer: George Culmer
Yeah you are right. There is a sort of diversion. I talk about, I can talk about what is going on with complaint levels and talk about the cost and why you get slightly different trends on those. And again we have increased the provision because while that complaints are down, the 8 per cent is slightly lower than we were projecting. We were projecting something closer to what we had seen in previous quarters. In terms of reasons for that, we know at the moment there is, and this partly links into your question as well, there is a lot of past business review activity going on at the moment, not just at Lloyds but in other banks. So we know there is an awful lot of cash payments being made in regards PPI across the UK as a whole at the moment. I think the FCA got some data out a few weeks back now which showed actually that the level I think last quarter's cash payments was as high as when PPI inbound complaints were at their peak. So you will see an awful lot of cheques and the basic things in terms of behaviour that actually the receipt of cash causes complaints if you like. And that, we think that is one of the things where we see a slight slowing down of the inbound complaints. Interestingly it is just since quarter end that actually we have seen, I think we talk about 11,000, since quarter end we have seen a significant reduction over the last two or three weeks down to about 8,500 type levels, almost a 20 per cent reduction now. It is too early to say you know that that's trend etc. But it is just interesting how variable it can be.

Part of it though, to your question, and part of it just talking there, part of the divergence between complaints and cash going out. And within the cash going out you have obviously got a fixed rump of the expense base that goes through and you have also got a lot of remediation and you have got increased levels of past book reviews. So the top chart, so the inbound if you like reactive complaints, what we pick up in the bottom chart as well is, a) the sort of general expenses of the business, and a large amount of the sort of proactive, the PBR type activity.

Now since the half year, at the half year we talked about being about sort of half way through that PBR activity, what has actually happened since then is actually we have increased the scope of that so I think we had about two and a half million, that is now up to about 2.9 million in terms of just, we increased the scope. We are now about half way through that expanded scope. We will be about 62 to 63 per cent on the old basis, but it is now about 50 per cent. And it is that past book activity and the costs as well as things like payment pulling forward, dealing with some of the FOS cases. That is why you have a divergence. Ultimately of course Raul, those costs should trend down and that is what we are looking for and you will see those costs follow what we see in terms of the reactive complaints as we get through the PBR activity which we expect to finish round about sort of Q1 of next year.

Raul
That is very helpful. Thanks very much.

Question 4: Andrew Coombs, Citi Group
Good morning. I have one follow-up question on PPI please and then two further questions, one on pensions and one on dividend. Firstly on PPI. You mention that the response rate has been higher than forecast and thank you for your comments in response to the previous question. Perhaps you could literally just update us on the expected response rate assumption you are now assuming? I think it was 27 per cent in June. I would be interested to know how that has increased?

Answer: George Culmer
27 is now more like about 33 per cent is what we are assuming in terms of what we have noted to date. So the 27 has gone to about 33.

Further question
Thank you. And then on the pension. I just have a quick question with regards to the pension revaluation that has been taken to the OCI. Perhaps you could elaborate on exactly what the cause of that is please?

Answer: George Culmer

Oh, it is just the quarterly valuation, Andrew and yeah it is interesting. It remains as a sort of you know emerging volatile item from a financial reporting basis. And what you predominantly see move over the year is the discount rate. So we came in the year with a discount rate of around about 4.6 per cent. By the half year that had moved up to about, I think it was approaching about 4.9 per cent. And that gave us a sort of benefit that comes through as at Q3 which is back down to about the 4.6 per cent. And it is that that drives the impact that you have seen in Q3 which is about an £800 million negative impact to the net asset position. So it is the discount rate fluctuations which I am afraid it is just a consequence of how you quarterly value your 50 year liability of the stuff, you know. It is how the accounting works. And it will move around and it will fluctuate and it will cause volatility. What matters I think going right back to Chris's question to start with, when you look at the economics, we have done a lot of the stuff of economically matching the pension scheme in terms of taking out risk, longevity rates, equities etc. And that is what really matters. But from an accounting perspective you will continue to get this volatility I am afraid.

Further question

Okay, that is very clear. And then just finally on the dividends. We talked about CP5/13 at the start and obviously we should have a bit more clarity there in December. But given that we are not going to get the methodology for the Bank of England's stress test until March or April of next year, I was just wondering how much of a hindrance that is to you when you are deciding on a dividend policy for this year?

Answer: George Culmer

It is good question, the thing is there is always another test isn't there. I think by the end, what happens at the moment, as we have said, we have initiated discussions. You know they have started well, all of those sorts of things. I think the discussions will go up a notch as you move towards the back end of this year because we can drop in our plans etc. We can show an update of those. Alongside those plans we do actually carry out our own stress test with that. And we will submit that to the PRA as well. So we will have as we move into November/December our updated financials, our stress testing of those financials. And probably as you would expect, given what happened this year, particularly, you know, with the particular stress testing that occurred in the first six months of this year, you know the PRA knows our portfolio pretty well and I certainly don't see that we will have to wait for another stress test. We are feeling you know, I can't pre-judge and I won't pre-judge the outcome to those discussions, but we feel in a good position, you have seen our capital numbers today. I think they are good. In an absolute sense they are good in a relative sense in terms of where we have come from over the year. And I think they are good in a relative sense in terms of how we compare with a number of our peers, a number of whom are obviously already paying dividends. So, you know, I won't pre-judge the outcome, but you know we feel we are in a good position.

Andrew

Thank you very much.

Question 5: Claire Kane, RBC

Hi there. Can I get a question please on the movements kind of in the equity base in the quarter. I think you followed up and you said it's £800 million negative from the pension. So, I think the equity has gone down by £2.5 billion. But common equity Tier 1 capital is only about £1.5 billion. So is the difference mainly related to the DTA? Can you give us what the updated balance of the DTA, I think £5.6 billion at the end of June, please?

And then my second question, just to follow-up on the PPI, of the kind of £1.6 billion net reserve or £1.7 billion, sorry. How much of that have you got in for admin expenses? And given the reduction in complaint volumes, could you start to see the kind of team you have working on that start to go down and the admin costs to go down? Thanks.

Answer: George Culmer

Hi Claire, it is George here. Yeah the DTA remains about the sort of £6 billion or so number. We saw some utilisation, but things like pension scheme we would add to that as well. So it's around about the £6 billion. In terms of sort of net assets and what is going on in terms of net assets, and you're right, there was a movement, significant movement in quarter. You know as I think we sort of call out in terms of the front sheet what that related to was a number of things. First up, obviously we have got the asset sale losses in quarter which are round about £600 million, but the point we would make here quite strongly is those asset sales which are led by Heidelberger Leben, which has come through, but

we have also had a reduction in shipping go through, also had some reduction in CRE. All those disposals basically serve to move us to a better position with regards to balance sheet. And you see that tangibly in terms of how they actually add to the capital accretion from our capital ratio. So if you like, we sort of take a P&L hit which goes to the NAV but it is at a cost of actually building the capital base of the business. And obviously also improving the financial strength of the business as well.

There are a couple of associated things as well. We talked about again, these are related to the disposals that we are taking whilst the Australian deal hasn't completed, we wrote off £350 million with regard to deferred tax assets that is directly related to that transaction, which again impacts the net assets. And then on top of that obviously you have also got continued spend on simplification, continued spend on Verde that will come through. You know, as we move forward, what would I expect to see? I think the £600 million in quarter on asset sales is an exceptional amount, I would expect to see that come down significantly, but also as Antonio was saying earlier, as we run down the size, the quantum of that book, I would therefore expect to see, as we look to manage it differently and more optimise value, smaller drags into P&L drags in terms of asset sales. Simplification and Verde simplification, I would expect probably something like another couple of hundred million I think for the rest of this year and then I think that will leave us with about £600 million to come next year. Verde is about £100 million of build costs and there is a bit of build costs next year. There will also, with Verde, as we move towards a deal, there will be some IPO costs that sit just transaction costs, that sit on top of that. And we will also for a while have some duplicate costs of carry. We have the business and we are just awaiting IPO and there is some duplication, but also we will be earning the income at that point on that.

So I hope that sort of helped you in terms of what has happened on the net assets and the size for tax. And PPI, sorry I forgot, oh PPI, sorry, I got carried away.

PPI, potential, it is around about 20 per cent. And you're dead right, in terms of the £1.7 billion on our new slide. About 20 per cent will cover costs. And you're dead right in terms of as we come the run-down we should be able to free up those costs and there should be a benefit to come through that. That is absolutely correct. And a lot of the costs as you would expect, you know a lot of the 6,000 people that are actually working on PPI, a lot of that is contracted out, which gives us obviously a variability in terms of that cost base.

Further question:
Could I get maybe one follow-up on the capital movement in the quarter? I would have assumed that the DTA coming down would have been the difference between why the capital base on a regulatory sector did not reduce as much as the statutory equity base. You do mention slide 14 changes deductions for excess expected loss and AFS reserve, is that what is boosting that line up versus the equity base?

Answer:
AFS reserves should be going through both the equity base and the capital base so that shouldn't be a particular difference. EEL is obviously a capital solo and that won't impact. So that will be a differential between capital base and equity base.

Claire
Okay, thanks.

Question 6: Jason Napier, Deutsche Bank
Morning to you both, just two quick ones if I might. The first, deposit performance in the core bank quarter on quarter, the balance is only up about half a per cent. And there has been some talk in the market of a slightly more aggressive stance from yourselves in the market for term deposits which is obviously somewhat in contrast to what Governor Carney is saying on liquidity requirements and is also in contrast to your own targets on LDR. I just wondered you know deposits have clearly been a source of upside and margin hitherto, is there any sort of reason why you would be looking to be more or less aggressive in the term market? Do you recognise that as a comment? And where do you see flow pricing for deposits now versus where the book is? If you could give us just a rough sense of the next, I don't know, 30 bps or so that would be really helpful?

Answer: António Horta-Osório

Jason good morning, this is António, I will answer that first question. That is a comment, to be very frank with you, I have heard before but which I don't really think reflects at all our strategy. And let me explain why. I mean first because everything you said is right. And second because we follow a multi-brand strategy and also multi-channel and so it's quite difficult I believe for our competitors to really understand our deposit strategy because you have to see it as a whole. And what we are doing is exactly the same that we have been doing. We've a caveat and that is why, as you said, our deposits on the core bank increased slightly only in the last quarter, which is as we reach 100 per cent core loan to deposit ratio in March, we then started as I think I have said before in other IMS presentations, we have started to manage all deposits in the bank mostly on value, except the relationship deposits. So the three brands. The three core brands, the Bank of Scotland, Halifax and Lloyds, which I think that approach has to be managed also in the context of market share, because retail as loyal customers have to be treated as customers. And therefore we have market share considerations.

So to summarise, given that we have now 100 per cent core loan to deposit ratio, we will continue to increase deposits to the extent that we increase core loans. Core loans are accelerating because we have accelerated SMEs and mid corps. But we have also returned mortgages to growth and therefore you will see deposits growing accordingly because we will keep the restriction of 100 per cent core loan to deposit ratio. It has been and it is continuing to be as we go through October, quite easy to attract deposits in the UK, at least for us, because as you know, deposits in the UK keep growing as people continue to deleverage in percentage terms. And therefore although they are spending more and the economic recovery is improving. In percentage terms, deposits, they save a bit more and deposits are continuing to grow. And in terms of that aggressive thing you mentioned, which I have as I told you, heard before, I don't think that has any type of substance. We do not need to do it as you just heard. Deposits are flowing very well and I don't see and I am sure you will not see, any type of difference in our strategy. We do use our non retail franchise brands like you know, Birmingham Midshires and others tactically and we do use the retail brands on a strategic sense and you will continue to see this in terms of multi-brand, multi-channel which as I said from the start since June '11 I think is a key core competitive advantage of positioning in the UK especially in the context of low interest rates because it enables us to satisfy different customer preferences in terms of brands, channel and other types of criteria, while at the same time maximising in my opinion the way that we manage the margin of the assets minus the margin of the liabilities.

Further question

Thank you. That's helpful. Certainly if we can't have a rational deposit market now as everyone having hit their LDR targets, the hopes for ever getting one are probably.... The second question that I had was regrettably sort of on below the line costs and we have sort of attacked PPI admin costs in a number of different ways in various questions. But you know, if you have got 6,000 outsourced folks you know you are basically looking at annual costs, if that's everything, of over £100.000 each and if I look at that and the cost of getting Verde done, I just wonder in terms of governance and accounting and so on, can we really draw a line through these things post Verde IPO, that is all gone, plus PPI, that it's all gone or is there a decent chunk of sort of in-house and expertise and effort going on in these things? I would have imagined there must be a decent chunk of these sorts of costs relating to folks that will stay on with the Group? Thank you.

Answer: George Culmer

Jason I mean you know the 6,000 as regards PPI and I think the figure you quoted for costs is significantly higher than the actual. But when you look at, the general question as well, if I look at below the line items which ones are going to be with me for life and which ones will drop away? I mean, you know Verde, will drop away, simplification expires 2014 and as I said, I think we have an extra about 200 [million] this year, 600, then we are through on that one. You know, PPI, you know of course it's frustrating to put up extra sums, extra monies each quarter. But the thing we would point to is that you know complaints do continue to track down and perhaps not at the rate that we wanted or projected but they are coming down. And as I said, interestingly they have come down quite significantly since the end of the quarter. So I wish I could give you an end date on that and all those sorts of things, but at least the trend is down. But I certainly see when you, when you look at you know the trends below the line, Verde will go, Simplification will finish, PPI will end. Asset sales as we were just talking about, we have completed the fundamental restructuring of the balance sheet, we have taken the big lumps, you know there was a larger than usual charge in Q3 but that was led by Heidelberger Leben which was a dead right deal to do, but as we move down to, more to optimisation, I would expect there would be some losses to be a lower quantum. So yes they have been a feature of the results this time, but I do expect them to fall away.

Question 7: Chintan Joshi, Nomura

Hi good morning. I have got two questions. The first one on the NII. If I look at your deposit margin, asset margin breakdown, it looks like deposit margins have increased in pace, improvement has increased in pace this quarter. Last quarter you were at 16 bps, this quarter 28 bps. But equally asset margin pressures have increased. Could you give us some colour into kind of the driver how on both sides at the half year stage you were kind of saying that the pace of deposit improvements should fall off but actually it has accelerated and asset margins have tended to be quite resilient. We have seen about a 5 bps deterioration. Some comments on both those would be helpful?

Answer: António Horta-Osório

Okay, look I will take that, answer that first question. I mean, I think you are absolutely right on what you say when you look at the slides, that you have to take into consideration that you have when you look at the slides you have the third quarter of '13 in but you also have the second quarter of 2012 out. So the fact that you have those different numbers in the comparison does not mean necessarily that there is a big change on the present situation. As I told to Jason, and I want to reiterate to you. Number one, what we really manage, as I said many times, is the difference in the margin between the asset side and the deposit side. Because given that the loan to deposit ratio in the UK is still higher than one, I think that is the right way to look at it, because for each pound of loans that we give, we need one pound of deposit to fund it, especially when we do as I think we do, we have a target of a core loan to deposit ratio of 100 per cent. So the right thing to manage is the difference of the two margins. And as I told to Jason as well, I think the trends in terms of deposits are exactly the ones I said to Jason. We have to understand, we have a multi-brand, multi-channel strategy which may look sometimes difficult to understand from the outside, but I think that is a key competitive advantage of our UK positioning. And on the asset side as I said to Chris in the beginning, although obviously when asset margins come down on mortgages, you have a higher risk of some cannibalisation because the prices are very low for SVR customers are relatively more attractive. I think the way the Help to Buy Scheme is priced, number one, and the fact that there were no loans available at above 80 per cent loan to value before, will mainly imply as you ask on your question, that we will do significantly higher volumes of 75 per cent adjusted LTV mortgages. We have quite attractive margins and we will substantially, that we will improve NII going forward and our story, our equity story going forward now that we have all of our core loan segments growing, is a story that will progressively shift from NIM which has been increasing throughout the year to a story of NII where you have to multiply NIM by increasing volumes over time on the core loan book.

But relating to your specific technical question, I can tell you that the present situation in terms of margins is very much in line with what I said at Quarter 2 and the difference of the two slides is more because you take away the second quarter of 2012 in your comparison.

Further question

I got that one. And the second question was kind of again a detailed question. If I look at your NIM your average interest-earning assets like back out non-banking and AIEA of about £100 million, is that direct calculation?

Answer: George Culmer

Sorry, what was the question again?

Further Question

If I look at your NIMs, if I look at your average interest-earning assets I can back out your non banking NII of about £100 million in the quarter, is that the right calculation? And also how should we think about that line going in the future?

Answer: George Culmer

Yes you can back out that amount, but I don't see that there will be any material shift in that going forward. So we will get, we will give you a ring if that's any different, okay, but I don't see there will be any shift in that. That's the right way to look at it and I don't see any material shift in going forwards. But if it is different from that we will get back to you.

Chintan Joshi

Okay, thank you.

Question 8: Arturo de Frias, Santander

Hi, good morning. May I ask you for volume growth next year? I think you have repeated it already twice in this call. But/that the story in 2014 is going to change from NIM improvement into NII improvement based on volumes. Can I, can I ask you specifically what, what kind of, I mean which of the different areas of lending mortgages or corporates or SMEs you think can give the positive surprise into 2014?

And also on the cost side, I know you have mentioned that you didn't want to give a guidance into 2014. Can I ask you in terms of cost/income ratios? Because a number of questions during the call have been mentioning reductions in costs coming from PPI management, coming from Verde, coming from a number of cost areas. So I think we should all expect substantial improvement in cost/income ratios in 2014. Thank you.

Answer: António Horta-Osório

Right. Thank you very much Arturo. So let me tell you something about those two questions. On the first one, I mean just to be very precise, I haven't said exactly that the story would change from NIM into volumes. What I said is that you should change the focus from NIM into NII which is a multiplication of NIM versus volumes, to be very precise. And I think it is important. And in terms of the volume specific part of the NII, the way I see it is quite simple. So I see mortgage growth in net terms raising from the 0.7 per cent of the latest Bank of England's Report on a 12-month basis. I think it will grow into the 2 to 3 per cent in the next 12 to 24 months, just an expectation because as I told you many times, I mean as I have said many times Arturo, what is important for us is to be right on the direction. And the intensity we will adjust along the way. So it will be up, it will clearly be up, we can see that through increased confidence in the Help to Buy Scheme. I think it will logically be up by 2 to 3 per cent in the next 18 months or 12 to 24 months. We want to grow as I said before within the market, in line with the market. So whatever the market grows we will be, will try to replicate the market so keep our mortgage market share around the 25 per cent level which is our natural market share in the retail UK market with an emphasis on first time buyers. So you can expect probably bigger market share in first time buyers, as I said before. But overall growing in line with the markets.

On the other segments, UPLs which is a focus of our retail division, as I said, during the year, in preparation of activity for next year in UPLs in credit cards, I think you can expect an inflexion both in the market and in ourselves where we see the volumes of the whole to stop falling and increasing slightly. And we want to increase our UPLs and credit card volumes as well. And more than the markets. Because while we have a 25 per cent market share post TSB, in current accounts, mortgages and savings, we have only around half that market share when you consider the unsecured market as a whole and the credit card markets. So you can expect us to progressively increase volumes next year and to start increasing more than the markets.

In terms of SMEs where we are growing 5 per cent in net terms and as per Bank of England numbers the market is falling 3 per cent, this 8 per cent difference versus the market, which, if you exclude us from the market we are 21 per cent of the market, is like a 10 per cent over-performance, outperformance of the market. I don't want to increase more than 10 per cent of the market. I think that the SME net lending growth of the market will progressively improve as the Funding for Lending Scheme gets through in SMEs and corporates, it takes longer than in mortgages. And I think the minus 3, which is the Bank of England number, will progressively be less negative by year end and probably positive some time next year. And you can expect us continue outperform the market but I don't want to increase the difference versus the market in terms of prudence of our approach and in terms of all considerations in the round. So you can expect us to continue to increase by at least 5 per cent and keeping a significance difference versus the market.

Where I think you will see another shift in our performance is in terms of the mid corporates sector where we started increasing in the beginning of the year and we are gaining momentum. And again while the Bank of England number is minus 4 per cent and we are positive, I think the minus 4 which will trend to better numbers as the economic recovery improves and we will also accelerate our growth. And so I think this covers all the segments.

So you can expect in summary our core loan growth to continue to accelerate and when you see the report of the first, of the Funding for Lending Scheme of Q3 which the Bank of England will report in the beginning of December, you will see exactly the numbers that can substantiate that.

Answer: George Culmer
And on costs Arturo, just, sorry we do have guidance for 2014, which is the 9.15 [billion], the earlier comment was whether we were updating it or providing it. So no, we will stick with existing guidance and we will update at the end of the year as required. But just, and then just in terms of how the numbers flow through, I mean, this is just in terms of how we present and cut the numbers, but as we stop, going back to Jason's question, we stop the below the line items, the PPIs, the simplification, they don't go into the cost/income ratio per se, because those are exceptional, one-offs. So the cessation of those activities which will come, doesn't flow directly into the cost/income ratio.

Answer: António Horta-Osório
Yes. That is a good point. We, I mean, as you know, we have given a guidance of 9150 for next year, I just want to remind you that the reason why it's a very strange number, 9150 is because it's basically £9 billion plus Verde and we were assuming in Q2 as we are assuming now, that the Verde IPO will be around mid year. So if we have Verde more time or less time, you will have more costs or less costs. But as George mentioned, we will also have more or less revenues of Verde. So it's a cost/income equation to, you were asking but our guidance is aggressive the same which is around £9 billion for ex-TSB, assuming TSB mid-year is 9150. As you correctly pointed out, our key strategic target is the cost to income and we do believe, that's why we have been giving guidance all the way through up to now, we do believe that on the first stages of the strategic plan you always have to focus on costs because as you lower the nominal costs, through the simplification of the bank from the customer's point of view, you create the competitive advantage in terms of cost to income that will progressively enable us to offer better value for money for customers and therefore to increase on a positive and healthy way our market share and share of wallet in all the segments where we are under-represented and this means you know insurance, we have 11 per cent, credit cards/UPLs we have around 15 as I said before, asset management sub 10. OOI of SMEs in transaction banking, debt capital markets, foreign exchange hedging etc. We are very small, so all of those will progressively increase based on what I think is the right policy which is sharing the cost savings of Simplification between customers and the investors.

And therefore as you, as you asked me, our cost to income ratio will continue to improve. As I said in my initial remarks, we are now already at the best of the main UK banks, with the 52 per cent excluding the SJP impact, while the sector is between 56 and 65. And I do believe, just to give you an idea, that our cost to income ratio will trend towards the 45 per cent level as interest rates start to normalise and will reach around the 2.5 per cent level. So just to be precise, normal interest rates in the UK context are probably interest rates around 4 per cent. As long as they reach around 2.5 per cent our cost to income should trend to around 45 per cent. If they normalise to 4 per cent it will trend lower, okay.

Further question
Thank you very much. That was extremely helpful. Can I ask you a very quick follow-on? Do you think you can still outgrow the SME UK market by 10 points next year?

Answer: António Horta-Osório
Good question. I am not sure about that Arturo, in the first steps the 10 per cent was an illustration to you of how much we are outperforming the market. But I do think that our growth to SMEs next year will be higher than this year. So more than the 5 per cent. Depending on how much the market improves and in which specific sub-segments it improves we will respond accordingly and again I don't want to be too precise on intensity. But for me it is very clear that the UK economic recovery is gathering pace and is spreading throughout the UK not only London and the South-East, point one.

Point two, I think SME net lending to the country as a whole will improve from the minus 3, as per latest Bank of England number, and therefore we will also increase our pace, if it will be 10 per cent or slightly less I don't know, but it will be more and I think it is very clear that economic recovery is gathering pace.

Arturo
Thank you very much.

End of Q&A