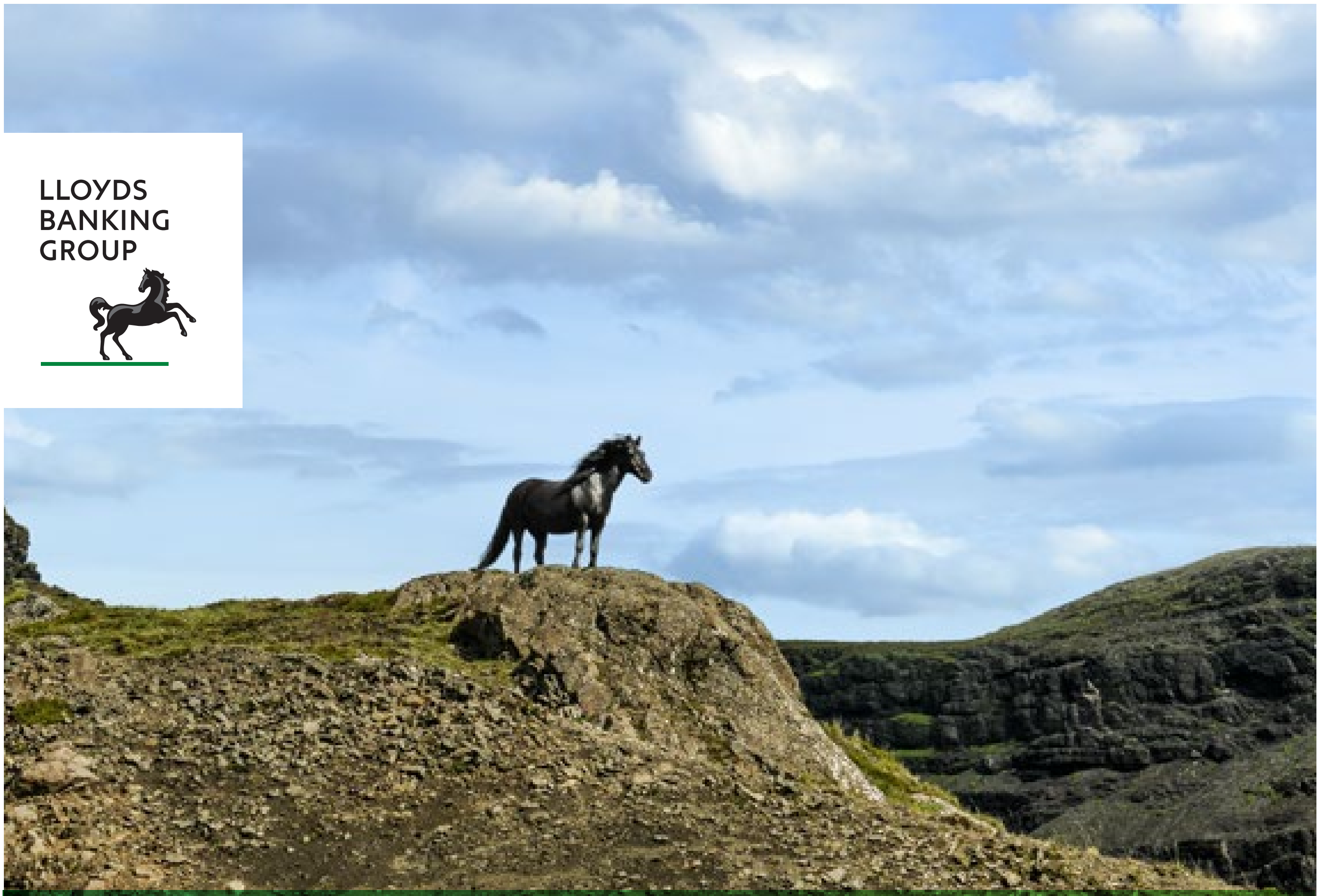
LLOYDS
BANKING
GROUP



HELPING BRITAIN PROSPER

Lloyds Banking Group
Capital and Risk Management Pillar 3 Report

2016

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Forward looking statements

This document contains certain forward looking statements with respect to the business, strategy and plans of Lloyds Banking Group and its current goals and expectations relating to its future financial condition and performance. Statements that are not historical facts, including statements about Lloyds Banking Group's or its directors' and/or management's beliefs and expectations, are forward looking statements. Words such as 'believes', 'anticipates', 'estimates', 'expects', 'intends', 'aims', 'potential', 'will', 'would', 'could', 'considered', 'likely', 'estimate' and variations of these words and similar future or conditional expressions are intended to identify forward looking statements but are not the exclusive means of identifying such statements. By their nature, forward looking statements involve risk and uncertainty because they relate to events and depend upon circumstances that will or may occur in the future.

Examples of such forward looking statements include, but are not limited to: projections or expectations of the Group's future financial position including profit attributable to shareholders, provisions, economic profit, dividends, capital structure, portfolios, net interest margin, capital ratios, liquidity, risk-weighted assets (RWAs), expenditures or any other financial items or ratios; litigation, regulatory and governmental investigations; the Group's future financial performance; the level and extent of future impairments and write-downs; statements of plans, objectives or goals of Lloyds Banking Group or its management including in respect of statements about the future business and economic environments in the United Kingdom (UK) and elsewhere including, but not limited to, future trends in interest rates, foreign exchange rates, credit and equity market levels and demographic developments; statements about competition, regulation, disposals and consolidation or technological developments in the financial services industry; and statements of assumptions underlying such statements.

Factors that could cause actual business, strategy, plans and/or results (including but not limited to the payments of dividends) to differ materially from the plans, objectives, expectations, estimates and intentions expressed in such forward looking statements made by the Group or on its behalf include, but are not limited to: general economic and business conditions in the UK and internationally; market related trends and developments; fluctuations in interest rates (including low or negative rates), exchange rates, stock markets and currencies; the ability to access sufficient sources of capital, liquidity and funding when required; changes to the Group's credit ratings; the ability to derive cost savings and other benefits including, but without limitation as a result of any acquisitions, disposals and other strategic transactions; changing customer behaviour including consumer spending, saving and borrowing habits; changes to borrower or counterparty credit quality; instability in the global financial markets, including Eurozone instability, the exit by the UK from the European Union (EU) and the potential for one or more countries to exit the EU or the Eurozone and the impact of any sovereign credit rating downgrade or other sovereign financial issues; technological changes and risks to cyber security; natural, pandemic and other disasters, adverse weather and similar contingencies outside the Group's control; inadequate or failed internal or external processes or systems; acts of war, other acts of hostility, terrorist acts and responses to those acts, geopolitical, pandemic or other such events; changes in laws, regulations, accounting standards or taxation, including as a result of the exit by the UK from the EU, or a further possible referendum on Scottish independence; changes to regulatory capital or liquidity requirements and similar contingencies outside the Group's control; the policies, decisions and actions of governmental or regulatory authorities or courts in the UK, the EU, the United States (US) or elsewhere including the implementation and interpretation of key legislation and regulation; the ability to attract and retain senior management and other employees; requirements or limitations imposed on the Group as a result of HM Treasury's investment in the Group; actions or omissions by the Group's directors, management or employees including industrial action; changes to the Group's post-retirement defined benefit scheme obligations; the extent of any future impairment charges or write-downs caused by, but not limited to, depressed asset valuations, market disruptions and illiquid markets; the value and effectiveness of any credit protection purchased by the Group; the inability to hedge certain risks economically; the adequacy of loss reserves; the actions of competitors, including non-bank financial services, lending companies and digital innovators and disruptive technologies; and exposure to regulatory or competition scrutiny, legal, regulatory or competition proceedings, investigations or complaints. Please refer to the latest Annual Report on Form 20-F filed with the US Securities and Exchange Commission for a discussion of certain factors, together with examples of forward looking statements.

Lloyds Banking Group may also make or disclose written and/or oral forward looking statements in reports filed with or furnished to the US Securities and Exchange Commission, Lloyds Banking Group annual reviews, half-year announcements, proxy statements, offering circulars, prospectuses, press releases and other written materials and in oral statements made by the directors, officers or employees of Lloyds Banking Group to third parties, including financial analysts. Except as required by any applicable law or regulation, the forward looking statements contained in this document are made as of the date hereof, and Lloyds Banking Group expressly disclaims any obligation or undertaking to release publicly any updates or revisions to any forward looking statements contained in this document to reflect any change in Lloyds Banking Group's expectations with regard thereto or any change in events, conditions or circumstances on which any such statement is based.

Executive summary

COMMON EQUITY TIER 1 RATIO

2016	13.6% (13.8% pro forma)
2015	12.8% (13.0% pro forma)

COMMON EQUITY TIER 1 RATIO

During 2016 the Group continued to strengthen its capital position with a fully loaded common equity tier 1 (CET1) ratio, after accruing for foreseeable dividends, of 13.6 per cent and 13.8 per cent on a pro forma basis upon recognition of the dividend paid by the Insurance business in February 2017 in relation to its 2016 earnings (31 December 2015: 13.0 per cent pro forma).

The increase in the CET1 ratio reflects both strong underlying capital generation and a reduction in risk-weighted assets. The strong capital generation has enabled the payment of an increased ordinary dividend and the payment of a special dividend whilst fully covering the estimated CET1 capital impact of the announced acquisition of MBNA.

TOTAL CAPITAL RATIO

2016	21.4%
2015	21.5%

TOTAL CAPITAL RATIO

The Group's transitional total capital ratio reduced by 0.1 per cent, primarily reflecting managed reductions in tier 2 capital, largely due to calls and redemptions offset by the increase in CET1 capital and the reduction in risk-weighted assets.

LEVERAGE RATIO

2016	4.9% (5.0% pro forma)
2015	4.8% (4.8% pro forma)

LEVERAGE RATIO

The leverage ratio, after accruing for foreseeable dividends, increased from 4.8 per cent to 4.9 per cent (5.0% on a pro forma basis), largely reflecting the increase in tier 1 capital.

RISK-WEIGHTED ASSETS

2016	£215.5bn
2015	£222.7bn

FULLY LOADED RISK-WEIGHTED ASSETS

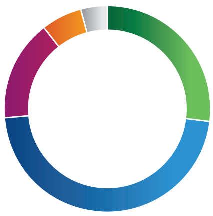
Risk-weighted assets reduced by 3 per cent, or £7.2bn to £215.5bn (2015: £222.7bn) most notably in the fourth quarter, largely relating to active portfolio management, disposals, an improvement in credit quality and capital efficient securitisation activity, offset by model updates related to the UK mortgage portfolio and foreign exchange movements reflecting the depreciation of Sterling.

SPLIT OF RISK-WEIGHTED ASSETS

Risk-weighted assets by risk type[1]

Credit risk (IRB) £147.7bn	(2015: £151.6bn)
Credit risk (SA) £19.0bn	(2015: £20.4bn)
CCR £9.6bn[2]	(2015: £10.2bn[2])
Market risk £3.1bn	(2015: £3.8bn)
Operational risk £25.3bn	(2015: £26.1bn)

Risk-weighted assets by division[1]



Retail £55.2bn	(2015: £54.6bn)
Commercial Banking £96.0bn	(2015: £103.2bn)
Consumer Finance £32.1bn	(2015: £30.7bn)
Central Items £12.9bn	(2015: £13.4bn)
Run-off £8.5bn	(2015: £10.2bn)

[1] Numbers do not include threshold risk-weighted assets.

[2] Counterparty credit risk includes contributions to the default fund of central counterparties and credit valuation adjustment risk.

The Group is a leading provider of financial services to individual and business customers in the UK.

The Group's approach to risk is founded on an effective control framework and a strong risk management culture which guides how our employees approach their work, the way they behave and the decisions they make.

The Group operates as a simple, low risk, Retail and Commercial bank with a culture founded on a prudent, through the economic cycle, appetite for risk.

The Retail business offers a broad range of products, including current accounts, savings and mortgages, to UK personal customers, including Wealth and small business customers.

The Commercial Banking business has been supporting British business for 250 years. It has a client led, capital efficient strategy, helping UK-based clients and international clients with a link to the UK.

The Consumer Finance business provides a range of products including motor finance, credit cards, and European mortgages and deposit taking, aiming to deliver sustainable growth within risk appetite.

Introduction

This document presents the consolidated Pillar 3 disclosures of Lloyds Banking Group plc ('the Group') as at 31 December 2016.

Pillar 3 requirements are set out under the Capital Requirements Directive & Regulation (CRD IV) and are designed to promote market discipline through the disclosure of key information around capital, risk exposures and risk management. The Group's year end disclosures comply with the requirements of CRD IV and associated European Banking Authority (EBA) guidelines and technical standards in force as at 31 December 2016.

In satisfaction of certain disclosure requirements, reference has been made to the 2016 Lloyds Banking Group plc Annual Report and Accounts (ARA). As such, this document should be read in conjunction with the Annual Report and Accounts, as highlighted throughout the remainder of the document.

In 2015 the Basel Committee on Banking Supervision published revised Pillar 3 disclosure requirements with the aim of improving the comparability and consistency of disclosures between banks and within the various disclosures made by individual banks. The EBA subsequently issued its finalised guidelines in December 2016 to ensure the harmonised and timely implementation of the Pillar 3 framework revisions within the European Union.

The EBA guidelines described above apply from 31 December 2017, except for institutions that, as at 1 January 2016, qualify as G-SIBs (in accordance with the Commission Implementing Regulation (EU) No 1030/2014). These institutions are encouraged to make every effort to comply with the guidelines from year-end 2016.

Although Lloyds Banking Group is not currently classed as a G-SIB, the Group has worked with other UK banks (via the British Banking Association working group) to adopt a forward-looking approach and has agreed with the Prudential Regulatory Authority (PRA) that they would early adopt a limited number of templates for December 2016 year end reporting. The templates that have been adopted include credit risk, counterparty credit risk and market risk type disclosures. A full listing of these early adopted templates can be found in Appendix 5.

In accordance with final EBA technical standards in relation to Article 440 (Capital Buffers), additional disclosures around the geographical distribution of credit exposures relevant for the calculation of the countercyclical capital buffer have been included.

RISK STATEMENT

A statement from the Board is included within the Governance section of the 2016 Lloyds Banking Group plc Annual Report and Accounts (page 67) that describes the Group's risk management arrangements as being sufficiently adequate with regard to the Group's profile and strategy. It states that the Audit Committee, in conjunction with the Board Risk Committee, concluded that the Group's risk management systems and internal controls were effective and adequate having regard to the Group's risk profile and strategy, and recommended that the Board approve them accordingly. A risk statement approved by the management body is included within the Risk Overview section of the 2016 Lloyds Banking Group Annual Report and Accounts (pages 26 to 31).

PILLAR 3 REQUIREMENTS NOT INCLUDED IN EITHER THE ANNUAL REPORT AND ACCOUNTS OR PILLAR 3 REPORT

G-SIB DISCLOSURE (to satisfy Article 441(1))

Although the Group is not currently classified as a Global Systemically Important Bank (G-SIB), by virtue of its leverage exposure measure exceeding €200bn, the Group is required to report G-SIB indicator metrics to the PRA. The Group's indicator metrics used within the 2016 Basel G-SIBs annual exercise will be disclosed from April 2017, and the results are expected to be made available by the Basel Committee later this year.

CAPITAL INSTRUMENTS DISCLOSURE (to satisfy Article 437(1)(b))

A description of the main features of CET1, AT1 and T2 instruments issued by the Group and its significant subsidiaries are included in a separate document on the Group's website located at **www.lloydsbankinggroup.com/investors/financial-performance/other-disclosures**

Disclosure policy

The following sets out a summary of the disclosure policy applied to the Lloyds Banking Group plc Pillar 3 disclosures, including the basis of preparation, frequency, media and location, verification and risk profile disclosure.

BASIS OF PREPARATION

This document contains the consolidated Pillar 3 disclosures of Lloyds Banking Group plc as at 31 December 2016, prepared in accordance with the requirements of Capital Requirements Regulation (CRR) Part 8 (Disclosure by Institutions) and associated EBA guidelines and technical standards in force at December 2016. A CRR mapping table has been included in Appendix 6, which details how the Group has complied with each article under Part 8.

A number of significant differences exist between accounting disclosures published in accordance with International Financial Reporting Standards (IFRS) and Pillar 3 disclosures published in accordance with prudential requirements, which prevent direct comparison in a number of areas. Of particular note are the differences surrounding scope of consolidation, the definition of credit risk exposure and the recognition, classification and valuation of capital securities.

Details on the scope of consolidation applied to the disclosures presented within this document are provided within the Scope of Consolidation section which follows.

Pursuant to the disclosure requirements under the Prudential Regulation Authority's Group Financial Support Instrument, and in accordance with the general principles set out in Articles 431-434 of the CRR, Lloyds Banking Group has not entered into any group financial support agreement.

Article 432 of the CRR on non-material, proprietary or confidential information permits institutions to omit one or more disclosures if the information provided by such a disclosure is not regarded as material. As the Group's portfolio of trading book securitisation positions is relatively small (£122m exposure, £17m risk-weighted assets) in the context of both the overall trading book and the Group's banking book securitisation positions, the Group has elected to provide only limited disclosure around its trading book securitisation positions as permitted by Article 432 and in accordance with related EBA guidelines.

The implementation of CRD IV is subject to transitional arrangements, with full implementation in the UK required by 1 January 2022 as per PRA policy statement PS7/13. Consequently, the Group's capital position is shown by applying both the transitional arrangements as implemented in the UK by PS7/13 (PRA transitional rules) and the end-point rules under PS7/13 (the 'fully loaded' basis). The minimum Pillar 1 capital requirements referred to in this document are calculated as 8 per cent of aggregated risk-weighted assets.

CRR requirements define credit risk exposures as the exposure at default (EAD), prior to the application of Credit Risk Mitigation (CRM) (Article 442). However, in accordance with the final EBA guidelines issued in December 2016, Tables 24-33 (on pages 57-66) and Table 37 (on page 71) have been presented on a post CRM basis. EAD is defined as the aggregate of drawn (on balance sheet) exposures, undrawn (off balance sheet) commitments and contingent liabilities, after application of credit conversion factors (CCF), and other relevant regulatory adjustments. Notable exceptions to this definition include securitisation positions, counterparty credit risk exposures and past due and impaired exposures. A summary, noting the definitions applied, is provided below.

Exposure type	Definition applied
Credit risk exposures (excluding securitisation positions)	EAD pre CRM[1,2]
Counterparty credit risk exposures	EAD post CRM
Securitisation positions	The aggregate of the Group's retained or purchased positions, excluding those positions rated below BB- or that are unrated and therefore deducted from capital.
Past due and impaired exposures	Accounting balance, defined in accordance with IFRS

[1] For credit risk exposures risk-weighted under the Standardised Approach, the EAD pre CRM value is stated net of specific credit risk adjustments (SCRAs). SCRAs relating to credit risk exposures risk-weighted under a relevant IRB Approach methodology are netted against expected losses as described on page 50.

[2] Unless otherwise stated.

FREQUENCY, MEDIA AND LOCATION

In accordance with Pillar 3 disclosure requirements the Group will continue to make available its full consolidated Pillar 3 disclosures on an annual basis. A standalone copy of these disclosures is located on the Lloyds Banking Group plc website (**www.lloydsbankinggroup.com/investors/financial-performance/other-disclosures**).

The EBA guidelines on Pillar 3 disclosure frequency that were formally adopted by the Group from October 2015, define key information that institutions in the EU banking sector should consider disclosing on a more frequent than annual basis under Pillar 3. The Group's assessment of these guidelines has resulted in the disclosure of specific capital and leverage information at the interim quarter ends with further detailed analysis provided at half-year.

VERIFICATION

The disclosures presented within this document are not required to be subjected to an external audit. Instead, the disclosures have been verified and approved through internal governance procedures in line with the Group's Pillar 3 Disclosure Policy, including the review and approval of the disclosures by the Group's Disclosure Committee and Audit Committee following the receipt of attestations in respect of both the quantitative and qualitative disclosures from Finance and Risk Directors at Divisional and Group level.

RISK PROFILE DISCLOSURE

In accordance with the requirements of CRR Part 8 (Disclosure by Institutions), the Group is required to assess whether its external disclosures taken as a whole (including the Group's News Release, Annual Report and Accounts and Pillar 3 disclosures) comprehensively portray its risk profile.

In this respect, the 2016 Lloyds Banking Group plc Annual Report and Accounts provides an in depth analysis of the principal risks and emerging risks to which the Group is exposed, together with further detail on the Group's key risk drivers.

The Group's Pillar 3 disclosures focus primarily on capital risk and the key risk drivers behind the Group's Pillar 1 capital requirements (credit, counterparty credit, market and operational risks), providing granular information and analysis in addition to that presented within the 2016 Lloyds Banking Group plc Annual Report and Accounts.

The relevant analysis is presented in the following sections of the 2016 Lloyds Banking Group plc Annual Report and Accounts:

– Risk overview, pages 26 to 31;
– Emerging risks, page 118;
– Risk drivers, page 123.

Scope of consolidation

The following information sets out the scope of consolidation applied to the disclosures presented within this document.

INTRODUCTION

As a banking conglomerate, Lloyds Banking Group is required to calculate consolidated capital requirements and consolidated capital resources based on the regulatory consolidation provisions applicable to banks under CRR (Part One, Title II, Chapter 2).

REGULATORY CONSOLIDATION

The scope of regulatory consolidation for the purposes of quantifying consolidated capital requirements and consolidated capital resources extends across the banking and investment operations of the Group. All banking and investment services related undertakings included within the scope of accounting consolidation are also included within the scope of regulatory consolidation. There are, however, a number of differences in the methods by which certain undertakings are consolidated for regulatory purposes.

Subsidiary undertakings included within the regulatory consolidation are fully consolidated, with capital resources determined on a line-by-line (accounting) consolidation basis. Capital requirements are determined either on a line-by-line (accounting) consolidation basis or by aggregating individual subsidiaries' risk capital requirements.

Undertakings in which the Group or its subsidiaries hold a 'participation', where it is deemed that the Group exerts significant influence over the undertaking, are generally consolidated within the regulatory calculations on a proportional (pro-rata) basis. This follows line-by-line (accounting) consolidation based on the ownership share in the particular undertaking. Such undertakings may include joint ventures and associates, as defined under IFRS accounting standards, and specified venture capital investments. In certain circumstances, participations are deducted from capital rather than proportionally consolidated.

Insurance undertakings are excluded from the calculation of consolidated capital requirements and consolidated capital resources. The Group's investments in insurance undertakings are instead subject to threshold rules under CRD IV that determine the extent to which the investments are deducted from capital with remaining amounts risk-weighted in accordance with the rules. The regulatory consolidation group diagram presented on page 6 highlights the key insurance undertakings of the Group that are excluded from the scope of regulatory consolidation.

The new Solvency II regime for insurers and insurance groups came into force from 1 January 2016. The capital requirements and the capital available to meet them are regularly estimated in order to ensure that capital insurance businesses are required to calculate solvency capital requirements and available capital on a risk-based approach. The minimum required capital must be maintained at all times throughout the year.

Investments held by the Group in respect of which it does not have the ability to exert significant influence are included within the calculation of capital requirements, being treated as equity exposures. The underlying assets of these investments are neither consolidated nor deducted.

Management practice and policy ensures that capital adequacy is maintained at all levels of banking and insurance consolidation within the Group in accordance with the appropriate regulatory requirements.

The legal and regulatory structure of the Group provides a capability for the prompt transfer of surplus capital resources over and above regulatory and internal risk appetite requirements or repayment of liabilities when due throughout the Group. There are no current or foreseeable material, practical or legal impediments to such transfers or repayments, other than the constraints imposed over the available capital resources of the Group's life assurance businesses.

SUBSIDIARY GROUP DISCLOSURES

Additional disclosures surrounding the consolidated capital resources, leverage exposures and capital requirements of Lloyds Bank plc ('Lloyds Bank Group') and Bank of Scotland plc ('BOS Group') have been provided within Appendix 3 and 4 to this document together with analysis of their credit risk exposures, credit risk mitigation and impairments. These disclosures are provided in fulfilment of the significant subsidiary disclosure requirements under CRR Article 13 (Application of disclosure requirements on a consolidated basis).

SOLO CONSOLIDATION

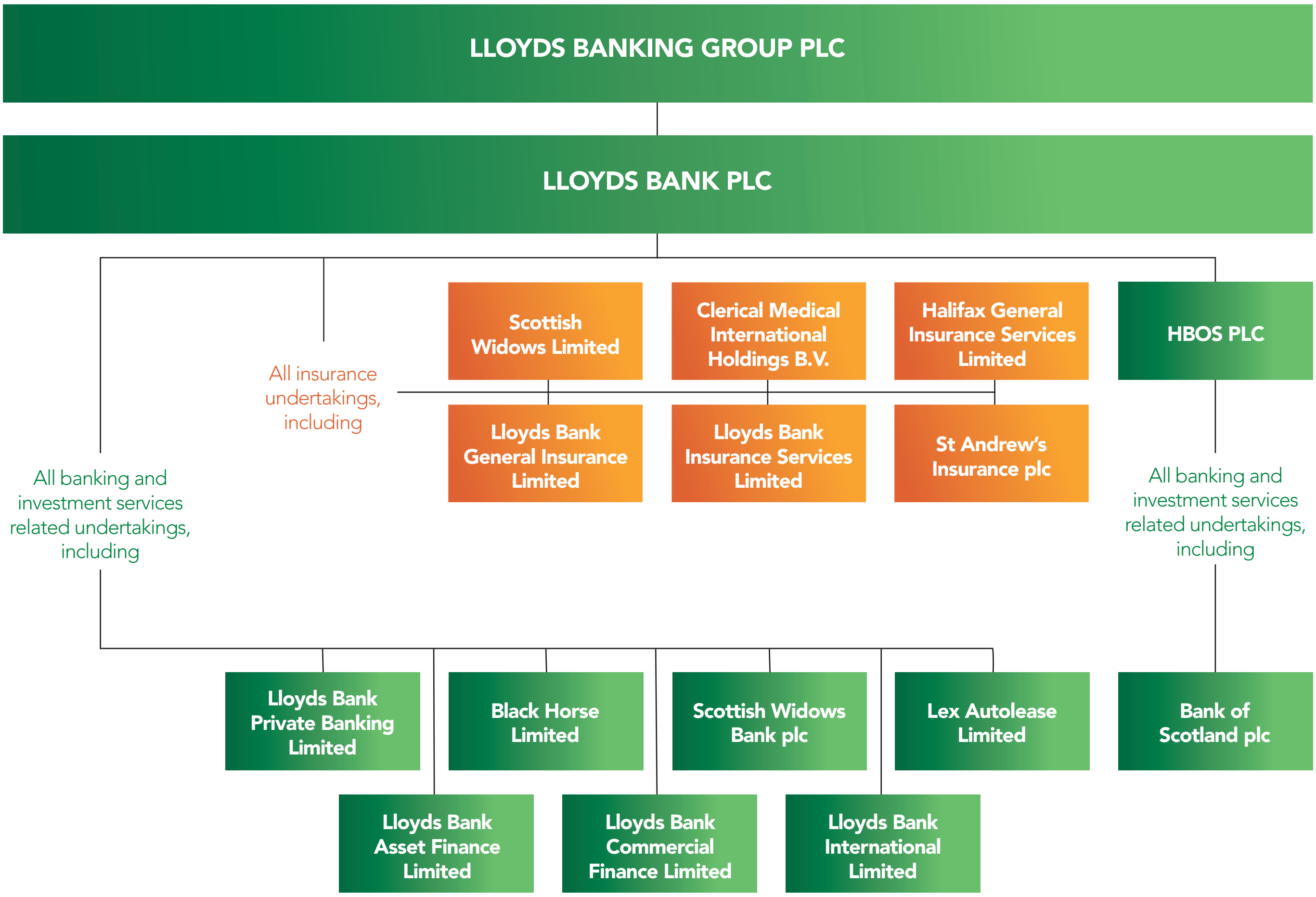
The Group makes use of the solo consolidation provisions set out under CRR (Part One Title II Chapter 1). This allows the capital resources and capital requirements of certain specified subsidiary undertakings of Lloyds Bank plc and Bank of Scotland plc to be included within the respective bank's individual capital resources and capital requirements calculations.

The application of solo consolidation provisions is subject to PRA approval and is performed in line with the terms established by the PRA for each individual bank.

Scope of consolidation continued

REGULATORY CONSOLIDATION GROUP

A summarised diagrammatical representation (as at 31 December 2016) of the regulatory consolidation group upon which the disclosures presented within this document are based is provided below.



KEY

Undertakings included within the Pillar 3 regulatory consolidation group

Undertakings excluded from the Pillar 3 regulatory consolidation group

CONSOLIDATED BALANCE SHEET UNDER THE REGULATORY SCOPE OF CONSOLIDATION

The following table provides a reconciliation of the Group's consolidated balance sheet as at 31 December 2016 on an accounting consolidation basis (as presented on pages 181 and 182 of the 2016 Lloyds Banking Group plc Annual Report and Accounts) to the Group's consolidated balance sheet under the regulatory scope of consolidation. It also breaks down how carrying values under the scope of regulatory consolidation are allocated to the different risk frameworks laid out in Part Three of the CRR.

Table 1: Differences between accounting and regulatory scopes of consolidation and mapping of financial statement categories with regulatory risk categories (LI1)

	2016						
	a	b	c	d	e	f	g
			Carrying values of items:				
	Carrying values as reported in published financial statements £m	Carrying values under regulatory scope of consolidation £m	Subject to credit risk framework £m	Subject to CCR framework £m	Subject to securitisation framework £m	Subject to market risk framework £m	Not subject to capital requirements or subject to deduction from capital £m
Assets							
Cash and balances at central banks	47,452	45,527	45,527	–	–	–	–
Items in the course of collection from banks	706	–	–	–	–	–	–
Trading and other financial assets at fair value through profit or loss	151,174	52,046	3,827	33,454	–	45,247	2,012
Derivative financial instruments	36,138	33,863	–	33,863	–	30,951	–
Loans and receivables:	488,257	461,069	435,097	13,581	11,813	–	578
Loans and advances to banks	26,902	7,469	4,642	2,827	–	–	–
Loans and advances to customers	457,958	449,705	427,138	10,754	11,813	–	–
Debt securities	3,397	3,895	3,317	–	–	–	578
Available-for-sale financial assets	56,524	58,395	55,049	–	3,346	–	–
Investment in group undertakings	–	7,999	3,416	–	–	–	4,583
Value of in-force business	5,042	–	–	–	–	–	–
Goodwill	2,016	194	–	–	–	–	194
Other intangible assets	1,681	1,520	–	–	–	–	1,520
Property, plant and equipment	12,972	9,294	9,294	–	–	–	–
Current tax recoverable	28	28	28	–	–	–	–
Deferred tax assets	2,706	3,645	984	–	–	–	2,661
Retirement benefit assets	342	342	–	–	–	–	342
Other assets	12,755	2,906	2,906	–	–	–	–
Total Assets	817,793	676,828	556,128	80,898	15,159	76,198	11,890

Scope of consolidation continued

	2016						
	a	b	c	d	e	f	g
			Carrying values of items:				
	Carrying values as reported in published financial statements £m	Carrying values under regulatory scope of consolidation £m	Subject to credit risk framework £m	Subject to CCR framework £m	Subject to securitisation framework £m	Subject to market risk framework £m	Not subject to capital requirements or subject to deduction from capital £m
Liabilities							
Deposits from banks	16,384	–	–	–	–	–	–
Customer deposits	415,460	433,173	–	–	–	–	433,173
Items in course of transmission to banks	548	–	–	–	–	–	–
Trading and other financial liabilities at fair value through profit or loss	54,504	54,504	–	54,504	–	45,079	–
Derivative financial instruments	34,924	33,503	–	33,503	–	30,143	–
Notes in circulation	1,402	–	–	–	–	–	–
Debt securities in issue	76,314	75,037	–	–	–	–	75,037
Liabilities arising from insurance contracts and participating investment contracts	94,390	–	–	–	–	–	–
Liabilities arising from non-participating investment contracts	20,112	–	–	–	–	–	–
Other liabilities	29,193	6,774	–	–	–	–	6,774
Retirement benefit obligations	822	692	–	–	–	–	692
Current tax liabilities	226	146	–	–	–	–	146
Deferred tax liabilities	–	–	–	–	–	–	–
Other provisions	4,868	4,600	–	–	–	–	4,600
Subordinated liabilities	19,831	18,215	–	–	–	–	18,215
Total Liabilities	768,978	626,644	–	88,007	–	75,222	538,637

Columns (a) and (b): As insurance undertakings are excluded from the scope of the Group's regulatory consolidation, assets and liabilities relating to the Group's insurance undertakings require to be removed from the regulatory balance sheet (column (b)). The regulatory consolidation group diagram on page 6 highlights the key insurance undertakings of the Group that are excluded from the scope of regulatory consolidation.

Columns (c) to (g): Break down how the amounts reported in the consolidated regulatory balance sheet correspond to regulatory risk framework categories. Certain items are subject to regulatory capital charges under more than one risk framework, and as such are reported under each relevant risk framework. As a consequence, the sum of amounts in columns (c) to (g) may be greater than the amount in column (b).

Column (f): Carrying value of items subject to the market risk framework. Refer also to Table 62: Market risk linkages to the balance sheet.

Column (g): Includes items which are not subject to capital requirements, as well as assets that are ultimately deducted from own funds and which are therefore not risk-weighted. See Table 75: Items extracted from the consolidated regulatory balance sheet and reconciliation of own funds items to audited financial statements.

REGULATORY BALANCE SHEET ASSETS RECONCILIATION TO EXPOSURE AT DEFAULT (EAD)

A reconciliation of the consolidated regulatory balance sheet to EAD for items subject to the credit risk, CCR and securitisation frameworks is presented below.

Table 2: Main sources of differences between regulatory exposure amounts and carrying values in financial statements (LI2)

		2016		
		Items subject to:		
		Credit risk framework £m	CCR framework £m	Securitisation framework £m
1	**Asset carrying value amount under scope of regulatory consolidation (as per template LI1)**	556,128	80,898	15,159
2	Liabilities carrying value amount under regulatory scope of consolidation (as per template LI1)	–	88,007	–
3	Total net amount under the regulatory scope of consolidation	556,128	(7,109)	15,159
4	Off balance sheet amounts	82,179	–	12,091
5	Differences due to specific regulatory adjustments	8,888	–	–
6	Differences due to consideration of provisions	3,202	–	–
7	Net potential future exposures	–	13,176	–
8	Difference due to netting rules, other than those already included in row 3 and other regulatory adjustments	–	24,191	–
	Exposure amounts considered for regulatory purposes	650,397	30,258	27,250

Rows 1 and 2: Amounts in rows 1 and 2 correspond to the amounts in columns (c) to (e) of Table 1.

Row 3: Total net amount under the regulatory scope of consolidation. This row is presented as a simple calculation of row 1 (assets) less row 2 (liabilities), and takes no account of the eligibility of those assets and liabilities for the specific netting rules in the application of Part Three, Title II, Chapters 4 and 5, as well as of Title IV in the CRR.

Row 4: Off balance sheet items are stated after the application of credit conversion factors. Off balance sheet items under the credit risk framework principally consist of undrawn credit facilities.

Row 5: Differences due to specific regulatory adjustments primarily represent the uplift from gross exposure to modelled exposure at default for Retail IRB exposures.

Row 6: Differences due to consideration of provisions relates to the grossing up of provisions related to IRB exposures.

Row 7: Net potential future exposures relating to CCR exposures.

Row 8: Primarily relates to differences due to different netting rules other than those already captured in row 3, as well as the impact of credit risk mitigation and other CCR related adjustments.

Risk management

THE GROUP'S APPROACH TO RISK

The Group operates a prudent approach to risk with rigorous management controls to support sustainable business growth and minimise losses. Through a strong and independent risk function (Risk Division) a robust control framework is maintained to identify and escalate current and emerging risks with Board Risk Appetite and through good risk reward decision making.

Risk culture

The Board ensures that senior management implements risk policies and risk appetites that either limit or, where appropriate, prohibit activities, relationships and situations that could be detrimental to the Group's risk profile.

As part of a conservative business model that embodies a risk culture founded on a prudent approach to managing risk, the Group reviewed its Codes of Business and Personal Responsibility in 2016 reinforcing its approach where colleagues are accountable for the risks they take and where the needs of customers are paramount.

The focus remains on building and sustaining long-term relationships with customers cognisant of the economic climate.

Risk as a strategic differentiator

Group strategy and risk appetite are developed together to ensure one informs the other to deliver on our purpose to help Britain prosper whilst becoming the best bank for customers.

Risks are identified, managed and mitigated using our comprehensive Risk Management Framework and our clearly defined risk appetite, embedded in policies, authorities and limits provides a clear framework for effective business decision making. The principal risks we face, which could significantly impact the delivery of our strategy, are discussed in detail on pages 28 to 31 of the 2016 Lloyds Banking Group plc Annual Report and Accounts.

The Group believe effective risk management can be a strategic differentiator, in particular:

- **Prudent approach to risk:** Implementing a prudent approach to risk appetite across the Group, aligned to the embedding of a strong risk culture, driven both from the top and across the wider business, ensures we operate within risk appetite.
- **Strong control framework:** The Group's Risk Management Framework (RMF) acts as the foundation for the delivery of effective risk control and ensures that the Group risk appetite is continually developed and adhered to.
- **Business focus and accountability:** Effective risk management is a key focus and is included in key performance measures against which individual business units are assessed. The business areas in the first line of defence are accountable for risk but with oversight from a strong and importantly independent, second line of defence Risk Division.
- **Effective risk analysis, management and reporting:** Continuing to deliver close monitoring and stringent reporting to all levels of management and the Board on a regular basis ensures appetite limits are maintained and subject to stressed analysis at a risk type and portfolio level.
- **Sustainable growth:** Embedding a risk culture that ensures proactive support and constructive challenge takes place across the business is important for delivering sustainable growth.

Risk appetite

- Risk appetite is defined as 'the amount and type of risk that the Group is prepared to seek, accept or tolerate.'
- Risk appetite is documented in a Board Risk Appetite Statement which is reviewed by the Board Risk Committee (BRC) and approved annually by the Board.
- The Board metrics are supported by more detailed sub Board functional and divisional risk appetite metrics.
- The Board Risk Appetite is aligned to the Risk Appetite Framework, and in turn the Risk Management Framework and Group Risk Principles.
- Risk appetite is embedded within principles, policies, authorities and limits across the Group and continues to evolve to reflect external market developments and composition of the Group.
- The Group's strategy operates in tandem with the Board Risk Appetite and business planning is undertaken with a view to meeting the requirements of the Board Risk Appetite.
- Performance is optimised by allowing business units to operate within approved risk appetite and limits.
- The BRC is responsible for overseeing the development, implementation and maintenance of the Group's overall risk management framework and its risk appetite, to ensure they are in line with emerging regulatory, corporate governance and industry best practice.

Governance and control

- The Group's approach to risk is founded on a robust control framework and a strong risk management culture which are the foundation for the delivery of effective risk management and guide the way all employees approach their work, behave and make decisions.
- Governance is maintained through delegation of authority from the Board down to individuals through the management hierarchy. Senior executives are supported by a committee based structure which is designed to ensure open challenge and support effective decision making.
- The Group's risk appetite, principles, policies, procedures, controls and reporting are regularly reviewed and updated where needed to ensure they remain fully in line with regulations, law, corporate governance and industry good practice.
- The interaction of the executive and non-executive governance structures relies upon a culture of transparency and openness that is encouraged by both the Board and senior management.
- Board-level engagement, coupled with the direct involvement of senior management in Group wide risk issues at Group Executive Committee level, ensures that escalated issues are promptly addressed and remediation plans are initiated where required.
- Line management is directly accountable for identifying and managing risks in their individual businesses, ensuring that business decisions strike an appropriate balance between risk and reward consistent with the Group's risk appetite.
- Clear responsibilities and accountabilities for risk are defined across the Group through a Three Lines of Defence model which ensures effective independent oversight and assurance in respect of key decisions.

Risk decision making and reporting

- Taking risks which are well understood, consistent with strategy and with appropriate return is a key driver of shareholder value.
- Risk analysis and reporting supports the identification of opportunities as well as risks.
- An aggregate view of the Group's overall risk profile, key risks and management actions, and performance against risk appetite, is reported to and discussed monthly at the Group Risk Committee (and a subset at the Group Asset and Liability Committee), with regular reporting to the BRC and the Board.
- Rigorous stress testing exercises are carried out to assess the impact of a range of adverse scenarios with different probabilities and severities to inform strategic planning.
- The Chief Risk Officer regularly informs the BRC of the aggregate risk profile and as a member of the Board, has direct access to the Chairman and members of BRC.

The most significant risks the Group faces which could impact delivery of its strategy together with key mitigating actions, in line with the Risk Management framework, are outlined in the Risk Review section of the 2016 Lloyds Banking Group plc Annual Report and Accounts, pages 28 to 31.

Details of the Group's application of stress testing, the methodologies applied, use of reverse stress testing and governance are presented in the Risk Management section of the 2016 Lloyds Banking Group plc Annual Report and Accounts, page 119.

Further details on the Group's risk governance are presented in the Risk Management section of the 2016 Lloyds Banking Group plc Annual Report and Accounts, pages 121 and 122.

Further details on the Group's risk management processes in relation to the key risk drivers that do not fall under the scope of the Group's Pillar 3 disclosures are presented in the Risk Management section of the 2016 Lloyds Banking Group plc Annual Report and Accounts, as follows:

Conduct risk page 145; Funding and liquidity risk, pages 154 to 158; Capital risk, pages 159 to 166; Regulatory and legal risk, pages 166 and 167; Insurance risk, page 167; People risk, page 168; Financial reporting risk, pages 168 and 169; and Governance risk, page 169.

The regulatory capital framework

The Group's regulatory capital framework is defined by CRD IV as implemented in the UK by the PRA.

The framework consists of various classifications of capital resources – Common Equity Tier 1 (CET1), Additional Tier 1(AT1) and Tier 2 (T2) – to meet a stack of regulatory capital requirements and buffers, over and above which the Board maintains a management buffer to grow the business and cover uncertainties and future regulatory developments.

REGULATORY CAPITAL RESOURCES

The Group's capital resources are classified depending on the degree of permanency and loss absorbency exhibited:

Common equity tier 1 capital

This represents the strongest form of capital consisting of shareholders' equity (ordinary share capital and reserves) after a number of regulatory adjustments and deductions are applied. Of these, the most significant for the Group are the deduction of part of the Group's equity investment in its Insurance business and a large part of the Group's deferred tax assets. Other significant deductions consist of the elimination of the cash flow hedging reserve and deductions applied for goodwill, other intangible assets and defined benefit pension surpluses.

Additional tier 1 capital

AT1 capital instruments are non-cumulative perpetual securities containing a specific provision to write down the security or convert it to equity should the CET1 ratio fall to a defined trigger limit. The Group's current AT1 securities contain a trigger limit of 7 per cent.

Under the CRD IV transitional rules, securities that do not qualify in their own right as AT1 but were issued and eligible as tier 1 capital prior to CRD IV can be partially included within AT1, until they are phased out altogether in 2022. To the extent that these securities do not qualify as AT1 they may nevertheless still qualify as tier 2 capital.

Also under CRD IV transitional rules, a portion of the subordinated debt issued by the Group's Insurance business and held by the Group is deducted from AT1 capital. The remaining portion is deducted from T2 capital.

CET1 and AT1 together form Tier 1 Capital (T1).

Tier 2 capital

T2 capital comprises certain other subordinated debt securities that do not qualify as AT1. They must have an original term of at least 5 years, cannot normally be redeemed within their first 5 years and are phased out as T2 regulatory capital in the final 5 years before maturity.

Again, CRD IV transitional rules operate allowing securities that do not qualify in their own right as T2 but which were issued and eligible as T2 capital prior to CRD IV to be partially included as T2 capital, until they are phased out altogether in 2022.

There are two further adjustments: any excess of IRB loan loss provisions over the corresponding expected losses is added back to T2 capital subject to a percentage cap based on IRB risk-weighted assets; and a deduction is made for part of the subordinated debt issued by the Group's Insurance business that is not deducted from AT1 capital.

T1 and T2 together form Total Capital.

REGULATORY CAPITAL REQUIREMENTS AND BUFFERS

Prudential requirements under the Basel framework are categorised under three pillars: Pillar 1 – Minimum Capital Requirements; Pillar 2 – Supervisory Review Process; and Pillar 3 – Market Discipline.

PILLAR 1 – MINIMUM CAPITAL REQUIREMENTS

Pillar 1 of the regulatory framework focuses on the determination of risk-weighted assets and expected losses in respect of the firm's exposure to credit, counterparty credit, market and operational risks.

The minimum amount of total capital, under Pillar 1 of the regulatory framework, is determined as 8 per cent of aggregate risk-weighted assets. At least 4.5 per cent of risk-weighted assets are required to be covered by CET1 capital and at least 6 per cent of risk-weighted assets are required to be covered by tier 1 capital. These minimum Pillar 1 requirements are supplemented by additional minimum requirements under Pillar 2 of the regulatory framework and a number of regulatory capital buffers as described on page 14.

A range of approaches, varying in sophistication, are available under the CRD IV framework to use in measuring risk-weighted assets to determine the minimum level of capital required. Within the Group, risk-weighted assets are predominantly calculated using internal models that are prudently calibrated based on internal loss experience and are subject to a number of internal controls and external approval from the PRA. A brief summary of the different approaches for the different risk types and their application by the Group is disclosed on page 13, with further detail provided in each of the sections as indicated.

Further details on the Group's application of the IRB Approach (credit and counterparty credit risks) and the Internal Models Approach (market risk) are provided on pages 35 to 37 and 101 to 102, respectively.

Regulatory expected losses under the Foundation IRB, Advanced IRB and Retail IRB approaches are calculated by multiplying regulatory EAD by probability of default (PD) and loss given default (LGD), which are determined for each Approach as outlined on page 13, with the exception of defaulted exposures on the Advanced IRB Approach where the best estimate of expected loss (BEEL) is used. For exposures on the Supervisory Slotting and Equity Simple Risk Weight approaches, regulatory expected losses are determined by prescribed percentages from the regulator.

PILLAR 1 CAPITAL REQUIREMENTS

Risk type	Approaches	Application within the Group
Credit risk	Credit Risk risk-weighted assets represent a measure of on and off balance sheet exposures weighted according to risk as specified under CRD IV, either directly, or derived from a formula. There are two key approaches under CRD IV: **Standardised Approach (STA)** This is the most basic approach which applies a specified set of risk weights to exposures. Under this approach banks can utilise external credit ratings to determine risk weights for rated counterparties. **IRB Approach (IRB)** There are two main approaches for commercial exposures – Foundation IRB and Advanced IRB. For Retail exposures, Retail IRB is available. A prescribed regulatory formula is used to calculate risk-weighted assets which incorporates PD, LGD and EAD in addition to other variables such as maturity and correlation. Under CRD IV there are also adjustments applied to the calculation of risk-weighted assets in respect of an uplift for Financial Institutions Interconnectedness (FII) and a reduction for exposure to SMEs. *Foundation IRB Approach (FIRB)* The FIRB Approach uses internal assessments of a counterparty's PD (subject to certain floors) together with regulatory defined assessments for LGD and EAD. *Advanced IRB Approach (AIRB)* The AIRB Approach uses internal assessments of PD, EAD and LGD (subject to certain floors). *Retail IRB Approach* The Retail IRB Approach is a version of the AIRB Approach tailored to Retail exposures. *Other IRB Approaches* For certain specialised lending exposures there is also a supervisory slotting approach which assigns regulatory prescribed risk weights to assets based on the characteristics of each exposure. A number of alternative methodologies exist for other areas such as equity exposures, securitisation positions and contributions to the default fund of a central counterparty.	The Group applies the Standardised Approach to a small number of portfolios. These portfolios are mostly portfolios awaiting roll-out under the Group's IRB roll-out plan and portfolios permanently exempt from the IRB Approach which includes the majority of the Group's central government and central bank exposures. The FIRB Approach is used for the majority of Group's commercial exposures as the Group does not have permission to utilise the AIRB Approach for these portfolios. The Group has permission to utilise Advanced IRB Approach for Retail portfolios only and it applies the Retail IRB Approach (a version of Advanced IRB Approach) for the vast majority of its retail exposures. The Group applies the Supervisory Slotting Approach to certain corporate specialised lending exposures comprising mainly its commercial real estate exposures. The Simple Risk Weight Method is applied to the Group's equity exposures. Securitisation positions are predominantly risk-weighted under the Ratings Based Approach (RBA), with limited use made of the Internal Assessment Approach (IAA) and Standardised Approach.
Counterparty credit risk	There are three approaches to measuring exposure for counterparty credit risk, as below, which when combined with an appropriate PD and LGD feeds into the relevant IRB approach or alternatively capital requirements are calculated under the Standardised Approach, or supervisory slotting. **Standardised Method** The exposure value is calculated by applying a multiplier to the market value, dependent on the type of contract. **Mark-to-Market Method** Under this method, an add-on for potential future exposure (PFE) is applied to the balance sheet value of the instrument to give the overall exposure. **Internal Models Method (IMM)** Under the IMM approach, the fair value on the balance sheet is replaced by an exposure value calculated using internal models.	The Group's counterparty credit risk exposures are first measured under the Mark-to-Market Method, prior to being risk weighted under the Standardised or IRB Approach.
Market risk	The two key approaches for Market Risk are as follows: **Standardised Approach (SA)** This requires the calculation of position risk requirements (PRR) for each type of market risk in the trading book in accordance with standard rules set by the PRA. **Internal Models Approach (IMA)** Following PRA approval, involves the use of internal Value at Risk (VaR) and other models to determine appropriate capital requirements based on the market risks in the trading book.	The majority of the Group's trading book positions are assigned a capital requirement under the Internal Models Approach with the remainder following the Standardised Approach.
Operational risk	There are 3 approaches for Operational Risk: **Basic Indicator Approach (BIA)** A low risk sensitivity approach which calculates the capital requirement as a percentage of average net interest and non-interest income. **Standardised Approach (TSA)** A medium risk sensitivity approach where the capital requirement is derived from the three year average of the aggregate risk-weighted relevant indicators of the underlying business. **Advanced Measurement Approach (AMA)** A high risk sensitivity approach where, following PRA approval, the capital requirement is determined through the use of an internal operational risk measurement model.	The Group currently measures its operational risk requirement using the SA.

The regulatory capital framework continued

PILLAR 2 – SUPERVISORY REVIEW PROCESS

The Pillar 1 minimum requirement for capital is supplemented by Pillar 2A firm specific Individual Capital Guidance (ICG) and a framework of regulatory capital buffers.

INDIVIDUAL CAPITAL GUIDANCE

Under Pillar 2A, additional minimum requirements are set by the PRA by the issuance of bank specific ICG. This reflects a point-in-time estimate by the PRA, which may change over time, of the minimum amount of capital that is needed by the bank. It includes the assessment of risks that are not fully covered by Pillar 1 such as credit concentration and operational risk, and those risks not covered at all by Pillar 1 such as pensions and interest rate risk in the banking book (IRRBB).

During 2016 the Group's ICG was reduced from 4.6 per cent to 4.5 per cent of risk-weighted assets of which 56 per cent (2.5 per cent of risk-weighted assets) has to be covered by CET1 capital. The Group is not permitted by the PRA to give any further details of the quantum of the individual components.

A key input into the PRA's ICG setting process is a bank's own assessment of the amount of capital it needs, a process known as the Internal Capital Adequacy Assessment Process (ICAAP). The LBG ICAAP supplements the Pillar 1 capital requirements for credit risk, counterparty credit risk, operational risk and traded market risk by assessments of the material risks not covered or not fully captured under Pillar 1. This not only has the advantage of consistency with Pillar 1 but also allows the Group to leverage the considerable investment it has made in developing the component Pillar 1 models. This includes a detailed internal review of the models, their embedding in business use and an external review of these models by the PRA.

Some of the key risks assessed within the ICAAP include:

Risks not fully captured under Pillar 1

– Concentration risk – greater loss volatility arising from a higher level of loan default correlation than is assumed by the Pillar 1 assessment. Such correlation can arise from, for example, geographic, industry sector and single name concentrations.
– Underestimation risk – where it is considered that the Pillar 1 capital assessments for credit, market or operational risk underestimate the risk. This assessment includes consideration of conduct risk but, for credit risk, excludes the risk arising as a result of loan default correlation which is covered by the concentration risk assessment.

Risks not covered at all by Pillar 1

– Pension obligation risk – the potential for additional unplanned costs that the Group would incur in the event of a significant deterioration in the funding position of the Group's defined benefit pension schemes.
– Interest rate risk in the banking book – the potential losses in the non-trading book resulting from interest rate changes or widening of the spread between Bank Base Rate and LIBOR rates.

The detailed ICAAP document is subject to a robust review process, approved by the Board and submitted to the PRA for consideration when setting ICG.

REGULATORY CAPITAL BUFFERS

The Group is also required to maintain a number of regulatory capital buffers, which are required to be met with CET1 capital.

Systemic buffers

Systemic buffers are designed to hold systemically important banks to higher capital standards, so that they can withstand a greater level of stress before requiring resolution.

There are three systemic buffers in the Capital Requirements Directive:

– The G-SII buffer is applied to global systemically important institutions. The Group has not been classified as a G-SII.
– The O-SII buffer may be applied to other systemically important institutions. The Group has been classified as an O-SII by the PRA, but the O-SII buffer is set to zero in the UK.
– The Systemic Risk Buffer (SRB) will be applied to ring-fenced banks from 2019. In July 2016 the Financial Policy Committee (UK) published their methodology for quantifying the buffer for each ring-fenced bank and in December 2016 the PRA published their statement of policy on the approach for implementing the SRB. The size of buffer applied to the Group's ring-fenced bank (RFB) sub-group in 2019 will be dependent upon the total assets of the sub-group. The largest buffer the FPC anticipates applying to any ring-fenced bank is 2.5 per cent.

Although the SRB will apply at a sub consolidated level within the Group's structure, the PRA have indicated that they will include in the PRA Buffer (as described on page 15) that applies to the Group an amount equivalent to the Ring Fenced Bank's Systemic Risk Buffer. The amount included in the PRA Buffer is expected to be lower as a percentage of Group risk-weighted assets reflecting the assets of the Group that will not be held in the RFB sub-group and to which the SRB will not apply.

Capital conservation buffer

The capital conservation buffer (CCB) is a standard buffer of 2.5 per cent of risk-weighted assets designed to provide for losses in the event of stress and is being phased in from 1 January 2016 to 1 January 2019. During 2016 it was 0.625 per cent and during 2017 it is 1.25 per cent.

Countercyclical capital buffer

The countercyclical capital buffer (CCYB) is time-varying and is designed to require banks to hold additional capital to remove or reduce the build up of systemic risk in times of credit boom, providing additional loss absorbing capacity and acting as an incentive for banks to constrain further credit growth. The amount of the buffer is determined by reference to buffer rates set by the FPC for the individual countries where the Group has relevant credit risk exposures.

The buffer is currently set at zero for the UK, however, non-zero rates for Norway, Sweden and Hong Kong were in place at 31 December 2016. Given that the Group has minimal exposures to these jurisdictions, the overall requirement is negligible as outlined below.

The UK CCYB rate was set to increase from zero per cent to 0.5 per cent of risk-weighted assets on 29 March 2017, at which time the overlapping aspects of Pillar 2 supervisory capital buffers would be removed or reduced. However, following the EU referendum, on 5 July 2016 the FPC announced in their Financial Stability Report that the planned 0.5 per cent UK CCYB would not be implemented in March 2017 and the zero per cent rate was expected to remain until at least June 2017.

The FPC also recommended that where existing Pillar 2 supervisory buffers reflect risks that would be captured by a UK CCYB rate, the PRA should reduce those buffers by an amount of capital which is equivalent to the effect of a UK CCYB rate of 0.5 per cent.

The FPC has also indicated that it expects to review the UK CCYB and to set a rate in the region of 1 per cent of risk-weighted assets when risks are judged to be neither subdued nor elevated, but the rate can be set in excess of this level. Any increase in CCYB would take effect one year after it is set.

The Group's countercyclical capital buffer requirement at 31 December 2016 was £5.0m (2015: £2.8m).

Additional disclosures around the geographical distribution of credit exposures relevant to the calculation of the countercyclical capital buffer have been included for the Group and its significant subsidiaries in Appendix 1, 3 and 4.

Sectoral capital requirements

The FPC can also set sectoral capital requirements which are temporary increases to banks' capital requirements on exposures to specific sectors, if the FPC judges that exuberant lending to those sectors poses risks to financial stability. No sectoral capital requirements currently apply to the Group.

PRA buffer

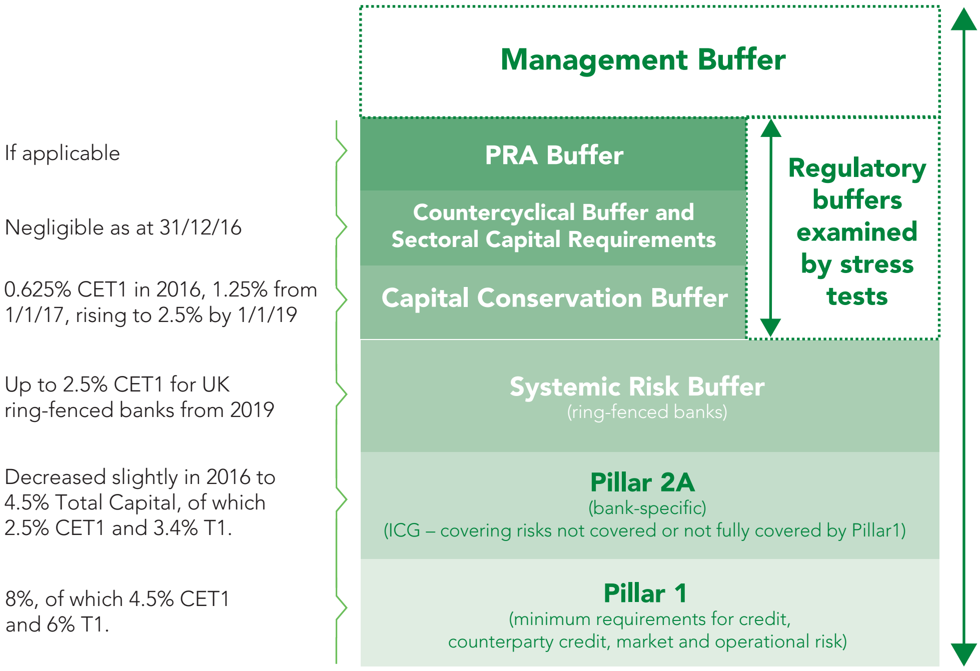
As part of the capital planning process, forecast capital positions are subjected to extensive stress analyses to determine the adequacy of the Group's capital resources against the minimum requirements, including ICG. The PRA uses the outputs from some of these stress analyses as one of the outputs that inform the setting of a bank-specific capital buffer for the Group, known as the PRA Buffer. The PRA Buffer also takes into account the CCB, CCYB and any sectoral capital requirements that already apply to the Group. The PRA requires the PRA Buffer to remain confidential between the Group and the PRA.

Further details on the Group's stress testing processes and the 2016 PRA stress testing results are included on page 165 of the 2016 Lloyds Banking Group plc Annual Report and Accounts.

All buffers

All buffers are required to be met with CET1 capital. A breach of the PRA buffer would trigger a dialogue between the Group and the PRA to agree what action is required whereas a breach of the CRD IV combined buffer (all regulatory buffers excluding the PRA buffer) would also give rise to automatic constraints upon any discretionary capital distributions by the Group.

The following diagram summarises the capital framework requirements across the various tiers of capital and the Group's latest view on the amount of capital to be held. Percentages referenced below are against risk-weighted assets.



Following their annual review the PRA has reduced the Group's PRA buffer to reflect the significant de-risking undertaken by the Group in recent years. Going forward, there remain a number of capital developments (including the introduction of the systemic risk buffer in 2019) and as a result the Board's view of the current level of CET1 capital required to grow the business, meet regulatory requirements and cover uncertainties, remains unchanged at 13 per cent.

The regulatory capital framework continued

PILLAR 3 – MARKET DISCIPLINE

The third pillar addresses the external publication of disclosures surrounding a firm's risk management practices, its approach to capital management, its capital resources and Pillar 1 capital requirements and a detailed analysis of its credit risk exposures.

The Basel III framework sets out the minimum disclosures required under Pillar 3. Together with additional minimum disclosure requirements imposed through amendments to the original CRD, these form the basis of the disclosures the Group is required to make under the relevant CRR provisions (Part 8 – Disclosure by institutions).

LEVERAGE FRAMEWORK

In addition to the risk-based capital framework outlined above, the Group is also subject to minimum capital requirements under the UK Leverage Ratio Framework. The leverage ratio is calculated by dividing fully loaded tier 1 capital resources by a defined measure of on-balance sheet assets and off-balance sheet items.

The minimum leverage ratio in the UK is 3 per cent, in line with current Basel requirements. In addition the UK framework requires two buffers to be maintained: an Additional Leverage Ratio Buffer (ALRB), which is calculated as 35 per cent of the Systemic Risk Buffer (applicable from 2019) and a time-varying Countercyclical Leverage Buffer (CCLB) which is calculated as 35 per cent of the countercyclical capital buffer rate (currently set at zero per cent). At least 75 per cent of the minimum 3 per cent requirement and the entirety of any buffers that may apply must be met by CET1 capital.

The Group also calculates the leverage ratio on a modified basis, excluding qualifying central bank claims from the leverage exposure measure. This follows the rule modification applied to the UK Leverage Ratio Framework by the PRA in August 2016 as a result of recommendations made by the Financial Policy Committee.

The Financial Policy Committee has indicated that it intends to recalibrate the UK framework in 2017 in order to adjust for the impact of the rule modification, thereby ensuring that levels of capital currently required to meet leverage ratio minimums are maintained. The modified UK leverage ratio should therefore be considered in the context of the proposed recalibration.

The leverage ratio framework does not currently give rise to higher capital requirements for the Group than the risk-based capital framework.

RING-FENCING AND RESOLUTION

Good progress continues to be made towards compliance with ring-fencing legislation (Financial Services (Banking Reform) Act) in advance of 1 January 2019. The vast majority of our business will sit within the ring-fence, and we therefore expect ring-fencing to be less onerous for the Group than many of our UK peers.

FUTURE REGULATORY DEVELOPMENTS

Introduction

The Group's 2016 year end disclosures comply with all relevant CRD IV requirements and associated EBA guidelines and technical standards in force at 31 December 2016. It is important to note that specific aspects of the CRD IV text remain dependent upon the issuance of final EBA technical standards, guidelines and Q&As as well as PRA policy and standards in relation to areas of national discretion. The Group continues to closely monitor regulatory developments at global, European and UK levels in order to best position the Group to adapt to any changes arising.

Some of the key areas of development are discussed further:

Disclosure requirements

In December 2016 the EBA published its Final Report on the implementation of the Basel Committee on Banking Supervision (BCBS) Phase 1 revisions to the Pillar 3 framework. Although not applicable to the Group until year end 2017, a number of the revised disclosures are included in this document, as set out in Appendix 5. The Basel Committee is expected to publish its final 'Phase 2' requirements in 2017.

Changes to the capital framework

- **Standardised credit risk framework** – The Basel Committee published a second consultation on revisions to the Standardised credit risk framework in December 2015 and the impact of these revisions was assessed through a Quantitative Impact Study (QIS) during 2016. The proposed revisions are designed to increase the risk sensitivity of the framework and to better align with IRB approaches. Final rules have not yet been agreed.
- **IRB credit risk framework** – In March 2016 the Basel Committee issued a consultation on reducing variation in credit risk-weighted assets through implementing constraints on the use of internal model approaches. This included proposals to remove or limit the use of IRB approaches for certain asset classes, including low-default portfolios (banks, other financials and large corporates), and to introduce model-parameter floors across PD, LGD and EAD measures. As with the proposed revisions to the Standardised credit risk framework the impact of the proposed constraints on the use of internal model approaches was assessed through a QIS during 2016, with final rules yet to be agreed.
- **Operational risk framework** – The Basel Committee is proposing major revisions to the Operational risk framework by replacing the current approaches with a new Standardised Measurement Approach (SMA). A second consultation was published during the first half of 2016. Final rules have not yet been agreed.
- **Market risk** – The Basel Committee issued its final standards on the Fundamental Review of the Trading Book (FRTB) in January 2016. The standard includes a move away from VaR based metrics under the internal models approach to a new expected shortfall measure of risk under stress, a revised Standardised approach for calculating market risk capital to a more risk-sensitive approach, incorporation of the risk of market illiquidity and a revised boundary between the banking book and the trading book. Application of the new framework is currently expected to be implemented by 2020.
- **Capital floors** – The Basel Committee proposes to introduce a new capital floors framework based on the revised Standardised frameworks in order to improve comparability and to constrain variation in model-derived risk-weighted assets. Final proposals including the calibration of the floors are expected to be published in line with the finalisation of the revised Standardised frameworks.
- **Standardised counterparty credit risk framework (SA-CCR)** The Basel Committee issued its final revisions to the Standardised counterparty credit risk framework in March 2014. The new requirements will impact upon the calculation of CCR exposures under the Standardised approach and are expected to be implemented by 2020 at the earliest.
- **Review of the credit valuation adjustments (CVA) framework** The EBA has recommended the removal of exemptions from the current CVA framework over the medium term ahead of the implementation of final Basel Committee proposals on revisions to the CVA framework following completion of the FRTB. In the short term the EBA has proposed additional measures under Pillar 2A.

- **Revisions to the securitisation framework** – The Basel Committee issued final rules in December 2014 on introducing new risk weight methodologies for securitisation positions that have implications for the minimum risk weights applied. The new framework remains the subject of EU negotiations and is expected to be implemented by 2018.
- **Sovereign risk** – The Basel Committee has initiated a review of the regulatory treatment of sovereign risk and is expected to consult on this in 2017. In addition the EBA issued a consultation in November 2016 regarding the reporting of sovereign exposures.
- **Interest rate risk in the banking book (IRRBB)** – The Basel Committee issued a final standard in April 2016 on IRRBB. In response to industry feedback the Committee reverted to an enhanced Pillar 2A approach abandoning proposals to establish a Pillar I measure. It is expected that the new standard will apply from 2018.
- **IRB Repair Programme** – The EBA has issued a consultation on revised Guidelines on PD, LGD and the treatment of default which will be subject to a QIS to assess the impact during 2017. A further consultation on Downturn Conditions is expected in early 2017. The effect of these proposed changes will also be impacted by the finalisation of the BCBS IRB credit risk framework proposals.
- **Mortgage Risk Weights** – A PRA consultation issued in July 2016 proposed changes to the methodologies used in the modelling of residential mortgage book probability of default and outlined expectations for the house price fall assumptions to be used when calculating the expected loss given default in economic downturn conditions. The consultation has now closed.

EU Risk Reduction Package

In November 2016, the European Commission published a substantial package of draft reforms aimed at further strengthening the resilience of banks across the EU. This package comprises draft legislative texts updating the Capital Requirements Directive and Regulation (CRD IV) to include, amongst other reforms, the implementation of further Basel III Framework revisions, including market risk, SA-CCR, leverage and Pillar 3. These reforms are currently under negotiation and expected to be implemented by 2020 at the earliest.

Minimum requirement for own funds and eligible liabilities (MREL)

The purpose of MREL is to require firms to maintain sufficient equity and liabilities that are capable of credibly bearing losses in resolution. MREL can be satisfied by a combination of regulatory capital and certain unsecured debt resources (which must be subordinate to a firm's operating liabilities).

In November 2016 the Bank of England published a statement of policy on its approach for setting MREL in line with EU requirements. Application of this policy to the Group would mean that from 2020 it would be required to meet an MREL equivalent to double its Pillar 1 capital requirement (i.e. 2 x 8 per cent of risk-weighted assets) plus one times its Pillar 2A requirement and its regulatory capital buffers, and from 2022 this would increase to double its Pillar 1 and Pillar 2A requirements plus one times its regulatory capital buffers. The Bank of England has stated that it intends to review its current expectation of the calibration and transition of MREL by the end of 2020, before setting end-state MREL requirements by 2022. This review will take into consideration any changes to the capital framework including those emanating from the Basel Committee.

Capital management

This section details Lloyds Banking Group's approach to capital management, focusing on measures including Common Equity Tier 1 (CET1), Additional Tier 1 (AT1), Tier 2 (T2) and the Leverage Ratio.

CET1 ratio of 13.6% (13.8% pro forma)

Transitional T1 capital ratio of 17.0%

Transitional total capital ratio of 21.4%

Leverage ratio of 4.9% (5.0% pro forma)

- The Group has a capital management framework that is designed to ensure that it operates within its risk appetite, uses its capital resources efficiently and continues to comply with regulatory requirements.
- CET1 capital resources increased by £0.7bn in the year largely as a result of profit generation in the year, dividends received from the Insurance business and the favourable movement in the available-for-sale reserve following the accounting reclassification of gilts from held-to-maturity to available for sale.
- AT1 capital resources reduced by £0.7bn in the year, primarily reflecting the annual reduction in the transitional limit applied to grandfathered AT1 capital instruments and an increase in the significant investments deduction.
- T2 capital resources reduced by £1.9bn in the year largely reflecting calls, redemptions and amortisations, partly offset by the issuance of a new tier 2 instrument and foreign exchange movements on subordinated debt.
- A description of the main features of CET1, AT1 and T2 instruments issued by the Group and its significant subsidiaries are included in a separate document on the Group's website. Summary information on movements and the underlying terms and conditions of capital securities is presented in Note 39 (Subordinated Liabilities) of the 2016 Lloyds Banking Group plc Annual Report and Accounts.
- The Group's fully loaded leverage ratio increased by 0.1 per cent to 4.9 per cent reflecting the impact of both the increase in tier 1 capital and the £5.1bn reduction in the exposure measure, the latter largely reflecting the reduction in liquid asset holdings.

THE GROUP'S APPROACH TO CAPITAL RISK

DEFINITION
Capital risk is defined as the risk that the Group has a sub-optimal quantity or quality of capital or that capital is inefficiently deployed across the Group.

RISK APPETITE
Capital risk appetite is set by the Group Board, reflecting the Group's strategic plans, regulatory capital constraints and market expectations. It is defined by a number of minimum capital ratios, a minimum leverage ratio and a minimum buffer over regulatory solvency requirements for the Insurance business set by the Insurance Board. The Group monitors its actual and forecast capital positions aiming to remain within its appetite at all times.

EXPOSURES
A capital risk exposure arises when the Group has insufficient capital resources to support its strategic objectives and plans, and to meet external stakeholder requirements and expectations. This could arise due to a depletion of the Group's capital resources as a result of the crystallisation of any of the risks to which it is exposed. Alternatively a shortage of capital could arise from an increase in the amount of capital that is needed to be held. The Group's capital management approach is focused on maintaining sufficient capital resources to prevent such exposures while optimising value for shareholders.

MEASUREMENT
The Group measures the amount of capital it holds using the regulatory framework defined by CRD IV as implemented in the UK by the PRA. Full details of the Group's regulatory capital framework are on pages 12 to 17.

MITIGATION
The Group has a capital management framework including policies and procedures that are designed to ensure that it operates within its risk appetite, uses its capital resources efficiently and continues to comply with regulatory requirements.

The Group is able to accumulate additional capital through the retention of profits over time, which can be enhanced through cutting costs and reducing or cancelling dividend payments, by raising new equity via, for example, a rights issue or debt exchange and by raising AT1 or T2 capital through issuing tier 1 instruments or subordinated liabilities. The cost and availability of additional capital is dependent upon market conditions and perceptions at the time. The Group is also able to manage the demand for capital through management actions including adjusting its lending strategy, risk hedging strategies and through business disposals.

Additional measures to manage the Group's capital position include seeking to optimise the generation of capital demand within the Group's businesses to strike an appropriate balance of capital held within the Group's Insurance and banking subsidiaries and through improving the quality of its capital through liability management exercises.

MONITORING
Capital is actively managed and regulatory ratios are a key factor in the Group's planning processes and stress analyses. Multi-year forecasts of the Group's capital position, based upon the Group's operating plan, are produced at least annually to inform the Group's capital strategy whilst shorter term forecasts are more frequently undertaken to understand and respond to variations of the Group's actual performance against the plan. The capital plans are tested for capital adequacy using a range of stress scenarios covering adverse economic conditions as well as other adverse factors could impact the Group and the Group maintains a Recovery Plan which sets out a range of potential mitigating actions that could be taken in response to a stress.

Regular reporting of actual and projected ratios, including those in stressed scenarios, is undertaken, including submissions to the Group Capital Risk Committee (GCRC), Group Financial Risk Committee (GFRC), Group Asset and Liability Committee (GALCO), Group Risk Committee (GRC), Board Risk Committee (BRC) and the Board. Capital policies and procedures are subject to independent oversight.

The regulatory framework within which the Group operates continues to evolve and further detail of this can be found under the Future Regulatory Developments heading within the Regulatory Capital Framework section of this report. The Group continues to monitor these developments very closely, analysing the potential capital impacts to ensure that, through organic capital generation, the Group continues to maintain as strong capital position that exceeds the minimum regulatory requirements and the Group's risk appetite and is consistent with market expectations.

TARGET CAPITAL RATIOS
The Board's view of the current level of CET1 capital required to grow the business, meet regulatory requirements and cover uncertainties and future regulatory developments remains at around 13 per cent.

This takes into account, amongst other things:

- the Pillar 2A Individual Capital Guidance (ICG) set by the PRA, reflecting their point in time estimate, which may change over time, of the amount of capital that is needed in relation to risks not covered by Pillar 1. During the year the PRA updated the Group's ICG representing a reduction from 4.6 per cent to 4.5 per cent of risk-weighted assets at 31 December 2016, of which 2.5 per cent has to be covered by CET1 capital.
- the PRA buffer, which they set taking into account the results of the PRA stress tests, as well as outputs from our internal stress tests and other information. In November 2016 the PRA published the results of its 2016 stress tests which showed the Group's capital depletion to be 2.5 per cent after management actions compared to 3.3 per cent in the 2015 PRA stress tests and 4.8 per cent in the 2014 PRA stress tests. The PRA requires the PRA buffer to remain confidential between the Group and the PRA.
- future regulatory developments, including the introduction of the Systemic Risk buffer in 2019.

In addition, the Group targets a transitional total capital ratio of around 20 per cent.

Capital management continued

DIVIDEND POLICY

The Group has established a dividend policy that is both progressive and sustainable. We expect ordinary dividends to increase over the medium term to a dividend payout ratio of at least 50 per cent of sustainable earnings. The Board interprets progressive to indicate a dividend per share that is expected to increase over the medium term. Sustainable earnings represents the long term earnings generation of the business. Sustainable earnings are defined as earnings after tax attributable to ordinary shareholders adjusted to remove the effects of market volatility, exceptional conduct or litigation events, major liability management or restructuring and other one off items such as the sale of businesses, and exceptional underlying business performance.

The Board also gives due consideration to the distribution of surplus capital through the use of special dividends or share buy-backs. Surplus capital represents capital over and above the amount management wish to retain to grow the business, meet regulatory requirements and cover uncertainties. The amount of required capital may vary from time to time depending on circumstances and the Board will continue to give due consideration, subject to the situation at the time, to the distribution of any surplus capital. By its nature, there can be no guarantee that this level of special dividends or any surplus capital distribution will be appropriate in future years.

The ability of the Group to pay a dividend is also subject to constraints including the availability of distributable reserves, legal and regulatory restrictions and the financial and operating performance of the entity.

Distributable reserves are determined as required by the Companies Act 2006 by reference to a company's individual financial statements. At 31 December 2016 Lloyds Banking Group plc ('the Company') had accumulated distributable reserves of approximately £8.5bn. Substantially all of the Company's merger reserve is available for distribution under UK company law as a result of transactions undertaken to recapitalise the Company in 2009.

Lloyds Banking Group plc acts as a holding company which also issues capital and other securities to capitalise and fund the activities of the Group. The profitability of the holding company, and consequently its ability to sustain dividend payments, is therefore dependent upon the continued receipt of dividends from its subsidiaries (representing both banking and Insurance). A number of Group subsidiaries, principally those with banking and insurance activities, are also subject to regulatory capital requirements. These require entities to maintain minimum amounts of capital related to their size and risk. The principal operating subsidiary is Lloyds Bank plc, the consolidated capital position for which is presented in Appendix 3. The Group actively manages the capital of its subsidiaries, which includes monitoring the regulatory capital ratios for its banking and insurance subsidiaries against approved risk appetite limits. It operates a formal capital management policy which requires all subsidiary entities to remit any surplus capital to their parent companies.

During 2016 the Group has continued to simplify the Group's internal capital structure and to ensure that profits generated by subsidiary entities can be more easily remitted to the Company. This included the court approved capital reduction by Lloyds Bank plc.

ANALYSIS OF CAPITAL POSITION

During 2016 the Group continued to strengthen its capital position with a fully loaded CET1 ratio, after accruing for foreseeable dividends, of 13.6 per cent and 13.8 per cent on a pro forma basis upon recognition of the dividend paid by the Insurance business in February 2017 in relation to its 2016 earnings (31 December 2015: 13.0 per cent pro forma). The accrual for foreseeable dividends includes the announced full year ordinary dividend of 2.55 pence per ordinary share and a special dividend of 0.5 pence per ordinary share.

The CET1 ratio on a pro forma basis reflects the prudent retention of circa 0.8 per cent of capital, above the current targeted level, to cover the estimated capital impact of the MBNA transaction that was announced in December 2016.

Over the year the Group generated around 1.9 per cent of CET1 capital on a pro forma basis, pre dividend, primarily as a result of the following:

- Strong underlying capital generation of 2.2 per cent, largely driven by underlying profits;
- The dividend paid by the Insurance business in February 2017 in relation to its 2016 earnings of 0.2 per cent;
- Impact of conduct charges of (1.0) per cent;
- Impact of market movements, netting to 0.2 per cent. This included 0.8 per cent from the impact of the accounting reclassification of c.£20bn of gilts within the liquidity portfolio from 'held-to-maturity' to 'available-for-sale', offset by a number of market related movements, including an adverse impact of movements in the defined benefit pension schemes of (0.4) per cent;
- Other items largely representing a reduction in risk-weighted assets, most notably in the fourth quarter, largely relating to active portfolio management, disposals, an improvement in credit quality and capital efficient securitisation activity, partially offset by model updates related to UK mortgage portfolios and the impact of the redemption of the remaining series of Enhanced Capital Notes in the first quarter.

After accruing for foreseeable dividends, the transitional total capital ratio reduced by 0.1 percentage points to 21.4 per cent, primarily reflecting managed reductions in tier 2 capital, largely due to calls and redemptions, offset by the increase in CET1 capital and the reduction in risk-weighted assets.

In 2020 the Group will have to meet a Minimum Requirement for Own Funds and Eligible Liabilities (MREL). During 2016 the Group commenced issuance of senior unsecured securities from Lloyds Banking Group plc which, while not included in total capital, are eligible to meet MREL. £2.5bn (Sterling equivalent) was issued in 2016 and a further £2.2bn (Sterling equivalent) was issued in January 2017 leaving the Group well positioned to meet MREL requirements from 2020.

The leverage ratio, after accruing for foreseeable dividends, increased from 4.8 per cent to 4.9 per cent (5.0 per cent on a pro forma basis), largely reflecting the increase in tier 1 capital.

An analysis of the Group's capital position as at 31 December 2016 is presented in the following section applying CRD IV transitional arrangements and also on a fully loaded CRD IV basis, both as implemented in the UK by the PRA.

LLOYDS BANKING GROUP CAPITAL RESOURCES

The table below summarises the consolidated capital position of the Group.

Table 3: Capital resources

	Transitional		Fully loaded	
	2016 £m	2015[1] £m	**2016 £m**	2015[1] £m
Common equity tier 1				
Shareholders' equity per balance sheet	**43,020**	41,234	**43,020**	41,234
Adjustment to retained earnings for foreseeable dividends	**(1,568)**	(1,427)	**(1,568)**	(1,427)
Deconsolidation adjustments[1]	**1,342**	1,119	**1,342**	1,119
Adjustment for own credit	**87**	67	**87**	67
Cash flow hedging reserve	**(2,136)**	(727)	**(2,136)**	(727)
Other adjustments[1]	**(276)**	(97)	**(276)**	(97)
	40,469	40,169	**40,469**	40,169
Less: deductions from common equity tier 1				
Goodwill and other intangible assets	**(1,623)**	(1,719)	**(1,623)**	(1,719)
Prudent valuation adjustment	**(630)**	(372)	**(630)**	(372)
Excess of expected losses over impairment provisions and value adjustments	**(602)**	(270)	**(602)**	(270)
Removal of defined benefit pension surplus	**(267)**	(721)	**(267)**	(721)
Securitisation deductions	**(217)**	(169)	**(217)**	(169)
Significant investments[1]	**(4,282)**	(4,500)	**(4,282)**	(4,529)
Deferred tax assets	**(3,564)**	(3,874)	**(3,564)**	(3,884)
Common equity tier 1 capital	**29,284**	28,544	**29,284**	28,505
Additional tier 1				
Other equity instruments	**5,320**	5,355	**5,320**	5,355
Preference shares and preferred securities[2]	**4,998**	4,728	**–**	–
Transitional limit and other adjustments	**(1,692)**	(906)	**–**	–
	8,626	9,177	**5,320**	5,355
Less: deductions from tier 1				
Significant investments[1]	**(1,329)**	(1,177)	**–**	–
Total tier 1 capital	**36,581**	36,544	**34,604**	33,860
Tier 2				
Other subordinated liabilities[2]	**14,833**	18,584	**14,833**	18,584
Deconsolidation of instruments issued by insurance entities[1]	**(1,810)**	(1,665)	**(1,810)**	(1,665)
Adjustments for transitional limit non-eligible instruments	**1,351**	(52)	**(1,694)**	(3,066)
Amortisation and other adjustments	**(3,447)**	(3,880)	**(3,597)**	(4,885)
	10,927	12,987	**7,732**	8,968
Eligible provisions	**186**	221	**186**	221
Less: deductions from tier 2				
Significant investments[1]	**(1,571)**	(1,756)	**(2,900)**	(2,933)
Total Capital Resources	**46,123**	47,996	**39,622**	40,116
Risk-weighted assets	**215,534**	222,845	**215,534**	222,747
Common equity tier 1 capital ratio[3]	**13.6%**	12.8%	**13.6%**	12.8%
Tier 1 capital ratio	**17.0%**	16.4%	**16.1%**	15.2%
Total capital ratio	**21.4%**	21.5%	**18.4%**	18.0%

[1]For regulatory capital purposes, the Group's Insurance business is deconsolidated and replaced by the amount of the Group's investment in the business. A part of this amount is deducted from capital (shown as 'significant investments' in the table above) and the remaining amount is risk-weighted, forming part of threshold risk-weighted assets. The presentation of the deconsolidation of the Group's insurance entities has been amended for 2016 with comparative figures restated accordingly.

[2]Preference shares, preferred securities and other subordinated liabilities are categorised as subordinated liabilities in the balance sheet.

[3]The common equity tier 1 ratio is 13.8% on a pro forma basis upon recognition of the dividend paid by the Insurance business in February 2017 in relation to its 2016 earnings (31 December 2015: 13.0% pro forma).

The key differences between the transitional capital calculation as at 31 December 2016 and the fully loaded equivalent are as follows:

– Capital securities that previously qualified as T1 or T2 capital, but do not qualify under CRD IV, can be included in T1 or T2 capital (as applicable) up to specified limits which reduce by 10 per cent per annum until 2022.

– The significant investment deduction from AT1 will gradually transition to T2.

Capital management continued

MOVEMENTS IN CAPITAL

The movements in the transitional CET1, AT1, T2 and total capital positions in the period are provided below.

Table 4: Movements in capital

	Common equity tier 1 £m	Additional tier 1 £m	Tier 2 £m	Total capital £m
At 31 December 2015	28,544	8,000	11,452	47,996
Profit attributable to ordinary shareholders[1]	2,070	–	–	2,070
Movement in foreseeable dividends[2]	(141)	–	–	(141)
Dividends paid out on ordinary shares during the year	(2,014)	–	–	(2,014)
Dividend in respect of 2015 earnings received from the Insurance business[1]	500	–	–	500
Movement in treasury shares and employee share schemes	134	–	–	134
Pension movements:	–	–	–	–
Removal of defined benefit pension surplus	454	–	–	454
Movement through other comprehensive income	(954)	–	–	(954)
Available-for-sale reserve	1,197	–	–	1,197
Prudent valuation adjustment	(258)	–	–	(258)
Deferred tax asset	310	–	–	310
Goodwill and other intangible assets	96	–	–	96
Excess of expected losses over impairment provisions and value adjustments	(332)	–	–	(332)
Significant investments	218	(152)	185	251
Eligible provisions	–	–	(35)	(35)
Movements in subordinated debt:	–	–	–	–
Repurchases, redemptions and other	–	(551)	(3,211)	(3,762)
Issuances	–	–	1,151	1,151
Other movements	(540)	–	–	(540)
At 31 December 2016	**29,284**	**7,297**	**9,542**	**46,123**

[1] Under the regulatory framework, the profits made by Insurance are removed from CET1 capital. However, when dividends are paid to the Group by Insurance these are recognised through CET1 capital.

[2] Includes the accrual for increased 2016 full year ordinary and special dividends and the reversal of the accrual for the 2015 full year ordinary and special dividends which were paid during the year.

CET1 capital resources have increased by £0.7bn in the year largely as a result of profit generation in the year, dividends received from the Insurance business and the favourable movement in the available-for-sale reserve following the accounting reclassification of gilts within the liquidity portfolio from held-to-maturity. These movements in CET 1 capital were partially offset by dividends paid out during the year, movements in the defined benefit pension schemes largely driven by the impact of credit spreads, an increase in the excess of expected losses over impairment provisions and value adjustments primarily as a result of the implementation of recently published EBA guidance restricting prudent valuation adjustments eligible for offset against expected losses, and the accrual of the full year ordinary and special dividends, representing returns to ordinary shareholders following strong capital generation.

AT1 capital resources have reduced by £0.7bn in the year, primarily reflecting the annual reduction in the transitional limit applied to grandfathered AT1 capital instruments and an increase in the significant investments deduction.

Tier 2 capital resources have reduced by £1.9bn in the year largely reflecting calls and redemptions, including the redemption of all remaining series of Enhanced Capital Notes (ECNs) under the Regulatory Call Right and the amortisation of dated tier 2 instruments, partly offset by the issuance of a new dated tier 2 instrument, foreign exchange movements on subordinated debt, the transitioning of grandfathered AT1 instruments to tier 2 and a reduction in the significant investments deduction.

The redemption of the remaining series of ECNs followed the decision of the Court of Appeal in December 2015 that a Capital Disqualification Event (CDE) in relation to the ECNs had occurred. The Group subsequently exercised its option to redeem them in the first quarter of 2016. In June 2016 the Supreme Court confirmed the decision of the Court of Appeal.

CAPITAL INSTRUMENTS

A description of the main features of CET1, AT1 and T2 instruments issued by the Group and its significant subsidiaries are included in a separate document on the Group's website located at www.lloydsbankinggroup.com/investors/financial-performance/other-disclosures

Summary information on movements in subordinated liabilities and share capital and the terms and conditions applying to these instruments is presented in the Notes to the Consolidated Financial Statements of the 2016 Lloyds Banking Group plc Annual Report and Accounts on page 232.

The full terms and conditions attached to capital instruments are also available on the Group's website at http://www.lloydsbankinggroup.com/investors/fixed-income-investors/

The recognition, classification and valuation of these instruments within the Group's regulatory capital resources are subject to the requirements of CRD IV. This can lead to a different treatment from the IFRS accounting approach upon which the disclosures within the 2016 Lloyds Banking Group plc Annual Report and Accounts are based. Not all subordinated liabilities qualify as regulatory capital, and for those that do, differences between the accounting and the regulatory value can arise in relation to fair value hedge accounting adjustments, accrued interest and the regulatory amortisation of dated securities.

OWN FUNDS DISCLOSURES

Additional disclosures on own funds, in accordance with the requirements of the EBA technical standard on Own Funds Disclosure, are provided in Appendix 1. These consist of a detailed analysis of the components of the Group's transitional own funds and a reconciliation of own funds items to the statutory balance sheet. Separate own funds disclosures are provided for the Group's significant subsidiaries and are located in Appendix 3 and 4.

LEVERAGE RATIO

Table 5: Leverage ratio

	Fully loaded 2016 £m	2015 £m
Total tier 1 capital for leverage ratio		
Common equity tier 1 capital	**29,284**	28,505
Additional tier 1 capital	**5,320**	5,355
Total tier 1 capital	**34,604**	33,860
Exposure measure		
Statutory balance sheet assets		
Derivative financial instruments	**36,138**	29,467
Securities financing transactions (SFTs)	**42,285**	34,136
Loans and advances and other assets	**739,370**	743,085
Total assets	**817,793**	806,688
Deconsolidation adjustments[1]		
Derivatives financial instruments	**(2,403)**	(1,510)
Securities financing transactions (SFTs)	**112**	(441)
Loans and advances and other assets	**(142,955)**	(133,975)
Total deconsolidation adjustments	**(145,246)**	(135,926)
Derivatives adjustments		
Adjustment for regulatory netting	**(20,490)**	(16,419)
Adjustment for cash collateral	**(8,432)**	(6,464)
Net written credit protection	**699**	682
Regulatory potential future exposure	**13,188**	12,966
Total derivatives adjustments	**(15,035)**	(9,235)
SFT adjustments	**39**	3,361
Off-balance sheet items	**58,685**	56,424
Regulatory deductions and other adjustments	**(9,128)**	(9,112)
Total exposure	**707,108**	712,200
Leverage ratio[2]	**4.9%**	4.8%
Average leverage ratio[3]	**4.9%**	
Average leverage ratio exposure measure[4]	**718,926**	

[1] Deconsolidation adjustments predominantly reflect the deconsolidation of assets related to Group subsidiaries that fall outside the scope of the Group's regulatory capital consolidation (primarily the Group's Insurance entities).

[2] The countercyclical leverage ratio buffer is currently nil.

[3] The average leverage ratio is based on the average of the month end tier 1 capital and exposure measures over the quarter (30 September 2016 to 31 December 2016). The average of 4.9 per cent compares to 4.8 per cent at the start and 4.9 at the end of the quarter.

[4] The average leverage ratio exposure measure is based on the average of the month end exposure measures over the quarter (30 September 2016 to 31 December 2016).

Key movements

– The Group's fully loaded leverage ratio increased by 0.1 per cent to 4.9 per cent reflecting the impact of both the increase in tier 1 capital and the £5.1bn reduction in the exposure measure, the latter largely reflecting the reduction in liquid asset holdings.

– The derivatives exposure measure, representing derivative financial instruments per the balance sheet net of deconsolidation and derivatives adjustments, reduced marginally with market movements and trading activity broadly offset through netting and cash collateral inflows.

– The increase in SFT assets over the period, reflecting increased customer volumes, was offset by the reduction in SFT adjustments reflecting both the recognition of additional eligible netting adjustments and a reduction in the counterparty credit risk add-on.

– Off-balance sheet items increased by £2.3bn, primarily reflecting a change in the profile and subsequent classification of commercial off-balance sheet items and a net increase in securitisation financing facilities, partially offset by a planned drawdown on certain liquidity facilities supporting the Group's conduit programme to provide funding alongside the proceeds of the ABCP issuance.

– The average leverage ratio of 4.9 per cent over the quarter reflected a strengthening tier 1 capital position prior to the accrual for the announced full year special dividend and the reduction in balance sheet assets during the quarter, largely reflecting the reduction in liquid asset holdings.

Modified UK leverage ratio

The Group's leverage ratio on a modified basis, excluding qualifying central bank claims from the leverage exposure measure, is 5.2 per cent.

Events since the balance sheet date

On 2 March 2017 the Financial Conduct Authority confirmed that the deadline by which consumers will need to make their payment protection insurance (PPI) complaints will be 29 August 2019 and that the final rules and guidance that should apply when firms handle PPI complaints in light of the UK Supreme Court's decision in Plevin v Paragon Personal Finance Limited ([2014] UKSC 61) will come into force in August 2017. The Group has reassessed its provisioning for conduct charges in light of this guidance, leading to an additional charge of £350m.

The Group's Pillar 3 disclosures represent supplementary analysis of approved accounting statements and are therefore presented in line with the published Annual Report and Accounts for the year ended 2016 for Lloyds Banking Group. If the additional charge had been reflected, the Group's common equity tier 1 capital ratio at 31 December 2016 would have been 0.2 per cent lower at 13.4 per cent, the transitional tier 1 capital ratio 0.2 per cent lower at 16.8 per cent, the transitional total capital ratio 0.2 per cent lower at 21.2 per cent and the leverage ratio by 0.1 per cent lower at 4.8 per cent.

Pillar 1 Capital requirements: Overview of risk-weighted assets

This section details Lloyds Banking Group's risk-weighted assets and pillar 1 capital requirements.

– The risk-weighted assets movement table provides analysis of the reduction in risk-weighted assets in the period by risk type and an insight into the key drivers of the movements. The key driver analysis is compiled on a monthly basis through the identification and categorisation of risk-weighted asset movements and is subject to management judgment.

– Credit risk-weighted assets account for 77 per cent of fully loaded risk-weighted assets.

Table 6: Risk-weighted assets movement by key driver

	Credit Risk IRB £m	Credit Risk STA £m	Credit Risk Total[1] £m	Counterparty Credit Risk[2] £m	Market Risk £m	Operational Risk £m	Total £m
Fully loaded risk-weighted assets as at 31 December 2015							**222,747**
Less: total threshold risk-weighted assets[3]							**(10,690)**
Risk-weighted assets at 31 December 2015	**151,563**	**20,443**	**172,006**	**10,153**	**3,775**	**26,123**	**212,057**
Asset size	**(4,453)**	**(440)**	**(4,893)**	**(1,542)**	**(139)**	**–**	**(6,574)**
Acquisitions and disposals	**(3,406)**	**(435)**	**(3,841)**	**(183)**	**–**	**–**	**(4,024)**
Model updates	**4,363**	**–**	**4,363**	**99**	**(951)**	**–**	**3,511**
Methodology and policy	**(1,215)**	**(1,184)**	**(2,399)**	**–**	**–**	**–**	**(2,399)**
Asset quality	**(2,989)**	**(75)**	**(3,064)**	**729**	**(200)**	**–**	**(2,535)**
Movement in risk levels (Market risk only)	**–**	**–**	**–**	**–**	**662**	**–**	**662**
Foreign exchange	**3,802**	**647**	**4,449**	**367**	**–**	**–**	**4,816**
Other	**–**	**–**	**–**	**–**	**–**	**(831)**	**(831)**
Risk-weighted assets at 31 December 2016	**147,665**	**18,956**	**166,621**	**9,623**	**3,147**	**25,292**	**204,683**
Threshold risk-weighted assets[3]							**10,851**
Total risk-weighted assets as at 31 December 2016[4]							**215,534**

[1] Credit risk includes securitisation risk-weighted assets.

[2] Counterparty credit risk includes movements in contributions to the default fund of central counterparties and movements in credit valuation adjustment risk.

[3] Threshold risk-weighted assets reflect the element of significant investments and deferred tax assets that are permitted to be risk-weighted instead of being deducted from CET1 capital. Significant investments primarily arise from investments in the Group's Insurance business.

[4] At 31 December 2016 there was no difference between transitional and fully loaded risk-weighted assets.

Key movements

Movements in **credit risk-weighted assets** in the twelve months to 31 December 2016 were driven by the following:

– Asset size movements. Credit risk-weighted assets decreased by £4.9bn, primarily due to active portfolio management, partially offset by continued growth in targeted customer segments.

– Disposal of the Group's interest in strategic equity investments and other targeted disposals reduced credit risk-weighted assets by £3.8bn.

– Model update increases of £4.4bn were mainly related to the Mainstream and Buy to Let UK mortgage portfolios.

– Methodology and policy reductions of £2.4bn are principally due to securitisation activity.

– Asset quality movements capture movements due to changes in borrower risk, including changes in the economic environment. Net reductions in credit risk-weighted assets of £3.1bn primarily relate to model calibrations and a net change in credit quality, reflecting improvements in the economic climate, partially offset by increases in valuation of centrally held strategic equity investments.

– Foreign exchange movements reflect the depreciation of Sterling which has contributed to a £4.4bn increase in credit risk-weighted assets.

Counterparty credit risk assets decreased by £0.5bn mainly driven by increased capital relief from CVA related hedges, partially offset by increased trading activity, foreign exchange and yield curve movements.

Market risk-weighted assets reduced by £0.6bn due to a reduction in the Value-at-Risk multiplier, improvements to the VaR model and active portfolio management.

Operational risk-weighted assets reduced by £0.8bn due to the annual update of the income based TSA operational risk calculation.

Table 7: Overview of risk-weighted assets (OV1)

		2016 RWA £m	2015 RWA £m	2016 Minimum capital Requirements £m	2015 Minimum capital Requirements £m
1	**Credit risk (excluding counterparty credit risk)**	**162,650**	168,740	**13,012**	13,499
2	Of which standardised approach	**18,688**	20,443	**1,495**	1,635
3	Of which the foundation rating-based (FIRB) approach	**51,438**	54,596	**4,115**	4,368
4	Of which the retail IRB (RIRB) approach	**64,970**	63,912	**5,198**	5,113
	Of which corporates – specialised lending	**13,469**	14,394	**1,077**	1,152
	Of which non-credit obligation assets	**6,427**	5,502	**514**	440
5	Of which equity IRB under the simple risk -weight or the internal models approach	**7,658**	9,893	**613**	791
6	**Counterparty credit risk**	**9,623**	10,153	**770**	813
7	Of which marked to market	**7,552**	7,261	**604**	581
8	Of which original exposure	**–**	–	**–**	–
9	Of which the standardised approach	**–**	–	**–**	–
10	Of which internal ratings-based model method (IMM)	**–**	–	**–**	–
	Of which comprehensive approach for credit risk mitigation (for SFTs)	**712**	576	**57**	46
	Of which exposures to central counterparties (including trades, default fund contributions and initial margin)	**495**	632	**40**	51
12	Of which credit valuation adjustment (CVA)	**864**	1,684	**69**	135
13	**Settlement risk**	**–**	–	**–**	–
14	**Securitisation exposures in banking book[1]**	**3,971**	3,266	**318**	261
15	Of which IRB ratings-based approach (RBA)	**2,878**	2,379	**231**	190
16	Of which IRB supervisory formula approach (SFA)	**–**	–	**–**	–
17	Of which internal assessment approach (IAA)	**825**	887	**66**	71
18	Of which standardised approach	**268**	–	**21**	–
19	**Market risk**	**3,147**	3,775	**252**	302
20	Of which standardised approach	**352**	551	**28**	44
21	Of which internal model approaches	**2,795**	3,224	**224**	258
22	**Large exposures**	**–**	–	**–**	–
23	**Operational risk**	**25,292**	26,123	**2,023**	2,090
24	Of which basic indicator approach	**–**	–	**–**	–
25	Of which standardised approach	**25,292**	26,123	**2,023**	2,090
26	Of which advanced measurement approach	**–**	–	**–**	–
27	Amounts below the thresholds for deduction (subject to 250% risk weight)	**10,851**	10,788	**868**	863
28	Floor adjustment	**–**	–	**–**	–
29	**Total – transitional**	**215,534**	222,845	**17,243**	17,828

[1] Securitisations are shown separately within this table, however, are included within credit risk throughout the remainder of the disclosures.

A detailed analysis of the key movements in exposures and risk-weighted assets is provided in Table 22.

Pillar 1 Capital requirements: Overview of risk-weighted assets continued

DIVISIONAL RISK-WEIGHTED ASSETS

The risk-weighted assets of the divisions as at 31 December 2016 are presented in the table below.

Table 8: Divisional risk-weighted assets

	2016 Retail £m	2016 Commercial Banking £m	2016 Consumer Finance £m	2016 Central Items £m	2016 Run-off £m	2016 Total £m
CREDIT RISK						
Exposures subject to the IRB approach						
Foundation IRB approach						
Corporate – main	–	37,221	3,186	5	759	41,171
Corporate – SME	1	7,707	28	–	144	7,880
Corporate – specialised lending	–	2	–	–	–	2
Central governments and central banks	–	–	–	1,430	–	1,430
Institutions	–	639	67	251	–	957
Retail IRB approach						
Retail mortgages	32,102	2,481	1,380	–	3,587	39,550
of which: residential mortgages (SME)	166	2,481	15	–	–	2,662
of which: residential mortgages (non-SME)	31,936	–	1,365	–	3,587	36,888
Qualifying revolving retail exposures	3,756	–	8,317	–	–	12,073
Other SME	736	884	108	–	–	1,728
Other non-SME	–	–	11,618	–	–	11,618
Other IRB approaches[1]						
Corporate – specialised lending	–	12,867	–	–	600	13,467
Equities – exchange traded	–	–	–	1,336	1	1,337
Equities – private equity	–	3,813	–	682	414	4,909
Equities – other	–	–	–	1,383	30	1,413
Securitisation positions[2]	–	2,726	–	143	834	3,703
Non-credit obligation assets[3]	151	68	1,686	4,509	13	6,427
Total – IRB approach	36,746	68,408	26,390	9,739	6,382	147,665
Exposures subject to the standardised approach						
Central governments and central banks	–	–	–	–	–	–
Public sector entities	–	2	–	–	–	2
Multilateral development banks	–	–	–	–	–	–
International organisations	–	–	–	–	–	–
Institutions	1	7	22	86	1	117
Corporates	637	7,778	612	1,238	536	10,801
Retail	385	971	781	–	624	2,761
Secured by mortgages on immovable property	1,407	107	62	–	405	1,981
of which: residential property	1,404	107	62	–	405	1,978
of which: commercial property	3	–	–	–	–	3
Exposures in default	464	148	90	–	181	883
Exposures associated with particularly high risk	–	–	–	–	–	–
Covered bonds	–	–	–	–	–	–
Securitisation positions	–	268	–	–	–	268
Short-term Claims on institutions and corporates	–	–	–	–	–	–
Collective investment undertakings (CIUs)	–	–	–	45	–	45
Equity exposures	–	–	–	–	–	–
Other items[3]	96	517	589	755	141	2,098
Total – standardised approach	2,990	9,798	2,156	2,124	1,888	18,956
Total credit risk	39,736	78,206	28,546	11,863	8,270	166,621
Threshold – significant investments	–	–	–	8,392	–	8,392
Threshold – deferred tax	–	–	–	2,459	–	2,459
Total credit risk (transitional)	39,736	78,206	28,546	22,714	8,270	177,472

	2016 Retail £m	2016 Commercial Banking £m	2016 Consumer Finance £m	2016 Central Items £m	2016 Run-off £m	2016 Total £m
COUNTERPARTY CREDIT RISK						
IRB approach	–	7,245	–	446	–	7,691
Standardised approach	–	249	–	324	–	573
Central counterparties	–	155	–	–	–	155
Settlement risk	–	–	–	–	–	–
Contributions to the default fund of a central counterparty	–	340	–	–	–	340
Total counterparty credit risk	–	7,989	–	770	–	8,759
Credit valuation adjustment						
Standardised method	–	586	–	278	–	864
Total credit valuation adjustment	–	586	–	278	–	864
MARKET RISK						
Internal models approach	–	2,795	–	–	–	2,795
Standardised approach						
Interest rate position risk requirement	–	297	–	–	–	297
of which: specific interest rate risk of Securitisation positions	–	17	–	–	–	17
Equity position risk requirement	–	–	–	–	–	–
Foreign exchange position risk requirement	–	59	–	(4)	–	55
Commodity position risk requirement	–	–	–	–	–	–
Total market risk	–	3,151	–	(4)	–	3,147
OPERATIONAL RISK						
Standardised approach	15,498	6,057	3,504	–	233	25,292
Total operational risk	15,498	6,057	3,504	–	233	25,292
Total risk-weighted assets	55,234	95,989	32,050	23,758	8,503	215,534

Pillar 1 Capital requirements: Overview of risk-weighted assets continued

	2015 Retail £m	2015 Commercial Banking £m	2015 Consumer Finance £m	2015 Central Items £m	2015 Run-off £m	2015 Total £m
CREDIT RISK						
Exposures subject to the IRB approach						
Foundation IRB approach						
Corporate – main	–	39,297	2,907	5	796	43,005
Corporate – SME	27	8,570	16	–	202	8,814
Corporate – specialised lending	–	8	–	–	–	8
Central governments and central banks	–	–	–	1,347	–	1,347
Institutions	–	909	56	463	2	1,430
Retail IRB approach						
Retail mortgages	30,202	3,059	1,338	–	3,653	38,252
of which: residential mortgages (SME)	137	3,059	18	–	–	3,214
of which: residential mortgages (non-SME)	30,065	–	1,320	–	3,653	35,038
Qualifying revolving retail exposures	4,536	–	7,965	–	–	12,501
Other SME	633	1,077	97	–	–	1,807
Other non-SME	–	–	11,349	–	3	11,352
Other IRB approaches[1]						
Corporate – specialised lending	–	13,338	–	–	1,048	14,386
Equities – exchange traded	–	–	–	2,568	269	2,837
Equities – private equity	–	4,477	–	649	538	5,664
Equities – other	–	–	–	1,342	50	1,392
Securitisation positions[2]	–	2,052	–	181	1,033	3,266
Non-credit obligation assets[3]	109	73	1,396	3,912	12	5,502
Total – IRB approach	35,507	72,859	25,123	10,466	7,606	151,563
Exposures subject to the standardised approach						
Central governments and central banks	–	–	–	–	–	–
Public sector entities	–	2	–	–	–	2
Multilateral development banks	–	–	–	–	–	–
International organisations						
Institutions	1	3	19	–	1	24
Corporates	757	8,661	448	1,167	887	11,921
Retail	404	1,369	567	–	539	2,880
Secured by mortgages on immovable property	1,548	86	52	–	423	2,109
of which: residential property	1,545	58	52	–	423	2,078
of which: commercial property	3	28	–	–	–	31
Exposures in default	437	264	130	–	367	1,198
Exposures associated with particularly high risk	–	–	–	–	–	–
Covered bonds	–	–	–	–	–	–
Securitisation positions	–	–	–	–	–	–
Short-term Claims on institutions and corporates	–	–	–	–	–	–
Collective investment undertakings (CIUs)	–	–	–	–	–	–
Equity exposures	–	–	–	–	–	–
Other items[3]	135	361	593	1,099	120	2,309
Total – standardised approach	3,283	10,746	1,808	2,266	2,338	20,443
Total credit risk	38,791	83,606	26,933	12,732	9,944	172,006
Threshold – significant investments	–	–	–	7,817	–	7,817
Threshold – deferred tax	–	–	–	2,971	–	2,971
Total credit risk (transitional)	38,791	83,606	26,933	23,520	9,944	182,794

	2015 Retail £m	2015 Commercial Banking £m	2015 Consumer Finance £m	2015 Central Items £m	2015 Run-off £m	2015 Total £m
COUNTERPARTY CREDIT RISK						
IRB approach	–	7,152	–	176	–	7,328
Standardised approach	–	229	–	280	–	509
Central counterparties	–	144	–	–	–	144
Settlement risk	–	–	–	–	–	–
Contributions to the default fund of a central counterparty	–	488	–	–	–	488
Total counterparty credit risk	–	8,013	–	456	–	8,469
Credit valuation adjustment						
Standardised method	–	1,594	–	90	–	1,684
Total credit valuation adjustment	–	1,594	–	90	–	1,684
MARKET RISK						
Internal models approach	–	3,224	–	–	–	3,224
Standardised approach						
Interest rate position risk requirement	–	477	–	–	–	477
of which: specific interest rate risk of Securitisation positions	–	78	–	–	–	78
Equity position risk requirement	–	–	–	–	–	–
Foreign exchange position risk requirement	–	24	–	50	–	74
Commodity position risk requirement	–	–	–	–	–	–
Total market risk	–	3,725	–	50	–	3,775
OPERATIONAL RISK						
Standardised approach	15,841	6,263	3,769	–	250	26,123
Total operational risk	15,841	6,263	3,769	–	250	26,123
Total risk-weighted assets	54,632	103,201	30,702	24,116	10,194	222,845

[1] Credit risk exposures subject to other IRB approaches include corporate specialised lending exposures risk-weighted in accordance with supervisory slotting criteria, equity exposures risk-weighted in accordance with the Simple Risk Weight Method and securitisation positions risk-weighted in accordance with the IAA and the RBA.

[2] Securitisation positions exclude amounts allocated to the 1,250 per cent risk weight category. These amounts are deducted from capital, after the application of SCRAs, rather than being risk-weighted.

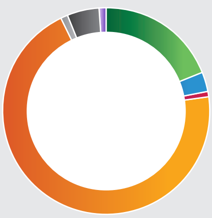
[3] Other items (Standardised approach) and non-credit obligation assets (IRB Approach) predominantly relate to other balance sheet assets that have no associated credit risk. These comprise various non-financial assets, including fixed assets, cash, items in the course of collection, prepayments and sundry debtors.

Pillar 1 Capital requirements: Credit risk

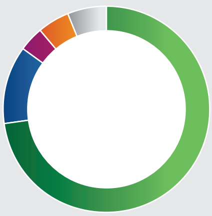
This section details Lloyds Banking Group's credit risk profile, focusing on regulatory measures such as exposure at default and risk-weighted assets.

- The Group's strategy remains focused on the UK, which generates over 85% of credit risk exposures.
- Credit risk exposures (excluding thresholds) decreased by 2% to £673.3bn, largely driven by active portfolio management and disposals, partially offset by foreign exchange movements and model updates.
- Of the Group's credit risk exposures, 83% (£561.8bn) are risk-weighted under the IRB approach, with the remainder (£111.5bn) risk-weighted using the Standardised approach.
- Total credit risk risk-weighted assets (excluding thresholds) decreased by 3% to £166.6bn, primarily due to active portfolio management disposals and securitisation activity, offset by foreign exchange movements and model updates.
- The Group's average risk weight for credit risk exposures (excluding thresholds) remained stable.
- During 2016 both expected losses and SCRAs have reduced by £0.7bn, largely as a result of active portfolio management and model updates. Excess expected loss has increased by £0.3bn, largely due to refinements to the PVA.
- The Group's models maintain a conservative approach, with the majority of predicted model outputs exceeding actual amounts observed in 2015.

IRB exposures



Standardised exposures



[1] Other includes regional governments or local authorities, public sector entities, multilateral development banks, institutions, exposures in default, securitisation positions and other balance sheet assets that have no associated credit risk.

Table 9: Risk-weighted assets flow statement of credit risk exposures (CR8)

		Credit Risk IRB RWA amount Total £m	Credit Risk IRB Capital requirements Total £m	Credit Risk SA RWA amount Total £m	Credit Risk SA Capital requirements Total £m
1	**Risk-weighted assets at 31 December 2015**	**151,563**	**12,125**	**20,443**	**1,635**
2	Asset size	**(4,453)**	**(356)**	**(440)**	**(35)**
3	Asset quality	**(2,989)**	**(239)**	**(75)**	**(6)**
4	Model updates	**4,363**	**349**	**–**	**–**
5	Methodology and policy	**(1,215)**	**(97)**	**(1,184)**	**(95)**
6	Acquisitions and disposals	**(3,406)**	**(272)**	**(435)**	**(35)**
7	Foreign exchange movements	**3,802**	**304**	**647**	**52**
8	Other	**–**	**–**	**–**	**–**
9	**Risk-weighted assets at 31 December 2016**	**147,665**	**11,814**	**18,956**	**1,516**

OVERVIEW

DEFINITION

Credit Risk is defined as the risk that parties with whom the Group has contracted fail to meet their financial obligations (both on or off balance sheet).

RISK APPETITE

The Group has a conservative and well balanced credit portfolio through the economic cycle.

EXPOSURES

The principal sources of credit risk within the Group arise from loans and advances, contingent liabilities, commitments, debt securities and equity to customers, financial institutions and sovereigns. Credit risk exposures are categorised as 'retail', arising primarily in the Retail, Consumer Finance and Run-off divisions, and some small and medium sized enterprises (SMEs) and 'corporate' (including larger SMEs, corporates, banks, financial institutions and sovereigns) arising primarily in Commercial Banking, Run-off and Group Corporate Treasury (GCT) divisions.

In terms of loans and advances (for example loans and overdrafts) and contingent liabilities (for example credit instruments such as guarantees and standby, documentary and commercial letters of credit), credit risk arises both from amounts advanced, and commitments to extend credit to a customer or bank.

With respect to commitments to extend credit, the Group is potentially exposed to loss in an amount equal to the total unused commitments. However, the likely amount of loss is less than the total unused commitments, as most retail commitments to extend credit may be cancelled and the creditworthiness of customers is monitored regularly. Most commercial term commitments to extend credit are contingent upon customers maintaining specific credit standards, which together with the creditworthiness of customers, are monitored regularly.

The credit risk exposures of the Group from a regulatory capital perspective, as defined by the CRR, are included throughout the Pillar 3 disclosures.

MEASUREMENT

In measuring the credit risk of loans and advances to customers and to banks at a counterparty level, the Group reflects three components:

(i) the PD by the counterparty on its contractual obligations;

(ii) current exposures to the counterparty and their likely future development, from which the Group derives the 'exposure at default' (EAD); and

(iii) the likely loss ratio on the defaulted obligations (the LGD).

For regulatory capital purposes the Group's credit risk exposures are primarily measured using Internal-Ratings Based systems approach, with the remainder measured under the Standardised approach. The Group's application of these approaches is explained in more detail on pages 35 to 37.

MONITORING

In conjunction with Risk Division, businesses identify and define portfolios of credit and related risk exposures and the key benchmarks, behaviours and characteristics by which those portfolios are managed and monitored. This entails the production and analysis of regular portfolio monitoring reports for review by senior management. Risk Division in turn produces an aggregated review of credit risk throughout the Group, including reports on significant credit exposures, which are presented to the Divisional Risk Committees, Group Risk Committee and the Board Risk Committee.

The performance of all rating models is monitored on a regular basis, as outlined on pages 39 and 40.

Further details are provided on pages 124 to 127 of the Risk Management section of the 2016 Lloyds Banking Group plc Annual Report and Accounts.

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Pillar 1 Capital requirements: Credit risk continued

CREDIT RISK MITIGATION

The Group uses a range of approaches to mitigate credit risk. For detailed information on approaches to mitigate credit risk, including details of the Group's policies and principles, see pages 124 and 125 of the 2016 Lloyds Banking Group plc Annual Report and Accounts.

EXPOSURES COVERED BY ELIGIBLE COLLATERAL, GUARANTEES AND CREDIT DERIVATIVES

Only certain types of collateral are deemed eligible for internal risk management and regulatory capital purposes. The recognition of eligible collateral requires a number of factors to be considered such as legal certainty of charge, frequency and independency of revaluation and correlation of the value of the underlying asset to the obligor.

COLLATERAL

The Group maintains appetite guidelines on the acceptability of specific classes of collateral.

Collateral held as security for financial assets other than loans and advances is determined by the nature of the underlying exposure. Debt securities including treasury and other bills, are generally unsecured, with the exception of asset-backed securities (ABS) and similar instruments such as covered bonds, which are secured by portfolios of financial assets. Collateral is generally not held against loans and advances to financial institutions, except where securities are held as part of reverse repurchase or securities borrowing transactions or where a collateral agreement has been entered into under a master netting agreement.

No collateral is held in respect of retail credit cards, overdrafts or unsecured personal lending. For non-mortgage retail lending to small businesses, collateral may include second charges over residential property and the assignment of life cover.

The additional mitigation for Retail and Consumer Finance and Commercial customers is explained in more detail on page 125 of the 2016 Lloyds Banking Group plc Annual Report and Accounts.

Where collateral is held, the eligible collateral for loans and advances and contingent liabilities is classified as either financial collateral or other collateral, as outlined below:

Eligible financial collateral

- Eligible financial collateral includes cash on deposit with the bank, gold, rated debt securities (subject to certain restrictions), equities or convertible bonds included in a main index and units in certain collective investment undertakings or mutual funds.
- The Group predominantly applies cash collateral to its corporate (IRB and Standardised) and institutions (IRB) exposures.
- For Standardised counterparty credit risk exposures, the Group largely applies cash collateral to its central government and central banks and institution exposures.

Other eligible collateral

- Real estate collateral includes charges over residential and commercial properties, for example, for the Group's mainstream mortgages.
- Other eligible collateral includes real estate, short term financial receivables, credit insurance, life policies and other physical collateral for example, motor cars in providing the criteria for eligibility are met.
- The Group largely applies other eligible collateral to the IRB corporate main, corporate SME and retail asset classes.

Collateral values are assessed at the time of loan origination. The Group requires collateral to always be realistically valued by an appropriately qualified source, independent of both the credit decision process and the customer, at the time of borrowing. In certain circumstances, for Retail residential mortgages this may include the use of automated valuation models based on market data, subject to accuracy criteria and loan to value limits. Collateral values are reviewed on a regular basis and will vary according to the type of lending, collateral involved and account performance. Such reviews are undertaken to confirm that the value recorded in the Bank's systems remains appropriate and whether revaluation is required, considering for example, account performance, market conditions and any information available that may indicate that the value of the collateral has materially declined. In such instances, the Group may seek additional collateral. For Retail residential mortgages, the Group adjusts open market property values to take account of the costs of realisation and any discount associated with the realisation of the collateral when estimating credit losses.

The Group considers risk concentrations by collateral providers and collateral type, as appropriate, with a view to ensuring that any potential undue concentrations of risk are identified and suitably managed by changes to strategy, policy and/or business plans.

Refer to page 126 of the Risk Management section and Note 52 (Financial Risk Management) of the 2016 Lloyds Banking Group plc Annual Report and Accounts for further information on collateral.

OTHER CREDIT RISK TRANSFERS

The Group also undertakes credit derivative based transactions as a means of mitigating or reducing credit risk, taking into account the nature of assets and the prevailing market conditions.

- Credit derivatives are a method of transferring credit risk from one counterparty (the protection buyer) to another (the protection seller). Capital relief under regulatory requirements is restricted to the following types of credit derivative: credit default swaps (CDS); total return swaps; and credit linked notes (CLN) (to the extent of their cash funding).
- The Group makes limited use of credit derivatives as credit risk mitigation from a capital perspective.
- Further details on the application within the Group are included within the Counterparty credit risk section of the document on page 89.

Guarantees

– In addition, guarantees from eligible protection providers including governments, institutions and corporates, can also provide regulatory capital relief, although there are minimum operational and legal requirements which must be met before reflecting the risk mitigating effect. On the basis that these requirements are met, alternative forms of protection, for example indemnities, may be classified as a guarantee for regulatory capital purposes. Export Credit agencies can provide risk mitigation in the form of a guarantee (typically up to 85% – 95% of a contract value) providing cover and guarantee of payment in relation to commercial and political risk.

– Regulatory capital relief is taken for guarantees provided by appropriate sovereigns, institutions or corporates, as well as for collateralised guarantees from corporates where available.

APPLICATION OF CREDIT RISK MITIGATION

The Group's application of different types of credit risk mitigation from a regulatory capital perspective is outlined below:

	Standardised		IRB		
	EAD	Other	EAD	LGD	PD
Eligible financial collateral					
trading book	✓		✓		
non-trading book	✓			✓	
Other eligible collateral					
real estate collateral[1]		✓		✓	✓
other physical collateral				✓	✓
credit insurance[2]		✓			✓
receivables	✓			✓	
life policies	✓			✓	
Credit derivatives[2]		✓			✓
Collateralised guarantees[2]		✓		✓	
Non collateralised guarantees[2]		✓			✓

[1] Real estate collateral determines the exposure class as explained below.

[2] As per application under the PD Substitution Approach, as explained below.

Application under the Standardised Approach

Where a credit risk exposure subject to the Standardised Approach is covered by a form of eligible financial collateral the EAD value is adjusted accordingly under the Financial Collateral Comprehensive Method (FCCM) applying adjustments for volatility and currency mismatch, in addition to maturity mismatches for all collateral types.

For unfunded credit protection, for example where guarantees or credit derivatives apply, the exposure class and therefore risk weight applied to the portion of the exposure covered by the protection provider is based on the exposure class of the provider, referred to as the Substitution Approach. The covered portion is determined after the application of 'haircuts' for currency and maturity mismatch applied to the protection provided. The risk weight applied to the uncovered portion of the exposure is not impacted.

Real estate collateral does not impact EAD directly under the Standardised Approach, however, it instead determines the exposure class and directly impacts the risk-weight applied to the exposure.

The use of credit derivatives and collateral in respect of securitisation and counterparty credit risk exposures are discussed further within the Securitisation and Counterparty credit risk section of the document.

Collateral may also be used as an input for modelling SCRAs against exposures, which will also indirectly reduce the EAD for exposures subject to the Standardised Approach.

Application under the IRB approach

In recognising eligible financial collateral under the FIRB Approach, the Group adjusts the relevant LGD value in accordance with the application of the FCCM, applying adjustments for volatility and currency mismatch, in addition to maturity mismatches for all collateral types.

Other eligible collateral, collateralised guarantees and real estate collateral applied under the FIRB Approach will typically result in an adjustment to the regulatory LGD value, subject to floors as prescribed in the CRR. The adjustment applied is dependent on the value and type of collateral used.

Where appropriate guarantees or credit derivatives apply, the PD applied to the portion of the exposure covered by the protection provider is based on the PD of the provider, referred to as the PD substitution approach. The covered portion is determined after the application of 'haircuts' for currency and maturity mismatch applied to the protection provided. The PD applied to the uncovered portion of the exposure is not impacted.

Under the Retail IRB Approach, own estimates of LGD are used, taking into account eligible collateral, including real estate collateral or other physical collateral, among other factors. As well as impacting LGD, real estate collateral may also influence a counterparty's PD under the Retail IRB approach in certain cases, for example, for residential mortgages.

Pillar 1 Capital requirements: Credit risk continued

ANALYSIS OF CREDIT RISK MITIGATION

The following tables provide an analysis of FIRB Approach, IRB Supervisory Slotting Approach and Standardised Approach credit risk exposures covered by eligible financial collateral, other eligible collateral, guarantees or credit derivatives.

The analysis excludes exposures covered by forms of credit risk mitigation that do not provide own estimates of LGDs or conversion factors.

Table 10: Eligible financial collateral and other eligible collateral

	2016 Exposures covered by eligible financial collateral £m	2016 Exposures covered by other eligible collateral £m	2016 Total £m	2015 Exposures covered by eligible financial collateral £m	2015 Exposures covered by other eligible collateral £m	2015 Total £m
Exposures subject to the IRB approach						
Foundation IRB approach						
Corporate – main	1,225	8,970	10,195	1,244	8,698	9,942
Corporate – SME	8	7,363	7,371	9	7,422	7,431
Institutions	902	–	902	536	–	536
Other IRB approach						
Corporate – specialised lending	845	–	845	837	–	837
Total – IRB approach	2,980	16,333	19,313	2,626	16,120	18,746
Exposures subject to the standardised approach						
Corporates	855	5	860	937	4	941
Institutions	47	–	47	62	–	62
Exposures in default	–	6	6	–	10	10
Total – standardised approach	902	11	913	999	14	1,013
Total	3,882	16,344	20,226	3,625	16,134	19,759

Unfunded credit protection: Guarantees and credit derivatives

Protection provider	2016 Credit protection provided in the form of guarantees £m	2016 Credit protection provided in the form of credit derivatives £m	2016 Total £m	2015 Credit protection provided in the form of guarantees £m	2015 Credit protection provided in the form of credit derivatives £m	2015 Total £m
Exposures subject to the IRB approach						
Corporate – main	352	–	352	220	–	220
Central governments and central banks	–	–	–	–	–	–
Institutions	24	143	167	–	34	34
Total – IRB approach	376	143	519	220	34	254
Exposures subject to the standardised approach						
Corporates[1]	218	–	218	–	–	–
Central governments and central banks	280	–	280	90	–	90
Total – standardised approach	498	–	498	90	–	90
Total	874	143	1,017	310	34	344

[1] 2015 restated to exclude credit protection relevant to CCR exposures only.

Further details on collateral held as security for financial assets, collateral pledged as security and collateral repossessed can be found in Note 52 (Financial risk management) of the 2016 Lloyds Banking Group plc Annual Report and Accounts.

REGULATORY APPROACH TO CREDIT RISK
EXPOSURES SUBJECT TO THE STANDARDISED APPROACH

Under CRD IV, the Standardised Approach relies on the application of a prescribed set of risk weights to credit risk exposures, dependant on a number of factors including the applicable asset class and underlying credit quality.

The Standardised Approach takes account of credit risk mitigation and specific credit risk adjustments that the Group has against an exposure, before the relevant risk weight is applied to the adjusted exposure amount. Unlike exposures modelled using the Group's internal ratings, there is no distinction made between expected and unexpected losses for exposures on the Standardised Approach.

Under this approach banks can utilise risk assessments from External Credit Assessment Institutions (ECAIs) for a number of exposure classes that cover loaded counterparties, including corporates, central governments and central banks and institutions. Where a credit assessment is used this must be provided by an eligible ECAI from the PRA's approved list. The appropriate risk weight to apply to the credit risk exposure is determined by assigning the exposure to the relevant credit quality step under CRD IV, based on the PRA's mapping of credit assessments to credit quality steps as detailed under policy statement PS07/13.

The Group makes limited use of ECAIs assessments for its Standardised exposures. This typically applies in the case of certain central government and central bank and institution exposures. The Group makes use of credit assessments provided by Standard & Poor's, Moody's and Fitch. Where there are no available credit assessments to utilise, risk weights are assigned to these exposures in accordance with CRD IV requirements for unrated exposures.

Within the Group, the Standardised Approach is applied to portfolios that are either on the Group's roll-out plan or are permanently exempt from the IRB approach under the terms of the Group's IRB Waiver permission. The IRB Roll-out is now largely complete with only a small number of portfolios remaining on roll-out or deferred review. Little movement in the roll-out position is expected in 2017. The most significant portfolio on permanent exemption relates to sovereign exposures within the UK and EEA. The Group's permanent exemption list together with the IRB roll-out plan are reviewed on a regular basis internally and by the PRA.

Table 37 on page 71 indicates the respective risk weights applied to credit risk exposures subject to the Standardised Approach, by asset class, together with the associated exposure.

EXPOSURES SUBJECT TO THE INTERNAL RATINGS BASED APPROACH

There are two main IRB approaches for corporate exposures: Foundation IRB (FIRB) and Advanced IRB (AIRB). For Retail exposures, the Retail IRB (RIRB) Approach is available.

For all approaches, firms are required to use their own internal assessment of counterparty PDs. In addition, firms applying the AIRB and/or RIRB approaches are required to use internal assessments of EAD and LGD parameters. Firms applying the FIRB approach use EAD and LGD parameters set by the regulator.

The PD, LGD and EAD of an exposure form the base inputs to the calculation used to derive the risk-weighted assets and Expected Loss (EL) of that exposure. Where EL exceeds SCRAs linked to the underlying credit risk exposures the resultant excess expected loss (EEL) is deducted from capital resources. Where SCRAs exceed ELs, a 'surplus provision' may be recognised in T2 capital subject to certain restrictions. Further information on the comparison of EL and SCRA, which form the calculation of Excess EL can be found on page 50.

Pillar 1 Capital requirements: Credit risk continued

INTERNAL RATING SCALES

Within the Group, PD internal rating scales are used in assessing the credit quality of the FIRB and Retail IRB portfolios. Two master scales are used for reporting purposes within the business – a Corporate Master Scale which covers all relevant corporate, central government and central bank and institution portfolios and a Retail Master Scale which covers all relevant retail portfolios.

PD master scales

Table 11: Internal Corporate master scale

In commercial portfolios the PD models segment counterparties into a number of rating grades, with each grade representing a defined range of default probabilities, and there are a number of different model rating scales. Counterparties/exposures migrate between rating grades if the assessment of the PD changes. The modelled PDs 'map' through local scales to a single Corporate (non-retail) master scale comprising of 19 non-default ratings. Together with four default ratings the Corporate master scale forms the basis on which internal reporting is completed. These ratings scales can also be mapped to External Ratings as shown below.

	Range			
PD Grades	Lower	Mid	Upper	External S&P Rating (Approximate Equivalent)
1-4	0.000%	0.018%	0.035%	AAA to AA-
5	0.036%	0.043%	0.050%	A+
6	0.051%	0.060%	0.080%	A
7	0.081%	0.110%	0.140%	A-
8	0.141%	0.180%	0.220%	BBB+
9	0.221%	0.280%	0.340%	BBB
10	0.341%	0.420%	0.500%	BBB-
11	0.501%	0.630%	0.760%	BB+
12	0.761%	1.000%	1.240%	BB
13	1.241%	1.620%	2.000%	BB-
14	2.001%	2.600%	3.200%	B+
15	3.201%	4.200%	5.200%	B+
16	5.201%	6.200%	7.200%	B
17	7.201%	8.700%	10.200%	B-
18	10.201%	12.000%	13.800%	B-
19	13.801%	31.000%	99.999%	CCC to C
20 – 23 (Default)	100.000%	100.000%	100.000%	Default

Table 12: Internal Retail master scale

In the principal retail portfolios, EAD and loss given default models are also in use. For reporting purposes, customers are segmented into a number of rating grades, each representing a defined range of default probabilities and exposures migrate between rating grades if the assessment of the counterparty PD changes. The Retail master scale comprises 13 non-default ratings and 1 default rating.

	Range		
PD Grades	Lower	Mid	Upper
0	0.000%	0.050%	0.100%
1	0.101%	0.251%	0.400%
2	0.401%	0.601%	0.800%
3	0.801%	1.001%	1.200%
4	1.201%	1.851%	2.500%
5	2.501%	3.501%	4.500%
6	4.501%	6.001%	7.500%
7	7.501%	8.751%	10.000%
8	10.001%	12.001%	14.000%
9	14.001%	17.001%	20.000%
10	20.001%	25.001%	30.000%
11	30.001%	37.501%	45.000%
12	45.001%	72.500%	99.999%
Default	100.000%	100.000%	100.000%

SCOPE OF THE IRB PERMISSION

The Group has regulatory approval, subject to annual Capital Requirements Regulation (CRR) attestations, to use its internal models in the calculation of the majority of its credit risk capital requirements. The Group currently has permission to use both the FIRB Approach (for corporate exposures) and the RIRB Approach (for retail exposures).

The Group applies the Supervisory Slotting Approach to certain corporate specialised lending exposures (including the Group's commercial real estate exposures) and applies the Simple Risk Weight Method to equity exposures. Securitisation positions are predominantly risk-weighted under the RBA, with some use made of the IAA and SA.

Under the Group's IRB rating permission, the following list comprises the models (excluding those on the Supervisory Slotting and Simple Risk Weight approaches) that could be viewed as significant at a group level, each having risk-weighted assets in excess of £2.5bn (based on RWA figures in the CRR attestation, June 2016). This is a reduction on last year's "threshold" and has been prompted by a desire to have a greater RWA coverage in the PD backtesting analysis later in this section; the models listed here are the same ones reported in the PD backtesting analysis with the exception of PELF.

Approach	Basel asset class	Ratings system	Associated portfolio (risk-weighted assets)	Model type
FIRB	Corporate main, Corporate SME	Unquoted	>£15bn	PD
FIRB	Corporate main	Publicly quoted	>£15bn	PD
RIRB	Retail mortgages	HBOS and Lloyds mainstream mortgages[1,2]	>£15bn	PD, EAD, LGD
FIRB/RIRB	Corporate SME, Retail SME and Retail mortgages	Business Dynamic Credit Scoring (BDCS)[3]	£5bn – £10bn	PD, EAD, LGD
RIRB	Retail other	HBOS and Lloyds Bank personal loans[1]	£5bn – £10bn	PD, EAD, LGD
RIRB	Qualifying revolving retail exposure	HBOS and Lloyds Bank credit cards[1]	£5bn – £10bn	PD, EAD, LGD
RIRB	Retail mortgages	Buy-to-Let mortgages	£5bn – £10bn	PD, EAD, LGD
RIRB	Retail mortgages	Self Cert mortgages	£2.5bn – £5bn	PD, EAD, LGD
RIRB	Retail mortgages	BOS Ireland mortgages	£2.5bn – £5bn	PD, EAD, LGD
RIRB	Qualifying revolving retail exposure	HBOS and Lloyds Bank personal current accounts[1]	£2.5bn – £5bn	PD, EAD, LGD
FIRB	Corporate main	Private Equity & Loan Fund (PELF)	£2.5bn – £5bn	PD
FIRB	Corporate main	Consumer Finance Motor (Non-Retail)	£2.5bn – £5bn	PD
RIRB	Retail other	Consumer Finance Motor (Retail)	£2.5bn – £5bn	PD, EAD, LGD

[1] Separate rating systems exist for Lloyds and HBOS; but as the risk profiles and models used are very similar, they are grouped together in this table.

[2] Lloyds Bank Mortgages comprises three rating systems - Lloyds Mainstream Mortgages, Lloyds Near-Mainstream Mortgages and Lloyds Buy-to-Let Mortgages.

[3] There is a very small element of Corporate Main under the BDCS model.

Further details on other areas such as the Supervisory Slotting Approach for Corporate Specialised Lending exposures, Simple Risk Weight Method for Equities and various approaches for Securitisations can be found in the relevant sections later in the document.

DISTRIBUTION OF EXPOSURES BY APPROACH

To show the degree to which IRB models are used within the bank, the table below shows the EAD split between RIRB, FIRB and Standardised approaches across the different Basel asset classes for which IRB models are in place. Exposures presented in the table below are in line with Table 22, and are on a pre CRM and post CCF basis.

<table>
<tr><th></th><th>RIRB
£m</th><th>FIRB
£m</th><th>Standardised
£m</th></tr>
<tr><td>Corporate</td><td></td><td>90,508</td><td>13,511</td></tr>
<tr><td>Central governments and central banks</td><td></td><td>15,153</td><td>81,021</td></tr>
<tr><td>Institutions</td><td></td><td>6,011</td><td>279</td></tr>
<tr><td>Retail mortgages</td><td>335,510</td><td></td><td rowspan="4">4,114</td></tr>
<tr><td>Retail – Qualifying revolving retail exposures</td><td>36,984</td><td></td></tr>
<tr><td>Retail – Other SME</td><td>2,445</td><td></td></tr>
<tr><td>Retail – Other (non-SME)</td><td>16,026</td><td></td></tr>
<tr><td>Total</td><td>390,965</td><td>111,672</td><td>98,925</td></tr>
<tr><td>% coverage</td><td>65%</td><td>19%</td><td>16%</td></tr>
</table>

The IRB Roll-out is now largely complete with only a small number of portfolios remaining on roll-out or subject to deferred review.

Pillar 1 Capital requirements: Credit risk continued

KEY CHARACTERISTICS OF MATERIAL GROUP RATINGS SYSTEMS

PD Rating Philosophy

PD ratings generally adhere to either 'Point-in-time' (PIT) or 'Through-the-cycle' (TTC) rating approaches.

– For retail QRRE, Consumer Finance Motor (Retail) and Retail Other, PD ratings are constructed on a PIT basis. For all PIT PD ratings within Retail, a PD 'buffer' is added to the pure PIT PD to cover potential underestimation of default risk between regular calibrations.
– Retail mortgages use a TTC approach where this is available (Lloyds and Halifax Mainstream) and a PIT approach otherwise.
– Commercial Banking PD models are largely calibrated to a long-run of default experience, meaning the PD predictions are TTC in nature. The one exception is BDCS which is PIT.

With the exception of the UK mortgage portfolios, models use a 90 days-past-due backstop; UK mortgage portfolios (except Scottish Widows bank) use a 180 days-past-due backstop. Unlikeliness to pay triggers vary by portfolio.

The PD models are all 'bottom up' style models, based on a number of counterparty-specific or account-specific factors. In Retail portfolios this includes application and behavioural scorecards; in commercial portfolios this includes counterparty quantitative (eg financial) and qualitative (eg assessment of management) factors.

All of the Group's LGD and EAD models are calibrated on a downturn basis. Precise details vary by portfolio and are dependent upon the availability of downturn data.

Data history

The Group always seeks to use the longest history of available representative data when building its capital models:

– Mortgage models are built on data dating back to 1987
– Credit card models are built on data dating back to 2002
– Personal loans models are built on data dating back to 2002
– Personal current accounts are built on data dating back to 2002
– Unquoted companies models use data dating back to 2002
– Publicly quoted companies model uses data dating back to 2004
– PELF model uses data dating back to 2008
– Consumer Finance Motor (Retail) model uses data back to 2002
– Consumer Finance Motor (Non-Retail) model uses data back to 2008

When default volumes are sufficient, the Group's PD models are built using logistic regression. Where historical default volumes are low, alternative approaches are used; in the case of the publicly quoted model, a ratings replication approach has been taken, while the PELF model is designed to align to the rank-order assessment of default risk by portfolio experts, thus providing consistency in rating assessments.

INTERNAL DEVELOPMENT AND MONITORING OF IRB MODELS

Model Development and Review

Risk models (including all IRB models), and subsequent changes, are generally developed using internal data and standard statistical techniques by the relevant business area modelling teams on behalf of the business area. The models are challenged, both technically and from a business usage perspective, by an independent 'second line' unit (Risk Model Approval Team) which reports through an independent reporting line within the Risk division.

The Group's most material models are approved and monitored by the Group Risk Committee (GRC). GRC is the most senior executive risk committee in the Group, and its membership includes the Chief Financial Officer and the Chief Risk Officer, as well as representation from each division of the Group.

Lower materiality models are approved and monitored by the Model Governance Committee (MGC). MGC has delegated approval responsibility from GRC. MGC attendees include senior risk and business model owners responsible for the model under consideration.

Once a model has been approved, it is subject to ongoing monitoring and periodic validation requirements.

Where appropriate, typically where there is a regulatory requirement and/or where model weaknesses are observed, additional conservatism is applied to ensure capital adequacy. All new IRB models and all material model changes are subject to governance in line with regulatory guidance from the EBA and PRA. If a model or data weakness is identified that indicates the understatement of capital, the capital requirements are adjusted, on a temporary and immediate 'post model adjustment' basis, until the model is remediated to correct for the underlying weakness. All adjustments are subject to model governance and are shared with the regulator.

Relationships between risk management function and internal audit function

Group Audit (the 'third line' of defence) check that appropriate controls and processes are in place and operating effectively, across all aspects of capital models. Group Audit is independent from the first and second lines of defence, reporting through to the Group Audit Director, a Group Executive Committee attendee.

A summary of how GRC, MGC and the three lines of defence (business area modelling teams; Risk Model Approval Team; and Group Audit) fit in the overall corporate governance framework is given in the 2016 Lloyds Banking Group plc Annual Report & Accounts on pages 119 and 120.

Scope and main content of risk model reporting

A hierarchy of reporting exists for all risk models – detailed regular technical risk model performance (including rank ordering and predictive accuracy) is used to prioritise both model changes and corrective action for model underperformance. This is supplemented by more summarised half-yearly reporting to MGC and GRC. Half-yearly reporting of the most material models is provided to GRC with a broader model update (which includes all models) provided to GRC annually. Risk model reporting is also provided to the PRA on a regular basis.

Given the overarching governance framework, which is applied to exposures under each asset class, the risk model management information produced, and the effective controls and processes in place, the Group is comfortable that risk model performance is sufficient to ensure Pillar 1 capital requirements adequately reflect the Group's risk exposure.

OTHER APPLICATION OF IRB MODEL OUTPUTS

In addition to the regulatory capital calculation process, IRB models are also used for other purposes within the Group for example:

Credit approval: IRB models are strongly linked to the credit approval process, though the precise nature differs between asset classes. For retail exposures, operational, application and behavioural scorecards (primarily used to make retail credit approval and account management decisions) are key components of the PD. For corporate exposures, the PD model ascribes a credit risk grade to each customer and their exposures and this grade is used as a key input into the credit approval process.

Credit portfolio reporting and risk appetite: IRB parameters are embedded into management information at both Group and Divisional levels and are used to inform the setting of risk appetite.

Pricing: IRB outputs are used within pricing tools in the business to allow for risk-adjusted pricing and strategy decisions.

Calculating impairment: The calculation of impairment levels within each portfolio is subject to rigorous challenge and oversight from both Finance and Risk. In a limited number of instances IRB model outputs are used to inform the impairment provisioning process or as direct inputs to impairment models.

Stress Testing: IRB models are used within various stress testing exercises.

MODEL PERFORMANCE

This section splits into two parts. The first section provides an analysis of the performance of IRB models over the period 2014-2016. The second section focusses on the backtesting of PD models.

Summary Performance of IRB Models

The scope of this section includes all models using an RIRB or FIRB approach. In terms of risk metrics, the results show the predicted and actual PD, LGD, and EAD ratio (ratio of predicted to actual) by exposure class. No LGD or EAD information is provided for exposures modelled under the FIRB Approach since these are determined by regulatory values.

The calculations for PD consider the portfolio of non-defaulted accounts at the start of the period and compare the default level experienced during the year to the default level predicted by the Group's IRB models at the start of the period.

The calculations for LGD consider the set of obligors who have defaulted during the year and compare the loss level experienced on these accounts with the amounts predicted by the Group's IRB models at the start of the period. For those assets where losses are not yet realised the determination of actual LGD includes estimates of future recoveries.

For the purposes of comparison, EAD weighting has been used throughout. This approach can be sensitive to small numbers of high value defaults.

The calculation for the EAD ratio consider the set of defaulted accounts during the relevant period and compares the realised EAD for these accounts with the amounts predicted by the Group's IRB models at the start of the period. Where the predicted EAD was greater than the actual exposure on the date of default, the ratio will be greater than 100%.

Care should be taken in interpreting the predicted to actual ratios:

– 'Actual' (i.e. observed default and loss) outcome data is by its nature PIT and reflects the experience during a given year, whereas some model 'predicted' outputs are 'through-the-cycle' or 'downturn'. The gap between 'predicted' and 'actual' outcomes will therefore narrow or widen to reflect the current position in the economic cycle.

– PD models are built on an 'account-weighted' (rather than 'EAD weighted') basis meaning that comparisons across portfolios can be skewed.

– Changes in portfolio composition and client exposure can affect 'actual' observed defaults over the course of a year, but will not adjust the 'predicted' factors at the start of an outcome period.

– Data can also be impacted by small numbers of defaulted counterparties with relatively larger EAD values. This has been identified in a few portfolios over time.

Pillar 1 Capital requirements: Credit risk continued

MODEL PERFORMANCE DATA

Table 13: Model performance

IRB Exposure Class	Probability of default Predicted Dec 15 %	Probability of default Actual Dec 16 %	Loss given default of defaulted assets Predicted Dec 15 %	Loss given default of defaulted assets Actual Dec 16 %	EAD of defaulted assets Ratio of predicted to actual %
Central governments and central banks	0.05%	0.00%			
Institutions	0.21%	0.35%			
Corporate – total	0.69%	0.84%			
Retail – mortgage total	1.36%	0.77%	13.71%	4.86%	103%
Retail – SME	2.79%	1.67%	78.27%	72.61%	102%
Retail – Qualifying Revolving Retail Exposure (QRRE)	1.63%	1.31%	80.44%	60.10%	109%
Retail – other non-SME	2.65%	2.31%	70.01%	56.68%	111%

IRB Exposure Class	Probability of default Predicted Dec 14 %	Probability of default Actual Dec 15 %	Loss given default of defaulted assets Predicted Dec 14 %	Loss given default of defaulted assets Actual Dec 15 %	EAD of defaulted assets Ratio of predicted to actual %
Central governments and central banks	0.02%	0.00%			
Institutions	0.17%	0.00%			
Corporate – total	0.82%	0.70%			
Retail – mortgage total	1.48%	0.86%	13.98%	5.46%	103%
Retail – SME	3.20%	2.01%	68.19%	60.06%	101%
Retail – Qualifying Revolving Retail Exposure (QRRE)	1.96%	1.45%	80.26%	63.80%	112%
Retail – other non-SME	3.26%	2.46%	74.74%	62.29%	110%

IRB Exposure Class	Probability of default Predicted Dec 13 %	Probability of default Actual Dec 14 %	Loss given default of defaulted assets Predicted Dec 13 %	Loss given default of defaulted assets Actual Dec 14 %	EAD of defaulted assets Ratio of predicted to actual %
Central governments and central banks	0.02%	0.00%			
Institutions	0.21%	0.00%			
Corporate – total	0.99%	1.06%			
Retail – mortgage total	1.76%	1.04%	14.87%	7.42%	103%
Retail – SME	3.92%	2.69%	62.32%	58.35%	107%
Retail – Qualifying Revolving Retail Exposure (QRRE)	2.40%	1.85%	80.03%	68.08%	113%
Retail – other non-SME	4.26%	3.45%	78.52%	66.64%	109%

Key movements

The Group seeks to develop models which maintain a conservative approach overall. Specific comments are as follows:

- Within the Corporate asset class, PD estimates have fallen, reflecting improved credit quality within the portfolio. Single, large value defaulting exposures drive the PD under-prediction observed in the Institutions and Corporate asset classes. On an obligor weighted basis, the Corporate and Institution asset class predictions exceed actual default rates.
- For all Retail exposure classes the predicted and actual default rates have fallen in 2016. This reflects generally favourable economic conditions and improving credit quality.
- Predicted PD values exceeded actual default rates for all Retail portfolios in 2016 reflecting a mix of conservatism within the models and lower than expected default rates.
- For mortgages, actual LGDs have reduced further due to favourable movements in house prices. Actual LGDs remain well below Predicted LGDs due to the regulatory downturn calibration of the latter.
- EAD ratios within the Retail business are broadly consistent with 2015.

Backtesting of PD Models

This section focusses on the backtesting of PD models. The information in the following tables is based on the key portfolios noted earlier in this section with the exception of PELF. While PELF has risk-weighted-assets marginally above the threshold of £2.5bn, it has had no defaults over the three year period and hence its inclusion in a table would have limited value.

In line with EBA guidance this information is aggregated to Basel asset class, with exposures assessed under RIRB and FIRB shown in separate tables.

All tables follow the same format and adopt the following definitions:

- The PD ranges are the respective Retail and Commercial internal master scales.
- The external rating equivalent is the equivalent S&P rating described on page 36.
- The weighted average PD is based on the regulatory PD (within that risk grade) at the start of the period. The weighting is based on the EAD at the start of the period.
- The arithmetic average PD is based on the regulatory PD at the start of the period. This PD is volume weighted.
- The number of obligors is shown at the beginning and end of the period. This represents the full book position at both points, with new obligors (opened during the period) included in the end of year position (if still on book). Obligors that left during the year are not included in the end of year position. Various definitions of obligor operate within the bank, reflecting how the exposures are managed within each area. Exposures that are 'connected' and share the same PD are classed as a single Obligor. This translates as follows:
  - **Retail Unsecured** aggregates at customer level within brand and product (an obligor's accounts are aggregated if they share the same brand and product).
  - **Retail Secured** and **Consumer Finance Motor (Retail Other)** is based on account level. An obligor with two accounts would have two PDs.
  - The **Commercial Banking** and **Consumer Finance Motor (Non-Retail)** definition is essentially legal entity by source system. This means that one legal entity might be represented by one or more obligors in the data if that entity has borrowing across one or more business.
- The number of defaults during the year is the total number of non-defaulted obligors at the start of the year that subsequently defaulted at any point in the following 12 months. The allocation to a risk grade is based on the regulatory PD at the start of the year. Exposures opened during the year are not included.
- 'Defaulted obligors – new exposures' relates to obligors that opened during the year and subsequently defaulted. Only one figure is provided within this column and this is assigned to the row 'New to Book'. This figure is currently unavailable for the Corporate SME and Corporate Main tables.
- The average default rate is calculated as a simple (volume weighted) average of 5 annual default rates. As some models were implemented less than 5 years ago and in a desire for broad consistency in the mix of obligors within the asset class, some tables are based on 3 or 4 years rather than 5 years of data.

For each table, a risk-weighted-asset coverage per cent is shown. This represents the proportion of the total (not in default) IRB RWA within that Basel asset class that is covered by the backtesting analysis. For example, a figure of 95% would indicate that 5% of the IRB RWA for that Basel asset class has not been included – the 5% would relate to models not classed as significant.

The primary benefit of these tables is that they enable a comparison of predicted PD with actual default rate over both the short-term (12 months) and medium-term (3-5 years). When making this comparison, care needs to be taken with the interpretation as the result is partially dependent on the choice of PD approach (PIT or TTC).

As the PD backtesting tables have to be collated at Basel Asset Class level, the link between the Basel asset class and key rating systems has been summarised in the following table. All rating systems have been restricted to UK exposures only with the exception of Ireland Mortgages and Publicly Quoted which is a global model.

Basel Asset Class	Rating Systems Included
Corporate Main	Publicly quoted, Unquoted, Consumer Finance Motor (Non Retail)
Corporate SME	Unquoted, Publicly quoted, BDCS
Retail – Mortgages (UK)	HBOS and Lloyds mainstream mortgages, Buy-to-Let mortgages, Self-Cert mortgages, BDCS
Retail – Mortgages (Other)	Ireland mortgages
Retail SME	BDCS
Retail QRRE	Credit Cards and Personal Current Accounts
Retail Other – non SME	Personal Loans and Consumer Finance Motor (Retail)

There are no significant rating systems which contribute to either Institutions or Central Governments and Banks and hence no backtesting results are shown for these Basel asset classes.

Pillar 1 Capital requirements: Credit risk continued

In the following backtesting tables the results are based on the key rating systems shown in the table on page 41. Against each table we show the RWA coverage (RWA within the table as a proportion of total IRB RWA for that asset class). As these tables are based on key rating systems only, the number of obligors may not reconcile fully with figures shown elsewhere in this document.

Table 14A: Back-testing of PD per portfolio – Mortgages (CR9)

RWA coverage: 95-99%

PD Range	Weighted average PD	Arithmetic average PD by obligors	Number of obligors End of previous year	Number of obligors End of the year	Defaulted obligors in the year	of which: new defaulted obligors in the year	Average historical annual default rate
0.00 - 0.10%	0.21%	0.18%	1,621,780	1,758,967	546	N/a	0.07%
0.10 - 0.40%	0.55%	0.53%	1,020,545	809,952	1,769	N/a	0.25%
0.40 - 0.80%	1.30%	1.35%	168,205	150,359	1,007	N/a	0.60%
0.80 - 1.20%	2.07%	2.19%	51,920	38,058	546	N/a	0.96%
1.20 - 2.50%	4.50%	4.54%	65,217	54,080	1,106	N/a	1.63%
2.50 - 4.50%	7.42%	7.72%	35,963	28,675	1,309	N/a	2.78%
4.40 - 7.50%	11.90%	12.30%	20,922	17,993	1,283	N/a	4.59%
7.50 - 10.00%	17.15%	17.73%	8,690	7,322	803	N/a	7.31%
10.00 - 14.00%	19.25%	19.67%	8,971	7,528	963	N/a	9.27%
14.00 - 20.00%	30.25%	31.25%	8,981	6,189	1,746	N/a	14.52%
20.00 - 30.00%	42.46%	43.42%	5,299	5,395	1,681	N/a	22.82%
30.00 - 45.00%	52.53%	53.13%	5,571	5,986	2,323	N/a	34.17%
45.00 -99.99%	73.51%	73.92%	6,061	7,103	3,769	N/a	54.79%
In Default	100.00%	100.00%	32,217	31,567	N/a	N/a	N/a
New to Book	N/a	N/a	–	234,982	N/a	9	N/a

Key movements

– The observed average default rate aligns well to the assigned PD Band.

– Average PDs are in excess of average default rates due to the use of TTC methodology for the majority of obligors and the presence of a PD buffer on the PIT PD models.

– Similarly, the average PDs generally exceed the PD range since the average PDs are based on regulatory PDs but obligors are allocated to risk grades based on the (currently lower) PIT PDs (with the exception of BDCS which uses regulatory PD).

Table 14B: Back-testing of PD per portfolio – QRRE (CR9)

RWA coverage: 100%

PD Range	Weighted average PD	Arithmetic average PD by obligors	Number of obligors End of previous year	Number of obligors End of the year	Defaulted obligors in the year	of which: new defaulted obligors in the year	Average historical annual default rate[1]
0.00 - 0.10%	0.05%	0.05%	8,200,723	8,539,152	1,964	N/a	0.05%
0.10 - 0.40%	0.22%	0.23%	8,702,313	8,161,096	11,985	N/a	0.14%
0.40 - 0.80%	0.57%	0.58%	2,822,852	3,684,842	12,031	N/a	0.43%
0.80 - 1.20%	0.99%	0.99%	1,429,456	1,477,550	11,786	N/a	0.83%
1.20 - 2.50%	1.75%	1.75%	2,178,348	2,172,031	32,211	N/a	1.58%
2.50 - 4.50%	3.33%	3.32%	1,331,550	1,274,787	37,647	N/a	2.95%
4.40 - 7.50%	6.05%	5.92%	1,019,615	987,176	46,260	N/a	4.64%
7.50 - 10.00%	8.31%	8.27%	519,359	543,869	32,944	N/a	7.10%
10.00 - 14.00%	11.47%	11.58%	239,606	244,141	24,966	N/a	9.92%
14.00 - 20.00%	16.40%	16.50%	160,829	160,385	24,584	N/a	14.99%
20.00 - 30.00%	24.17%	24.23%	106,813	106,142	24,180	N/a	22.21%
30.00 - 45.00%	36.18%	36.20%	62,172	64,872	20,860	N/a	31.85%
45.00 -99.99%	67.49%	69.40%	73,512	74,086	42,669	N/a	57.63%
In Default	100.00%	100.00%	195,794	158,866	N/a	N/a	N/a
New to Book	N/a	N/a	–	2,953,799	N/a	25,885	N/a

[1] Default rates based on 4 years of data.

Key movements

– The observed average default rate aligns well to the assigned PD Band.

– Average PDs are in excess of average default rates due to the presence of a PD buffer; all PD models are PIT.

Table 14C: Back-testing of PD per portfolio – Retail Other (Non-SME) (CR9)

RWA coverage: 100%

PD Range	Weighted average PD	Arithmetic average PD by obligors	Number of obligors: End of previous year	Number of obligors: End of the year	Defaulted obligors in the year	of which: new defaulted obligors in the year	Average historical annual default rate[1]
0.00 - 0.10%	0.08%	0.08%	19,840	24,986	15	N/a	0.09%
0.10 - 0.40%	0.35%	0.34%	262,955	377,085	1,209	N/a	0.48%
0.40 - 0.80%	0.68%	0.66%	298,353	307,152	1,985	N/a	0.62%
0.80 - 1.20%	1.00%	0.99%	166,120	178,697	1,203	N/a	0.76%
1.20 - 2.50%	1.69%	1.69%	565,751	533,164	7,562	N/a	1.39%
2.50 - 4.50%	3.29%	3.33%	237,548	226,393	6,580	N/a	2.61%
4.40 - 7.50%	5.86%	5.85%	111,805	104,397	5,987	N/a	5.01%
7.50 - 10.00%	8.56%	8.58%	26,365	24,785	2,103	N/a	7.24%
10.00 - 14.00%	11.08%	11.29%	27,749	28,114	2,765	N/a	9.47%
14.00 - 20.00%	17.88%	17.71%	15,730	21,063	1,650	N/a	12.07%
20.00 - 30.00%	21.80%	22.06%	12,436	14,465	2,120	N/a	17.44%
30.00 - 45.00%	35.07%	35.92%	12,271	14,316	3,957	N/a	31.12%
45.00 -99.99%	72.07%	72.17%	12,972	13,006	8,388	N/a	66.35%
In Default	100.00%	100.00%	24,314	24,944	N/a	N/a	N/a
New to Book	N/a	N/a	–	605,946	N/a	3,554	N/a

[1] Default rates based on 4 years of data.

Key movements

– The observed average default rate aligns well to the assigned PD Band.
– Average PDs are generally in excess of average default rates due to the presence of a PD buffer on all models.

Table 14D: Back-testing of PD per portfolio – Retail SME[1] (CR9)

RWA coverage: 100%

PD Range	Weighted average PD	Arithmetic average PD by obligors	Number of obligors: End of previous year	Number of obligors: End of the year	Defaulted obligors in the year	of which: new defaulted obligors in the year	Average historical annual default rate[2]
0.00 - 0.10%	0.00%	0.00%	–	–	–	N/a	0.00%
0.10 - 0.40%	0.00%	0.00%	–	–	–	N/a	0.00%
0.40 - 0.80%	0.61%	0.59%	54,238	55,108	137	N/a	0.22%
0.80 - 1.20%	1.12%	1.12%	21,482	13,523	160	N/a	0.73%
1.20 - 2.50%	1.67%	1.67%	11,196	12,840	141	N/a	1.27%
2.50 - 4.50%	2.62%	2.62%	11,436	11,867	259	N/a	1.98%
4.40 - 7.50%	5.67%	5.67%	8,673	12,176	346	N/a	3.75%
7.50 - 10.00%	8.04%	8.04%	714	576	10	N/a	1.59%
10.00 - 14.00%	10.61%	10.66%	24,692	4,937	888	N/a	4.51%
14.00 - 20.00%	18.02%	18.02%	2,143	20,193	345	N/a	14.18%
20.00 - 30.00%	0.00%	0.00%	–	–	–	N/a	0.00%
30.00 - 45.00%	34.10%	34.10%	971	1,375	272	N/a	27.27%
45.00 -99.99%	78.18%	78.18%	1,112	1,862	330	N/a	29.93%
In Default	100.00%	100.00%	8,770	8,796	N/a	N/a	N/a
New to Book	N/a	N/a	N/a	N/a	N/a	N/a	N/a

[1] Exposures have been transferred from Corporate RMS to Retail RMS which leads to some 'gaps' in the risk grades.
[2] Default rates based on 3 years of data.

Key movements

– Average default rate is slightly volatile due to low volumes in some risk grades. However, in all cases the default rates is within or below the associated risk grade.

Pillar 1 Capital requirements: Credit risk continued

Table 14E: Back-testing of PD per portfolio – Ireland Mortgages (CR9)

RWA coverage: 100%

			Number of obligors				
PD Range	Weighted average PD	Arithmetic average PD by obligors	End of previous year	End of the year	Defaulted obligors in the year	of which: new defaulted obligors in the year	Average historical annual default rate
0.00 - 0.10%	0.00%	0.00%	–	–	–	N/a	0.00%
0.10 - 0.40%	0.32%	0.33%	470	1,281	–	N/a	0.00%
0.40 - 0.80%	0.63%	0.61%	4,060	5,042	33	N/a	0.76%
0.80 - 1.20%	1.01%	1.00%	3,893	4,935	27	N/a	0.95%
1.20 - 2.50%	1.70%	1.66%	6,704	4,351	95	N/a	1.13%
2.50 - 4.50%	3.31%	3.24%	2,378	1,765	39	N/a	1.72%
4.40 - 7.50%	5.63%	5.73%	826	533	26	N/a	2.76%
7.50 - 10.00%	8.66%	8.67%	282	192	19	N/a	4.49%
10.00 - 14.00%	11.66%	11.82%	228	184	16	N/a	5.32%
14.00 - 20.00%	16.40%	16.42%	189	125	24	N/a	9.46%
20.00 - 30.00%	24.64%	24.66%	166	157	19	N/a	12.02%
30.00 - 45.00%	36.34%	35.54%	113	86	28	N/a	22.04%
45.00 -99.99%	57.28%	56.94%	154	130	78	N/a	44.76%
In Default	100.00%	100.00%	782	797	N/a	N/a	100.00%
New to Book	N/a	N/a	-	-	N/a	–	N/a

Key movements

– The observed average default rate aligns well to the assigned PD bond.
– Average PDs are generally in excess of average default rates due to the presence of a PD buffer on all models.

Table 14F: Back-testing of PD per portfolio – Corporate Main (CR9)

RWA coverage: 75-80%

				Number of obligors				
PD Range	External rating equivalent	Weighted average PD	Arithmetic average PD by obligors	End of previous year	End of the year	Defaulted obligors in the year	of which: new defaulted obligors in the year	Average historical annual default rate[1]
0.00 - 0.035%	AAA to AA-	0.03%	0.03%	265	263	–	N/a	0.29%
0.035 - 0.050%	A+	0.04%	0.05%	569	521	–	N/a	0.00%
0.050 - 0.080%	A	0.06%	0.06%	149	133	–	N/a	0.00%
0.080 - 0.140%	A-	0.11%	0.11%	473	505	–	N/a	0.14%
0.140 - 0.220%	BBB+	0.18%	0.19%	1,293	1,241	1	N/a	0.09%
0.220 - 0.340%	BBB	0.28%	0.28%	1,111	1,214	2	N/a	0.12%
0.340 - 0.500%	BBB-	0.42%	0.43%	3,117	2,975	6	N/a	0.32%
0.500 - 0.760%	BB+	0.63%	0.64%	2,841	3,335	13	N/a	0.58%
0.760 - 1.240%	BB	1.00%	1.00%	2,695	2,866	14	N/a	0.58%
1.240 - 2.000%	BB-	1.62%	1.61%	1,881	2,168	19	N/a	1.27%
2.000 - 3.200%	B+	2.60%	2.60%	632	654	23	N/a	3.04%
3.200 - 5.200%	B+	4.12%	3.82%	1,106	1,298	30	N/a	1.64%
5.200 - 7.200%	B	6.20%	6.15%	125	289	5	N/a	3.39%
7.200 - 10.200%	B-	8.70%	8.79%	57	102	2	N/a	1.84%
10.200 - 13.800%	B-	11.99%	11.61%	46	74	6	N/a	6.27%
13.800 - 99.99%	CCC to C	25.23%	25.27%	93	142	8	N/a	8.35%
In Default	Default	100.00%	100.00%	533	480	N/a	N/a	N/a
New to Book	N/a	N/a	N/a	N/a	N/a	N/a	N/a	N/a

[1] Default rates based on 3 years of data.

Key movements

– Models in this segment are calibrated on a TTC basis. Relatively low default volumes lead to volatility in default rates within a given PD range.

Table 14G: Back-testing of PD per portfolio – Corporate SME (CR9)

RWA coverage: 80-85%

PD Range	External rating equivalent	Weighted average PD	Arithmetic average PD by obligors	Number of obligors: End of previous year	Number of obligors: End of the year	Defaulted obligors in the year	of which: new defaulted obligors in the year	Average historical annual default rate[1]
0.00 - 0.035%	AAA to AA-	0.03%	0.03%	6	5	–	N/a	0.00%
0.035 - 0.050%	A+	0.04%	0.04%	4	2	–	N/a	0.00%
0.050 - 0.080%	A	0.06%	0.06%	228	215	–	N/a	0.00%
0.080 - 0.140%	A-	0.11%	0.11%	1,260	1,551	–	N/a	0.11%
0.140 - 0.220%	BBB+	0.18%	0.18%	851	613	–	N/a	0.06%
0.220 - 0.340%	BBB	0.28%	0.28%	650	640	2	N/a	0.58%
0.340 - 0.500%	BBB-	0.42%	0.42%	545	580	–	N/a	0.33%
0.500 - 0.760%	BB+	0.63%	0.62%	2,938	3,836	15	N/a	0.49%
0.760 - 1.240%	BB	1.07%	1.09%	2,006	1,941	17	N/a	1.14%
1.240 - 2.000%	BB-	1.65%	1.65%	1,205	1,546	13	N/a	0.95%
2.000 - 3.200%	B+	2.61%	2.61%	1,137	1,221	29	N/a	2.83%
3.200 - 5.200%	B+	4.20%	4.20%	140	221	2	N/a	1.72%
5.200 - 7.200%	B	5.99%	5.75%	489	789	22	N/a	3.68%
7.200 - 10.200%	B-	8.21%	8.25%	127	183	–	N/a	2.08%
10.200 - 13.800%	B-	10.67%	10.70%	277	230	24	N/a	8.94%
13.800 - 99.99%	CCC to C	27.44%	28.04%	128	271	24	N/a	23.07%
In Default	Default	100.00%	100.00%	320	251	N/a	N/a	N/a
New to Book	N/a	N/a	N/a	N/a	N/a	N/a	N/a	N/a

[1] Default rates based on 3 years of data.

Key movements

– Observed default rates generally rise through the PD ranges as expected. In most instances, actual default rates fall within or below the PD ranges.

Pillar 1 Capital requirements: Credit risk continued

PAST DUE EXPOSURES, IMPAIRED EXPOSURES AND IMPAIRMENT PROVISIONS

DEFINITION

For accounting purposes, past due exposures, impaired exposures and impairment provisions are defined as follows:

- **Past due exposures:** An exposure is past due when a counterparty has failed to make a payment when contractually due.
- **Impaired exposures:** An exposure where the Group does not expect to collect all the contractual cash flows or to collect them when they are contractually due.
- **Impairment provisions:** Impairment provisions (also referred to as impairment allowances) are a provision held on the balance sheet as a result of the raising of a charge against profit for the incurred loss inherent in the lending book. An impairment provision may either be individually or collectively assessed.

ACCOUNTING POLICY

References to the Group's accounting policy in respect of impaired exposures ('financial assets') and impairment provisions raised in respect of loans and receivables are provided below.

Impairment of financial assets, Note 2 (Accounting policies) of the 2016 Lloyds Banking Group plc Annual Report and Accounts:

- (1) Assets accounted for at amortised cost, pages 189 and 190
- (2) Available-for-sale financial assets, page 190

MANAGING IMPAIRED EXPOSURES AND IMPAIRMENT PROVISIONS

Provisioning Policy

The high level principles and policies of the Group in respect of the management of impaired exposures, the setting of impairment provisions and the write off of impaired exposures are contained within the Group Credit Policies and are maintained by the Risk Division, and Group's Accounting Policies which are maintained by the Finance Division, all of which are renewed and approved on an annual basis.

Adequacy reviews

Any assessment of impairment must be based on the information and events that have already occurred as at the review or balance sheet date. Events that occur after such date may be taken into account only where they inform the position at that date.

The process for estimating impairment must consider all credit exposures and not only those in default or low credit quality.

Assets previously identified as impaired are reviewed to ensure that the objective evidence of impairment remains valid, that cashflow projections (including any potential net proceeds from realisation of collateral) remain appropriate and that the impairment loss recorded in the Group's books continues to reflect the difference between the net present value and the carrying value of the asset. In the event that the future expected cashflow has changed from the previous assessment, an adjustment to the level of loss allowance is made as appropriate.

Where these impaired assets are within a pool of similar assets and are assessed collectively, the relevance of the pool within which the asset has been placed and the assumptions regarding cashflow emanating from the pool are considered.

Upon review, if it can be evidenced that the impairment event has passed without detriment to the future expected cashflow and the net present value is greater than the carrying value of the asset, the asset can be re-categorised as unimpaired and the loss allowance released.

Reporting

The Business and Risk Division monitor impairment provisions on a continuous basis throughout the year.

A consolidated risk report is produced on a monthly basis for the Group Risk Committee. This report includes comparison of actual performance against budget for the main balance sheet and income statement metrics, including asset balances, impaired assets, income statement impairment charges and balance sheet provisions.

Additionally, on a regular basis, an analysis of impaired exposure and impairment allowances (including potential risks not identified within models for collective provisioning) are provided to Board and Audit Committee.

MANAGEMENT OF CUSTOMERS EXPERIENCING FINANCIAL DISTRESS

Information and analysis on the measures adopted by the Group to support retail and commercial customers experiencing financial difficulty is provided in the Risk Management section of the 2016 Lloyds Banking Group plc Annual Report and Accounts on pages 127 to 129.

ANALYSIS OF PAST DUE AND IMPAIRED LOANS AND ADVANCES TO CUSTOMERS

The analysis provided within this section has been presented on an accounting consolidation basis rather than a regulatory consolidation basis.

As at 31 December 2016, past due but not impaired exposures in respect of loans and advances to customers amounted to £8.0bn (2015: £9.1bn). Impaired exposures in respect of loans and advances to customers amounted to £8.5bn (2015: £9.6bn), of which £1.9bn (2015: £2.5bn) were classified as 'impaired – no provision required' and the remaining £6.6bn (2015: £7.1bn) as 'impaired – provision held'.

Analysis by industry

An analysis of past due but not impaired loans and advances to customers and impaired loans and advances to customers as at 31 December 2016, by major industrial sector, is provided in the table below.

Table 15: Past due but not impaired and impaired loans and advances analysed by major industrial sector

	Past due but not impaired		Impaired		Past due but not impaired		Impaired	
	2016		2016		2015		2015	
	£m	As a % of credit risk exposure	£m	As a % of credit risk exposure	£m	As a % of credit risk exposure	£m	As a % of credit risk exposure
Agriculture, forestry and fishing	78	1.33%	141	2.41%	97	1.30%	123	1.65%
Energy and water supply	1	0.02%	4	0.08%	2	0.04%	134	2.35%
Manufacturing	17	0.10%	293	1.78%	31	0.20%	122	0.78%
Construction	22	0.45%	334	6.85%	39	0.84%	283	6.07%
Transport, distribution and hotels	93	0.42%	342	1.56%	131	0.59%	511	2.31%
Postal and communications	3	0.11%	5	0.18%	1	0.02%	296	6.49%
Property companies	81	0.25%	1,284	3.92%	189	0.57%	2,065	6.26%
Financial, business and other services	92	0.05%	784	0.45%	62	0.03%	985	0.54%
Personal: mortgages	7,340	2.21%	4,320	1.30%	8,233	2.43%	4,001	1.18%
Personal: other	201	0.43%	801	1.71%	227	0.48%	980	2.09%
Lease financing	–	–	–	–	–	–	13	0.38%
Hire purchase	103	0.90%	187	1.63%	77	0.82%	77	0.82%
Total	8,031	1.19%	8,495	1.26%	9,089	1.32%	9,590	1.40%

Analysis by geography

An analysis of past due but not impaired loans and advances to customers and impaired loans and advances to customers as at 31 December 2016, by geographical region, based on the country of residence of the customer, is provided in the table below.

Table 16: Past due but not impaired and impaired loans and advances analysed by geographical region

	Past due but not impaired		Impaired		Past due but not impaired		Impaired	
	2016		2016		2015		2015	
	£m	As a % of credit risk exposure	£m	As a % of credit risk exposure	£m	As a % of credit risk exposure	£m	As a % of credit risk exposure
United Kingdom	7,641	1.33%	8,019	1.40%	8,761	1.49%	9,021	1.53%
Rest of Europe	389	0.97%	314	0.78%	299	0.73%	303	0.74%
United States of America	1	–	95	0.25%	–	–	108	0.30%
Asia-Pacific	–	–	13	0.65%	28	1.40%	93	4.63%
Other	–	–	54	0.95%	1	0.02%	65	1.25%
Total	8,031	1.19%	8,495	1.26%	9,089	1.32%	9,590	1.40%

Pillar 1 Capital requirements: Credit risk continued

ANALYSIS OF SPECIFIC CREDIT RISK ADJUSTMENTS (SCRA) IN RESPECT OF LOANS AND ADVANCES TO CUSTOMERS

SCRAs include accounting impairment provisions and certain acquisition related fair value adjustments. These acquisition related fair value adjustments are offset against EEL, in relation to Retail IRB residential mortgages.

The analysis provided within this section has been presented on an accounting consolidation basis rather than a regulatory consolidation basis.

The movement in impairment provisions, from 1 January 2016 to 31 December 2016, in respect of loans and advances to customers, banks and debt securities is provided below.

Table 17: Movement in impairment provisions

	2016			2015		
	Loans and advances to customers £m	**Debt securities £m**	**Total £m**	Loans and advances to customers £m	Debt securities £m	Total £m
At 1 January	**3,033**	**97**	**3,130**	6,414	126	6,540
Exchange and other adjustments	**69**	**–**	**69**	(246)	–	(246)
Disposal of businesses	**–**	**–**	**–**	(82)	–	(82)
Advances written off	**(2,111)**	**(22)**	**(2,133)**	(4,204)	(31)	(4,235)
Recoveries of advances written off in previous years	**861**	**1**	**862**	764	4	768
Unwinding of discount	**(32)**	**–**	**(32)**	(56)	–	(56)
Charge (release) to the income statement	**592**	**–**	**592**	443	(2)	441
At 31 December	**2,412**	**76**	**2,488**	3,033	97	3,130

The movement in acquisition related fair value adjustments, from 1 January 2016 to 31 December 2016, in respect of loans and advances to customers within portfolios applying the IRB approach is provided below.

Table 18: Movement in acquisition related fair value adjustments (loans and advances to customers)

	2016 £m	2015 £m
At 1 January	**276**	393
Fair value unwind[1]:		
in respect of impairment losses	**(68)**	(95)
other, including market liquidity	**(31)**	(22)
At 31 December	**177**	276

[1] The fair value adjustments relating to loans and advances were those required to reflect the HBOS assets in the Group's consolidated financial records at their fair value and took into account both the ELs and market liquidity at the date of acquisition. The unwind relating to future impairment losses requires significant management judgement to determine its timing which includes an assessment of whether the losses incurred in the current period were expected at the date of acquisition and assessing whether the remaining losses expected at the date of acquisition will still be incurred. The element related to market liquidity unwinds to the income statement over the estimated expected lives of the related assets although if an asset is written-off or suffers previously unexpected impairment then this element of the fair value will no longer be considered a timing difference (liquidity) but permanent (impairment). The fair value unwind in respect of impairment losses incurred for loans and advances to customers within portfolios applying the IRB Approach was £68m for the period ended 31 December 2016.

Analysis by industry

An analysis of closing impairment provisions, the net charge to the income statement and acquisition related fair value adjustments in respect of loans and advances to customers, by major industrial sector, is provided in the table below.

Table 19: Impairment provisions, net charge and acquisition related fair value adjustments analysed by major industrial sector

	2016 Impairment provisions[1] £m	2016 Net charge[1] £m	2016 Acquisition related fair value adjustments[2] £m	2015 Impairment provisions[1] £m	2015 Net charge[1] £m	2015 Acquisition related fair value adjustments[2] £m
Agriculture, forestry and fishing	13	3	–	15	1	–
Energy and water supply	6	(4)	–	20	35	–
Manufacturing	84	(48)	–	70	27	–
Construction	319	143	–	165	15	–
Transport, distribution and hotels	161	(35)	–	219	(77)	–
Postal and communications	5	191	–	4	(2)	–
Property companies	470	(166)	–	790	(91)	–
Financial, business and other services	312	6	–	811	96	–
Personal: mortgages	1,695	47	177	1,618	134	276
Personal: other	356	433	–	388	429	–
Lease financing	–	15	–	–	31	–
Hire purchase	110	72	–	72	23	–
	3,531	657	177	4,172	621	276
Fair value and other adjustments	(1,119)	(65)		(1,139)	(178)	
Total	2,412	592	177	3,033	443	276

[1] Analysis of closing impairment provisions and the net charge to the income statement in respect of loans and advances to customers, by major industrial sector, has been presented prior to the application of fair value and other adjustments. A similar analysis presented on a statutory basis is included in the 'Summary of Loan Less Experience' analysis on pages 76 to 80 of the 2016 Form 20-F.

[2] The acquisition related fair value adjustments represent SCRAs recognised in the calculation of EEL amounts for exposures subject to the IRB Approach (as presented on page 48).

Analysis by geography

An analysis of closing impairment provisions, the net charge to the income statement and acquisition related fair value adjustments in respect of loans and advances to customers, by geographical region, based on the country of residence of the customer, is provided in the table below.

Table 20: Impairment provisions, net charges and acquisition related fair value adjustments analysed by geographical region

	2016 Impairment provisions[1] £m	2016 Net charge[1] £m	2016 Acquisition related fair value adjustments[2] £m	2015 Impairment provisions[1] £m	2015 Net charge[1] £m	2015 Acquisition related fair value adjustments[2] £m
United Kingdom	3,189	727	177	3,726	687	276
Rest of Europe	270	(68)	–	323	43	–
United States of America	9	–	–	74	(18)	–
Asia-Pacific	9	–	–	19	(4)	–
Other	54	(2)	–	30	(87)	–
	3,531	657	177	4,172	621	276
Fair value and other adjustments	(1,119)	(65)		(1,139)	(178)	
Total	2,412	592	177	3,033	443	276

[1] Analysis of closing impairment provisions and the net charge to the income statement in respect of loans and advances to customers, by geographical region, has been presented prior to the application of fair value and other adjustments. Further details on the fair value and other adjustments applied in respect of impairment provisions can be found on page 263 of the 2016 Lloyds Banking Group plc Annual Report and Accounts.

[2] The acquisition related fair value adjustments represent SCRAs recognised in the calculation of EEL amounts for exposures subject to the IRB Approach (as presented on page 48).

Pillar 1 Capital requirements: Credit risk continued

FACTORS IMPACTING LOSS EXPERIENCE

The total impairment charge on an underlying basis increased to £645m (2015: £568m) with the asset quality ratio increasing slightly to 15 basis points, but this was largely due to lower provision releases and write backs.

Impaired loans as a percentage of closing loans and advances reduced to 1.8 per cent at 31 December 2016, from 2.1 per cent at 31 December 2015 with impaired loans reducing by £1.1bn due to further reductions in the Commercial Banking, Consumer Finance and Run-off portfolios.

COMPARISON OF EXPECTED LOSSES TO SPECIFIC CREDIT RISK ADJUSTMENTS

The table on page 51 provides a comparison of regulatory ELs to SCRAs on loans and receivables (impairment provisions and acquisition related fair value adjustments), in respect of credit risk exposures subject to the IRB Approach. The Group does not recognise any general credit risk adjustments (GCRAs) as defined by the EBA.

The definition, calculation and treatment of regulatory ELs are covered on page 35.

In comparing regulatory ELs to accounting measures of impairment, significant differences in the calculation and scope of each must be taken into account. IRB models are developed to meet precise regulatory requirements and as such the ELs generated by these models are not directly comparable to impairment losses or allowances derived under current IFRS accounting standards. In particular:

- SCRAs seek to measure loss on the basis of economic conditions at the balance sheet date. However, regulatory EL calculations are predicated on loss estimates that are based on economic downturn conditions;
- Regular detailed analysis of modelled SCRAs outputs is undertaken to ensure that the models adequately capture all incurred losses. Where this is considered not to be the case, additional SCRAs allowances are applied to capture the risk;
- Regulatory EL calculations forecast potential losses arising from all accounts including those that currently exhibit no indication of impairment;
- Regulatory ELs in relation to portfolios that are based on TTC or hybrid PD estimates utilise historic default experience, whereas accounting impairment losses and allowances are based on the losses that have been incurred at the balance sheet date;
- Regulatory EL calculations anticipate additional drawings made by customers who are yet to default (EAD estimate). Accounting impairment losses reflect drawn balances and conditions at the balance sheet date; and
- Regulatory ELs generated under the Foundation IRB Approach make use of LGD parameters and CCF (applied in the calculation of EAD) that are set by the regulator. The assumptions inherent within these regulatory measures may differ significantly to the assumptions applied when estimating future cash flows for use in accounting impairment loss calculations.

In addition, regulatory ELs in relation to credit portfolios that have rolled out onto IRB models during the year will not be reflected in the ELs total at the start of the year as these portfolios were, at the time, subject to the Standardised Approach. Accounting impairment losses for the year will reflect losses in relation to all portfolios that were subject to the IRB Approach during the year.

In comparing regulatory ELs to the accounting allowance for impairment losses, consideration of the above should be taken into account.

Table 21: Regulatory expected losses and specific credit risk adjustments

	2016 Regulatory expected losses £m	2016 Specific credit risk adjustments £m	2016 Excess expected losses £m	2015 Regulatory expected losses £m	2015 Specific credit risk adjustments £m	2015 Excess expected losses £m	2014 Regulatory expected losses £m	2014 Specific credit risk adjustments £m	2014 Excess expected losses £m
CREDIT RISK									
Foundation IRB approach									
Corporates	**884**	**632**	**252**	1,103	1,060	43	1,420	1,368	52
Central governments and central banks	**1**	**–**	**1**	1	–	1	1	–	1
Institutions	**21**	**13**	**8**	12	17	(5)	11	21	(10)
Retail IRB approach									
Residential mortgages	**880**	**1,543**	**(663)**	1,094	1,465	(371)	1,259	1,518	(259)
QRRE	**640**	**241**	**399**	611	244	367	711	269	442
Other SME	**78**	**13**	**65**	77	14	63	91	22	69
Other non-SME	**384**	**201**	**183**	332	180	152	465	238	227
Other IRB approaches									
Corporate – specialised lending	**632**	**381**	**251**	941	654	287	2,288	2,237	51
Equities	**34**	**–**	**34**	41	–	41	31	–	31
Counterparty credit risk	**64**	**–**	**64**	80	–	80	229	–	229
	3,618	**3,024**	**594**	4,292	3,634	658	6,506	5,673	833
Fair value adjustments[1]		**177**			276			393	
Total prior to additional adjustments	**3,618**	**3,201**	**417**	4,292	3,910	382	6,506	6,066	440
Other adjustments[2]			**185**			(112)			125
Total excess expected losses			**602**			270			565

Reconciliation of SCRAs to statutory consolidated balance sheet allowance for impairment losses on loans and receivables

	2016	2015	2014
Total SCRAs applied against expected losses	**3,201**	3,910	6,066
SCRAs (excluding fair value adjustments) applied to Standardised Approach and other exposures[3]	**406**	359	1,712
Additional fair value and other adjustments	**(1,119)**	(1,139)	(1,238)
Total per statutory consolidated balance sheet	**2,488**	3,130	6,540

[1] The calculation of EEL amounts, where regulatory ELs are netted against SCRAs on IRB portfolios, is subject to the application of acquisition related fair value adjustments.

[2] Other adjustments include an increase for SCRAs in excess of EL on defaulted exposures which, under CRD IV, may not be offset against non-defaulted EEL, and prudent valuation adjustments (for 2014 and 2015 only).

[3] SCRAs applied to Standardised Approach exposures and other adjustments including allowances for impairment losses on debt securities.

Further details on the fair value and other adjustments applied in respect of impairment losses charged to the income statement and allowances for impairment losses on loans and receivables can be found on pages 130 and 263, respectively, of the 2016 Lloyds Banking Group plc Annual Report and Accounts.

Pillar 1 Capital requirements: Credit risk continued

Key movements (2016)

FIRB Corporates

– The expected loss reduction of £0.2bn to £0.9bn and the SCRA reduction of £0.4bn to £0.6bn are primarily driven by asset reductions and active portfolio management including the disposal of more highly provided defaulted exposures.

Retail IRB Residential Mortgages

– The expected loss reduction of £0.2bn to £0.9bn is driven by model updates, favourable HPI and improvements in credit quality. The Group continues to maintain a prudent provisioning policy over its Residential Mortgage portfolio and this has resulted in SCRAs exceeding regulatory ELs despite the majority of ELs being calculated using TTC PD model.

Other Retail IRB (QRRE, Other SME and Other non-SME)

– The Group's Other Retail IRB portfolios are based on model methodologies where the impact of model conservatism results in regulatory ELs being in excess of SCRAs. Model updates, partially offset by continued improvements in credit quality and a favourable credit environment in 2016 have driven an increase in regulatory ELs for these portfolios.

Specialised Lending

– The expected loss reduction of £0.3bn to £0.6bn and the SCRA reduction of £0.3bn to £0.4bn is primarily driven by asset reductions, active portfolio management including disposals and write-offs of defaulted exposures.

Fair value adjustments

– Fair value adjustments applied within the EEL calculation have reduced by £0.1bn to £0.2bn due to the fair value unwind over the course of the year, as outlined in Table 18 on page 48.

Other adjustments

– Other adjustments have increased by £0.3bn following revised guidance issued by the EBA relating to prudent valuation adjustments.

Key movements (2015)

FIRB Corporates

– ELs and SCRAs both reduced by £0.3bn to £1.1bn, primarily driven by asset reductions in the Run-off portfolio and targeted portfolio management.

Retail IRB Residential Mortgages

– The expected loss reductions of £0.2bn to £1.1bn is driven by improvements in credit quality and favourable movements in external economic factors, primarily HPI.

– The Group continues to maintain a prudent provisioning policy over Residential Mortgage portfolios. This has resulted in SCRAs exceeding regulatory ELs for Retail IRB Residential Mortgage portfolios, despite the majority of ELs being calculated using a TTC PD model.

Other Retail IRB

– The Group's Other Retail IRB portfolios are based on model methodologies where the impact of model conservatism results in regulatory ELs being in excess of SCRAs. Continued improvement in credit quality and favourable credit environment in 2015 has driven reductions in both regulatory ELs and SCRAs for these portfolios.

Specialised Lending

– The expected loss reduction from £1.4bn to £0.9bn, and SCRA reduction from £1.5bn to £0.7bn for Corporate Specialised Lending exposures is primarily driven by disposals of defaulted exposures in the Irish commercial property portfolio and other exits in the run-off business.

– The disposals of the highly provided for Irish exposures have resulted in an increase in EEL from £0.1bn to £0.3bn.

Fair value adjustments

– Fair value adjustments applied within the EEL calculation have reduced from £0.1bn to £0.3bn due to the fair value unwind over the course of the year.

Other adjustments

– Other adjustments consist of SCRAs in excess of expected loss on defaulted exposures (which, under CRD IV may not be offset against non-defaulted EEL) as well as PVAs linked to IRB portfolios. These adjustments were recognised for the first time in 2014 in line with CRD IV requirements.

– Total other adjustments have reduced in 2015 from £0.1bn to £(0.1)bn due to lower surplus SCRAs driven by continued disposals of defaulted exposures in Ireland as well as refinements to the PVA.

ANALYSIS OF CREDIT RISK EXPOSURES BY ASSET CLASS

CREDIT RISK EXPOSURES

The following tables show the Group's credit exposures split by Basel exposure class, together with associated risk-weighted assets and average risk weight.

Table 22: Credit risk exposures

Exposure class	2016 Credit risk exposure £m	2016 Risk-weighted assets £m	2016 Minimum capital requirements £m	2016 Average risk weight[4] %	2016 Average credit risk exposure[5] £m
Exposures subject to the IRB approach					
Foundation IRB approach					
Corporate – main	78,527	41,171	3,294	52%	80,060
Corporate – SME	11,981	7,880	630	66%	12,777
Corporate – specialised lending	2	2	–	137%	3
Central governments and central banks	15,153	1,430	114	9%	17,597
Institutions	6,011	957	77	16%	6,861
Retail IRB approach					
Retail mortgages	335,510	39,550	3,164	12%	338,097
of which: residential mortgages (SME)	10,211	2,662	213	26%	10,393
of which: residential mortgages (non-SME)	325,299	36,888	2,951	11%	327,704
Qualifying revolving retail exposures	36,984	12,073	966	33%	37,059
Other SME	2,445	1,728	138	71%	2,506
Other non-SME	16,026	11,618	930	72%	15,280
Other IRB approaches[1]					
Corporate – specialised lending	18,814	13,467	1,077	72%	19,678
Equities – exchange traded	461	1,337	107	290%	737
Equities – private equity	2,583	4,909	393	190%	2,916
Equities – other	382	1,413	113	370%	432
Securitisation positions[2]	26,066	3,703	296	14%	22,613
Non-credit obligation assets[3]	10,890	6,427	514	59%	9,639
Total – IRB approach	561,835	147,665	11,813	26%	566,255
Exposures subject to the standardised approach					
Central governments and central banks	81,021	–	–	–	91,330
Regional governments or local authorities	–	–	–	–	1
Public sector entities	2	2	–	100%	2
Multilateral development banks	1,753	–	–	–	1,412
International organisations	–	–	–	–	–
Institutions	279	117	9	42%	193
Corporates	13,511	10,801	864	80%	14,202
Retail	4,114	2,761	221	67%	4,546
Secured by mortgages on immovable property	5,504	1,981	159	36%	5,703
of which: residential property	5,501	1,978	159	36%	5,684
of which: commercial property	3	3	–	100%	19
Exposures in default	789	883	71	112%	916
Exposures associated with particularly high risk	–	–	–	–	–
Securitisation positions	1,184	268	21	23%	237
Short term claims on institutions and corporates	–	–	–	–	–
Collective investment undertakings (CIUs)	224	45	4	20%	45
Other items[3]	3,091	2,098	168	68%	3,372
Total – standardised approach	111,472	18,956	1,517	17%	121,959
Total	673,307	166,621	13,330	25%	688,214
Threshold – significant investments	3,357	8,392	671	250%	3,277
Threshold – deferred tax	984	2,459	197	250%	1,173
Total credit risk	677,648	177,472	14,198	26%	692,664

Pillar 1 Capital requirements: Credit risk continued

Exposure class	2015 Credit risk exposure £m	2015 Risk-weighted assets £m	2015 Minimum capital requirements £m	2015 Average risk weight[4] %	2015 Average credit risk exposure[5] £m
Exposures subject to the IRB approach					
Foundation IRB approach					
Corporate – main	80,629	43,005	3,441	53%	79,610
Corporate – SME	12,964	8,814	705	68%	13,350
Corporate – specialised lending	6	8	1	120%	60
Central governments and central banks	15,716	1,347	108	9%	21,395
Institutions	7,364	1,430	114	19%	7,421
Retail IRB approach					
Retail mortgages	341,807	38,252	3,060	11%	347,021
of which: residential mortgages (SME)	10,517	3,214	257	31%	10,867
of which: residential mortgages (non-SME)	331,290	35,038	2,803	11%	336,154
Qualifying revolving retail exposures	36,975	12,501	1,000	34%	37,400
Other SME	2,661	1,807	145	68%	2,618
Other non-SME	14,331	11,352	908	79%	14,373
Other IRB approaches[1]					
Corporate – specialised lending	19,887	14,386	1,151	72%	21,293
Equities – exchange traded	978	2,837	227	290%	904
Equities – private equity	2,981	5,664	453	190%	3,068
Equities – other	376	1,392	111	370%	102
Securitisation positions[2]	22,125	3,266	261	15%	18,162
Non-credit obligation assets[3]	9,228	5,502	440	60%	8,624
Total – IRB approach	568,028	151,563	12,125	27%	575,401
Exposures subject to the standardised approach					
Central governments and central banks	88,415	–	–	–	96,082
Regional governments or local authorities	1	–	–	20%	–
Public sector entities	2	2	–	100%	8
Multilateral development banks	997	–	–	–	77
International organisations	–	–	–	–	–
Institutions	170	24	2	14%	175
Corporates	14,463	11,921	954	82%	14,147
Retail	4,438	2,880	230	65%	3,837
Secured by mortgages on immovable property	5,840	2,109	168	36%	7,098
of which: residential property	5,809	2,078	166	36%	7,075
of which: commercial property	31	31	2	100%	23
Exposures in default	1,005	1,198	96	119%	1,120
Exposures associated with particularly high risk	–	–	–	–	–
Securitisation positions	–	–	–	–	–
Short term claims on institutions and corporates	–	–	–	–	–
Collective investment undertakings (CIUs)	–	–	–	–	–
Other items[3]	3,204	2,309	185	72%	4,500
Total – standardised approach	118,535	20,443	1,635	17%	127,044
Total	686,563	172,006	13,760	25%	702,445
Threshold – significant investments	3,127	7,817	625	250%	3,342
Threshold – deferred tax	1,188	2,971	238	250%	938
Total credit risk	690,878	182,794	14,623	26%	706,725

[1] Credit risk exposures subject to other IRB approaches include corporate specialised lending exposures risk-weighted in accordance with supervisory slotting criteria, equity exposures risk-weighted in accordance with the Simple Risk Weight Method and securitisation positions risk-weighted in accordance with the IAA and the RBA.

[2] Securitisation positions exclude amounts allocated to the 1,250 per cent risk weight category. These amounts are deducted from capital, after the application of SCRAs, rather than being risk-weighted at 1,250 per cent.

[3] Other items (Standardised Approach) and non-credit obligation assets (IRB approach) predominantly relate to other balance sheet assets that have no associated credit risk. These comprise various non-financial assets, including fixed assets, cash, items in the course of collection, prepayments and sundry debtors.

[4] Average risk weight is risk-weighted assets expressed as a percentage of credit risk exposure (which is EAD pre-CRM, but post-CCF).

[5] Average credit risk exposure represents the average exposure across the year to 31 December.

Exposures subject to the IRB approach – key movements

FIRB Corporate Main

– Corporate Main exposures decreased by £2.1bn and risk-weighted assets reduced by £1.8bn driven by active portfolio management, partially offset by new lending.

FIRB Corporate SME

– Corporate SME exposures and risk-weighted assets have decreased by £1.0bn and £0.9bn respectively mainly driven by securitisation activity. The average risk-weight has reduced to 66% per cent, driven by continued new lending which has resulted in a modest improvement in credit quality across the portfolio.

Institutions

– Institutions exposures decreased by £1.4bn to £6.0bn mainly driven by a portfolio rebalancing exercise on the Groups bond portfolio with average risk-weight reducing from 19 per cent to 16 per cent as a result of improved credit quality across the portfolio.

Retail IRB Residential mortgages

– Retail mortgage exposures decreased by £6.3bn reflecting the Group's focus on balancing margin and risk considerations with volume growth in the current competitive low growth market. The small increase in average risk weighting was driven by model updates on the Mainstream and Buy-to-Let portfolios.

Qualifying revolving retail exposures

– Qualifying revolving retail exposures remained relatively flat with continued growth in Credit Cards offset by model calibrations. Risk-weighted assets decreased by £0.4bn and average risk weight reduced by 1 per cent to 33 per cent largely due to model updates and model calibrations on both credit cards and personal current accounts.

Retail Other (non-SME)

– Other (non-SME) exposures increased by £1.7bn and average risk weights reduced from 79 per cent to 72 per cent as a result of continued growth in the lower risk-weighted UK Motor Finance business.

Corporate – Specialised lending (slotting)

– Corporate specialised lending (slotting) exposures and risk-weighted assets reduced by £1.1bn and £0.9bn respectively largely due to active portfolio management.

Equities

– Equity exposures decreased by £0.9bn during the year and risk-weighted assets reduced by £2.2bn largely due to the disposal of certain strategic investments, partly offset by increases to the valuation of centrally held investments.

Securitisation positions

– Securitisation exposures and risk-weighted assets increased by £3.9bn and £0.4bn respectively primarily as a result of new capital efficient commercial asset backed securitisation transactions and an increase in investment grade investor positions, partially offset by sales and maturities.

Non-Credit obligation assets

– Non-Credit obligation asset exposures and risk-weighted assets have increased by £1.7bn and £0.9bn respectively largely due to growth in Operating Lease residual values.

Exposures subject to the Standardised Approach – key movements

Standardised Central governments and central banks.

– Exposures decreased by £7.4bn primarily due to management of the liquid asset portfolio.

Standardised Corporates

– Exposures and risk-weighted assets decreased by £1.0bn and £1.1bn respectively primarily driven by securitisations and continued portfolio management activity, partially offset by new lending.

Standardised Securitisation positions

– Exposures increased by £1.2bn and risk-weighted assets increased by £0.3bn as a result of a new capital efficient commercial asset backed securitisation.

Pillar 1 Capital requirements: Credit risk continued

An analysis of total credit risk exposures by division is provided below.

Table 23: Divisional credit risk exposures

Division	Risk Weight approach	2016 Credit risk exposure £m	2016 Risk-weighted assets £m	2016 Average risk weight %	2015 Credit risk exposure £m	2015 Risk-weighted assets £m	2015 Average risk weight %
Retail	IRB	331,730	36,746	11%	340,413	35,508	10%
	Standardised	5,949	2,990	50%	6,486	3,283	51%
Commercial Banking	IRB	139,050	68,408	49%	138,408	72,859	53%
	Standardised	13,115	9,798	75%	13,241	10,747	81%
Consumer Finance	IRB	53,429	26,390	49%	48,213	25,123	52%
	Standardised	3,001	2,156	72%	2,365	1,809	76%
Central Items	IRB	27,533	9,739	35%	29,458	10,466	36%
	Standardised	86,135	2,124	2%	92,701	2,266	2%
Run-off	IRB	10,092	6,382	63%	11,536	7,606	66%
	Standardised	3,273	1,888	58%	3,742	2,338	62%
Total		673,307	166,621	25%	686,563	172,006	25%

Key movements

Retail credit risk-weighted assets increased by £0.9bn to £39.7bn reflecting the Group's focus on balancing margin and risk considerations offset by a more prudent approach to secured risk-weighted asset modelling.

Commercial Banking credit risk-weighted assets decreased by £5.4bn, reflecting the disciplined approach to capital management, including capital efficient securitisation activity.

Consumer Finance credit risk-weighted assets increased by £1.6bn as a result of continued growth in the lower risk-weighted UK motor finance business.

Run-off credit risk-weighted assets decreased by £1.7bn driven by disposals.

ANALYSIS OF CREDIT RISK EXPOSURES SUBJECT TO THE FOUNDATION IRB APPROACH

This section provides a detailed analysis, by PD Grade, of credit risk exposures subject to the FIRB Approach. Exposures are presented on a post CRM and post CCF basis.

Disclosures provided in the tables below take into account PD floors specified by regulators in respect of the calculation of regulatory capital requirements.

The EBA guidelines include a single prescribed scale for presenting the credit quality of all IRB portfolios by asset class. The tables that follow present the prescribed scale. This does not map directly to the internal scales per tables 11 and 12, but is apportioned on the same basis.

Throughout this section 'RWA density' represents the 'average risk weight'. 'Number of obligors' corresponds to the number of individual PDs (in each band). In the case of Corporate Main and Corporate SME, as customers may have exposures in both Commercial Banking and Consumer Finance Motor divisions, an individual corporate obligor may be counted twice.

Table 24: IRB – Credit risk exposures by portfolio and PD range – Corporate Main (CR6)

PD Scale Corporates – Main	2016 a Original on-balance sheet gross exposure £m	2016 b Off balance sheet exposures pre CCF £m	2016 c Average CCF %	2016 d EAD post CRM and post CCF £m	2016 e Average PD %	2016 f Number of Obligors #	2016 g Average LGD %	2016 h Average Maturity (years) #	2016 I RWA £m	2016 j RWA density %	2016 k EL £m	2016 l Value adjustments and Provisions £m
0.00 to <0.15	**16,090**	**18,757**	**76.18%**	**29,898**	**0.07%**	**2,191**	**42.13%**	**3.0**	**8,157**	**27.28%**	**8**	
0.15 to <0.25	**7,035**	**8,560**	**75.94%**	**13,528**	**0.18%**	**1,495**	**44.09%**	**2.1**	**5,407**	**39.97%**	**11**	
0.25 to <0.50	**9,632**	**11,516**	**71.36%**	**16,791**	**0.34%**	**4,490**	**43.75%**	**2.4**	**9,833**	**58.56%**	**25**	
0.50 to <0.75	**3,291**	**2,626**	**63.92%**	**4,751**	**0.63%**	**6,260**	**43.74%**	**2.5**	**3,781**	**79.58%**	**13**	
0.75 to <2.50	**6,735**	**4,053**	**68.40%**	**9,012**	**1.24%**	**14,235**	**43.35%**	**2.3**	**8,772**	**97.34%**	**49**	
2.50 to <10.00	**2,637**	**1,082**	**70.44%**	**3,273**	**4.29%**	**4,647**	**42.85%**	**2.4**	**4,592**	**140.32%**	**60**	
10.00 to <100.00	**172**	**138**	**68.11%**	**263**	**24.79%**	**599**	**44.49%**	**1.9**	**629**	**239.14%**	**29**	
100.00 (Default)	**793**	**110**	**65.55%**	**864**	**100.00%**	**857**	**42.89%**	**1.9**	**–**	**–**	**370**	
Sub-total	**46,385**	**46,842**	**73.41%**	**78,380**	**1.67%**	**34,774**	**43.10%**	**2.6**	**41,171**	**52.53%**	**565**	**488**

PD Scale Corporates – Main	2015 a Original on-balance sheet gross exposure £m	2015 b Off balance sheet exposures pre CCF £m	2015 c Average CCF %	2015 d EAD post CRM and post CCF £m	2015 e Average PD %	2015 f Number of Obligors #	2015 g Average LGD %	2015 h Average Maturity (years) #	2015 I RWA £m	2015 j RWA density %	2015 k EL £m	2015 l Value adjustments and Provisions £m
0.00 to <0.15	16,745	17,609	75.67%	29,915	0.07%	2,294	42.07%	3.1	8,080	27.01%	9	
0.15 to <0.25	6,070	9,154	74.04%	12,519	0.18%	1,548	43.98%	2.2	5,267	42.07%	10	
0.25 to <0.50	10,975	14,424	74.28%	20,043	0.35%	4,801	43.95%	2.4	12,048	60.11%	31	
0.50 to <0.75	3,789	2,503	70.29%	5,351	0.63%	6,836	44.11%	2.4	4,201	78.52%	15	
0.75 to <2.50	5,599	3,343	70.13%	7,750	1.25%	13,903	43.68%	2.3	7,676	99.04%	42	
2.50 to <10.00	2,776	1,596	72.70%	3,873	3.81%	3,831	42.62%	2.5	5,296	136.75%	62	
10.00 to <100.00	139	74	72.11%	192	18.38%	487	44.32%	1.4	437	227.85%	15	
100.00 (Default)	861	159	82.58%	986	100.00%	965	42.77%	1.4	–	–	422	
Sub-total	46,954	48,862	74.22%	80,629	1.75%	34,665	43.16%	2.6	43,005	53.34%	606	669

Key movements

– EAD post CRM and post CCF decreased £2.2bn to £78.4bn and risk-weighted assets decreased £1.8bn to £41.2bn, with underlying reductions driven by active portfolio management, partially offset by new lending.

– The active portfolio management described above also led to a 0.81% reduction in risk weight.

Pillar 1 Capital requirements: Credit risk continued

Table 25: IRB – Credit risk exposures by portfolio and PD range – Corporate SME (CR6)

PD Scale Corporates – SME	2016 a Original on-balance sheet gross exposure £m	2016 b Off balance sheet exposures pre CCF £m	2016 c Average CCF %	2016 d EAD post CRM and post CCF £m	2016 e Average PD %	2016 f Number of Obligors #	2016 g Average LGD %	2016 h Average Maturity (years) #	2016 i RWA £m	2016 j RWA density %	2016 k EL £m	2016 l Value adjustments and Provisions £m
0.00 to <0.15	853	337	78.86%	1,127	0.08%	253	40.75%	3.5	311	27.61%	–	
0.15 to <0.25	179	206	73.35%	329	0.18%	206	43.31%	2.6	121	36.72%	–	
0.25 to <0.50	947	554	73.48%	1,339	0.37%	1,197	41.54%	2.1	616	45.97%	2	
0.50 to <0.75	1,364	294	69.84%	1,583	0.58%	3,464	37.97%	3.2	906	57.23%	4	
0.75 to <2.50	3,424	839	72.53%	4,012	1.23%	8,412	38.03%	2.9	2,849	71.03%	19	
2.50 to <10.00	2,382	406	74.71%	2,693	4.32%	5,044	37.91%	2.7	2,628	97.57%	44	
10.00 to <100.00	315	27	72.64%	335	20.66%	1,544	37.22%	2.6	449	133.95%	26	
100.00 (Default)	543	28	66.18%	563	100.00%	962	39.71%	2.1	–	–	224	
Sub-total	10,007	2,691	73.55%	11,981	6.79%	21,082	38.85%	2.8	7,880	65.77%	319	144

PD Scale Corporates – SME	2015 a Original on-balance sheet gross exposure £m	2015 b Off balance sheet exposures pre CCF £m	2015 c Average CCF %	2015 d EAD post CRM and post CCF £m	2015 e Average PD %	2015 f Number of Obligors #	2015 g Average LGD %	2015 h Average Maturity (years) #	2015 i RWA £m	2015 j RWA density %	2015 k EL £m	2015 l Value adjustments and Provisions £m
0.00 to <0.15	752	326	68.40%	977	0.07%	300	40.12%	3.6	237	24.29%	–	
0.15 to <0.25	205	137	70.60%	299	0.18%	214	42.22%	2.7	108	36.03%	–	
0.25 to <0.50	865	642	78.20%	1,347	0.37%	1,212	41.27%	2.3	650	48.28%	2	
0.50 to <0.75	1,502	451	71.71%	1,822	0.58%	3,300	39.26%	2.9	1,047	57.47%	4	
0.75 to <2.50	3,658	786	71.48%	4,217	1.23%	7,576	38.19%	3.1	3,074	72.88%	20	
2.50 to <10.00	2,684	395	71.60%	2,973	4.28%	4,286	38.89%	2.9	3,182	107.04%	50	
10.00 to <100.00	350	28	61.44%	368	16.42%	1,587	37.50%	3.0	516	140.42%	23	
100.00 (Default)	921	49	74.30%	961	100.00%	1,202	41.35%	2.2	–	–	398	
Sub-total	10,937	2,814	72.62%	12,964	9.39%	19,677	39.27%	2.9	8,814	67.99%	497	390

Key movements

– EAD post CRM and post CCF decreased by £1.0bn mainly driven by securitisation activity.
– The average PD has decreased 2.60% to 6.79%, driven by a reduction in defaulted exposure due to write-offs.
– The average risk-weight decreased 2.22% to 65.77%, driven by continued new lending resulting in a modest improvement in credit quality across the portfolio.

Table 26: IRB – Credit risk exposures by portfolio and PD range – Central government and central banks (CR6)

PD Scale Central governments and central banks	2016 a Original on-balance sheet gross exposure £m	2016 b Off balance sheet exposures pre CCF £m	2016 c Average CCF %	2016 d EAD post CRM and post CCF £m	2016 e Average PD %	2016 f Number of Obligors #	2016 g Average LGD %	2016 h Average Maturity (years) #	2016 I RWA £m	2016 j RWA density %	2016 k EL £m	2016 l Value adjustments and Provisions £m
0.00 to <0.15	15,153	–	–	15,153	0.01%	6	45.00%	3.0	1,430	9.44%	1	
0.15 to <0.25	–	–	–	–	–	–	–	–	–	–	–	
0.25 to <0.50	–	–	–	–	–	–	–	–	–	–	–	
0.50 to <0.75	–	–	–	–	–	–	–	–	–	–	–	
0.75 to <2.50	–	–	–	–	–	–	–	–	–	–	–	
2.50 to <10.00	–	–	–	–	–	–	–	–	–	–	–	
10.00 to <100.00	–	–	–	–	–	–	–	–	–	–	–	
100.00 (Default)	–	–	–	–	–	–	–	–	–	–	–	
Sub-total	15,153	–	–	15,153	0.01%	6	45.00%	3.0	1,430	9.44%	1	–

PD Scale Central governments and central banks	2015 a Original on-balance sheet gross exposure £m	2015 b Off balance sheet exposures pre CCF £m	2015 c Average CCF %	2015 d EAD post CRM and post CCF £m	2015 e Average PD %	2015 f Number of Obligors #	2015 g Average LGD %	2015 h Average Maturity (years) #	2015 I RWA £m	2015 j RWA density %	2015 k EL £m	2015 l Value adjustments and Provisions £m
0.00 to <0.15	15,716	–	–	15,716	0.01%	12	45.00%	2.7	1,347	8.57%	1	
0.15 to <0.25	–	–	–	–	–	–	–	–	–	–	–	
0.25 to <0.50	–	–	–	–	–	–	–	–	–	–	–	
0.50 to <0.75	–	–	–	–	–	–	–	–	–	–	–	
0.75 to <2.50	–	–	–	–	–	–	–	–	–	–	–	
2.50 to <10.00	–	–	–	–	–	–	–	–	–	–	–	
10.00 to <100.00	–	–	–	–	–	–	–	–	–	–	–	
100.00 (Default)	–	–	–	–	–	–	–	–	–	–	–	
Sub-total	15,716	–	–	15,716	0.01%	12	45.00%	2.7	1,347	8.57%	1	–

Pillar 1 Capital requirements: Credit risk continued

Institution exposures

Table 27: IRB – Credit risk exposures by portfolio and PD range – Institutions (CR6)

PD Scale Institutions	2016 a Original on-balance sheet gross exposure £m	2016 b Off balance sheet exposures pre CCF £m	2016 c Average CCF %	2016 d EAD post CRM and post CCF £m	2016 e Average PD %	2016 f Number of Obligors #	2016 g Average LGD %	2016 h Average Maturity (years) #	2016 i RWA £m	2016 j RWA density %	2016 k EL £m	2016 l Value adjustments and Provisions £m
0.00 to <0.15	3,668	1,873	74.08%	5,250	0.05%	375	22.18%	2.1	535	10.18%	1	
0.15 to <0.25	215	194	65.42%	365	0.18%	33	45.00%	1.2	130	35.64%	–	
0.25 to <0.50	211	264	76.52%	413	0.33%	63	44.84%	1.3	200	48.35%	1	
0.50 to <0.75	3	12	21.92%	5	0.62%	34	44.23%	1.4	4	85.13%	–	
0.75 to <2.50	80	54	35.16%	99	1.03%	49	38.98%	0.9	83	83.95%	–	
2.50 to <10.00	4	1	0.01%	4	3.89%	17	41.22%	1.3	5	144.91%	–	
10.00 to <100.00	–	–	–	–	–	6	–	–	–	–	–	
100.00 (Default)	42	–	–	42	100.00%	10	45.00%	1.6	–	–	19	
Sub-total	4,223	2,398	72.48%	6,178	0.78%	587	25.50%	2.0	957	15.50%	21	13

PD Scale Institutions	2015 a Original on-balance sheet gross exposure £m	2015 b Off balance sheet exposures pre CCF £m	2015 c Average CCF %	2015 d EAD post CRM and post CCF £m	2015 e Average PD %	2015 f Number of Obligors #	2015 g Average LGD %	2015 h Average Maturity (years) #	2015 i RWA £m	2015 j RWA density %	2015 k EL £m	2015 l Value adjustments and Provisions £m
0.00 to <0.15	4,770	2,004	74.36%	6,301	0.05%	400	22.26%	2.6	712	11.31%	1	
0.15 to <0.25	233	18	52.15%	242	0.18%	32	45.00%	1.4	105	43.38%	–	
0.25 to <0.50	238	256	76.02%	432	0.35%	73	44.87%	1.8	277	64.04%	1	
0.50 to <0.75	284	11	52.99%	290	0.73%	25	45.00%	0.3	218	75.00%	1	
0.75 to <2.50	48	22	15.08%	51	1.12%	50	42.24%	1.1	49	96.47%	–	
2.50 to <10.00	3	5	63.44%	7	4.28%	20	43.64%	1.2	11	157.63%	–	
10.00 to <100.00	–	24	99.99%	24	14.50%	6	45.00%	1.0	58	247.44%	2	
100.00 (Default)	17	–	–	17	100.00%	7	45.00%	1.0	–	–	7	
Sub-total	5,593	2,340	73.94%	7,364	0.39%	613	25.52%	2.4	1,430	19.42%	12	17

Key movements

– EAD post CRM and post CCF decreased £1.2bn to £6.2bn predominantly driven by a portfolio rebalancing exercise on the Group's covered bond portfolio throughout 2016.
– The average risk-weight has decreased 3.92% to 15.50% as a result of improved credit quality across the portfolio.
– The average PD has increased 0.39% to 0.78% driven by a modest increase in the proportion of defaulted exposure.

ANALYSIS OF CREDIT RISK EXPOSURES SUBJECT TO THE RETAIL IRB APPROACH

This section provides a detailed analysis, by PD Grade, of credit risk exposures subject to the Retail IRB Approach. Exposures are presented on a post CRM and post CCF basis.

Disclosures provided in the tables below take into account PD floors and LGD floors specified by regulators in respect of the calculation of regulatory capital requirements.

The Basel guidelines include a single prescribed scale for presenting the credit quality of all IRB portfolios by asset class. The tables that follow present the prescribed scale. This does not map directly to the internal scales per tables 11 and 12, but is apportioned on the same basis.

Throughout this section 'RWA density' represents the 'average risk weight'.

'Number of obligors' corresponds to the number of individual PDs (in each band). This means that a customer may be counted more than once in the same asset class. In the case of Other Retail, for example, which includes both Motor Finance and Unsecured Personal Loans, a customer may have both of those products which would be reported as two separate obligors.

Table 28: IRB – Credit risk exposures by portfolio and PD range – Residential mortgages (SME) (CR6)

PD Scale Residential mortgages (SME)	2016 a Original on-balance sheet gross exposure £m	2016 b Off balance sheet exposures pre CCF £m	2016 c Average CCF %	2016 d EAD post CRM and post CCF £m	2016 e Average PD %	2016 f Number of Obligors #	2016 g Average LGD %	2016 i RWA £m	2016 j RWA density %	2016 k EL £m	2016 l Value adjustments and Provisions £m	2016 m Undrawn commitments (post CCF) £m
0.00 to <0.15	–	–	–	–	–	–	–	–	–	–		–
0.15 to <0.25	–	–	–	–	–	–	–	–	–	–		–
0.25 to <0.50	–	–	–	–	–	–	–	–	–	–		–
0.50 to <0.75	**3,154**	**327**	**97.94%**	**3,475**	**0.54%**	**24,378**	**16.01%**	**376**	**10.82%**	**3**		**321**
0.75 to <2.50	**3,983**	**322**	**97.45%**	**4,296**	**1.13%**	**26,873**	**17.45%**	**827**	**19.24%**	**9**		**313**
2.50 to <10.00	**1,621**	**89**	**96.81%**	**1,709**	**4.17%**	**11,333**	**18.23%**	**745**	**43.61%**	**13**		**87**
10.00 to <100.00	**481**	**19**	**96.47%**	**499**	**21.61%**	**4,006**	**19.11%**	**379**	**75.90%**	**21**		**18**
100.00 (Default)	**228**	**4**	**97.16%**	**232**	**100.00%**	**2,277**	**8.34%**	**335**	**144.48%**	**19**		**4**
Sub-total	**9,467**	**761**	**97.56%**	**10,211**	**4.68%**	**68,867**	**16.97%**	**2,662**	**26.07%**	**65**	**17**	**743**

PD Scale Residential mortgages (SME)	2015 a Original on-balance sheet gross exposure £m	2015 b Off balance sheet exposures pre CCF £m	2015 c Average CCF %	2015 d EAD post CRM and post CCF £m	2015 e Average PD %	2015 f Number of Obligors #	2015 g Average LGD %	2015 i RWA £m	2015 j RWA density %	2015 k EL £m	2015 l Value adjustments and Provisions £m	2015 m Undrawn commitments (post CCF) £m
0.00 to <0.15	–	–	–	–	–	–	–	–	–	–		–
0.15 to <0.25	–	–	–	–	–	–	–	–	–	–		–
0.25 to <0.50	–	–	–	–	–	–	–	–	–	–		–
0.50 to <0.75	2,582	349	97.84%	2,923	0.54%	20,835	15.98%	317	10.85%	3		340
0.75 to <2.50	4,588	330	97.57%	4,911	1.12%	31,003	17.86%	974	19.81%	10		322
2.50 to <10.00	1,557	67	97.44%	1,622	4.02%	10,390	19.16%	736	45.39%	13		65
10.00 to <100.00	664	22	96.69%	686	17.09%	5,430	20.39%	569	83.02%	24		22
100.00 (Default)	369	5	98.21%	375	100.00%	4,390	7.91%	618	164.85%	29		5
Sub-total	9,760	773	97.66%	10,517	5.98%	72,048	17.35%	3,214	30.56%	79	24	754

Key movements

– The average PD has decreased 1.30% to 4.68%, and average risk-weight decreased 4.49% to 26.07%, driven by a reduction in the proportion of defaulted exposure.

Pillar 1 Capital requirements: Credit risk continued

Table 29: IRB – Credit risk exposures by portfolio and PD range – Residential mortgages (non-SME) (CR6)

	2016 a Original on-balance sheet gross exposure £m	2016 b Off balance sheet exposures pre CCF £m	2016 c Average CCF %	2016 d EAD post CRM and post CCF £m	2016 e Average PD %	2016 f Number of Obligors #	2016 g Average LGD %	2016 i RWA £m	2016 j RWA density %	2016 k EL £m	2016 l Value adjustments and Provisions £m	2016 m Undrawn commitments (post CCF) £m
0.00 to <0.15	210,668	10,358	96.82%	231,330	0.23%	2,140,658	9.94%	11,547	4.99%	58		10,028
0.15 to <0.25	30,428	314	58.20%	32,105	0.61%	281,254	10.41%	3,228	10.06%	21		183
0.25 to <0.50	25,396	183	59.61%	26,717	0.96%	227,202	11.33%	3,889	14.56%	29		109
0.50 to <0.75	7,345	26	56.57%	7,698	1.60%	67,819	12.70%	1,685	21.89%	15		15
0.75 to <2.50	12,066	491	24.81%	12,686	3.37%	102,578	16.67%	5,078	40.03%	58		122
2.50 to <10.00	6,350	4	58.68%	6,600	10.92%	50,120	15.75%	4,603	69.74%	94		2
10.00 to <100.00	3,777	–	–	3,877	45.53%	31,529	12.29%	2,739	70.65%	212		–
100.00 (Default)	4,286	–	–	4,286	100.00%	31,100	14.12%	4,119	96.09%	328		–
Sub-total	**300,316**	**11,376**	**91.94%**	**325,299**	**2.56%**	**2,932,260**	**10.63%**	**36,888**	**11.34%**	**815**	**1,703**	**10,459**

PD Scale Residential mortgages (non-SME)	2015 a Original on-balance sheet gross exposure £m	2015 b Off balance sheet exposures pre CCF £m	2015 c Average CCF %	2015 d EAD post CRM and post CCF £m	2015 e Average PD %	2015 f Number of Obligors #	2015 g Average LGD %	2015 i RWA £m	2015 j RWA density %	2015 k EL £m	2015 l Value adjustments and Provisions £m	2015 m Undrawn commitments (post CCF) £m
0.00 to <0.15	198,116	8,988	93.58%	216,613	0.13%	2,144,401	9.47%	6,685	3.09%	32		8,412
0.15 to <0.25	39,493	855	96.45%	42,279	0.47%	352,832	10.92%	4,018	9.50%	26		824
0.25 to <0.50	27,926	519	94.11%	29,757	0.71%	228,649	11.98%	4,032	13.55%	28		489
0.50 to <0.75	9,012	88	97.50%	9,514	1.60%	71,967	14.00%	2,425	25.49%	22		86
0.75 to <2.50	16,567	317	56.30%	17,476	3.06%	139,187	15.32%	6,734	38.53%	80		178
2.50 to <10.00	6,837	6	87.37%	7,107	10.64%	53,184	16.94%	5,297	74.53%	114		5
10.00 to <100.00	4,403	3	89.44%	4,525	43.69%	35,002	13.18%	3,373	74.55%	281		2
100.00 (Default)	4,019	–	–	4,019	100.00%	29,823	14.46%	2,474	61.54%	432		–
Sub-total	306,373	10,776	92.76%	331,290	2.46%	3,055,045	10.59%	35,038	10.58%	1,015	1,718	9,996

Key movements

– EAD post CRM and post CCF decreased £6.0bn to £325.3bn reflecting the Group's continued focus on balancing margin and risk considerations with volume growth in the current competitive low growth market.
– The average risk-weight increased 0.76% to 11.34% driven by model updates on the mainstream and buy-to-let portfolios. These updates also contributed to the reduction in expected loss, which decreased £0.2bn to £0.8bn.
– The increase in risk-weighted assets on accounts in default of £1.6bn to £4.1bn, and the associated increase in average risk-weight, was driven by model updates within the mainstream portfolio, with no discernible deterioration in risk on the defaulted book being observed over the period.

Table 30: Residential mortgage exposures by major portfolio

Major Portfolio	2016 Credit risk exposure £m	2016 Exposure weighted average PD %	2016 Exposure weighted average LGD[1] %	2016 Average risk weight %	2016 Undrawn commitments (pre CCF)[2] £m	2016 Undrawn commitments (post CCF) £m
UK mainstream	**238,980**	**2.41%**	**9.83%**	**9.23%**	**8,766**	**8,502**
UK buy-to-let	**58,108**	**1.63%**	**10.78%**	**13.06%**	**1,621**	**1,578**
UK self certified	**16,390**	**7.38%**	**9.36%**	**14.48%**	**511**	**262**
Irish mortgages	**3,653**	**9.13%**	**43.20%**	**98.18%**	**–**	**–**
Dutch mortgages	**5,847**	**1.73%**	**24.40%**	**23.36%**	**478**	**117**
Other mortgages	**12,532**	**4.34%**	**16.03%**	**23.10%**	**761**	**743**
Total	**335,510**	**2.62%**	**10.82%**	**11.79%**	**12,137**	**11,202**

Major Portfolio	2015 Credit risk exposure[3] £m	2015 Exposure weighted average PD[3] %	2015 Exposure weighted average LGD[1,3] %	2015 Average risk weight[3] %	2015 Undrawn commitments (pre CCF)[2,3] £m	2015 Undrawn commitments (post CCF)[3] £m
UK mainstream	243,087	2.28%	9.71%	8.59%	8,146	7,766
UK buy-to-let	59,497	1.57%	11.26%	9.96%	1,920	1,907
UK self certified	18,107	6.50%	9.89%	15.24%	521	268
Irish mortgages	3,306	9.08%	45.31%	110.48%	–	–
Dutch mortgages	4,677	2.18%	24.93%	28.04%	190	56
Other mortgages	13,133	5.65%	16.44%	28.31%	773	755
Total	341,807	2.57%	10.80%	11.19%	11,550	10,752

1 The 10 per cent LGD floor that applies to residential mortgage exposures is not applied in alignment with the portfolios in the table above, rather at aggregated portfolio levels. This leads to the mainstream and self-certified portfolios having an average LDG lower than 10 per cent.

2 Undrawn commitments predominantly relate to pipeline mortgages, offered but not drawn down by the customer.

3 2015 comparatives have been restated to present Buy-to-Let and other mortgage exposures on a consistent basis with 2016. The mortgage classification is aligned to the IRB rating system. The Lloyds Buy-to-Let and other mortgages were previously rated with mainstream assets. They are now rated in a separate model, and the restated 2015 numbers reflect this.

Key movements

- UK mainstream exposures have decreased by £4.1bn reflecting the Group's focus on balancing margin and risk considerations with volume growth in the current competitive low growth market. The increase in PD and average risk weight primarily reflect the introduction of new models.
- The increase in the average risk weight in the Buy-to-Let portfolio was driven by model updates.
- Self-certified exposures have reduced in the year, reflecting run off of the portfolio.
- The year-on-year reduction in average LGDs for Buy-to-Let and self certified mortgages principally reflects the impact of HPI.
- Irish mortgages exposures have increased due to foreign currency movements and the average risk weight has fallen by 12.3% primarily due to the impact of HPI.
- Dutch mortgages exposures have increased due to foreign currency movements and an increase in new business. The average PD has reduced reflecting improvements in credit quality leading to a lower average risk weight.
- Other mortgages predominantly comprises of Commercial Banking loans secured by mortgages on property for SMEs, though also includes some retail mortgage exposures that do not fit into the other categories of this table. The decrease in PD and average risk weight is driven by model updates in these retail portfolios.

Pillar 1 Capital requirements: Credit risk continued

Table 31: IRB – Credit risk exposures by portfolio and PD range – Qualifying revolving retail exposures (CR6)

PD Scale Qualifying revolving retail exposures	2016 a Original on-balance sheet gross exposure £m	2016 b Off balance sheet exposures pre CCF £m	2016 c Average CCF %	2016 d EAD post CRM and post CCF £m	2016 e Average PD %	2016 f Number of Obligors #	2016 g Average LGD %	2016 l RWA £m	2016 j RWA density %	2016 k EL £m	2016 l Value adjustments and Provisions £m	2016 m Undrawn commitments (post CCF) £m
0.00 to <0.15	896	18,975	64.83%	13,198	0.07%	10,510,198	75.23%	446	3.38%	7		12,302
0.15 to <0.25	665	5,701	56.12%	3,864	0.20%	2,674,829	74.77%	328	8.49%	6		3,199
0.25 to <0.50	1,161	5,666	61.92%	4,669	0.36%	4,577,241	77.26%	649	13.89%	13		3,508
0.50 to <0.75	1,049	2,883	64.46%	2,908	0.62%	2,544,591	79.32%	644	22.13%	14		1,858
0.75 to <2.50	3,476	4,630	62.37%	6,364	1.41%	3,859,895	79.61%	2,636	41.42%	72		2,888
2.50 to <10.00	3,148	2,040	73.46%	4,648	5.06%	2,788,757	80.33%	4,733	101.84%	189		1,499
10.00 to <100.00	734	150	124.07%	924	23.17%	617,086	80.98%	1,850	200.15%	173		186
100.00 (Default)	409	45	0.02%	409	100.00%	165,350	37.59%	787	192.13%	166		–
Sub-total	**11,538**	**40,090**	**63.46%**	**36,984**	**2.70%**	**27,737,947**	**76.88%**	**12,073**	**32.64%**	**640**	**241**	**25,440**

PD Scale Qualifying revolving retail exposures	2015 a Original on-balance sheet gross exposure £m	2015 b Off balance sheet exposures pre CCF £m	2015 c Average CCF %	2015 d EAD post CRM and post CCF £m	2015 e Average PD %	2015 f Number of Obligors #	2015 g Average LGD %	2015 l RWA £m	2015 j RWA density %	2015 k EL £m	2015 l Value adjustments and Provisions £m	2015 m Undrawn commitments (post CCF) £m
0.00 to <0.15	894	19,075	66.34%	13,550	0.07%	10,100,495	75.65%	453	3.34%	6		12,655
0.15 to <0.25	612	5,572	60.47%	3,981	0.20%	3,343,072	76.26%	349	8.76%	6		3,370
0.25 to <0.50	1,105	5,542	62.24%	4,554	0.36%	4,493,692	77.49%	637	13.99%	13		3,449
0.50 to <0.75	886	2,467	61.55%	2,405	0.61%	1,623,414	78.77%	527	21.90%	12		1,519
0.75 to <2.50	3,294	4,484	66.32%	6,268	1.41%	3,912,904	79.34%	2,580	41.17%	70		2,974
2.50 to <10.00	3,149	1,927	82.59%	4,743	5.04%	2,864,606	80.00%	4,802	101.24%	192		1,592
10.00 to <100.00	764	144	141.69%	974	22.95%	641,798	80.32%	1,933	198.48%	180		205
100.00 (Default)	500	38	0.00%	500	100.00%	194,756	33.37%	1,220	243.96%	132		–
Sub-total	11,204	39,249	65.64%	36,975	2.97%	27,174,737	76.88%	12,501	33.81%	611	244	25,763

Key movements

– EAD post CRM and post CCF remained relatively flat during the year with continued growth in credit cards offset by model calibrations.

– The decrease in risk-weighted assets on accounts in default of £0.4bn to £0.8bn, and the associated decrease in average risk-weight, was driven by model updates on both credit cards and personal current accounts.

Table 32: IRB – Credit risk exposures by portfolio and PD range – Other SME (CR6)

PD Scale Other SME	2016 a Original on-balance sheet gross exposure £m	2016 b Off balance sheet exposures pre CCF £m	2016 c Average CCF %	2016 d EAD post CRM and post CCF £m	2016 e Average PD %	2016 f Number of Obligors #	2016 g Average LGD %	2016 l RWA £m	2016 j RWA density %	2016 k EL £m	2016 l Value adjustments and Provisions £m	2016 m Undrawn commitments (post CCF) £m
0.00 to <0.15	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**		**–**
0.15 to <0.25	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**		**–**
0.25 to <0.50	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**		**–**
0.50 to <0.75	**303**	**375**	**99.99%**	**678**	**0.54%**	**56,640**	**77.38%**	**345**	**50.86%**	**3**		**375**
0.75 to <2.50	**575**	**332**	**99.98%**	**907**	**1.15%**	**58,385**	**75.42%**	**622**	**68.60%**	**8**		**332**
2.50 to <10.00	**360**	**110**	**99.98%**	**470**	**4.52%**	**33,524**	**77.10%**	**451**	**96.16%**	**16**		**110**
10.00 to <100.00	**127**	**22**	**99.98%**	**148**	**23.00%**	**32,132**	**81.13%**	**198**	**133.37%**	**28**		**22**
100.00 (Default)	**238**	**3**	**99.86%**	**242**	**100.00%**	**10,207**	**9.39%**	**112**	**46.20%**	**23**		**3**
Sub-total	**1,603**	**842**	**99.98%**	**2,445**	**12.74%**	**190,888**	**70.10%**	**1,728**	**70.68%**	**78**	**13**	**842**

PD Scale Other SME	2015 a Original on-balance sheet gross exposure £m	2015 b Off balance sheet exposures pre CCF £m	2015 c Average CCF %	2015 d EAD post CRM and post CCF £m	2015 e Average PD %	2015 f Number of Obligors #	2015 g Average LGD %	2015 l RWA £m	2015 j RWA density %	2015 k EL £m	2015 l Value adjustments and Provisions £m	2015 m Undrawn commitments (post CCF) £m
0.00 to <0.15	–	–	–	–	–	–	–	–	–	–		–
0.15 to <0.25	–	–	–	–	–	–	–	–	–	–		–
0.25 to <0.50	–	–	–	–	–	–	–	–	–	–		–
0.50 to <0.75	287	406	99.98%	694	0.54%	55,656	75.93%	321	46.30%	3		406
0.75 to <2.50	706	318	99.98%	1,024	1.15%	67,284	74.91%	663	64.75%	9		318
2.50 to <10.00	486	84	99.98%	570	4.19%	28,299	75.34%	516	90.55%	18		84
10.00 to <100.00	140	24	99.98%	164	17.69%	33,100	81.02%	205	125.20%	24		24
100.00 (Default)	206	3	99.98%	209	100.00%	10,229	11.21%	102	48.63%	23		3
Sub-total	1,825	835	99.98%	2,661	10.43%	194,568	70.63%	1,807	67.91%	77	14	835

Key movements

– The average PD increased 2.31%, predominantly driven by a modest increase in defaulted exposure.

Pillar 1 Capital requirements: Credit risk continued

Table 33: IRB – Credit risk exposures by portfolio and PD range – Other non-SME (CR6)

PD Scale Other non-SME	2016 a Original on-balance sheet gross exposure £m	2016 b Off balance sheet exposures pre CCF £m	2016 c Average CCF %	2016 d EAD post CRM and post CCF £m	2016 e Average PD %	2016 f Number of Obligors #	2016 g Average LGD %	2016 I RWA £m	2016 j RWA density %	2016 k EL £m	2016 l Value adjustments and Provisions £m	2016 m Undrawn commitments (post CCF) £m
0.00 to <0.15	314	1	30.00%	315	0.09%	34,244	40.65%	32	10.15%	–		–
0.15 to <0.25	149	2	30.00%	152	0.21%	26,947	83.43%	56	36.79%	–		–
0.25 to <0.50	3,566	6	30.00%	3,580	0.37%	395,742	42.58%	980	27.39%	6		2
0.50 to <0.75	2,206	5	30.00%	2,219	0.71%	239,467	50.28%	1,002	45.14%	8		2
0.75 to <2.50	6,153	19	30.00%	6,199	1.54%	734,596	67.40%	5,169	83.39%	63		6
2.50 to <10.00	2,691	12	30.00%	2,721	4.30%	350,106	74.05%	3,087	113.47%	87		4
10.00 to <100.00	538	4	30.00%	546	28.63%	88,692	66.81%	793	145.41%	103		1
100.00 (Default)	294	–	–	294	100.00%	25,519	33.16%	499	169.46%	117		–
Sub-total	15,911	49	30.00%	16,026	4.32%	1,895,313	59.59%	11,618	72.50%	384	201	15

PD Scale Other non-SME	2015 a Original on-balance sheet gross exposure £m	2015 b Off balance sheet exposures pre CCF £m	2015 c Average CCF %	2015 d EAD post CRM and post CCF £m	2015 e Average PD %	2015 f Number of Obligors #	2015 g Average LGD %	2015 I RWA £m	2015 j RWA density %	2015 k EL £m	2015 l Value adjustments and Provisions £m	2015 m Undrawn commitments (post CCF) £m
0.00 to <0.15	264	–	20.00%	266	0.09%	26,855	40.90%	27	10.23%	–		–
0.15 to <0.25	137	1	20.00%	141	0.21%	25,694	81.74%	51	35.91%	–		–
0.25 to <0.50	2,903	4	20.00%	2,916	0.37%	352,970	43.48%	817	28.02%	5		1
0.50 to <0.75	1,798	4	20.00%	1,810	0.70%	211,633	51.79%	838	46.33%	6		1
0.75 to <2.50	5,770	16	20.00%	5,816	1.53%	731,812	70.82%	5,092	87.55%	64		3
2.50 to <10.00	2,562	10	20.00%	2,591	4.34%	355,585	76.71%	3,048	117.65%	86		2
10.00 to <100.00	445	2	20.00%	450	29.27%	79,690	69.36%	673	149.57%	91		–
100.00 (Default)	341	–	–	341	100.00%	26,777	28.29%	806	236.37%	80		–
Sub-total	14,220	37	20.00%	14,331	4.87%	1,811,016	62.41%	11,352	79.22%	332	180	7

Key movements

– EAD post CRM and post CCF increased £1.7bn to £16.0bn driven by continued growth in UK motor finance business.

– The average LGD decreased 2.82% to 59.59% and average risk-weight decreased 6.72% to 72.50% due to growth in the lower risk-weighted UK motor finance business with assets secured on vehicles.

ANALYSIS OF CREDIT RISK EXPOSURES SUBJECT TO OTHER IRB APPROACHES

Corporate specialised lending exposures subject to supervisory slotting

Corporate specialised lending exposures subject to the IRB Supervisory Slotting Approach are assigned to a grade, the determination of which takes into account the following factors:

- financial strength e.g. market conditions, financial ratios, stress analysis, financial structure, cash flow predictability, market liquidity and degree of over-collateralisation of trade;
- political and legal environment e.g. political risks, country risks, force majeure risks, government support, stability of legal and regulatory environment, enforceability of contracts and collateral and security;
- transaction and/or asset characteristics e.g. location, design and technology risks, construction risks, completion guarantees, financial strength of contractors and reliability, operating risks, off-take risks, supply risks, financing terms, resale values, value sensitivities and susceptibility to damage;
- strength of the sponsor and developer including any public private partnership income stream e.g. sponsor's financial strength, quality of financial disclosure, sponsor's support, reputation and track record, trading controls and hedging policies; and
- security package e.g. assignment of contracts and accounts, pledge of assets, lender's control over cash flow, covenant package, reserve funds, nature of lien, quality of insurance coverage, asset control and inspection rights.

Differing criteria apply to each of the four sub-classes of specialised lending recognised by the PRA: i.e. project finance, object finance, commodities finance and income-producing real estate.

Once assigned to a grade, the exposure is risk-weighted in accordance with the risk weight applicable to that grade and remaining maturity banding.

As at 31 December 2016, corporate specialised lending exposures subject to supervisory slotting amounted to £18.8bn (2015: £19.9bn). Risk-weighted assets arising from this amounted to £13.5bn (2015: £14.4bn) as analysed in the table below.

Table 34A: IRB (specialised lending) (CR10)

		2016					
		Specialised lending					
Regulatory Categories	Remaining maturity	On-balance sheet amount £m	Off-balance sheet amount £m	RW %	Exposure amount £m	RWA £m	Expected losses £m
1) Strong[1]	Less than 2.5 years	2,356	505	50%	2,772	1,192	–
	Equal to or more than 2.5 years	4,255	1,164	70%	5,090	3,307	19
2) Good	Less than 2.5 years	2,465	644	70%	3,004	2,102	12
	Equal to or more than 2.5 years	4,294	642	90%	4,890	4,312	38
3) Satisfactory	Less than 2.5 years	709	20	115%	736	843	21
	Equal to or more than 2.5 years	1,097	89	115%	1,183	1,349	33
4) Weak	Less than 2.5 years	29	1	250%	30	73	2
	Equal to or more than 2.5 years	116	–	250%	116	289	9
5) Default[2,3]	Less than 2.5 years	406	37	0%	655	–	328
	Equal to or more than 2.5 years	207	8	0%	338	–	170
Total	Less than 2.5 years	5,965	1,207		7,197	4,210	363
	Equal to or more than 2.5 years	9,969	1,903		11,617	9,257	269

		2015					
Regulatory Categories	Remaining maturity	On-balance sheet amount £m	Off-balance sheet amount £m	RW %	Exposure amount £m	RWA £m	Expected losses £m
1) Strong[1]	Less than 2.5 years	1,409	245	50%	1,597	798	–
	Equal to or more than 2.5 years	5,005	1,513	70%	6,260	3,864	22
2) Good	Less than 2.5 years	2,413	468	70%	2,799	1,955	11
	Equal to or more than 2.5 years	4,356	705	90%	4,942	4,358	39
3) Satisfactory	Less than 2.5 years	871	13	115%	912	1,045	26
	Equal to or more than 2.5 years	1,532	47	115%	1,596	1,822	45
4) Weak	Less than 2.5 years	5	–	250%	5	13	–
	Equal to or more than 2.5 years	206	7	250%	214	531	17
5) Default[2,3]	Less than 2.5 years	684	31	0%	1,099	–	550
	Equal to or more than 2.5 years	271	11	0%	463	–	232
Total	Less than 2.5 years	5,382	759		6,412	3,811	587
	Equal to or more than 2.5 years	11,369	2,283		13,475	10,575	354

[1] The average risk weight % in the Strong slotting grade is below the specified regulatory value as a result of exposures to customers which are classed as Strong, typically in the shipping industry, having facilities which have been structured such that the Group also benefits from additional financial collateral from third parties which is not ordinarily part of the security package for Slotting transactions. As a result, recognition of the collateral is applied outside the standard Slotting risk weights, in line with the IRB approach.

[2] Exposures categorised as 'default' do not attract a risk weighting but instead are treated as EL deductions at a rate of 50 per cent of the exposure value.

[3] Total for the on-balance sheet and off-balance sheet exposures in default is lower than the exposure amount (presented on a post CRM and post CCF basis). This is due to the offset of the impairment allowances against the on-balance sheet amounts In line with the specified EBA requirements for this table.

Key movements

- Corporate specialised lending (slotting) exposures and risk-weighted assets reduced by £1.1bn and £0.9bn respectively largely due to active portfolio management.

Pillar 1 Capital requirements: Credit risk continued

ANALYSIS OF EQUITY EXPOSURES

EQUITY EXPOSURES SUBJECT TO THE SIMPLE RISK WEIGHT METHOD

An analysis of equity exposures categorised and risk-weighted assets under the Simple Risk Weight Method is provided in the table below.

As at 31 December 2016, total credit risk exposures in respect of equities subject to the Simple Risk Weight Method amounted to £3.4bn (2015: £4.3bn). Risk-weighted assets arising from this amounted to £7.7bn (2015: £9.9bn).

Table 34B: Equity exposures subject to the simple risk weight method (CR10)

2016						
	Equities under the simple risk-weight approach					
Categories	On-balance sheet amount £m	Off-balance sheet amount £m	RW %	Exposure amount £m	RWA £m	Capital requirements £m
Exchange-traded equity exposures	461	–	290%	461	1,337	107
Private equity exposures	2,492	91	190%	2,583	4,909	393
Other equity exposures	382	–	370%	382	1,413	113
Total	3,335	91		3,426	7,659	613

2015						
Categories	On-balance sheet amount £m	Off-balance sheet amount £m	RW %	Exposure amount £m	RWA £m	Capital requirements £m
Exchange-traded equity exposures	978	–	290%	978	2,837	227
Private equity exposures	2,843	138	190%	2,981	5,664	452
Other equity exposures	376	–	370%	376	1,392	111
Total	4,198	138		4,335	9,893	790

Key movements

– Equity exposures and risk-weighted assets reduced by £0.9bn and £2.2bn respectively largely due to the disposal of certain strategic investments, partly offset by increases to the valuation of centrally held investments.

Non-trading book exposures in equities

Non-trading book exposures in equities held by the Group primarily arise within Commercial Banking and Central Items through a combination of individual transactions in the private equity market, debt for equity swaps and strategic equity investments.

The Group's strategic equity investments predominantly arise as a result of management actions undertaken by the Group resulting in equity holdings.

Private equity investments are generally medium term investments, held for gain and include limited partnership stakes and listed and unlisted equity shares. Private equity investments are managed, and evaluated, in accordance with a documented risk management or investment strategy and reported to key management personnel on that basis.

The accounting techniques and valuation methodologies applied are set out within the Group's accounting policies, references to which are provided below.

Available-for-sale financial assets, Note 2 (Accounting policies) of the 2016 Lloyds Banking Group plc Annual Report and Accounts.

Equity investments (including venture capital), Note 49 (Financial instruments) of the 2016 Lloyds Banking Group plc Annual Report and Accounts.

A reference to the Group's accounting policies in relation to the recognition of impairment losses on available-for-sale financial assets is provided on page 46.

The balance sheet value of non-trading book exposures in equities, as at 31 December 2016, is presented in the table below. There was no difference between the balance sheet value and the fair value of these exposures.

Table 35: Analysis of non-trading book exposures in equities

Equity grouping	2016 Balance sheet value £m	2015 Balance sheet value £m
Publicly quoted equities	**469**	475
Privately held equities	**1,571**	1,630
Total	**2,040**	2,105

There were £311m (2015: £nil) realised gains recognised in the year to 31 December 2016 in respect of the sale and liquidation of non-trading book exposures in equities.

As at 31 December 2016, net unrealised gains on available-for-sale equity investments amounted to £245m (2015: £82m).

Pillar 1 Capital requirements: Credit risk continued

ANALYSIS OF CREDIT RISK EXPOSURES SUBJECT TO THE STANDARDISED APPROACH

Standardised exposures in the table below are stated on two different basis (before CCF and CRM and after CCF and CRM).

Throughout this section 'RWA density' represents the 'average risk weight'.

As at 31 December 2016, credit risk exposures risk-weighted under the Standardised Approach after CCF and CRM, amounted to £109.4bn (2015: £117.5bn), generating risk-weighted assets of £18.7bn (2015: £20.4bn).

Table 36: Standardised approach – credit risk exposure and Credit Risk Mitigation (CRM) effects (CR4)

		2016					
		a	b	c	d	e	f
		Exposures before CCF and CRM		Exposures post-CCF and CRM		RWA and RWA density	
		On balance sheet amount £m	Off balance sheet amount £m	On balance sheet amount £m	Off balance sheet amount £m	RWA £m	RWA density[1] %
1	Central governments and central banks	**80,918**	**239**	**80,918**	**382**	**–**	**–**
2	Regional governments or local authorities	**–**	**–**	**–**	**–**	**–**	**–**
3	Public sector entities	**2**	**–**	**2**	**–**	**2**	**100%**
4	Multilateral development banks	**1,753**	**–**	**1,753**	**–**	**–**	**–**
5	International organisations	**–**	**–**	**–**	**–**	**–**	**–**
6	Institutions	**218**	**291**	**218**	**14**	**117**	**50%**
7	Corporates	**10,987**	**5,945**	**9,782**	**2,574**	**10,801**	**87%**
8	Retail	**3,963**	**837**	**3,963**	**151**	**2,761**	**67%**
9	Secured by mortgages on immovable property	**5,499**	**10**	**5,499**	**5**	**1,981**	**36%**
	of which: residential property	**5,496**	**10**	**5,496**	**5**	**1,978**	**36%**
	of which: commercial property	**3**	**–**	**3**	**–**	**3**	**100%**
10	Exposures in default	**781**	**17**	**781**	**8**	**883**	**112%**
11	Exposures associated with particularly high risk	**–**	**–**	**–**	**–**	**–**	**–**
12	Covered bonds	**–**	**–**	**–**	**–**	**–**	**–**
13	Short term claims on institutions and corporates	**–**	**–**	**–**	**–**	**–**	**–**
14	Collective investment undertakings (CIUs)	**224**	**–**	**224**	**–**	**45**	**20%**
15	Equity exposures	**–**	**–**	**–**	**–**	**–**	**–**
16	Other items	**3,016**	**75**	**3,016**	**75**	**2,098**	**68%**
17	**Total**	**107,361**	**7,414**	**106,156**	**3,209**	**18,688**	**17%**

		2015					
		a	b	c	d	e	f
		Exposures before CCF and CRM		Exposures post-CCF and CRM		RWA and RWA density	
		On balance sheet amount £m	Off balance sheet amount £m	On balance sheet amount £m	Off balance sheet amount £m	RWA £m	RWA density[1] %
1	Central governments and central banks	88,292	163	88,292	123	–	–
2	Regional governments or local authorities	1	–	1	–	–	20%
3	Public sector entities	2	–	2	–	2	100%
4	Multilateral development banks	997	–	997	–	–	–
5	International organisations	–	–	–	–	–	–
6	Institutions	103	318	103	5	24	22%
7	Corporates	11,597	6,369	10,853	2,673	11,921	88%
8	Retail	4,282	904	4,282	156	2,880	65%
9	Secured by mortgages on immovable property	5,834	11	5,834	6	2,109	36%
	of which: residential property	5,803	11	5,803	6	2,078	36%
	of which: commercial property	31	–	31	–	31	100%
10	Exposures in default	939	93	939	66	1,198	119%
11	Exposures associated with particularly high risk	–	–	–	–	–	–
12	Covered bonds	–	–	–	–	–	–
13	Short term claims on institutions and corporates	–	–	–	–	–	–
14	Collective investment undertakings (CIUs)	–	–	–	–	–	–
15	Equity exposures	–	–	–	–	–	–
16	Other items	3,204	–	3,204	–	2,309	72%
17	**Total**	115,251	7,858	114,507	3,029	20,443	17%

[1] RWA density is RWA expressed as a percentage of Exposures post-CCF and CRM.

Table 37: Standardised approach – exposures by asset class (CR5)

Standardised exposures in the table below are stated after CCF and CRM.

2016

		Risk Weight																
	Exposure Classes	**0% £m**	**2% £m**	**4% £m**	**10% £m**	**20% £m**	**35% £m**	**50% £m**	**70% £m**	**75% £m**	**100% £m**	**150% £m**	**250% £m**	**370% £m**	**1250% £m**	**Others £m**	**Total £m**	**Of which: Unrated[1] £m**
1	Central governments or central banks	81,300	–	–	–	–	–	–	–	–	–	–	–	–	–	–	81,300	81,300
2	Regional government or local authorities	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
3	Public sector entities	–	–	–	–	–	–	–	–	–	2	–	–	–	–	–	2	2
4	Multilateral development banks	1,753	–	–	–	–	–	–	–	–	–	–	–	–	–	–	1,753	1,753
5	International organisations	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
6	Institutions	–	–	–	–	115	–	47	–	–	70	–	–	–	–	–	232	10
7	Corporates	–	–	–	–	198	–	2,275	–	–	9,882	1	–	–	–	–	12,356	9,767
8	Retail	–	–	–	–	–	–	–	–	4,110	4	–	–	–	–	–	4,114	4,114
9	Secured by mortgages on immovable property	–	–	–	–	–	5,229	235	–	27	13	–	–	–	–	–	5,504	5,504
	of which: residential property	–	–	–	–	–	5,229	235	–	27	10	–	–	–	–	–	5,501	5,501
	of which: commercial property	–	–	–	–	–	–	–	–	–	3	–	–	–	–	–	3	3
10	Exposures in default	–	–	–	–	–	–	–	–	–	600	189	–	–	–	–	789	789
11	Higher-risk categories	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
12	Covered bonds	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
13	Institutions and corporations with a short term credit assessment	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
14	Collective investment undertakings	–	–	–	–	224	–	–	–	–	–	–	–	–	–	–	224	–
15	Equity	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
16	Other items	223	–	–	–	963	–	–	–	–	1,905	–	–	–	–	–	3,091	3,091
17	**Total**	**83,276**	**–**	**–**	**–**	**1,500**	**5,229**	**2,557**	**–**	**4,137**	**12,476**	**190**	**–**	**–**	**–**	**–**	**109,355**	**106,330**

2015

		Risk Weight																
	Exposure Classes	0% £m	2% £m	4% £m	10% £m	20% £m	35% £m	50% £m	70% £m	75% £m	100% £m	150% £m	250% £m	370% £m	1250% £m	Others £m	Total £m	Of which: Unrated[1] £m
1	Central governments or central banks	88,415	–	–	–	–	–	–	–	–	–	–	–	–	–	–	88,415	88,415
2	Regional government or local authorities	–	–	–	–	1	–	–	–	–	–	–	–	–	–	–	1	1
3	Public sector entities	–	–	–	–	–	–	–	–	–	2	–	–	–	–	–	2	–
4	Multilateral development banks	997	–	–	–	–	–	–	–	–	–	–	–	–	–	–	997	997
5	International organisations	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
6	Institutions	–	–	–	–	99	–	9	–	–	–	–	–	–	–	–	108	14
7	Corporates	–	–	–	–	336	–	1,967	–	–	11,223	–	–	–	–	–	13,526	11,562
8	Retail	–	–	–	–	–	–	–	–	4,432	6	–	–	–	–	–	4,438	4,438
9	Secured by mortgages on immovable property	–	–	–	–	–	5,544	248	–	13	35	–	–	–	–	–	5,840	5,840
	of which: residential property	–	–	–	–	–	5,544	248	–	13	4	–	–	–	–	–	5,809	5,809
	of which: commercial property	–	–	–	–	–	–	–	–	–	31	–	–	–	–	–	31	31
10	Exposures in default	–	–	–	–	–	–	–	–	–	620	385	–	–	–	–	1,005	990
11	Higher-risk categories	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
12	Covered bonds	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
13	Institutions and corporations with a short term credit assessment	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
14	Collective investment undertakings	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
15	Equity	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
16	Other items	263	–	–	–	790	–	–	–	–	2,151	–	–	–	–	–	3,204	3,132
17	**Total**	89,675	–	–	–	1,226	5,544	2,224	–	4,445	14,037	385	–	–	–	–	117,536	115,389

[1] Of which Unrated includes any exposure for which a credit assessment by a nominated ECAI is not available or that have specific risk weights applied depending on their class as specified in articles 113 to 134.

Pillar 1 Capital requirements: Credit risk continued

ANALYSIS OF CREDIT RISK EXPOSURES BY INDUSTRY

Credit risk exposures as at 31 December 2016, analysed by major industrial sector, are provided in the table below.

Table 38: Credit risk exposures analysed by major industrial sector

	2016 Agriculture, forestry and fishing £m	2016 Energy and water supply £m	2016 Manufacturing £m	2016 Construction £m	2016 Transport, distribution and hotels £m	2016 Postal and comms £m	2016 Property companies £m	2016 Financial, business and other services £m	2016 Personal: mortgages £m	2016 Personal: other £m	2016 Lease financing £m	2016 Hire purchase £m	2016 Total £m
Exposures subject to the IRB approach													
Foundation IRB approach													
Corporate – main	213	3,387	12,187	3,229	12,605	2,066	9,744	30,477	–	–	2,221	2,398	78,527
Corporate – SME	1,265	44	1,371	462	2,706	43	2,110	3,613	–	–	39	328	11,981
Corporate – specialised lending	–	–	–	–	–	–	2	–	–	–	–	–	2
Central governments and central banks	–	–	–	–	–	–	–	15,153	–	–	–	–	15,153
Institutions	–	3	–	10	–	–	–	5,901	–	–	55	42	6,011
Retail IRB approach													
Retail mortgages	1,512	7	346	321	1,707	32	4,324	1,960	325,299	2	–	–	335,510
of which: residential mortgages (SME)	1,512	7	346	321	1,707	32	4,324	1,960	–	2	–	–	10,211
of which: residential mortgages (non-SME)	–	–	–	–	–	–	–	–	325,299	–	–	–	325,299
Qualifying revolving retail exposures	–	–	–	–	–	–	–	–	–	36,984	–	–	36,984
Other SME	217	3	180	314	562	15	333	818	–	3	–	–	2,445
Other non-SME	–	–	–	–	–	–	–	–	–	7,816	–	8,210	16,026
Other IRB approaches													
Corporate – specialised lending	–	1,067	325	254	995	32	14,853	570	–	–	718	–	18,814
Equities – exchange traded	–	–	–	–	–	–	–	461	–	–	–	–	461
Equities – private equity	–	84	223	145	320	474	43	1,294	–	–	–	–	2,583
Equities – other	–	–	–	–	–	–	–	382	–	–	–	–	382
Securitisation positions	–	–	–	–	–	–	–	26,066	–	–	–	–	26,066
Total – IRB approach	3,207	4,595	14,632	4,735	18,895	2,662	31,409	86,695	325,299	44,805	3,033	10,978	550,945
Exposures subject to the standardised approach													
Central governments and central banks	–	–	–	–	–	–	–	81,021	–	–	–	–	81,021
Regional governments or local authorities	–	–	–	–	–	–	–	–	–	–	–	–	–
Public sector entities	–	–	–	–	–	–	–	2	–	–	–	–	2
Multilateral development banks	–	–	–	–	–	–	–	1,753	–	–	–	–	1,753
International organisations	–	–	–	–	–	–	–	–	–	–	–	–	–
Institutions	–	–	–	–	–	–	–	271	–	–	8	–	279
Corporates	1,565	322	1,791	103	2,862	103	1,022	4,177	96	948	475	47	13,511
Retail	1,060	3	23	20	148	1	225	176	977	1,040	–	441	4,114
Secured by mortgages on immovable property	–	–	1	–	–	–	1	253	5,249	1	–	–	5,504
of which: residential property	–	–	1	–	–	–	1	253	5,246	1	–	–	5,501
of which: commercial property	–	–	–	–	–	–	–	–	3	–	–	–	3
Exposures in default	13	–	6	15	25	–	136	33	476	82	1	2	789
Exposures associated with particularly high risk	–	–	–	–	–	–	–	–	–	–	–	–	–
Covered bonds	–	–	–	–	–	–	–	–	–	–	–	–	–
Securitisation positions	–	–	–	–	–	–	–	1,184	–	–	–	–	1,184
Short term claims on institutions and corporates	–	–	–	–	–	–	–	–	–	–	–	–	–
Collective investment undertakings (CIUs)	–	–	–	–	–	–	–	224	–	–	–	–	224
Equity Exposures	–	–	–	–	–	–	–	–	–	–	–	–	–
Total – standardised approach	2,638	325	1,821	138	3,035	104	1,383	89,094	6,798	2,071	484	490	108,381
Total	5,845	4,920	16,453	4,873	21,930	2,766	32,792	175,789	332,097	46,876	3,517	11,468	659,326
Other items													3,091
Non-credit obligation assets													10,890
Total credit risk exposure													673,307

	2015 Agriculture, forestry and fishing £m	2015 Energy and water supply £m	2015 Manufacturing £m	2015 Construction £m	2015 Transport, distribution and hotels £m	2015 Postal and comms £m	2015 Property companies £m	2015 Financial, business and other services £m	2015 Personal: mortgages £m	2015 Personal: other £m	2015 Lease financing £m	2015 Hire purchase £m	2015 Total £m
Exposures subject to the IRB approach													
Foundation IRB approach													
Corporate – main	219	4,050	11,291	2,835	12,347	3,743	9,697	31,944	–	3	2,235	2,265	80,629
Corporate – SME	1,383	53	1,672	450	2,919	40	1,902	4,197	–	–	43	305	12,964
Corporate – specialised lending	–	–	–	–	–	–	4	2	–	–	–	–	6
Central governments and central banks	–	–	–	–	–	–	–	15,716	–	–	–	–	15,716
Institutions	–	3	–	8	–	–	–	7,268	–	–	53	32	7,364
Retail IRB approach													
Retail mortgages	1,500	7	359	350	1,827	34	4,440	1,998	331,290	2	–	–	341,807
of which: residential mortgages (SME)	1,500	7	359	350	1,827	34	4,440	1,998	–	2	–	–	10,517
of which: residential mortgages (non-SME)	–	–	–	–	–	–	–	–	331,290	–	–	–	331,290
Qualifying revolving retail exposures	–	–	–	–	–	–	–	–	–	36,975	–	–	36,975
Other SME	241	2	190	303	595	16	441	870	–	3	–	–	2,661
Other non-SME	–	–	–	–	–	–	–	–	–	7,890	–	6,441	14,331
Other IRB approaches													
Corporate – specialised lending	–	1,298	345	346	1,039	167	14,861	1,127	–	–	704	–	19,887
Equities – exchange traded	–	–	–	–	–	–	92	886	–	–	–	–	978
Equities – private equity	–	102	296	136	430	547	87	1,383	–	–	–	–	2,981
Equities – other	–	–	–	–	–	–	–	376	–	–	–	–	376
Securitisation positions	–	–	–	–	–	–	–	22,125	–	–	–	–	22,125
Total – IRB approach	3,343	5,515	14,153	4,428	19,157	4,547	31,524	87,892	331,290	44,873	3,035	9,043	558,800
Exposures subject to the standardised approach													
Central governments and central banks	–	–	–	–	–	–	–	88,415	–	–	–	–	88,415
Regional governments or local authorities	–	–	–	–	–	–	–	1	–	–	–	–	1
Public sector entities	–	–	–	–	–	–	–	2	–	–	–	–	2
Multilateral development banks	–	–	–	–	–	–	–	997	–	–	–	–	997
International organisations	–	–	–	–	–	–	–	–	–	–	–	–	–
Institutions	–	–	–	–	–	–	–	165	–	–	5	–	170
Corporates	2,293	190	1,419	139	2,701	11	1,163	5,091	98	956	360	42	14,463
Retail	1,795	2	22	23	146	2	203	171	862	894	–	318	4,438
Secured by mortgages on immovable property	–	–	1	–	–	–	6	163	5,669	1	–	–	5,840
of which: residential property	–	–	1	–	–	–	6	135	5,666	1	–	–	5,809
of which: commercial property	–	–	–	–	–	–	–	28	3	–	–	–	31
Exposures in default	15	–	7	70	130	–	73	159	446	102	2	1	1,005
Exposures associated with particularly high risk	–	–	–	–	–	–	–	–	–	–	–	–	–
Covered bonds	–	–	–	–	–	–	–	–	–	–	–	–	–
Securitisation positions	–	–	–	–	–	–	–	–	–	–	–	–	–
Short term claims on institutions and corporates	–	–	–	–	–	–	–	–	–	–	–	–	–
Collective investment undertakings (CIUs)	–	–	–	–	–	–	–	–	–	–	–	–	–
Equity Exposures	–	–	–	–	–	–	–	–	–	–	–	–	–
Total – standardised approach	4,103	192	1,449	232	2,977	13	1,445	95,164	7,075	1,953	367	361	115,331
Total	7,446	5,707	15,602	4,660	22,134	4,560	32,969	183,056	338,365	46,826	3,402	9,404	674,131
Other items													3,204
Non-credit obligation assets													9,228
Total credit risk exposure													686,563

Pillar 1 Capital requirements: Credit risk continued

ANALYSIS OF CREDIT RISK EXPOSURES BY GEOGRAPHY

Credit risk exposures as at 31 December 2016, analysed by geographical region, based on the country of residence/incorporation of the customer, are provided in the table below.

Table 39: Credit risk exposures analysed by geographical region

	2016 United Kingdom £m	2016 Rest of Europe £m	2016 United States of America £m	2016 Asia-Pacific £m	2016 Other £m	2016 Total £m
Exposures subject to the IRB approach						
Foundation IRB approach						
Corporate – main	54,852	8,821	11,641	627	2,586	78,527
Corporate – SME	11,887	33	–	–	61	11,981
Corporate – specialised lending	2	–	–	–	–	2
Central governments and central banks	–	156	14,779	–	218	15,153
Institutions	1,793	2,039	1,252	424	503	6,011
Retail IRB approach						
Retail mortgages	326,000	9,504	–	1	5	335,510
of which: residential mortgages (SME)	10,201	4	–	1	5	10,211
of which: residential mortgages (non-SME)	315,799	9,500	–	–	–	325,299
Qualifying revolving retail exposures	36,984	–	–	–	–	36,984
Other SME	2,444	–	–	–	1	2,445
Other non-SME	15,974	52	–	–	–	16,026
Other IRB approaches						
Corporate – specialised lending	14,389	2,818	569	114	924	18,814
Equities – exchange traded	361	100	–	–	–	461
Equities – private equity	2,465	56	60	2	–	2,583
Equities – other	382	–	–	–	–	382
Securitisation positions[1]	17,776	1,366	6,734	–	190	26,066
Total – IRB approach	485,309	24,945	35,035	1,168	4,488	550,945
Exposures subject to the standardised approach						
Central governments and central banks	69,957	11,064	–	–	–	81,021
Regional governments or local authorities	–	–	–	–	–	–
Public sector entities	2	–	–	–	–	2
Multilateral development banks	41	397	1,283	32	–	1,753
International organisations	–	–	–	–	–	–
Institutions	90	101	87	1	–	279
Corporates	8,057	1,940	2,193	284	1,037	13,511
Retail	2,755	1,339	2	9	9	4,114
Secured by mortgages on immovable property	4,479	276	100	501	148	5,504
of which: residential property	4,476	276	100	501	148	5,501
of which: commercial property	3	–	–	–	–	3
Exposures in default	707	48	6	10	18	789
Exposures associated with particularly high risk	–	–	–	–	–	–
Covered bonds	–	–	–	–	–	–
Securitisation positions	1,184	–	–	–	–	1,184
Short term claims on institutions and corporates	–	–	–	–	–	–
Collective investment undertakings (CIUs)	224	–	–	–	–	224
Equity exposures	–	–	–	–	–	–
Total – standardised approach	87,496	15,165	3,671	837	1,212	108,381
Total	572,805	40,110	38,706	2,005	5,700	659,326
Other items						3,091
Non-credit obligation assets						10,890
Total credit risk exposure						673,307

[1] Securitisation positions (IRB Approach) have been analysed on a country of risk basis as this better reflects the profile of exposures held.

	2015 United Kingdom £m	2015 Rest of Europe £m	2015 United States of America £m	2015 Asia-Pacific £m	2015 Other £m	2015 Total £m
Exposures subject to the IRB approach						
Foundation IRB approach						
Corporate – main	57,356	8,518	11,603	703	2,449	80,629
Corporate – SME	12,936	18	–	–	10	12,964
Corporate – specialised lending	6	–	–	–	–	6
Central governments and central banks	–	27	15,552	–	137	15,716
Institutions	1,896	3,139	1,362	139	828	7,364
Retail IRB approach						
Retail mortgages	333,799	8,003	–	1	4	341,807
of which: residential mortgages (SME)	10,508	4	–	1	4	10,517
of which: residential mortgages (non-SME)	323,291	7,999	–	–	–	331,290
Qualifying revolving retail exposures	36,975	–	–	–	–	36,975
Other SME	2,661	–	–	–	–	2,661
Other non-SME	14,248	83	–	–	–	14,331
Other IRB approaches						
Corporate – specialised lending	14,855	3,327	646	209	850	19,887
Equities – exchange traded	876	102	–	–	–	978
Equities – private equity	2,759	81	82	17	42	2,981
Equities – other	370	6	–	–	–	376
Securitisation positions[1]	16,946	423	4,730	–	26	22,125
Total – IRB approach	495,683	23,727	33,975	1,069	4,346	558,800
Exposures subject to the standardised approach						
Central governments and central banks	75,315	13,100	–	–	–	88,415
Regional governments or local authorities	1	–	–	–	–	1
Public sector entities	2	–	–	–	–	2
Multilateral development banks	–	426	571	–	–	997
International organisations	–	–	–	–	–	–
Institutions	18	88	61	3	–	170
Corporates	9,216	2,355	1,838	389	665	14,463
Retail	3,485	935	2	6	10	4,438
Secured by mortgages on immovable property	4,776	286	92	526	160	5,840
of which: residential property	4,772	259	92	526	160	5,809
of which: commercial property	3	28	–	–	–	31
Exposures in default	845	108	5	14	33	1,005
Exposures associated with particularly high risk	–	–	–	–	–	–
Covered bonds	–	–	–	–	–	–
Securitisation positions	–	–	–	–	–	–
Short term claims on institutions and corporates	–	–	–	–	–	–
Collective investment undertakings (CIUs)	–	–	–	–	–	–
Equity exposures	–	–	–	–	–	–
Total – standardised approach	93,658	17,298	2,569	938	868	115,331
Total	589,341	41,025	36,544	2,007	5,214	674,131
Other items						3,204
Non-credit obligation assets						9,228
Total credit risk exposure						686,563

[1] Securitisation positions (IRB Approach) have been analysed on a country of risk basis as this better reflects the profile of exposures held.

Pillar 1 Capital requirements: Credit risk continued

Table 40: Credit risk exposures subject to the IRB approach analysed by geographical region

	2016 United Kingdom			2016 Rest of Europe			2016 United States of America			2016 Asia-Pacific			2016 Other			2016 Total		
	EAD £m	LGD %	PD %	EAD £m	LGD %	PD %	EAD £m	LGD %	PD %	EAD £m	LGD %	PD %	EAD £m	LGD %	PD %	EAD £m	LGD %	PD %
Exposures subject to the IRB approach																		
Foundation IRB approach																		
Corporate – main	54,852		2.23%	8,821		0.68%	11,641		0.21%	627		0.21%	2,586		0.20%	78,527		1.67%
Corporate – SME	11,887		6.82%	33		8.26%	–		–	–		–	61		0.67%	11,981		6.79%
Corporate – specialised lending	2		4.78%	–		–	–		–	–		–	–		–	2		4.78%
Central governments and central banks	–		–	156		0.01%	14,779		0.01%	–		–	218		0.01%	15,153		0.01%
Institutions	1,793		0.83%	2,039		0.07%	1,252		0.07%	424		6.94%	503		0.18%	6,011		0.78%
Total – Foundation IRB approach	68,534		2.99%	11,049		0.55%	27,672		0.10%	1,051		2.93%	3,368		0.20%	111,674		1.95%
Retail IRB approach																		
Retail mortgages	326,000	10.22%	2.56%	9,504	31.62%	4.57%	–	–	–	1	10.82%	0.63%	5	16.59%	2.48%	335,510	10.82%	2.62%
of which: residential mortgages (SME)	10,201	16.97%	4.69%	4	11.84%	2.03%	–	–	–	1	10.82%	0.63%	5	16.59%	2.48%	10,211	16.97%	4.68%
of which: residential mortgages (non-SME)	315,799	10.00%	2.50%	9,500	31.63%	4.58%	–	–	–	–	–	–	–	–	–	325,299	10.63%	2.56%
Qualifying revolving retail exposures	36,984	76.88%	2.70%	–	–	–	–	–	–	–	–	–	–	–	–	36,984	76.88%	2.70%
Other SME	2,444	70.10%	12.74%	–	–	–	–	–	–	–	–	–	1	62.78%	2.61%	2,445	70.10%	12.74%
Other non-SME	15,974	59.65%	4.33%	52	40.91%	1.17%	–	–	–	–	–	–	–	–	–	16,026	59.59%	4.32%
Total – Retail IRB approach	381,402	19.14%	2.72%	9,556	31.67%	4.56%	–	–	–	1	14.11%	0.81%	6	24.86%	2.50%	390,965	19.44%	2.76%

	2015 United Kingdom			2015 Rest of Europe			2015 United States of America			2015 Asia-Pacific			2015 Other			2015 Total		
	EAD £m	LGD %	PD %	EAD £m	LGD %	PD %	EAD £m	LGD %	PD %	EAD £m	LGD %	PD %	EAD £m	LGD %	PD %	EAD £m	LGD %	PD %
Exposures subject to the IRB approach																		
Foundation IRB approach																		
Corporate – main	57,356		2.31%	8,518		0.64%	11,603		0.21%	703		0.23%	2,449		0.20%	80,629		1.75%
Corporate – SME	12,936		9.39%	18		13.82%	–		–	–		–	10		4.73%	12,964		9.39%
Corporate – specialised lending	6		1.61%	–		–	–		–	–		–	–		–	6		1.61%
Central governments and central banks	–		–	27		0.01%	15,552		0.01%	–		–	137		0.01%	15,716		0.01%
Institutions	1,896		1.02%	3,139		0.11%	1,362		0.05%	139		0.18%	828		0.57%	7,364		0.39%
Total – Foundation IRB approach	72,194		3.55%	11,702		0.51%	28,517		0.09%	842		0.22%	3,424		0.29%	116,679		2.28%
Retail IRB approach																		
Retail mortgages	333,799	10.26%	2.51%	8,003	33.37%	5.03%	–	–	–	1	11.56%	0.78%	4	13.42%	1.20%	341,807	10.80%	2.57%
of which: residential mortgages (SME)	10,508	17.35%	5.98%	4	12.18%	1.45%	–	–	–	1	11.56%	0.78%	4	13.42%	1.20%	10,517	17.35%	5.98%
of which: residential mortgages (non-SME)	323,291	10.03%	2.39%	7,999	33.38%	5.04%	–	–	–	–	–	–	–	–	–	331,290	10.59%	2.46%
Qualifying revolving retail exposures	36,975	76.88%	2.97%	–	–	–	–	–	–	–	–	–	–	–	–	36,975	76.88%	2.97%
Other SME	2,661	70.63%	10.43%	–	–	–	–	–	–	–	–	–	–	–	–	2,661	70.63%	10.43%
Other non-SME	14,248	62.43%	4.89%	83	59.85%	2.19%	–	–	–	–	–	–	–	–	–	14,331	62.41%	4.87%
Total – Retail IRB approach	387,683	18.94%	2.69%	8,086	33.64%	5.00%	–	–	–	1	11.56%	0.78%	4	13.42%	1.20%	395,774	19.24%	2.74%

ANALYSIS OF CREDIT RISK EXPOSURES BY RESIDUAL MATURITY

Credit risk exposures as at 31 December 2016, analysed by residual contractual maturity, are provided in the table below.

Table 41: Credit risk exposures analysed by residual contractual maturity

	2016 On demand £m	2016 Repayable in 3 months or less £m	2016 Repayable between 3 months and 1 year £m	2016 Repayable between 1 and 5 years £m	2016 Repayable over 5 years or undated £m	2016 Total £m
Exposures subject to the IRB approach						
Foundation IRB approach						
Corporate – main	7,074	5,691	13,879	41,334	10,549	78,527
Corporate – SME	930	618	3,307	2,629	4,497	11,981
Corporate – specialised lending	–	–	–	–	2	2
Central governments and central banks	–	6,017	–	5,025	4,111	15,153
Institutions	245	1,298	1,690	2,382	396	6,011
Retail IRB approach						
Retail mortgages	1,427	1,195	13,504	19,063	300,321	335,510
of which: residential mortgages (SME)	217	531	1,008	1,211	7,244	10,211
of which: residential mortgages (non-SME)	1,210	664	12,496	17,852	293,077	325,299
Qualifying revolving retail exposures	36,984	–	–	–	–	36,984
Other SME	105	338	776	338	888	2,445
Other non-SME	18	274	1,365	13,396	973	16,026
Other IRB approaches						
Corporate – specialised lending	297	866	2,294	8,713	6,644	18,814
Equities – exchange traded	–	–	–	–	461	461
Equities – private equity	–	–	–	–	2,583	2,583
Equities – other	–	–	–	–	382	382
Securitisation positions	–	2,191	9,231	7,370	7,274	26,066
Total – IRB approach	47,080	18,488	46,046	100,250	339,081	550,945
Exposures subject to the standardised approach						
Central governments and central banks	29,220	8,995	549	10,251	32,006	81,021
Regional governments or local authorities	–	–	–	–	–	–
Public sector entities	–	–	–	–	2	2
Multilateral development banks	–	24	61	1,265	403	1,753
International organisations	–	–	–	–	–	–
Institutions	11	103	56	2	107	279
Corporates	807	822	1,984	3,954	5,944	13,511
Retail	198	43	117	1,312	2,444	4,114
Secured by mortgages on immovable property	666	35	122	496	4,185	5,504
of which: residential property	666	35	122	496	4,182	5,501
of which: commercial property	–	–	–	–	3	3
Exposures in default	55	12	42	177	503	789
Exposures associated with particularly high risk	–	–	–	–	–	–
Covered bonds	–	–	–	–	–	–
Securitisation positions	–	–	–	–	1,184	1,184
Short term claims on institutions and corporates	–	–	–	–	–	–
Collective investment undertakings (CIUs)	–	–	–	–	224	224
Equity exposures	–	–	–	–	–	–
Total – standardised approach	30,957	10,034	2,931	17,457	47,002	108,381
Total	78,037	28,522	48,977	117,707	386,083	659,326
Other items						3,091
Non-credit obligation assets						10,890
Total credit risk exposure						673,307

Pillar 1 Capital requirements: Credit risk continued

	2015 On demand £m	2015 Repayable in 3 months or less £m	2015 Repayable between 3 months and 1 year £m	2015 Repayable between 1 and 5 years £m	2015 Repayable over 5 years or undated £m	2015 Total £m
Exposures subject to the IRB approach						
Foundation IRB approach						
Corporate – main	6,110	4,555	16,343	42,504	11,117	80,629
Corporate – SME	888	546	3,357	3,104	5,069	12,964
Corporate – specialised lending	1	–	–	–	5	6
Central governments and central banks	–	8,549	99	3,252	3,816	15,716
Institutions	181	1,345	1,394	3,364	1,080	7,364
Retail IRB approach						
Retail mortgages	1,171	1,171	12,719	19,393	307,353	341,807
of which: residential mortgages (SME)	242	551	983	1,329	7,412	10,517
of which: residential mortgages (non-SME)	929	620	11,736	18,064	299,941	331,290
Qualifying revolving retail exposures	36,975	–	–	–	–	36,975
Other SME	110	341	780	356	1,074	2,661
Other non-SME	26	250	1,184	11,950	921	14,331
Other IRB approaches						
Corporate – specialised lending	238	924	1,755	8,476	8,494	19,887
Equities – exchange traded	–	–	–	–	978	978
Equities – private equity	–	–	–	–	2,981	2,981
Equities – other	–	–	–	–	376	376
Securitisation positions	–	1,195	4,685	8,766	7,479	22,125
Total – IRB approach	45,700	18,876	42,316	101,165	350,743	558,800
Exposures subject to the standardised approach						
Central governments and central banks	35,304	11,602	374	5,785	35,350	88,415
Regional governments or local authorities	–	–	–	–	1	1
Public sector entities	–	–	–	–	2	2
Multilateral development banks	–	–	27	608	362	997
International organisations	–	–	–	–	–	–
Institutions	11	90	62	1	6	170
Corporates	1,020	880	1,621	4,106	6,836	14,463
Retail	232	44	108	1,050	3,004	4,438
Secured by mortgages on immovable property	559	34	134	598	4,515	5,840
of which: residential property	558	34	134	570	4,513	5,809
of which: commercial property	1	–	–	28	2	31
Exposures in default	83	18	136	111	657	1,005
Exposures associated with particularly high risk	–	–	–	–	–	–
Covered bonds	–	–	–	–	–	–
Securitisation positions	–	–	–	–	–	–
Short term claims on institutions and corporates	–	–	–	–	–	–
Collective investment undertakings (CIUs)	–	–	–	–	–	–
Equity exposures	–	–	–	–	–	–
Total – standardised approach	37,209	12,668	2,462	12,259	50,733	115,331
Total	82,909	31,544	44,778	113,424	401,476	674,131
Other items						3,204
Non-credit obligation assets						9,228
Total credit risk exposure						686,563

Pillar 1 Capital requirements: Credit risk – securitisation

This section details Lloyds Banking Group's securitisation profile.

- The Group operates in the securitisation market in the following capacity:

  As an originator, sponsor of an asset-backed commercial paper conduit and as an arranger of and an investor in third party securitisations. It also holds a small portfolio of ABS trading book securitisation positions.

  Provides liquidity and funding facilities to own originated and sponsored positions as well as to third parties.

- Securitisations represent a small proportion (1.8%) (2015: 1.5%) of the Group's total risk-weighted assets

- Banking book securitisation exposures and risk-weighted assets increased by £5.1bn and £0.7bn in the year primarily as a result of new capital efficient commercial asset backed securitisation transactions and an increase in investment grade investor positions, partially offset by sales, maturities and amortisation.

% Exposure by securitisation type

% Risk-weighted assets by securitisation type

Pillar 1 Capital requirements: Credit risk – securitisation continued

The Group is an active participant in the securitisation market, operating as an originator, a sponsor of an asset-backed commercial paper (ABCP) conduit and as an arranger of and an investor in third party securitisations. The Group also provides liquidity and funding facilities to both own originated and sponsored securitisations as well as to third parties. In addition, the Group also holds a small portfolio of ABS trading book securitisation positions.

Banking book securitisation strategy and roles

The Group's objectives in relation to banking book securitisations are to manage risk concentrations in its balance sheet, to support relationships with customers and to manage its funding requirements and capital position. It undertakes the following roles to meet these objectives:

As an originator the Group uses securitisation as a means of managing its balance sheet. Although primarily a funding tool, the Group also uses originated securitisations to generate capital efficiencies through the use of synthetic loan securitisations which involve the use of credit derivatives.

Traditional originated securitisation transactions typically involve the sale of a group or portfolio of ring fenced loans to a structured entity (SE). An SE is a purposely created company within a group of companies where the ultimate holding company of the group is unrelated to the originator and is usually held by a trust. This means the Group does not legally own the SE. The Group does, however, administer the SE and the originating Group company receives fees from the SE for continuing to service the loans. Traditional securitisations are typically funding driven transactions where the most junior tranches are retained by the Group meaning there is effectively no significant risk transfer of credit risk away from the Group. Instead the vehicle serves as a diverse source of funding for the securitised assets.

Synthetic originated securitisations work in a similar way to the traditional version except that the economic risk of the assets is transferred using credit derivatives. In certain cases the Group will retain the risk on the senior tranches.

Where capital efficiency is sought, a test of significant risk transfer (SRT) is required. Passing the test allows the capital required on the underlying exposures to be replaced by the lower capital requirements of the retained positions in the securitisation.

Origination activities mainly extend around the Group's retail and commercial lending portfolios.

As a sponsor the Group manages and supports, through the provision of liquidity facilities, an ABCP conduit (Cancara) that invests in client receivables. Liquidity facilities provided to Cancara are risk-weighted using the internal assessment approach (IAA). The Group also holds some commercial paper (CP) issued by Cancara.

All the external assets in Cancara are consolidated for accounting purposes in the Group's financial statements, following similar accounting policies to those established for originated securitisations.

As an investor the Group invests directly in third party ABS and notes and provides liquidity facilities to other third party securitisations. Invested securitisation positions are risk-weighted using the ratings based approach (RBA).

Trading book securitisation strategy and roles

The Group's ABS trading book consists primarily of investments in third party securitisation positions and to a lesser extent, in the Group's sponsored securitisations.

The main objectives of the ABS trading book are;

- to create a secondary market through normal market making activity for the Group's related issuance where the underlying loans or receivables are originated by the Group;
- to support the development of a third party securitisation debt capital market business that generates fees for the Group by normal market making activities; and
- to carry out normal market making activities in support of the Group's clients.

The key risks attached to the Group's holding of trading book securitisation positions include price risk, credit risk, event risk, interest rate fluctuations, moral hazard and servicer risk. Liquidity risk is considered to be low as the Group's ABS trading book is relatively small, with maximum holding period limits and with positions held for the short term.

The trading desk does not undertake origination activities and does not structure transactions, nor does it re-structure or re-securitise securitisations for the purposes of holding them on the trading book.

As the Group's portfolio of trading book securitisation positions is relatively small (£122m exposure, £17m risk-weighted assets) in the context of both the overall trading book and the Group's banking book securitisation positions, the Group has elected to provide only limited disclosure around its trading book securitisation positions as permitted by CRR Article 432 and in accordance with related EBA guidelines.

Summary analysis

An analysis of securitisation exposures by book, type and risk weight approach, together with the associated capital requirement, is provided in the table below. In addition, the table provides an analysis of securitisation positions that have been deducted from capital.

Table 42: Summary of securitisation exposures and capital requirements

Securitisation type and risk weight approach	2016 Exposure value[1] £m	2016 Risk-weighted assets[2] £m	2016 Capital requirement £m	2016 Deduction from capital[3,5] £m	2015 Exposure value[1] £m	2015 Risk-weighted assets[2] £m	2015 Capital requirement £m	2015 Deduction from capital[3,5] £m
Originated:								
Ratings based approach (RBA)	**5,321**	**1,055**	**85**	**–**	3,850	856	68	–
Standardised approach	**1,184**	**268**	**21**	**–**	–	–	–	–
Sponsored and invested:								
Internal assessment approach (IAA)	**9,129**	**825**	**66**	**–**	9,710	887	71	–
Ratings based approach (RBA)	**11,616**	**1,823**	**146**	**217**	8,565	1,523	122	3
Total banking book[4]	**27,250**	**3,971**	**318**	**217**	22,125	3,266	261	3
Trading book – specific interest rate market risk	**122**	**17**	**1**	**–**	180	78	6	–
Total trading book	**122**	**17**	**1**	**–**	180	78	6	–

[1] Banking book exposure value is defined as the aggregate of the Group's gross retained or purchased positions, excluding those positions rated below BB- or that are unrated and therefore deducted from capital. Trading book exposure value is defined as the sum of the net long and net short positions as per CRD IV rules.

[2] Risk-weighted assets are stated net of SCRAs where applicable. These adjustments represent a combination of impairment writedowns, acquisition related fair value adjustments and other fair value adjustments.

[3] Retained or purchased positions rated below BB- or that are unrated are deducted from capital. The amount deducted is stated net of SCRAs.

[4] Excludes counterparty credit risk securitisation positions, further information on which can be found on page 91.

[5] No positions relating to counterparty credit risk securitisation positions were deducted from capital (2015: £166m).

Key movements

Banking book

– Originator: The increase during the year is the result of new capital efficient commercial asset backed securitisation transactions.

– Sponsor: The reduction in exposure reflects the net reduction in the liquidity facilities provided to the conduit programme. This is as a result of the sale of select portfolios of assets from the conduit purchasing companies to the Group and amortisations, offset by new client transactions. During the year certain liquidity facilities supporting the conduit programme were drawn down to provide funding alongside the proceeds of the ABCP issuance. Hence the conduit programme now contains both on and off-balance sheet positions.

– Investor: The increase in exposure primarily reflects a commitment to provide a new investment grade securitisation financing facility, a net increase in facilities provided to other third party clients and the sale of assets from the conduit programme to the Group (the latter reclassified from sponsored to invested). These were offset by sales and amortisation of other positions during the year.

Trading book

– The reduction in the trading book during the year is a result of significant de-risking activities.

Securitisation programmes and activity

The Group's securitisation programmes are predominantly funding transactions, including all of the residential mortgage programmes. The Group's principal originated securitisation programmes, together with the balances of the advances subject to securitisation and the carrying value of the notes in issue at 31 December, are outlined in Note 19 (Securitisations and Covered Bonds) of the 2016 Lloyds Banking Group plc Annual Report and Accounts.

During the year the risk and returns of a portfolio of commercial assets were sold to an SE, and subsequently derecognised, with a resultant gain for the Group of £1.7m (2015: nil). In addition the Group originated new capital efficient commercial asset backed securitisation transactions.

Re-securitisation

Re-securitisation transactions involve securitisations where the risk associated with the underlying pool of assets is tranched and at least one of the underlying assets is a securitisation position. The Group has no originated re-securitisation positions in either its banking or trading book and has minimal exposure through the invested portfolio in the banking book.

Risks inherent in banking book securitised assets

Where the Group acts as originator its securitisation programmes primarily include residential mortgage portfolios, credit card portfolios and commercial loan portfolios. In each case credit risk is the primary risk driver attached to the underlying asset pool. Assets securitised are predominantly originated from the Group's UK operations, other than for the Group's Dutch residential mortgage securitisation programmes and various assets within the Group's commercial securitisations.

The performance of the securitised assets is largely dependent on prevailing economic conditions, and in the case of residential mortgage assets, the health of the housing market. The likelihood of defaults in the underlying asset pool and the amounts that may be recovered in the event of default are related to a number of factors and may vary according to characteristics, product type, security, collateral and customer support initiatives. Significant changes in the national or international economic climate, regional economic or housing conditions, tax laws, interest rates, inflation, the availability of financing, yields on alternative investments, political developments and government policies or in the health of a particular geographic zone that represents a concentration in the securitised assets, could also affect the cashflows from the underlying asset pool.

Pillar 1 Capital requirements: Credit risk – securitisation continued

Liquidity risk arises where insufficient funds are received by the SE to service payments to the noteholders as they fall due. The receipt of funds is in part dependent on the level of repayment on the underlying asset pool. In general, where such a situation arises noteholders may not be paid in full and amounts may be deferred to subsequent periods. Such deferred amounts will be due but not payable until funds become available in accordance with the relevant priority of payments as set out in the programme documentation. Variations in the rate of prepayment of principal on the underlying loans may affect each series and class of notes differently.

In addition, both the notes in issue and the underlying asset pool are exposed to interest rate risk and, in certain cases, may be subject to foreign exchange risk.

Where the Group holds notes in a securitisation it is exposed to the credit performance of the underlying asset pool, the impact of interest rates and, in some cases, foreign exchange volatility on the value of the notes, and to the seniority of the notes held, the latter of which determines the extent to which the Group would suffer any loss as a result of a shortfall in funds received by the SE.

Monitoring changes in the credit risk of securitised exposures

The Group employs a range of measures to monitor changes in the credit risk of securitised assets. These include monitoring on a monthly basis of current exposures in the underlying pool (including credit events, default history and disposals), together with data tracking collateral cover and loan repayments which are tracked from the original amount advanced.

Monitoring changes in the credit risk of ABS portfolios

ABS exposures reside primarily in the residual non-core portfolio managed by Commercial Banking Client Asset Management. The Group also holds some small ABS exposures for liquidity coverage ratio (LCR) purposes which are managed by the Liquid Asset Portfolio team. Each team is therefore responsible for the monitoring of changes in the credit risk of ABS within its portfolio.

The credit process is the same across portfolios: credit reviews are produced at least annually for a particular sector or for a specific bond (or both) as well as for third party ABS liquidity facilities.

A credit review process will also be triggered where an ECAI applies a significant downgrade to a bond.

The Specialist Finance Credit (SFC) team provides an independent risk oversight for ABS credit reviews. It provides each ABS transaction with a credit risk classification (ranging from good to substandard), as well as sanctioning credit limits either locally or by referral to the credit committee.

Furthermore, additional monitoring measures are applied: monthly watch list meetings (including a review of downgraded bonds), quarterly preparation of International Accounting Standards (IAS) 39 attestations, stress testing of portfolios and in the case of the Liquid Asset Portfolio a quarterly risk review forum is also conducted.

Similar processes are used to monitor changes in the credit risk associated with re-securitisation positions.

Banking and trading book securitisation analysis

The table below discloses the Group's retained and purchased positions across the banking and trading book by exposure type and role.

Table 43: Value of exposures of retained and purchased positions in the banking and trading book by exposure type

	2016						2015					
	Banking book				Trading book		Banking book				Trading book	
Exposure type	Originator £m	Sponsor £m	Investor £m	Total £m	Investor £m	Total £m	Originator £m	Sponsor £m	Investor £m	Total £m	Investor £m	Total £m
Retail (total) of which	**–**	**5,223**	**7,920**	**13,143**	**52**	**52**	–	5,912	5,423	11,335	29	29
residential mortgage	**–**	**548**	**6,404**	**6,952**	**49**	**49**	–	661	5,191	5,852	5	5
credit card	**–**	**308**	**–**	**308**	**3**	**3**	–	350	–	350	24	24
leases and receivables	**–**	**2,576**	**–**	**2,576**	**–**	**–**	–	3,838	–	3,838	–	–
other retail	**–**	**1,791**	**1,516**	**3,307**	**–**	**–**	–	1,063	232	1,295	–	–
Commercial (total) of which	**6,505**	**3,906**	**3,696**	**14,107**	**70**	**70**	3,850	3,798	3,142	10,790	151	151
loans to corporates or SMEs	**4,997**	**1,492**	**1,362**	**7,851**	**–**	**–**	2,342	1,563	1,004	4,909	5	5
social housing associations	**1,508**	**–**	**–**	**1,508**	**–**	**–**	1,508	–	–	1,508	–	–
commercial mortgage	**–**	**–**	**1,366**	**1,366**	**–**	**–**	–	–	1,436	1,436	5	5
leases and receivables	**–**	**2,414**	**872**	**3,286**	**59**	**59**	–	2,235	577	2,812	19	19
other commercial	**–**	**–**	**91**	**91**	**11**	**11**	–	–	109	109	122	122
re-securitisation	**–**	**–**	**5**	**5**	**–**	**–**	–	–	16	16	–	–

All trading book securitisations are traditional securitisations.

ORIGINATED SECURITISATIONS

Regulatory treatment

In deriving credit risk exposures associated with originated securitisations, the Group takes into account that certain securitised assets, whilst held on the balance sheet for accounting purposes, are deemed to have met the prudential SRT tests when securitised. Meeting these tests allows the retained positions in the securitisations to be included within regulatory calculations, and the risk-weighted assets on the assets underlying the securitisation to be removed. Where the minimum requirements for recognition of SRT are not met, the underlying assets remain part of the relevant exposure class and are risk-weighted accordingly.

Capital requirements in relation to originated securitisation positions are determined under the RBA or the Standardised approach. Where appropriate, the Group utilises the ratings services of several ECAIs, including Standard & Poor's, Moody's and Fitch, to rate securitisation transactions and retained or purchased positions for risk weight allocation purposes under both the RBA and Standardised approach.

On a regulatory basis, the gross securitised exposures in relation to originated securitisations where significant risk transfer has been achieved amounted to £7.1bn (2015: £4.2bn) comprising synthetic originated securitisations. An analysis is provided in the table below together with the amount of impaired exposures and past due but not impaired exposures.

Table 44: Analysis of gross securitised exposures on a regulatory basis

	2016			2015		
	Gross securitised exposure			Gross securitised exposure		
	Synthetic £m	**Impaired exposures £m**	**Past due but not impaired exposures £m**	Synthetic £m	Impaired exposures £m	Past due but not impaired exposures £m
Commercial						
social housing associations	**1,562**	**–**	**–**	1,562	–	–
loans to corporates or SMEs	**5,527**	**48**	**3**	2,611	–	–
Total	**7,089**	**48**	**3**	4,173	–	–

The net charge to the income statement for the year to 31 December 2016 in respect of losses attributed to the gross securitised exposures noted above amounted to £10.9m (2015: £nil).

Originated securitisations subject to the RBA

The RBA utilises a set of defined risk weights prescribed by CRD IV rules. The appropriate risk weight is dependent on the rating of the position, its classification as a securitisation position or a re-securitisation position, the maturity and the seniority of the position and the granularity of the asset pool backing the position. As at 31 December 2016, securitisation positions arising from origination activities and risk-weighted under the RBA amounted to £5.3bn (2015: £3.9bn), generating a capital requirement of £85m (2015: £68m). An analysis of these positions, by risk weight category, is provided in the table below.

Table 45: Analysis of originated positions under the RBA by risk weight category

		Securitisation positions				**Total 2016**		Total 2015	
		Senior		**Non-Senior**					
S&P equivalent rating and RBA risk weight[1]		**Exposure £m**	**Cap req £m**	**Exposure £m**	**Cap req £m**	**Exposure £m**	**Cap req £m**	Exposure £m	Cap req £m
AAA	(7%, 12%)	**3,795**	**23**	**200**	**2**	**3,995**	**25**	2,792	17
AA+ to AA-	(8%, 15%)	**–**	**–**	**474**	**6**	**474**	**6**	371	5
A+	(10%, 18%)	**–**	**–**	**301**	**5**	**301**	**5**	257	4
A	(12%, 20%)	**–**	**–**	**77**	**1**	**77**	**1**	64	1
A-	(20%, 35%)	**–**	**–**	**52**	**1**	**52**	**1**	41	1
BBB+	(35%, 50%)	**–**	**–**	**156**	**7**	**156**	**7**	110	4
BBB	(60%, 75%)	**–**	**–**	**40**	**3**	**40**	**3**	31	5
BBB-	(100%, 100%)	**–**	**–**	**99**	**8**	**99**	**8**	81	4
BB+	(250%, 250%)	**–**	**–**	**121**	**26**	**121**	**26**	81	17
BB	(425%, 425%)	**–**	**–**	**3**	**1**	**3**	**1**	13	5
BB-	(650%, 650%)	**–**	**–**	**3**	**2**	**3**	**2**	9	5
Below BB- or unrated	Deduction	**–**	**–**	**–**	**–**	**–**	**–**	–	–
Total credit risk exposure/capital requirement[2]		**3,795**	**23**	**1,526**	**62**	**5,321**	**85**	3,850	68

[1] The RBA risk weights for each rating are listed in the following order: senior securitisation positions, non-senior securitisation positions. Positions rated below BB- or that are unrated are deducted from capital, net of SCRAs applied.

[2] Total credit risk exposure is defined as the aggregate of the Group's gross retained or purchased positions, excluding those positions rated below BB- or that are unrated and therefore deducted from capital. Capital requirements are stated net of SCRAs, where applicable. All retained positions are held on-balance sheet.

Pillar 1 Capital requirements: Credit risk – securitisation continued

Originated Securitisations subject to the Standardised approach

The Standardised approach utilises a set of defined risk weights prescribed by CRD IV rules. The appropriate risk-weight is dependent on the rating of the position and its classification as a securitisation position or re-securitisation position. As at 31 December 2016, securitisation positions arising from origination activities and risk-weighted under the Standardised approach amounted to £1.2m (2015: £nil) generating a capital requirement of £21m (2015: £nil). An analysis of these positions, by risk weight category, is provided in the table below.

Table 46: Analysis of originated positions under the Standardised approach by risk weight category

		Total 2016		Total 2015	
		Securitisation positions		Securitisation positions	
Fitch equivalent rating and Standardised approach risk weight		Exposure	Cap req	Exposure	Cap req
AAA to AA-	(20%)	**1,111**	**18**	–	–
A+ to A-	(50%)	**55**	**2**	–	–
BBB+ to BBB-	(100%)	**18**	**1**	–	–
BB+ to BB-	(350%)	**–**	**–**	–	–
Below B+ or unrated	Deduction	**–**	**–**	–	–
Total Credit Risk Exposure/Cap Requirement[1]		**1,184**	**21**	–	–

[1] Total credit risk exposure is defined as the aggregate of the Group's gross retained or purchased positions, excluding those positions rated below B+ or that are unrated and therefore deducted from capital. Capital requirements are stated net of SCRAs, where applicable. All retained positions are held on-balance sheet.

Accounting treatment

From an accounting perspective, the treatment of SEs is assessed in accordance with IFRS 10 which establishes the principles for when the Group is deemed to control another entity and therefore required to consolidate it through the Group's financial statements.

Under IFRS 10, the Group controls an entity where it is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through the exercise of power.

Where the transfer of the Group assets to an SE that it controls fails the 'derecognition' accounting tests under IAS 39, the transferred assets remain on the Group's balance sheet for accounting purposes. These assets are classified as loans and receivables on the balance sheet and the notes issued (excluding those held by the Group) classified as debt securities in issue. The assets and notes issued are held at amortised cost.

Securitised assets are only derecognised where the following conditions are met:

- substantially all of the risks and rewards associated with the assets have been transferred in which case they are derecognised in full; or
- a significant proportion but not all of the risks and rewards have been transferred, in which case the assets are either derecognised in full where the transferee has the ability to sell the assets, or continue to be recognised by the Group but only to the extent of its continuing involvement; or
- substantially all of the risks and rewards associated with a fully proportional share of all or of specifically identified cash flows have been transferred, in which case that proportion of the assets are derecognised.

A securitisation transaction is recognised as a sale or partial sale where derecognition is achieved. The difference between the carrying amount and the consideration received is recorded in the income statement. Securitisation transactions that do not achieve derecognition are treated as financing arrangements.

The Group's securitised residential mortgage assets are not derecognised because the Group retains substantially all the risks and rewards associated with the underlying portfolios of assets. In addition securitised commercial banking loans are not typically derecognised because the Group has not transferred the contractual rights to receive the cash flows from those loans nor has it assumed a contractual obligation to pay the cash flows from those loans to a third party.

Synthetic securitisations, where credit derivatives are used to transfer the economic risk of the underlying assets but the Group retains legal ownership of the assets, are accounted for under similar accounting policies to those summarised above, with the associated credit derivatives accounted for under the requirements of IAS 39.

Where internal transactions between the banking group and the insurance group achieve accounting derecognition from the underlying banking subsidiary balance sheet the assets continue to be fully consolidated from a Group perspective but may achieve derecognition under the regulatory scope of consolidation.

Liquidity lines provided to the conduits are accounted for in accordance with the accounting policies set out in the 2016 Lloyds Banking Group plc Annual Report and Accounts.

The Group's retained and purchased securitisation positions are valued for accounting purposes in accordance with the Group's accounting policies as outlined on Note 2(E) (Accounting Policies: Financial Assets and Liabilities) of the 2016 Lloyds Banking Group plc Annual Report and Accounts.

For those positions measured at fair value, further details on the valuation methodologies applied are outlined in Note 49(2) (Financial Instruments: Fair Value Measurement) of the 2016 Lloyds Banking Group plc Annual Report and Accounts.

Use of credit derivatives and guarantees

Synthetic securitisations, covering social housing associations and other loans to corporates and SMEs, involve the provision of protection to the Group through a combination of financial guarantees and credit protection agreements with the SE established under the transactions that results in a net protected position of a junior tranche of the securitised portfolio. The SE issues CLNs to pass on the risk associated with the net protected position to third party investors who primarily include other institutions and professional investors.

The Group does not typically make use of hedging against securitisation positions.

Assets awaiting securitisation

In 2012 the Group established a warehousing facility for a third party client with facility commitments amounting to £350m at 31 December 2016 (2015: £350m) with £82m of the facility having been drawn down (2015: £120m).

SPONSORED AND INVESTED SECURITISATIONS

Cancara – summary of activity

Cancara

General description	Cancara was established in 2002 by Lloyds Bank. It provides financing facilities to the Group's core corporate and financial institution clients, funded by ABCP.
Programme limit/CP outstanding as at 31 December 2016	\$20.0bn/\$4.9bn (£16.3bn/£4.0bn)
Conduit structure	Fully supported multi-seller
Credit enhancement	Full support liquidity
Liquidity provider	Lloyds Bank Plc and Bank of Scotland Plc

Structure and liquidity facilities

Cancara Asset Securitisation Limited is an ABCP conduit that buys assets from clients of the Group. The conduit funds the purchase of the assets primarily by issuing ABCP. Cancara Asset Securitisation LLC is a separate bankruptcy remote, special purpose limited liability company established to co-issue US Dollar domestic CP with Cancara Asset Securitisation Limited.

Assets purchased relate to pools of third party receivables.

A number of intermediary special purpose entities within the conduit structure are used to purchase the assets. Each purchasing company enters into a commissioning agreement with the issuer, which then advances funds to the purchasing company to buy the assets. The purchasing company issues a purchaser demand note to the issuer which benefits from security over the assets.

For each new asset purchase, Cancara enters into a liquidity facility with the Group, to cover any shortfall in repaying the ABCP notes. In the absence of market disruption the conduit will usually look to fund through issuing ABCP. During 2016 the addition of new client transactions was offset by the movement of a number of transactions to the balance sheet. Additionally, certain liquidity facilities supporting the program were drawn to provide funding alongside the proceeds of ABCP issuance. The overall impact of these funding changes was to reduce issued ABCP from £7.4bn at 31 December 2015 to £4.0bn at 31 December 2016.

Cancara Assets

All the external assets in the conduit are consolidated for accounting purposes in the Group's financial statements, following similar accounting policies to those established for originated securitisations. The total consolidated assets in the conduits are set out in Note 20 (Structured Entities) of the 2016 Lloyds Banking Group plc Annual Report and Accounts.

Pillar 1 Capital requirements: Credit risk – securitisation continued

Capital assessment

With regard to sponsored activities, the Group has approval to utilise the IAA for calculating capital requirements for the liquidity facilities provided to the conduit purchasing companies.

The Group's IAA model is a proprietary credit rating system. This model generates a rating equivalent to an external rating. This rating then feeds the Ratings Based Approach in order to calculate the capital requirement.

The model consists of a number of scorecards, one for each asset class. Unlike the Group's Foundation and Retail IRB models, the ABCP IAA model does not estimate the PD for the exposure, but instead is used to determine a model rating grade equivalent to an ECAI grade. The internal rating methodology must reflect the ECAI's methodology. Periodically, ECAIs publish updates to their methodologies relating to different asset classes. The Conduit Team monitors rating agency updates and undertakes regular reviews of the model to confirm that all relevant changes to rating methodologies have been reflected in the cashflow modelling and the IAA model.

Stress factor inputs play an important part in determining the rating of a transaction. Depending on the level of credit enhancement, the stress factor will determine the final rating a transaction would receive from an ECAI taking into account 'stressed scenarios' on the level of cash-flows generated by the underlying pool of assets.

The sponsored receivables facilities are modelled using a stress factor input which reflects the ability of the transaction to withstand a significant deterioration in the asset quality and is a through-the-cycle measure that is applied to a base case default rate. To determine the base case default rate historic loss data is used. For example, in its approach Standard & Poor's incorporates additional analysis into historic loss data to mitigate any effects of recent changes with the result that in many cases the base case loss rate assumed is above the historical average.

The model is subject to a robust governance framework. In line with the Rating Model Validation Framework, the Group undertakes an Annual Credit Rating Model Validation exercise to ensure that the model remains compliant with the requirements of CRR (Article 259) which establishes the criteria that must be met in order to apply the IAA to exposures relating to programmes such as liquidity facilities. A Risk Model Decision Forum ensures that re-approval of the model is conducted systematically, with appropriate peer challenge and review. Re-approval documentation is subject to the internal model approval processes in place within the Group.

An analysis of the total credit risk exposure and associated capital requirement by risk weight category under the ABCP IAA is provided in the table below.

Table 47: Analysis of sponsored positions by risk weight category

S&P equivalent rating and IAA risk weight		2016 Exposure £m	2016 Capital requirement £m	2015 Exposure £m	2015 Capital requirement £m
On Balance Sheet					
AAA	7%	**1,410**	**8**	–	–
AA+ to AA-	8%	**959**	**7**	–	–
A+	10%	**–**	**–**	–	–
A	12%	**683**	**7**	–	–
A-	20%	**–**	**–**	–	–
BBB	60%	**–**	**–**	–	–
Off Balance Sheet					
AAA	7%	**2,743**	**16**	4,554	27
AA+ to AA-	8%	**1,989**	**14**	2,848	19
A+	10%	**154**	**1**	295	3
A	12%	**1,175**	**12**	1,984	20
A-	20%	**–**	**–**	–	–
BBB	60%	**16**	**1**	29	2
Total credit risk exposure/capital requirement		**9,129**	**66**	9,710	71

Direct investments and liquidity facilities

In addition to sponsoring an ABCP conduit, the Group has invested directly in third party ABS and notes and is a provider of liquidity facilities to other third party securitisation. Investments in ABS are primarily part of the Group's residual run-off portfolio.

The majority of these direct investments are accounted for as loans and receivables on the balance sheet and held at amortised cost, with the remainder held as AFS or at fair value through profit and loss. Further details on the Group's holding of ABS are presented on pages 265 and 266 in Note 52(c) (Financial Risk Management: Credit Quality of Assets) of the 2016 Lloyds Banking Group plc Annual Report and Accounts.

Invested securitisations subject to the RBA

As at 31 December 2016, securitisation positions relating to the Group's direct investments in third party ABS and notes, commitment to provide a new investment grade securitisation financing facility and the provision of liquidity facilities to third party securitisations, risk weighted under the RBA, amounted to £11.6bn (2015: £8.6bn), generating a capital requirement of £146m (2015: £122m). An analysis of these positions, by risk weight category, is provided in the table below.

Table 48: Analysis of invested positions by risk weight category

		Securitisation positions 2016						Re-Securitisation positions 2016		2016		2015	
		Senior		Non-senior		Tranches backed by non granular pools		Senior		Total		Total	
S&P equivalent rating and RBA risk weight[1]		Exposure £m	Cap req £m	Exposure £m	Cap req £m	Exposure £m	Cap req £m	Exposure £m	Cap req £m	Exposure £m	Cap req £m	Exposure £m	Cap req £m
On Balance Sheet													
AAA	(7%, 12%, 20%, 20%)	3,567	20	–	–	26	1	5	–	3,598	21	4,583	27
AA+ to AA-	(8%, 15%, 25%, 25%)	257	1	16	1	420	9	–	–	693	11	1,082	12
A+	(10%, 18%, 35%, 35%)	–	–	203	3	101	3	–	–	304	6	113	2
A	(12%, 20%, 35%, 40%)	553	6	–	–	–	–	–	–	553	6	291	4
A-	(20%, 35%, 35%, 60%)	162	3	41	2	46	1	–	–	249	6	213	5
BBB+	(35%, 50%, 50%, 100%)	–	–	45	2	–	–	–	–	45	2	38	2
BBB	(60%, 75%, 75%, 150%)	59	3	30	2	18	1	–	–	107	6	92	5
BBB-	(100%, 100%, 100%, 200%)	–	–	50	4	–	–	–	–	50	4	29	3
BB+	(250%, 250%, 250%, 300%)	3	1	–	–	–	–	–	–	3	1	3	1
BB	(425%, 425%, 425%, 500%)	–	–	–	–	–	–	–	–	–	–	2	1
BB-	(650%, 650%, 650%, 750%)	–	–	–	–	–	–	–	–	–	–	–	–
Below BB- or unrated	Deduction	–	–	–	–	187	–	–	–	187	–	2	–
Off Balance Sheet													
AAA	(7%, 12%, 20%, 20%)	3,284	18	–	–	570	10	–	–	3,854	28	592	10
AA+ to AA-	(8%, 15%, 25%, 25%)	500	3	261	3	185	4	–	–	946	10	687	7
A+	(10%, 18%, 35%, 35%)	–	–	–	–	148	4	–	–	148	4	148	4
A	(12%, 20%, 35%, 40%)	91	1	231	4	274	8	–	–	596	13	366	10
A-	(20%, 35%, 35%, 60%)	5	1	–	–	167	5	–	–	172	6	190	6
BBB+	(35%, 50%, 50%, 100%)	–	–	–	–	52	2	–	–	52	2	19	1
BBB	(60%, 75%, 75%, 150%)	–	–	155	10	46	3	–	–	201	13	29	2
BBB-	(100%, 100%, 100%, 200%)	10	1	–	–	24	2	–	–	34	3	24	2
BB+	(250%, 250%, 250%, 300%)	–	–	–	–	–	–	–	–	–	–	26	5
BB	(425%, 425%, 425%, 500%)	2	1	–	–	9	3	–	–	11	4	38	13
BB-	(650%, 650%, 650%, 750%)	–	–	–	–	–	–	–	–	–	–	–	–
Below BB- or unrated	Deduction	–	–	–	–	30	–	–	–	30	–	1	–
Total		8,493	59	1,032	31	2,303	56	5	–	11,833	146	8,568	122
Deduction from capital										(217)	–	(3)	–
Total credit risk exposure/ capital requirement[2]										11,616	146	8,565	122

[1] The RBA risk weights for each rating are listed in the following order: senior securitisation positions, non-senior securitisation positions, tranches backed by non-granular pools, senior re-securitisation positions. Positions rated below BB- or that are unrated are deducted from capital, net of SCRA's applied.

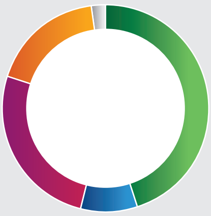
[2] Total credit risk exposure is defined as the aggregate of the Group's gross retained or purchased positions, excluding those positions rated below BB- or that are unrated and therefore deducted from capital. Capital requirements are stated net of SCRA's, where applicable.

Pillar 1 Capital requirements: Counterparty credit risk

This section details Lloyds Banking Group's counterparty credit risk profile, focussing on regulatory measures such as exposure at default and risk-weighted assets.

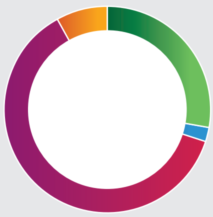
- The Group's counterparty credit risk strategy is to use collateral agreements and other risk management techniques, such as central clearing, to mitigate risk exposure.
- Counterparty credit risk (including CVA) represents a small proportion (4.5%) (2015: 4.6%) of the Group's total risk-weighted assets.
- Counterparty credit risk exposure increased by 8% to £30.3bn primarily due to foreign exchange and yield curve movements.
- Risk-weighted assets decreased by 5% to £9.6bn primarily due to capital relief from CVA related hedges.

IRB exposures



Corporate – main 45%	(2015: 45%)
Central governments and central banks 9%	(2015: 5%)
Institutions 26%	(2015: 28%)
Corporate – specialised lending 18%	(2015: 21%)
Securitisation positions 2%	(2015: 1%)

Standardised exposures



Central governments and central banks 28%	(2015: 33%)
International organisations 2%	(2015: 0%)
Institutions 62%	(2015: 59%)
Corporates 8%	(2015: 8%)

Table 49: Risk-weighted assets flow statement of CCR exposures[1]

	RWA amounts £m	Capital requirements £m
RWA as 31 December 2015	**10,153**	**812**
Asset size	**(1,542)**	**(123)**
Asset quality	**729**	**58**
Model updates	**99**	**8**
Methodology and policy	**–**	**–**
Acquisitions and disposals	**(183)**	**(14)**
Foreign exchange movements	**367**	**29**
Other	**–**	**–**
RWA as at 31 December 2016	**9,623**	**770**

[1] There are no exposures under the Internal Model Method requiring analysis under EBA template CCR7. The Group has elected to include the above risk-weighted assets flow statement of total CCR as a supplementary disclosure.

Key movements

– Counterparty credit risk and CVA reductions are driven mainly by increased capital relief from CVA related hedges partially offset by yield curve movements (the latter of which is included in "Asset quality") and foreign exchange.

DEFINITION

Counterparty credit risk is the risk that the counterparty to a transaction could default before the final settlement of the transaction's cash flows. Such transactions relate to contracts for financial instruments derivatives and repo contracts.

INTERNAL CAPITAL AND CREDIT LIMITS

The maximum credit risk appetite for counterparties is determined through a combination of credit quality (expressed as an internal credit rating) and size (measured by its capital and reserves). In general, activity of the Group is conducted with counterparties that have internal obligor ratings equivalent to investment grade as measured by external credit rating agencies.

Internal obligor ratings are mapped to modelled PDs, which when combined with LGDs and EADs determine EL. To calculate EAD, values for derivative products are determined by using the mark-to-market methodology for regulatory purposes and internally developed models for limit management.

Additionally a number of product specific, obligor quality limit guidelines and counterparty specific policies also serve to determine risk management and credit limit setting. Once commercial approval has been obtained for a counterparty, credit limits are established through the Group's credit approval framework on the basis of the projected maximum PFE of anticipated derivative transaction volumes, based on 95th percentile assumptions.

Credit limits are set by product and reflect documentation held for netting or collateral management purposes. Outstanding exposures are calculated on a PFE basis, based upon the transaction characteristics and documentation.

SECURING COLLATERAL AND ESTABLISHING CREDIT RESERVES

Use is made of collateral and risk mitigation techniques to reduce credit risks in various portfolios. These include the use of collateral (principally cash, government securities and guarantees), break clauses and netting. A significant amount of derivative exposure is cleared at Qualified Central Counterparties (QCCPs), which replaces exposure to individual counterparties with an exposure against the Central Counterparty (CCP).

Policy is set governing types of acceptable collateral and haircuts, in line with industry practice.

Collateral arrangements are governed by standard agreements (such as Global Master Repurchase Agreements and Credit Support Annexes (CSA) to International Swaps and Derivative Association ISDA Master Agreements). It is policy that appropriate documentation is put in place for all clients prior to trading, any exceptions being subject to specific approval from the appropriate Credit Sanctioner. Policy also defines minimum acceptable requirements for the negotiation of ISDA and CSA documentation. Derivative transactions with wholesale counterparties are typically collateralised under a Credit Support Annex (CSA) in conjunction with the ISDA Master Agreement. Derivative transactions with non-bank customers are not usually supported by a CSA.

To recognise the effects of credit risk mitigation, any agreements must be valid, enforceable, unconditional and irrevocable. In addition, collateral must be transferred to the bank through the passing of title and should be offset on a portfolio by portfolio basis. Once these conditions are met, the effect of collateral received is reflected in reductions to all applicable credit exposures and in capital adequacy calculations.

Collateral received is reviewed daily to ensure quality is maintained and concentrations are avoided as necessary.

It is credit policy that a Group approved Master Netting Agreement must be used for all transactions and must be in place prior to trading. Any exceptions must be approved by the Credit Sanctioner. Although master netting agreements do not generally result in an offset of balance sheet assets and liabilities for accounting purposes, as transactions are usually settled on a gross basis, within relevant jurisdictions and for appropriate counterparty types they do reduce the credit risk to the extent that, if an event of default occurs, all trades with the counterparty may be terminated and settled on a net basis. The Group's overall exposure to credit risk on derivative instruments subject to master netting agreements can change substantially within a short period, since this is the net position of all trades under the master netting agreement.

COLLATERAL REQUIREMENTS IN THE EVENT OF A DOWNGRADE IN CREDIT RATING

Internal stress testing results at 31 December 2016 showed that the Banking business had liquidity resources representing 167 per cent of modelled outflows from all wholesale funding sources, retail and corporate deposits, intra-day requirements and rating dependent contracts under the Group's most severe liquidity stress scenario.

A hypothetical idiosyncratic two notch downgrade of the Group's current long-term debt rating and accompanying short-term downgrade implemented instantaneously by all major rating agencies, could result in an outflow of £3.1bn of cash over a period of up to one year, £1.8bn of collateral posting related to customer financial contracts and £9.0bn of collateral posting associated with secured funding.

CORRELATION (WRONG WAY) RISK

The Group seeks to avoid correlation or wrong way risk where possible. Under repo policy, the issuer of the collateral and the repo counterparty should be neither the same nor connected. The same rule applies for derivatives. The Risk Division has the necessary discretion to extend this rule to other cases where there is significant correlation. Countries with a rating equivalent to AA- and above may be considered to have no adverse correlation between the counterparty domiciled in the country and that country of risk (issuer of securities).

DERIVATIVE VALUATION ADJUSTMENTS

Details on the application of derivative valuation adjustments, including Credit and Debit Valuation Adjustments (CVA and DVA), are provided in Note 49 (Financial instruments) of the 2016 Lloyds Banking Group plc Annual Report and Accounts.

Pillar 1 Capital requirements: Counterparty credit risk continued

COUNTERPARTY CREDIT RISK EXPOSURES: ANALYSIS BY MEASUREMENT APPROACH

The credit risk exposure value in respect of counterparty credit risk as at 31 December 2016 was £30.3bn (2015: £28.1bn). An analysis by measurement approach is presented in the table below.

Table 50: CCR: analysis by measurement approach

	2016 Credit risk exposure[1] £m	2015 Credit risk exposure[1] £m
CCR standardised approach	–	–
CCR mark-to-market method	14,526	13,757
CCR internal model method	–	–
SFT comprehensive approach	7,815	7,016
CCR central counterparty	7,752	7,189
Contributions to the default fund of a central counterparty	165	150
Total	**30,258**	28,112

[1]Counterparty credit risk exposures are stated on an EAD post CRM basis throughout this section.

Key movements

– Exposure increase of £2.1bn is primarily due to foreign exchange and yield curve movements.

Table 51: Credit valuation adjustment (CVA) capital charge (CCR2)

		2016 a Exposure value £m	2016 b RWA £m	2015 a Exposure value £m	2015 b RWA £m
1	Total portfolios subject to the Advanced CVA capital charge	–	–	–	–
2	(i) VaR component (including the 3×multiplier)	–	–	–	–
3	(ii) Stressed VaR component (including the 3×multiplier)	–	–	–	–
4	All portfolios subject to the Standardised Method	4,463	864	4,337	1,684
EU4	Based on Original Exposure Method	–	–	–	–
5	**Total subject to the CVA capital charge**	**4,463**	**864**	4,337	1,684

Key movements

– Credit valuation adjustment risk-weighted assets have reduced as a result of increased capital relief via CDS Index hedges.

COUNTERPARTY CREDIT RISK EXPOSURES: ANALYSIS BY EXPOSURE CLASS

An analysis of counterparty credit risk exposures by exposure class, is presented in the table below.

Table 52: CCR: analysis by exposure class

	2016 Credit risk exposure £m	2016 Risk-weighted assets £m	2015 Credit risk exposure £m	2015 Risk-weighted assets £m
Foundation IRB approach				
Corporate – main	**7,902**	**3,213**	7,079	2,837
Central governments and central banks	**1,599**	**79**	761	45
Institutions	**4,420**	**1,828**	4,359	1,791
Other IRB approach				
Corporate – specialised lending[1]	**3,206**	**2,453**	3,230	2,510
Securitisation positions[2]	**343**	**118**	317	145
Total IRB approach	**17,470**	**7,691**	15,746	7,328
Exposures subject to the standardised approach				
Central governments and central banks	**3,597**	**3**	4,047	–
Multilateral development banks	**19**	**–**	37	–
International organisations	**209**	**–**	–	–
Institutions	**7,761**	**158**	7,202	146
Corporates	**1,037**	**567**	930	507
Total standardised approach	**12,623**	**728**	12,216	653
Contributions to the default fund of a central counterparty	**165**	**340**	150	488
Credit valuation adjustment[3]		**864**		1,684
Total	**30,258**	**9,623**	28,112	10,153

[1] Exposures subject to the IRB Supervisory Slotting Approach.

[2] No positions relating to counterparty credit risk securitisation positions were deducted from capital (2015: £166m).

[3] CVA exposure value of £4.5bn (2015: £4.3bn) are embedded in the exposure class analysis above.

Key movements

– IRB counterparty credit risk exposures increased by £1.7bn primarily due to increased trading volumes with Corporate customers and Clearing Houses. IRB risk-weighted assets have increased by proportionately less, £0.4bn, reflecting the lower risk weight on Central Governments and Central Banks.

– Credit Valuation Adjustment risk-weighted assets reduced through increased capital relief as a result of hedging using a CDS Index.

Pillar 1 Capital requirements: Counterparty credit risk continued

COUNTERPARTY CREDIT RISK EXPOSURES: FURTHER ANALYSIS OF IRB EXPOSURES

Further analysis, by PD Grade, of counterparty credit risk exposures subject to the Foundation IRB Approach and the IRB Supervisory Slotting Approach are provided in the tables below.

Throughout this section 'RWA density' represents the average risk weight.

Table 53: IRB – CCR exposure by portfolio and PD range – Corporate Main (CCR4)

	2016						
	a	b	c	d	e	f	g
PD Scale	EAD post CRM	Average PD	Number of obligors	Average LGD	Average Maturity	RWA	RWA density
Corporate – Main	£m	%	#	%	years	£m	%
0.00 to <0.15	**4,783**	**0.07%**	**624**	**45.0%**	**3.2**	**1,336**	**27.95%**
0.15 to <0.25	**767**	**0.18%**	**240**	**45.0%**	**3.0**	**375**	**48.98%**
0.25 to <0.50	**1,831**	**0.33%**	**774**	**45.0%**	**1.7**	**948**	**51.79%**
0.50 to <0.75	**103**	**0.63%**	**256**	**45.0%**	**2.5**	**84**	**81.15%**
0.75 to <2.50	**234**	**1.20%**	**403**	**45.0%**	**2.7**	**249**	**106.34%**
2.50 to <10.00	**137**	**4.50%**	**189**	**45.0%**	**3.1**	**220**	**160.24%**
10.00 to <100.00	**0**	**31.62%**	**27**	**45.0%**	**1.7**	**1**	**210.59%**
100.00 (Default)	**47**	**100.00%**	**14**	**45.0%**	**2.3**	**–**	**–**
Sub-total	**7,902**	**0.85%**	**2,527**	**45.0%**	**2.8**	**3,213**	**40.67%**

	2015						
	a	b	c	d	e	f	g
PD Scale	EAD post CRM	Average PD	Number of obligors	Average LGD	Average Maturity	RWA	RWA density
Corporate – Main	£m	%	#	%	years	£m	%
0.00 to <0.15	4,472	0.06%	598	45.0%	2.9	1,085	24.27%
0.15 to <0.25	612	0.18%	199	45.0%	3.0	313	51.13%
0.25 to <0.50	1,486	0.34%	719	45.0%	1.9	838	56.40%
0.50 to <0.75	115	0.63%	184	45.0%	2.5	95	83.31%
0.75 to <2.50	255	1.34%	278	45.0%	2.8	287	112.84%
2.50 to <10.00	116	3.33%	155	45.0%	3.2	175	150.38%
10.00 to <100.00	16	30.59%	486	45.0%	3.4	44	274.69%
100.00 (Default)	7	100.00%	14	45.0%	2.1	–	–
Sub-total	7,079	0.40%	2,633	45.0%	2.7	2,837	40.09%

Key movements

– The average PD increased 0.45% predominately driven by a modest increase in defaulted exposures.

Table 54: IRB – CCR exposure by portfolio and PD range – Central government and central banks (CCR4)

	2016						
	a	b	c	d	e	f	g
PD Scale	**EAD post CRM**	**Average PD**	**Number of obligors**	**Average LGD**	**Average Maturity**	**RWA**	**RWA density**
Central governments and central banks	**£m**	**%**	**#**	**%**	**years**	**£m**	**%**
0.00 to <0.15	**1,599**	**0.04%**	**11**	**45.0%**	**0.0**	**79**	**4.96%**
0.15 to <0.25	–	–	–	–	–	–	–
0.25 to <0.50	–	–	–	–	–	–	–
0.50 to <0.75	–	–	–	–	–	–	–
0.75 to <2.50	–	–	–	–	–	–	–
2.50 to <10.00	–	–	–	–	–	–	–
10.00 to <100.00	–	–	–	–	–	–	–
100.00 (Default)	–	–	–	–	–	–	–
Sub-total	**1,599**	**0.04%**	**11**	**45.0%**	**0.0**	**79**	**4.96%**

	2015						
	a	b	c	d	e	f	g
PD Scale	EAD post CRM	Average PD	Number of obligors	Average LGD	Average Maturity	RWA	RWA density
Central governments and central banks	£m	%	#	%	years	£m	%
0.00 to <0.15	761	0.05%	13	45.0%	0.1	45	5.86%
0.15 to <0.25	–	–	–	–	–	–	–
0.25 to <0.50	–	–	–	–	–	–	–
0.50 to <0.75	–	–	–	–	–	–	–
0.75 to <2.50	–	–	–	–	–	–	–
2.50 to <10.00	–	–	–	–	–	–	–
10.00 to <100.00	–	–	–	–	–	–	–
100.00 (Default)	–	–	–	–	–	–	–
Sub-total	761	0.05%	13	45.0%	0.1	45	5.86%

Key movements

– The increase in exposure of £0.8bn reflects additional volumes of transactions via Central Banks.

Pillar 1 Capital requirements: Counterparty credit risk continued

Table 55: IRB – CCR exposure by portfolio and PD range – Institutions (CCR4)

	2016						
	a	b	c	d	e	f	g
PD Scale	**EAD post CRM**	**Average PD**	**Number of obligors**	**Average LGD**	**Average Maturity**	**RWA**	**RWA density**
Institutions	**£m**	**%**	**#**	**%**	**years**	**£m**	**%**
0.00 to <0.15	**3,905**	**0.05%**	**264**	**45.0%**	**3.4**	**1,397**	**35.75%**
0.15 to <0.25	**312**	**0.18%**	**40**	**45.0%**	**4.6**	**252**	**80.82%**
0.25 to <0.50	**182**	**0.32%**	**50**	**45.0%**	**3.6**	**160**	**88.00%**
0.50 to <0.75	**10**	**0.63%**	**7**	**45.0%**	**1.4**	**8**	**86.41%**
0.75 to <2.50	**9**	**1.04%**	**8**	**45.0%**	**1.1**	**7**	**80.47%**
2.50 to <10.00	**1**	**4.20%**	**2**	**45.0%**	**1.9**	**2**	**141.90%**
10.00 to <100.00	**1**	**31.00%**	**1**	**45.0%**	**5.0**	**2**	**317.22%**
100.00 (Default)	**–**	**–**	**–**	**–**	**–**	**–**	**–**
Sub-total	**4,420**	**0.08%**	**372**	**45.0%**	**3.5**	**1,828**	**41.35%**

	2015						
	a	b	c	d	e	f	g
PD Scale	EAD post CRM	Average PD	Number of obligors	Average LGD	Average Maturity	RWA	RWA density
Institutions	£m	%	#	%	years	£m	%
0.00 to <0.15	4,011	0.05%	152	45.0%	3.4	1,471	36.69%
0.15 to <0.25	69	0.18%	35	45.0%	2.8	40	57.55%
0.25 to <0.50	175	0.31%	48	45.0%	3.2	145	82.38%
0.50 to <0.75	39	0.74%	12	45.0%	1.0	33	84.75%
0.75 to <2.50	25	2.05%	12	45.0%	0.2	28	111.52%
2.50 to <10.00	40	3.12%	10	45.0%	3.8	74	185.35%
10.00 to <100.00	–	–	–	–	–	–	–
100.00 (Default)	0	100.00%	2	45.0%	1.0	–	–
Sub-total	4,359	0.11%	271	45.0%	3.4	1,791	41.07%

Table 56: CCR corporate exposures subject to supervisory slotting

2016						
Specialised lending						
Regulatory Categories	Remaining maturity	On-balance sheet amount £m	Off-balance sheet amount £m	RW %	Exposure amount £m	RWA £m
1) Strong	Less than 2.5 years	94	–	50%	95	47
	Equal to or more than 2.5 years	2,184	–	70%	2,165	1,517
2) Good	Less than 2.5 years	146	–	70%	147	103
	Equal to or more than 2.5 years	433	–	90%	488	439
3) Satisfactory	Less than 2.5 years	4	–	115%	1	1
	Equal to or more than 2.5 years	201	–	115%	278	320
4) Weak	Less than 2.5 years	–	–	250%	–	–
	Equal to or more than 2.5 years	9	–	250%	11	26
5) Default	Less than 2.5 years	–	–	0%	–	–
	Equal to or more than 2.5 years	17	–	0%	21	–
Total	Less than 2.5 years	244	–		243	151
	Equal to or more than 2.5 years	2,844	–		2,963	2,302

2015						
Specialised lending						
Regulatory Categories	Remaining maturity	On-balance sheet amount £m	Off-balance sheet amount £m	RW %	Exposure amount £m	RWA £m
1) Strong	Less than 2.5 years	100	–	50%	102	51
	Equal to or more than 2.5 years	2,063	–	70%	2,203	1,542
2) Good	Less than 2.5 years	37	–	70%	37	26
	Equal to or more than 2.5 years	364	–	90%	390	351
3) Satisfactory	Less than 2.5 years	29	–	115%	29	33
	Equal to or more than 2.5 years	304	–	115%	350	403
4) Weak	Less than 2.5 years	–	–	250%	–	–
	Equal to or more than 2.5 years	38	–	250%	42	104
5) Default	Less than 2.5 years	3	–	0%	3	–
	Equal to or more than 2.5 years	71	–	0%	74	–
Total	Less than 2.5 years	169	–		171	110
	Equal to or more than 2.5 years	2,840	–		3,059	2,400

Pillar 1 Capital requirements: Counterparty credit risk continued

Table 57: Standardised approach – CCR exposures by regulatory portfolio and risk (CCR3)

2016

	Exposure Classes	0% £m	2% £m	4% £m	10% £m	20% £m	50% £m	70% £m	75% £m	100% £m	150% £m	Others £m	Total £m	Of which: Unrated[1] £m
1	Central governments and central banks	3,592	–	–	–	–	5	–	–	–	–	–	3,597	3,592
4	Multilateral development banks	19	–	–	–	–	–	–	–	–	–	–	19	19
5	International organisations	209	–	–	–	–	–	–	–	–	–	–	209	209
6	Institutions	–	7,752	–	–	4	5	–	–	–	–	–	7,761	7,752
7	Corporates	–	–	–	–	139	715	–	–	183	–	–	1,037	180
17	**Total – Standardised Approach**	3,820	7,752	–	–	143	725	–	–	183	–	–	12,623	11,752

2015

	Exposure Classes	0% £m	2% £m	4% £m	10% £m	20% £m	50% £m	70% £m	75% £m	100% £m	150% £m	Others £m	Total £m	Of which: Unrated[1] £m
1	Central governments and central banks	4,047	–	–	–	–	–	–	–	–	–	–	4,047	4,047
4	Multilateral development banks	37	–	–	–	–	–	–	–	–	–	–	37	37
5	International organisations	–	–	–	–	–	–	–	–	–	–	–	–	–
6	Institutions	–	7,189	–	–	13	–	–	–	–	–	–	7,202	7,189
7	Corporates	–	–	–	–	136	629	–	–	165	–	–	930	140
17	**Total – Standardised Approach**	4,084	7,189	–	–	149	629	–	–	165	–	–	12,216	11,413

[1] Of which Unrated includes any exposure for which a credit assessment by a nominated ECAI is not available or that have specific risk weights applied depending on their class as specified in articles 113 to 134 and in article 306 (for exposures cleared through a qualifying central counterparty).

COUNTERPARTY CREDIT RISK EXPOSURES: ANALYSIS BY CONTRACT TYPE

An analysis of counterparty credit risk exposures as at 31 December 2016, by contract type, is presented in the table below.

Table 58: CCR: analysis by contract type

	2016 Credit risk exposure £m	2015 Credit risk exposure £m
Interest rate and inflation contracts	15,725	14,868
Foreign exchange contracts	5,400	4,201
Equity contracts	182	243
Credit derivatives	336	381
Commodity contracts	163	442
Securities financing transactions	8,287	7,827
Contributions to the default fund of central counterparty	165	150
Total	**30,258**	28,112
Of which central counterparty	7,752	7,189

NET DERIVATIVES CREDIT EXPOSURE

The gross positive fair value of contracts, netting benefits, netted current credit exposure, net potential future credit exposure (PFE), collateral held and resultant 'net derivatives credit exposure', as at 31 December 2016, are presented separately in the table below.

Table 59: Net derivatives credit exposure

	2016 Credit risk exposure £m	2015 Credit risk exposure £m
Gross positive fair value of contracts	92,410	60,723
Netting benefits	(77,957)	(49,614)
Netted current credit exposure	14,453	11,109
Net potential future credit exposure	13,176	12,601
Collateral held[1]	(5,823)	(3,575)
Total net derivatives credit exposure	**21,806**	20,135
of which CCP	7,280	6,377
Securities financing transactions	8,287	7,827
Contributions to the default fund of central counterparty	165	150
Total counterparty credit risk exposure	**30,258**	28,112
of which CCP	7,752	7,189

[1] Collateral held primarily relates to cash and government securities.

An analysis of derivative notional balances, indicating amounts transacted on recognised exchanges and amounts transacted over-the-counter (OTC) (further subanalysed by those settled by central counterparties and those not settled by central counterparties) is provided on page 131 of the 2016 Lloyds Banking Group plc Annual Report and Accounts.

NOTIONAL VALUE OF CREDIT DERIVATIVE TRANSACTIONS

The notional value of credit derivative transactions outstanding at 31 December 2016 was £19.0bn (2015: £20.9bn). These transactions relate to CDS's, total return swaps and other credit derivatives. All total return swaps, including those with gilts underlying, are classified as credit products and are reported in the table below.

Table 60: Notional value of credit derivative transactions

	2016 Notional value £m	2015 Notional value £m
Own credit portfolio – protection bought[1]	3,598	5,438
Own credit portfolio – protection sold[2]	15,422	15,451
Total	**19,020**	20,889

[1] Own credit portfolio (protection bought) comprises £2,961m (2015: £2,095m) of CDS's and £637m (2015: £3,343m) of total return swaps.

[2] Own credit portfolio (protection sold) comprises £973m (2015: £1,385m) of CDS's, £9,006m (2015: £8,623m) of total return swaps and £5,443m (2015: £5,443m) of other credit derivatives, (which relate to providing protection to another part of the Group).

Pillar 1 Capital requirements: Market risk

This section details Lloyds Banking Group's market risk profile, focussing in particular on the Group's internally modelled market risk measures.

- Board Risk Appetite for market risk is set at group level covering market risk across all divisions and is reviewed and approved annually.
- Market risk represents a small proportion (1.5%) (2015: 1.7%) of the Group's total risk-weighted assets.
- Risk-weighted assets reduced by 17% to £3.1bn due to a reduction in the Value-at-Risk multiplier, improvements to the VaR model and active portfolio management.
- Details of market value sensitivity and net interest income sensitivity measures provided in respect of banking activities (non-trading book) can be found in the 2016 Lloyds Banking Group plc Annual Report and Accounts on pages 146 to 151.

Table 61: Market risk own funds requirements

	2016 Risk-weighted assets £m	2016 Capital requirements £m	2015 Risk-weighted assets £m	2015 Capital requirements £m
Internal models approach	**2,795**	**224**	3,224	258
VaR	**207**	**17**	369	30
SVaR	**1,008**	**81**	1,157	92
Incremental risk charge	**143**	**11**	515	41
Comprehensive risk measure	**–**	**–**	–	–
Risks not in VaR	**1,437**	**115**	1,183	95
Standardised approach	**352**	**28**	551	44
Interest rate risk (general and specific)	**280**	**23**	399	32
Equity risk (general and specific)	**–**	**–**	–	–
Foreign exchange risk	**55**	**4**	74	6
Commodity risk	**–**	**–**	–	–
Specific interest rate risk of securitisation positions	**17**	**1**	78	6
Total	**3,147**	**252**	3,775	302

DEFINITION

Market risk is defined as the risk that unfavourable market moves (including changes in and increased volatility of interest rates, market-implied inflation rates, credit spreads and bond prices, foreign exchange rates, equity, property and commodity prices and other instruments), lead to reductions in earnings and/or value. Details of risk appetite, measurement, mitigation and monitoring can be found in the Risk Management section of the 2016 Lloyds Banking Group plc Annual Report and Accounts (Market Risk section, pages 146 to 151).

EXPOSURES

Market risk balance sheet linkages

The information provided in the table below aims to facilitate the understanding of linkages between balance sheet items and the positions disclosed in the Group's market risk disclosures. This breakdown of financial instruments included and not included in trading book VaR provides a linkage with the market risk measures reported later on in the market risk section. It is important to highlight that this table does not reflect how the Group manages trading book market risk, since it does not discriminate between assets and liabilities in its VaR model.

The table below shows relevant balance sheet items relating to banking and trading activities. The trading book VaR sensitivity inputs are separately identified.

As Insurance undertakings are excluded from the scope of the Group's regulatory consolidation, market risks in respect of the assets and liabilities relating to the Group's insurance operations are covered in more detail in the Market Risk section of the 2016 Lloyds Banking Group plc Annual Report and Accounts.

Table 62: Market risk linkages to the balance sheet

		Banking			
31 December 2016	Balance sheet total £m	Trading book only £m	Non-trading £m	Insurance £m	Primary risk factor
Assets					
Cash and balances at central banks	47,452	–	47,452	–	Interest rate
Trading and other financial assets at fair value through profit or loss	151,174	45,247	4,039	101,888	Interest rate, foreign exchange, credit spread
Derivative financial instruments	36,138	30,951	2,713	2,474	Interest rate, foreign exchange, credit spread
Loans and receivables:					
Loans and advances to banks	26,902	–	5,583	21,319	Interest rate
Loans and advances to customers	457,958	–	457,958	–	Interest rate
Debt securities	3,397	–	3,397	–	Interest rate, credit spread
	488,257	–	466,938	21,319	
Available-for-sale financial assets	56,524	–	56,522	2	Interest rate, foreign exchange, credit spread
Value of in-force business	5,042	–	–	5,042	Equity
Other assets	33,206	–	16,811	16,395	Interest rate
Total assets	817,793	76,198	594,475	147,120	
Liabilities					
Deposits from banks	16,384	–	16,384	–	Interest rate
Customer deposits	415,460	–	415,460	–	Interest rate
Trading and other financial liabilities at fair value through profit or loss	54,504	45,079	9,425	–	Interest rate, foreign exchange
Derivative financial instruments	34,924	30,143	1,967	2,814	Interest rate, foreign exchange, credit spread
Debt securities in issue	76,314	–	76,314	–	Interest rate, credit spread
Liabilities arising from insurance and investment contracts	114,502	–	–	114,502	Credit spread
Subordinated liabilities	19,831	–	18,012	1,819	Interest rate, foreign exchange
Other liabilities	37,059	–	9,376	27,683	Interest rate
Total liabilities	768,978	75,222	546,938	146,818	

Pillar 1 Capital requirements: Market risk continued

The Group's trading book assets and liabilities are originated by Financial Markets within the Commercial Banking division. Within the Group's balance sheet these fall under the trading assets and liabilities and derivative financial instruments. The assets and liabilities are classified as trading books if they have been acquired or incurred for the purpose of selling or repurchasing in the near future. These consist of government, corporate and financial institution bonds and loans/deposits and repos.

Derivative assets and liabilities are held by the Group for three main purposes; to provide risk management solutions for clients, to manage portfolio risks arising from client business and to manage and hedge the Group's own risks. The majority of derivatives exposure arises within Financial Markets.

The Group ensures that it has adequate cash and balances at central banks and stocks of high-quality liquid assets (e.g. Gilts or US Treasury Securities) that can be converted easily into cash to meet liquidity requirements. The majority of these assets are held as AFS with the remainder held as financial assets at fair value through profit and loss. Further information on these balances can be found under the Risk Management section – Funding and Liquidity Risk, pages 154 to 158 of the Lloyds Banking Group plc Annual Report and Accounts.

The majority of debt issuance originates from the Issuance, Capital Vehicles and Medium Term Notes desks and the IRR of the debt issued is hedged by swapping them into a floating rate.

Trading portfolios

The Group's trading activity is small relative to its peers and the Group does not have a programme of proprietary trading activities. The Group's trading activity is undertaken solely to meet the financial requirements of commercial and retail customers for foreign exchange, credit and interest rate products. These activities support customer flow and market making activities.

All trading activities are performed within the Commercial Banking division. While the trading positions taken are generally small, any extreme moves in the main risk factors and other related risk factors could cause significant losses in the trading book depending on the positions at the time.

Trading market risk measures are applied to all the Group's regulatory trading books and they include daily VaR sensitivity based measures, and stress testing calculations.

Structure and organization

Market Risk follows the Group's Risk Management Framework. For further information please see "Risk governance" and "How risk is managed in Lloyds Banking Group" sections on pages 27 and 119 of the 2016 Lloyds Banking Group plc Annual Report and Accounts.

Banking activities

The Group's banking activities expose it to the risk of adverse movements in market prices, predominantly interest rates, credit spreads, exchange rates and equity prices. The volatility of market values can be affected by both the transparency of prices and the amount of liquidity in the market for the relevant asset or liability.

Further details of the Group's risks in the banking book, including market value sensitivity and net interest income sensitivity measures provided in respect of banking activities (non-trading book) are presented in the Market Risk section of the 2016 Lloyds Banking Group plc Annual Report and Accounts.

Table 63: Key market risks for the Group by individual business activity (profit before tax impact measured against Group single stress scenarios)

	Risk Type					
2016	**Interest rate**	**Basis risk**	**FX**	**Credit spread**	**Equity**	**Inflation**
Banking activities[1]	●	●	–	●	●	–
Defined benefit pension schemes[1]	●	–	–	■	–	–
Insurance portfolios[1]	●	–	–	●	●	–
Trading portfolios[2]	–	–	–	–	–	–

Profit before tax:	Loss	Gain
>£500m	●	■
£250m – £500m	●	■
£50m – <£250m	●	■
Immaterial/zero	–	–

[1] Banking Activities: Insurance and Pensions stresses; Interest rate - 100bps; Basis 3 month Libor + 100bps/Bank Base Rate -25bps, FX -15 per cent GBP.

[2] Trading Portfolios; Interest rate -30bps, FX -5 per cent GBP, Credit spread +20 per cent, inflation +30bps.

For further information on the key market risks by defined benefit pension schemes and Insurance portfolios refer to pages 149 and 150 of the 2016 Lloyds Banking Group plc Annual Report and Accounts.

Review of internal models

The Group's internal market risk model permission allows it to calculate Pillar 1 market risk capital requirements for the trading book using internal models. The Lloyds Banking Group model permission covers general interest rate and foreign exchange risk across both Lloyds Bank and HBOS portfolios. The capital charge is based on the 10-day 99 per cent VaR and Stressed VaR calculated by the models. The Stressed VaR is the measure of VaR using a continuous one year window based on a period of market stress. In addition the model permission covers specific IRR and the capital charge incorporates specific IRR through VaR and Stressed VaR. The VaR model allows diversification across the different risk factors. The Pillar 1 market risk capital requirements also include an Incremental Risk Charge (IRC) for the trading book.

The Group uses an historical simulation methodology to calculate VaR for the trading book. This methodology consists of calculating historical daily price movements for a full range of market risk factors. The historical daily price movements are applied to positions to create a distribution of hypothetical daily profit and loss scenarios. The hypothetical daily changes in portfolio value are ranked, and the 95th and 99th percentile worst losses are identified. The same VaR model is applied for both management purposes and regulatory purposes. A 1-day 95th percentile VaR is used for internal management purposes, and a 10-day 99th percentile VaR and Stressed VaR is applied for regulatory capital calculation purposes. The 10-day VaR uses a rolling 10 day history and this is updated daily. The VaR and Stressed VaR are also integrated into the risk management process for efficient capital management and to highlight potentially significant exposures based on previous market volatility.

Stressed VaR uses historical market data from a continuous one year period of significant financial stress which is relevant to the trading book positions. The one year dataset is taken from any period since the beginning of 2007 and therefore potentially includes the market movements experienced during the financial crisis. Stressed VaR is calibrated at least quarterly to the period of stress which generates the highest Stressed VaR with the current exposures in the Group's trading books.

The IRC measures the risks arising from both default and loss-inducing rating migrations in the trading book. The charge is computed over a one year capital horizon with the 99.9th percentile worst loss taken as the value of the charge. A Monte Carlo approach is used to simulate the profit and loss changes arising from migration and default for each portfolio position in turn. The profit and loss changes from each position contribute to the overall loss distribution. The calculation uses a multi-factor Gaussian Copula model. A one year liquidity horizon is applied for all positions within this portfolio.

LBG ensures that the IRC model is consistent with the soundness standard comparable to that of the internal-ratings based approach for credit risk. The Lloyds IRC model employs a confidence interval of 99.9% and both its liquidity and risk horizons are set to be one year. This is fully consistent with the EBAs soundness standard for IRC models. The annual validation of the IRC model ensures that the soundness standard comparable to IRB is maintained.

Any material risk factors that fall within the scope of the trading books using internal models and are insufficiently captured by the VaR model are identified and measured as a Risk Not in VaR (RNIV). Identification of risks is performed at least quarterly and through the new product review process to ensure any additional risks outside of VaR and IRC models are captured as RNIV's. Where risk factors are incorporated into the RNIV framework they are quantified either through a VaR-based RNIV approach or a stress test approach. RNIVs can arise for a number of reasons such as where there is limited historical market data, event risks not captured in the current historical data or limited variability in the market data or risks not captured elsewhere such as cross risks, basis risks and higher-order risks.

Validation of the risk models uses a number of methods including but not limited to stress tests, sensitivity analyses and scenarios analyses. The risk models, including the RNIVs, are reviewed independently of the development team and model adequacy and conservatism is re-assessed should the portfolio change over time. Model performance, including backtesting analysis, is regularly reviewed by the Model Governance Committee.

Key characteristics of market risk models

Component modelled	Significant models and associated capital requirement	Model description and methodology	Number of days of market data	Applicable regulatory thresholds for the industry
VaR	1Model: (£17m)	Historical simulation to create a distribution of potential daily P&Ls from market moves. P&Ls are calculated from a grid of full revaluation based sensitivities to approximate/ estimate full revaluation.	300 daily P&Ls, Simple weighting.	Regulatory VaR is computed with 10 day holding period and 99% confidence level. The 10-day VaR is based on rolling 10-day periods.
SVaR	1Model: (£81m)	Same as VaR model.	250 day period of significant stress. Simple weighting. VaR calibration updated quarterly.	Same as VaR model.
IRC	1Model: (£11m)	Monte Carlo approach is used to simulate the profit and loss changes arising from rating migration and default.	Credit Ratings data (1981 – current), CDS bond basis data (2007- current), LGD data (1991-current).	IRC is computed with a 1 year holding period and 99.9% confidence level.

Pillar 1 Capital requirements: Market risk continued

Stress testing

The Group has a comprehensive trading book stress testing programme. Economic scenarios representing extreme but plausible stressed market events are applied to the trading book. These scenarios stress numerous risk factors including interest rates, interest rate spreads, interest rate volatilities, inflation swap rates, inflation volatilities, FX rates, FX volatilities and credit spreads.

There are two sets of stress-testing applied to the trading book: macro-economic and asset class specific. The macro-economic scenarios apply a set of historical events such as the Lehmans default, possible economic events such as what might happen if the Euro breaks up and also regulator provided scenarios such as the EBA stress tests. The macro-economic scenarios are intended to be severe but holistic and plausible. The asset class specific scenarios, also known as desk specific, are intended to apply extreme events to individual risk factors with stresses being applied in groups and to identify points of weakness at both asset class and trading book level.

The market risk function produce stress testing daily and these are reviewed by Financial Markets businesses weekly to facilitate the management of the market risk within their businesses. Limits and triggers apply to stress testing as part of the market risk limit framework. If any of the daily reports show stress testing concerns these are raised with the business immediately.

The stress testing programme is reviewed monthly and new stress tests are introduced when deemed necessary.

Backtesting of VaR models

The Group compares both hypothetical and clean profit or loss with the VaR calculated at a 1-day 99 per cent confidence level on a daily basis. The purpose of this analysis is to provide an indication of how well the VaR model's output, a VaR forecast, has described the corresponding trading outcome. Analysis is performed at the aggregate trading book level, and the business unit level. Hypothetical profit or loss is the change in the valuation of the portfolio due to market moves that would have resulted assuming that the portfolio remains unchanged. Clean profit or loss is hypothetical profit or loss with the additional profit or loss from the change in the portfolio's value due to time. Fees and commissions do not feed into either profit and loss measure.

A backtesting overshoot is generated when loss is greater than the 1-day 99 per cent VaR for a given day. Please see commentary below Table 65 for information on backtesting performance.

Each individual entity is required to have sufficient capital to meet their solo capital requirements. Hence VaR model performance monitoring needs to be performed separately across Lloyds Bank and HBOS heritage portfolios. The Group manages its market risk at a consolidated basis and this is reflected in a single Internal Model Approval Market Risk Permission. Hence backtesting is also done at a consolidated basis to monitor VaR model performance at a consolidated Group level. Below the entity level there is backtesting performed at business area level. The number of overshoots in these portfolios at business area level do not necessarily add up to the number of overshoots in the consolidated portfolio.

Table 64: Backtesting results (VaR models)

2016 backtesting results		Number of reported overshoots	
	Multiplier[1]	Hypothetical	Clean
Entity Level			
Lloyds Bank	3.00	–	–
HBOS	3.00	2	2
LBG	3.00	3	3
Major Business Area			
Rates product		3	2
FX product		5	3
Credit product		1	1
Repo product		5	5

[1] The decrease in the number of backtesting overshoots outstanding over the last 250 business days has resulted in the VaR multiplier used for internal model capital requirements decreasing for Lloyds Bank and LBG to 3.0 from 3.85 and 3.65 respectively as at 31 December 2016.

Key movements

- Statistically the Group would expect to see losses in excess of VaR two to three times over a one-year period. Details of LBG loss overshoots are provided in the backtesting chart comparing VaR to hypothetical and clean profit and loss (Table 66).
- The Group continues to review and improve its VaR model to better capture all relevant risks in its trading portfolio. All significant profit and loss events are investigated as part of normal business. In addition all backtesting results are reported to senior management, internal auditors and the PRA.
- The number of overshoots was lower in 2016 than 2015 due to a number of measures taken to improve VaR model performance. Further measures to improve VaR performance are planned in 2017.

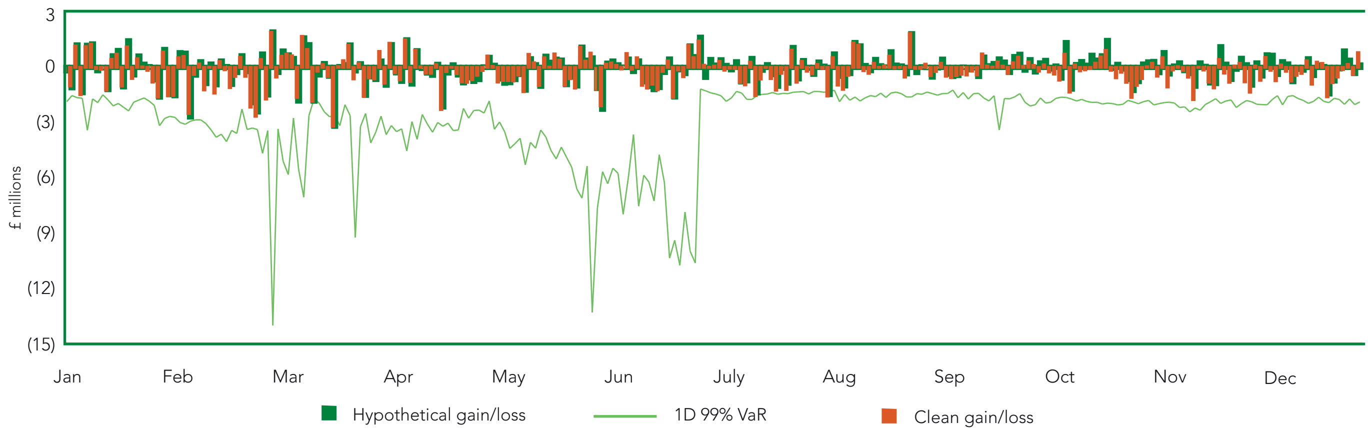
COMPARISON OF VAR TO HYPOTHETICAL AND CLEAN PROFIT AND LOSS

The following chart provides a comparison of VaR (1-day 99 per cent confidence level) to the hypothetical and clean profit and loss on a daily basis over the course of 2016.

Note that the profit and loss used in back-testing represents gains and losses based on the change in valuation of the portfolio due to market moves and is not reflective of the total profit and loss from Financial Markets.

Table 65: Comparison of VaR estimates with gains/losses (MR4)

LLOYDS BANKING GROUP



Key movements

– The significant movements in 1D99 VaR over H1 2016 reflected the impact of low to negative interest EUR rates upon the results. The sharp reduction in the 1D99 VaR at the end of June was as a result of model improvements made to the standard VaR model.

Information behind the backtesting overshoots at LBG level is listed below.

Backtesting Overshoot Date	Hypothetical / Clean Exception	Excess (VaR – P&L) (£000's)	Key driver(s)
11th March 2016	Hypothetical	98	Driven by GBP FX spot rate appreciating versus the USD.
	Clean	84	
17th March 2016	Hypothetical	554	Driven by a statement from the FOMC which impacted both foreign exchange and interest rate markets. Key drivers were large falls in USD interest rates, which led to falls in GBP and EUR interest rates combined with a fall in USD foreign exchange rate against other currencies.
	Clean	559	
4th August 2016	Hypothetical	201	Driven by interest rate moves following the BOE's cut in the base rate.
	Clean	112	

Valuation principles

Trading securities, other financial assets and liabilities at fair value through profit or loss, derivatives and AFS financial assets are stated at fair value. The fair value of these financial instruments is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. It is a measure at a specific date and may be significantly different from the amount which will actually be paid or received on maturity or settlement date.

Wherever possible, fair values have been calculated using unadjusted quoted market prices in active markets for identical instruments held by the Group. Where quoted prices are not available or are unreliable because of poor liquidity, fair values have been determined using valuation techniques which to the extent possible, use market observable inputs, but in some cases use non-market observable inputs. Valuation techniques used include discounted cash flow analysis and pricing models and where appropriate, comparison to instruments with characteristics similar to those of the instruments held by the Group.

The key elements of the control framework for the valuation of financial instruments include model validation, product implementation review and independent price verification. These functions are carried out by appropriately skilled risk and finance teams, independent of the business area responsible for the products.

Model validation covers both qualitative and quantitative elements relating to new models. In respect of new products, a product implementation review is conducted pre and post-trading. Pre-trade testing ensures that the new model is integrated into the Group's systems and that the profit and loss and risk reporting are consistent throughout the trade life cycle. Post-trade testing examines the explanatory power of the implemented model, actively monitoring model parameters and comparing in-house pricing to external sources. Independent price verification procedures cover financial instruments carried at fair value. The frequency of the review is matched to the availability of independent data, monthly being the minimum. Valuation differences in breach of established thresholds are escalated to senior management. The results from independent pricing and valuation reserves are reviewed monthly by senior management.

Formal committees, consisting of senior risk, finance and business management, meet at least quarterly to discuss and approve valuations in more judgemental areas, in particular for unquoted equities, structured credit, over-the-counter options and the Credit Valuation Adjustment (CVA) reserve.

Full details on the use of valuation models and related adjustments are provided in Note 49 (Financial instruments) of the 2016 Lloyds Banking Group plc Annual Report and Accounts.

Pillar 1 Capital requirements: Market risk continued

Trading portfolios

The Group internally uses VaR as the primary risk measure for all trading book positions.

The table below provides relevant statistics for the Group's 10-day 99 per cent confidence level VaR that are based on 300 historical consecutive business days to year end 2016 and year end 2015. Also included are statistics for the Incremental Risk Change for 2016 and 2015.

The risk of loss measured by the VaR model is the minimum expected loss in earnings given a 99 per cent confidence. The total and average trading VaR numbers reported below have been obtained after the application of diversification benefits across the different risk types, interest rate, foreign exchange, credit spread and inflation risk.

Table 66: IMA values for trading portfolios (MR3)

		2016 a £m	2015 a £m
	VaR (10 day 99%)		
1	Maximum value	**42.7**	23.8
2	Average value	**10.3**	7.8
3	Minimum value	**2.7**	2.0
4	Period end	**4.1**	4.7
	Stressed VaR (10 day 99%)		
5	Maximum value	**38.3**	55.5
6	Average value	**19.5**	27.0
7	Minimum value	**8.7**	10.5
8	Period end	**13.4**	22.9
	Incremental Risk Charge (99.9%)		
9	Maximum value	**30.5**	124.1
10	Average value	**13.5**	39.3
11	Minimum value	**6.1**	17.6
12	Period end	**8.3**	41.2
	Comprehensive Risk capital charge (99.9%)		
13	Maximum value	**–**	–
14	Average value	**–**	–
15	Minimum value	**–**	–
16	Period end	**–**	–

Key movements

- The reduction in the average SVaR and IRC over 2016 from 2015 was mainly due to a reduction in positions over the year. The VaR (10 day 99%) average and maximum values were significantly higher up to the end of June 2016 as a result of the impact of low to negative EUR interest rates which resulted in an overstatement in the VaR. Model improvements to more accurately reflect the risk and align the model with SVaR methodology were implemented in June 2016 following PRA approval. This resulted in a lower average VaR from June 2016.

Table 67: Market risk under internal models approach (MR2-A)

		2016 a RWA £m	2016 b Capital requirements £m	2015 a RWA £m	2015 b Capital requirements £m
1	**VaR (higher of values a and b)**	207	17	369	30
(a)	Previous day's VaR (Article 365(1) (VaRt-1))		4		5
(b)	Average of the daily VaR (Article 365(1)) on each of the preceding 60 business days (VaRavg) x multiplication factor (mc) in accordance with Article 366)		17		30
2	**SVaR (higher of values a and b)**	1,008	81	1,157	92
(a)	Latest SVaR (Article 365(2) (sVaRt-1))		13		23
(b)	Average of the SVaR (Article 365(2) during the preceding 60 business days (sVaRavg) x multiplication factor (ms) (Article 366)		81		92
3	**Incremental risk charge – IRC (higher of values a and b)**	143	11	515	41
(a)	Most recent IRC value (incremental default and migration risks calculated in accordance with articles 370/371)		8		41
(b)	Average of the IRC number over the preceding 12 weeks		11		26
4	**Comprehensive Risk Measure – CRM (higher of values a, b and c)**	–	–	–	–
(a)	Most recent risk number for the correlation trading portfolio (article 377)		–		–
(b)	Average of the risk number for the correlation trading portfolio over the preceding 12 weeks		–		–
(c)	8% of the own funds requirement in SA on most recent risk number for the correlation trading portfolio (Article 338(4))		–		–
5	**Other**	1,437	115	1,183	95
6	**Total**	2,795	224	3,224	258

Table 68: RWA flow statements of market risk exposures under an IMA (MR2-B)

		a VaR £m	b SVaR £m	c IRC £m	d CRM £m	e Other £m	f Total RWA[1] £m	g Total capital requirements £m
1	RWA as at 31 December 2015	369	1,157	515	–	1,183	3,224	258
2	Movement in risk levels	450	51	(372)	–	393	522	42
3	Model updates/changes	(612)	(200)	–	–	(139)	(951)	(76)
4	Methodology and policy	–	–	–	–	–	–	–
5	Acquisitions and disposals	–	–	–	–	–	–	–
7	Other	–	–	–	–	–	–	–
8	**RWA at 31 December 2016**	207	1,008	143	–	1,437	2,795	224

[1] The table above relates solely to movement in exposures under an IMA approach. Total Market Risk risk-weighted assets are disclosed by key driver in Table 6. Note: the asset size driver disclosed therein is encompassed in movement in risk levels above.

Key movements

– Internal models approach risk-weighted assets decreased due to a reduction in the VaR multiplier, improvements to the standard VaR model and a reduction in IRC due to smaller Gilt positions. This was partially offset by an increase in exposures for VaR, SVaR and Risks not in VaR or SVaR to changes in interest rates.

– Other represents the risk factors that fall within market risk under the internal models approach and are insufficiently captured by the VaR model and hence captured as a Risk Not in VaR (RNIV), as described in the "Review of internal models" section on page 101. A number of risks captured as RNIVs were moved into the VaR model in 2016 and plans are in place to transfer a material proportion of the remaining RNIVs during 2017.

Pillar 1 Capital requirements: Market risk continued

Table 69: Market risk under Standardised approach (MR1)

		2016 a Risk-weighted assets £m	2016 b Capital requirements £m	2015 a Risk-weighted assets £m	2015 b Capital requirements £m
	Outright Products				
1	Interest rate risk (general and specific)	**280**	**23**	399	32
2	Equity risk (general and specific)	**–**	**–**	–	–
3	Foreign exchange risk	**55**	**4**	74	6
4	Commodity Risk	**–**	**–**	–	–
8	Securitisation (specific risk)[1]	**17**	**1**	78	6
	Options			–	–
5	Simplified approach	**–**	**–**	–	–
6	Delta-plus method	**–**	**–**	–	–
7	Scenario approach	**–**	**–**	–	–
9	**Total**	**352**	**28**	551	44

[1] Further details of the specific interest rate risk of securitisation positions are provided in Table 42.

Key movements
– Market risk under the Standardised approach decreased mainly due to a reduction in Credit Trading and ABS positions.

Pillar 1 Capital requirements: Operational risk

This section details Lloyds Banking Group's operational risk profile, with capital requirements determined under the Standardised Approach.

- Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events.
- The aim of operational risk management is to manage operational risks, protecting customers and the Group, whilst delivering sustainable growth. Operational risks are managed in line with defined appetites through the Group Operational Risk Management Framework, evaluating key exposures, measuring risks, mitigating risks, and monitoring risks on an ongoing basis.
- The Group calculates its operational risk capital requirements using the Standardised Approach. As at 31 December 2016, the capital requirement in respect of operational risk amounted to £2,023m (2015: £2,090m).
- In addition, operational risk scenarios and actual losses are used by the Group to calculate the appropriate holding of operational risk regulatory capital under the Internal Capital Adequacy Assessment Process.
- Details of the Group's Operational Risk Management Framework can be found in the Risk Management section of the 2016 Lloyds Banking Group plc Annual Report and Accounts (pages 152 and 153).

Remuneration disclosures

This section provides an analysis of remuneration awards made by the Group to its Material Risk Takers, together with an explanation of the Group's remuneration policies, structure and governance.

- The Group has a robust governance framework, with the Remuneration Committee reviewing all compensation decisions for Executive Directors, Senior Management, Senior Risk and Compliance Officers, High Earners and any other Material Risk Takers.
- The following groups of individuals have been identified as meeting the criteria for Material Risk Takers being those who have a material impact on the Group's risk profile:
  - Senior Management, Executive Board Directors, members of the Group Executive Committee (GEC) and their respective direct reports;
  - Non-Executive Directors;
  - Approved Persons performing Significant Influence Functions and/or all colleagues performing a Senior Management Function; and
  - Other highly remunerated individuals whose activities could have an impact on the Group's risk profile.
- The overall total of Material Risk Takers increased from 266 to 281 during 2016, primarily as a consequence of internal restructuring and reporting line changes, resulting in more colleagues being identified as 'other Material Risk Takers' under the European Banking Authority Regulatory Technical Standard criteria.
- The Group's remuneration policy fosters a performance-driven and meritocratic culture, encouraging effective risk disciplines and is in line with relevant regulations and codes of best practice.

REMUNERATION DISCLOSURES

This section discloses the remuneration awards made by the Group to Material Risk Takers in respect of the 2016 performance year. Additional information summarising the Group's decision-making policies for remuneration is also provided. These disclosures deliver the requirements of CRR Article 450, to the extent applicable to the 2016 performance year and should be read in conjunction with the disclosures for Executive Directors contained in the Directors' Remuneration Report, within the 2016 Lloyds Banking Group plc Annual Report and Accounts.

Aggregate remuneration expenditure (Material Risk Takers)

Table 70: Analysis of aggregate remuneration expenditure by division

	2016 Retail £m	2016 Commercial Banking £m	2016 Consumer Finance £m	2016 Insurance £m	2016 Group Operations £m	2016 Group Functions £m	2016 Digital £m	2016 Customer Products & Marketing £m	2016 Total £m
Aggregate remuneration expenditure	**8.7**	**52.5**	**4.1**	**4.7**	**15.1**	**71.7**	**3.2**	**5.2**	**165.2**

	2015 Retail £m	2015 Commercial Banking £m	2015 Consumer Finance £m	2015 Insurance £m	2015 Group Operations £m	2015 Group Functions £m	2015 Digital £m	2015 Customer Products & Marketing £m	2015 Total £m
Aggregate remuneration expenditure	8.2	50.7	4.8	1.9	9.0	64.6	3.7	6.2	149.1

Fixed and Variable Remuneration

Table 71: Analysis of remuneration between fixed and variable amounts

	2016 Total	2016 Management Body[1]	2016 Senior Management[2]	2016 Others	2015 Total	2015 Management Body[1]	2015 Senior Management[2]	2015 Others
Number of Material Risk Takers	**281**	**14**	**124**	**143**	266	14	124	128
	£m	£m	£m	£m	£m	£m	£m	£m
Fixed:								
Cash based	**71.5**	**2.6**	**35.9**	**33.0**	66.6	2.5	34.4	29.7
Share based	**11.8**	**1.9**	**7.2**	**2.7**	12.2	1.9	7.1	3.2
Total fixed pay	**83.3**	**4.5**	**43.1**	**35.7**	78.8	4.4	41.5	32.9
Variable:								
Cash	**0.6**	**–**	**0.3**	**0.3**	0.4	–	0.2	0.2
Retained shares[3]	**36.0**	**0.9**	**17.2**	**17.9**	22.8	–	10.3	12.5
Deferred shares	**16.0**	**1.4**	**7.1**	**7.5**	21.9	1.8	10.7	9.4
Total variable pay	**52.6**	**2.3**	**24.6**	**25.7**	45.1	1.8	21.2	22.1
LTIP[4]	**29.2**	**3.9**	**18.7**	**6.6**	25.1	3.8	16.1	5.2

[1] Management Body is defined as the three Group Executive Directors and the Group Non-Executive Directors.

[2] Senior Management are defined as Group Executive Committee (GEC) members/attendees (excluding Group Executive Directors and Non-Executive Directors) and their direct reports (excluding those direct reports who do not materially influence the risk profile of any in-scope group firm).

[3] Shares subject to retention period.

[4] Based on fair value at grant.

Remuneration disclosures continued

Deferred remuneration

Table 72: Analysis of deferred remuneration

	2016 Material Risk Takers £m	2016 Management Body £m	2016 Senior Management £m	2016 Others £m	2015 Material Risk Takers £m	2015 Management Body £m	2015 Senior Management £m	2015 Others £m
Deferred remuneration at 31 December								
Outstanding, vested	–	–	–	–	–	–	–	–
Outstanding, unvested[1]	215.7	22.8	109.8	83.1	257.0	31.9	140.7	84.4
Awarded during the financial year	94.0	8.3	50.5	35.2	98.3	8.9	55.1	34.3
Paid out	94.0	11.9	50.2	31.9	118.8	15.6	66.1	37.1
Reduced through performance adjustment[2]	0.2	–	–	0.2	5.1	0.6	4.3	0.2

[1] 2015 numbers have been restated to include the 2014 Commercial Banking Transformation plan.

[2] This figure does not include the adjusted value of awards which were forfeited by colleagues upon leaving the Group.

High earners by band

Table 73: Analysis of high earners by band

Number of material risk takers paid €1 million[1,2] or more	2016 Material risk takers[3]	2015 Material risk takers
€1.0m – €1.5m	31	38
€1.5m – €2.0m	8	10
€2.0m – €2.5m	4	4
€2.5m – €3.0m	3	4
€3.0m – €3.5m	3	5
€3.5m – €4.0m	3	1
€4.0m – €4.5m	–	3
€4.5m – €5.0m	–	–
€5.0m – €5.5m	–	–
€5.5m – €6.0m	–	–
€6.0m – €6.5m	–	–
€6.5m – €7.0m	1	–
€7.0m – €7.5m	–	1

[1] Converted to Euros using the exchange rate €1 = £0.84815 (average exchange rate 1 December 2016 – 31 December 2016, based on the European Commission Budget exchange rates). The exchange rate used for 2015 was €1 = £0.7029.

[2] Values for LTIP awards based on an expected value of 50 per cent of maximum value.

[3] Total number of Material Risk Takers earning more than €1m has decreased from 66 in 2015 to 53 in 2016. This is due to exchange rate movements.

There were no sign-on awards or severance payments made to Material Risk Takers during 2016 (2015: nil).

Decision making process for remuneration policy

The Group has a strong belief in aligning the pay delivered to the Group's executives with the successful performance of the business and, through this, the delivery of long-term, superior and sustainable returns to shareholders. It has continued to seek the views of shareholders and other key stakeholders with regard to remuneration policy and seeks to motivate, incentivise and retain talent while being mindful of the economic outlook. An essential component of the Group's approach to remuneration is the governance process that underpins it. This ensures that the policy is robustly applied and risk is managed appropriately.

The overarching purpose of the Remuneration Committee is to consider, agree and recommend to the Board an overall remuneration policy and philosophy for the Group that is defined by, supports and is closely aligned to its long-term business strategy, business objectives, risk appetite and values and recognises the interests of relevant stakeholders. The Group has a conservative business model characterised by a risk culture founded on prudence and accountability. The remuneration policy and philosophy covers the whole Group, but the Committee pays particular attention to the top management population, including the highest paid employees in each division, those colleagues who perform significant influence functions for the Group and those who could have a material impact on the Group's risk profile.

The Group has a robust governance framework, with the Remuneration Committee reviewing all compensation decisions for Executive Directors, Senior management, senior risk and compliance officers, high earners and any other Material Risk Takers. This approach to governance is cascaded through the Group with the Executive Compensation Committee having oversight for all other employees. Divisional Remuneration Committees, which include independent representation from control functions, provide an additional layer of governance. Control function employees themselves are assessed and their remuneration determined by the appropriate Control Function Director, and oversight is provided by a Functional Remuneration Committee.

The Group's remuneration policy is based on principles which are applicable to all employees within the Group and in particular the principle that the reward package should support the delivery of our strategic aim to be the 'Best Bank for Customers' whilst delivering superior and sustainable returns to shareholders. It fosters a performance-driven and meritocratic culture, encourages effective risk disciplines and is in line with relevant regulations and codes of best practice. There is no significant difference between the policy for Executive Directors and that for other senior employees. If a significant difference for any individual were proposed, this would be subject to approval by the Remuneration Committee (within regulatory requirements).

The Group continues to maintain an open and transparent dialogue with shareholders. This valuable engagement is something the Group will seek to continue into 2017, given the responsibilities it has to the providers of the equity capital in setting fair and appropriate remuneration policies.

The Group continues to place great importance on ensuring that there is a clear link between remuneration and the Group's business strategy.

Composition of the Remuneration Committee

The members of the Committee during 2016 were Anita Frew (chairman), Lord Blackwell, Alan Dickinson, Dyfrig John (until 11/05/16), Stuart Sinclair (from 04/01/16), Anthony Watson and Sara Weller.

For further information about meetings and principal matters considered, as well as advice to the Committee please refer to the Directors' Remuneration Report within the 2016 Lloyds Banking Group plc Annual Report and Accounts.

Role of the relevant stakeholders

During 2016, the Committee has consulted extensively with a number of shareholders and key stakeholders, such as the Group's main regulators, the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA). The chairman of the Remuneration Committee has also met with the Group's recognised unions. Formal consultation on the remuneration of Executive Directors is not undertaken with employees. The Group conducts colleague surveys every six months to measure engagement and culture. The engagement survey includes specific questions relating to reward and discussions on the Group's remuneration approach takes place with union representatives during the annual pay review cycle and on relevant employee reward matters.

Link between pay and performance

The Group's approach to reward is intended to provide a clear link between remuneration and delivery of its key strategic objectives, supporting the aim of becoming the best bank for customers, and through that, for shareholders. To this end, the performance management process has been developed, with the close participation of the Group's Risk team, to embed performance measures across the Group's reward structure which are challenging and reflect Group and divisional achievement in addition to personal contribution.

The use of a balanced scorecard approach to measure long-term performance enables the Remuneration Committee to assess the performance of the Group and its senior executives in a consistent and performance-driven way. The Group's remuneration policy continues to support the business values and strategy, based on building long-term relationships with customers and employees and managing the financial consequences of business decisions across the entire economic cycle.

The policy is intended to ensure that the Group's remuneration proposition is both cost effective and enables us to attract and retain Executive Directors and senior management of the highest calibre, motivating them to perform to the highest standards. The objective is to align individual reward with the Group's performance, the interests of its shareholders, and a prudent approach to risk management. In this way, the requirements of the Group's various stakeholders – its customers, shareholders, employees and regulators – are balanced. This approach is in line with the Investment Association's principles on remuneration, the PRA Rulebook and the FCA Remuneration Code, as the policy seeks to reward long-term value creation whilst not encouraging excessive risk-taking.

Long-term incentives are based on stretching performance objectives and targets in the Group Balanced Scorecard. This Balanced Scorecard is derived from the Group's operating plan which defines the financial and non-financial targets within the agreed risk appetite over a three year period.

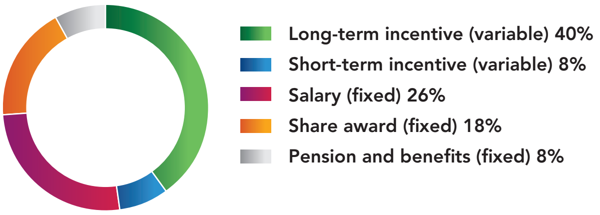
Annual incentives are based on stretching financial targets and objectives in divisional/functional balanced scorecards which are aligned to the Group's strategy.

Remuneration disclosures continued

Design and structure of remuneration

Reward is delivered via a combination of fixed and variable pay. Taking into account the expected value of awards, the performance-related elements of pay make up a considerable proportion of the total remuneration package for Material Risk Takers, whilst maintaining an appropriate balance between the fixed and variable elements.

The approximate make-up of the main components of the package for Executive Directors on an expected value basis is shown below:



The overall policy objective is met by a focus on the particular aspects detailed below.

Base salary

All Material Risk Takers receive either salaries or fees (Non-Executive Directors). Base salaries are reviewed annually, taking into account individual performance and market information. Non-Executive Directors fees are reviewed periodically by the Board.

Fixed share award

The fixed share award, made annually, delivers Lloyds Banking Group shares over a period of five years. It ensures that total fixed remuneration is commensurate with the role and to provide a competitive reward package, with an appropriate balance of fixed and variable remuneration, in line with regulatory requirements

Annual bonus

All Material Risk Takers, excluding Non-Executive Directors, are eligible to be considered for an annual bonus. The annual bonus plan is designed to reflect specific goals linked to the performance of the business.

Awards are based upon individual contribution, overall Group results and divisional/functional Balanced Scorecard ratings. Opportunity is driven by Group performance based on underlying profit, together with divisional/functional achievement and individual performance. Stretching objectives relevant to improving overall business performance and aligned with the Group's strategy are contained in Balanced Scorecards and are grouped under the following headings: Customer, People, Control Environment, Building the Business and Finance.

The Remuneration Committee reviewed performance in depth to determine ratings for the Group and each division, including consideration of risk matters arising in 2016. The overall rating for the Group was strong plus. Collective performance adjustment consideration was given to items not factored into the Group underlying profit or divisional/functional Balanced Scorecards. These included the provisions for legacy conduct-related matters relevant to the year.

As a result of these items, the Remuneration Committee approved an overall adjustment of approximately 19 per cent, resulting in a final bonus outcome of £392.9 million.

To ensure fairness for our shareholders, the total bonus outcome is subject to a limit of 10 per cent of pre-bonus underlying profit. For 2016, the bonus outcome of £392.9 million is significantly below the limit of 10 per cent of underlying profit.

The Remuneration Committee believes that the structure of the annual bonus – in particular the use of risk-adjusted and non-financial measures – has been highly successful in promoting a long-term focus within the senior management team.

Deferral and vesting

To ensure that the interests of Lloyds Banking Group and its employees are aligned with those of the shareholders, and that the approach to risk management supports the interests of all stakeholders, a proportion of bonus above certain thresholds is deferred into Lloyds Banking Group Shares. For all Material Risk Takers, bonus is deferred in line with the regulatory requirements. This deferred amount is subject to performance adjustment (malus) in accordance with the Group's Deferral and Performance Adjustment Policy. Further information on the application of performance adjustment can be found in the Directors' Remuneration Report within the 2016 Lloyds Banking Group plc Annual Report and Accounts.

Furthermore, vested variable remuneration can be recovered from employees up to seven years after the date of award in the case of a material or severe risk event (clawback). This period may be extended to ten years where there is an ongoing internal or regulatory investigation. Clawback is used alongside other performance adjustment processes.

The Committee reserves the right to exercise its discretion in reducing any payment that otherwise would have been earned, if they deem this appropriate.

Long-term incentives

From 2017, the long-term incentive plan will be known as the Group Ownership Share plan. It is a core part of the reward strategy and an important tool for aligning the Group's reward strategy to the performance of the business. Through the application of carefully considered, stretching target measures, the Group can ensure that awards are forfeited or restricted where performance does not meet the desired level. This directly connects the financial reward for the executive and senior management team with the growth and prosperity of the Company and motivates them to demonstrate appropriate behaviours across all areas of the business.

The Group Ownership Share plan pays out in shares based on performance against Group financial and other non-financial strategic targets over a three year period.

In addition to the financial measures of Economic Profit, Total Shareholder Return and Cost-Income ratio, the performance conditions for the 2017 Group Ownership Share plan will comprise measures linked to the Group's strategic targets that reflect the wider Group objectives. These measures are customer complaints handling, customer satisfaction, digital active customer growth and employee engagement. Any shares released are subject to a further holding period in line with regulatory requirements and market practice.

The performance conditions for the Group Ownership Share plan are included in the Directors' Remuneration Report within the 2016 Lloyds Banking Group plc Annual Report and Accounts.

Governance and risk management

An essential component of the approach to remuneration is the governance process that underpins it. This ensures that the policy is robustly applied and risk is managed appropriately.

In addition to setting the overall remuneration policy and philosophy for the Group, the Remuneration Committee ensures that colleagues who could have a material impact on the Group's risk profile are provided with appropriate incentives and reward to encourage them to enhance the performance of the Group and that they are recognised for their individual contribution to the success of the organisation, whilst ensuring that there is no reward for excessive risk taking. The Remuneration Committee works closely with the Risk Committee in ensuring the bonus pool is moderated. The two Committees determine whether the proposed bonus pool and performance assessments adequately reflect the risk appetite and framework of the Group; whether it took account of current and future risks; and whether any further adjustment is required or merited. The Group and the Remuneration Committee are determined to ensure that the aggregate of the variable remuneration for all colleagues is appropriate and balanced with the interests of shareholders and all other stakeholders.

The Remuneration Committee's terms of reference are available from the Company Secretary and are displayed on the Group's website, **www.lloydsbankinggroup.com**. These terms are reviewed each year to ensure compliance with the remuneration regulations.

Further details on directors' remuneration and Board Governance can be found in the Governance section of the 2016 Lloyds Banking Group plc Annual Report and Accounts on pages 51 to 114.

Appendix 1: Lloyds Banking Group

OWN FUNDS DISCLOSURE TEMPLATE

Table 74: Lloyds Banking Group own funds template

	Transitional rules		Fully loaded rules	
	At 31 Dec 2016 £m	At 31 Dec 2015[1] £m	**At 31 Dec 2016 £m**	At 31 Dec 2015[1] £m
Common equity tier 1 (CET1) capital: instruments and reserves				
Capital instruments and related share premium accounts	**24,768**	24,558	**24,768**	24,558
of which: called up share capital	**7,146**	7,146	**7,146**	7,146
of which: share premium	**17,622**	17,412	**17,622**	17,412
Retained earnings[1]	**7,716**	7,755	**7,716**	7,755
Accumulated other comprehensive income and other reserves (including unrealised gains and losses)	**11,718**	10,182	**11,718**	10,182
Foreseeable dividend	**(1,568)**	(1,427)	**(1,568)**	(1,427)
Common equity tier 1 (CET1) capital before regulatory adjustments	**42,634**	41,068	**42,634**	41,068
Common equity tier 1 (CET1) capital: regulatory adjustments				
Additional value adjustments	**(630)**	(372)	**(630)**	(372)
Intangible assets (net of related tax liability)	**(1,623)**	(1,719)	**(1,623)**	(1,719)
Deferred tax assets that rely on future profitability, excluding those arising from temporary differences (net of related tax liability where the conditions in Article 38 (3) of the CRR are met)	**(3,564)**	(3,874)	**(3,564)**	(3,874)
Fair value reserves related to gains or losses on cash flow hedges	**(2,136)**	(727)	**(2,136)**	(727)
Negative amounts resulting from the calculation of expected loss amounts	**(602)**	(270)	**(602)**	(270)
Gains or losses on liabilities valued at fair value resulting from changes in own credit standing	**(2)**	5	**(2)**	5
Defined benefit pension fund assets	**(267)**	(721)	**(267)**	(721)
Direct and indirect holdings by the Group of own CET1 instruments	**(27)**	(177)	**(27)**	(177)
Direct, indirect and synthetic holdings by the Group of the CET1 instruments of financial sector entities where the Group has a significant investment in those entities (amount above 10% threshold and net of eligible short positions)[1]	**(4,282)**	(4,500)	**(4,282)**	(4,500)
Exposure amount of the following items which qualify for a risk weight of 1,250%, where the Group has opted for the deduction alternative	**(217)**	(169)	**(217)**	(169)
of which: securitisation positions	**(217)**	(169)	**(217)**	(169)
Amount exceeding the 15% threshold	**–**	–	**–**	(39)
of which: direct and indirect holdings by the institution of the CET1 instruments of financial sector entities where the institution has a significant investment in those entities	**–**	–	**–**	(29)
of which: deferred tax assets arising from temporary differences	**–**	–	**–**	(10)
Total regulatory adjustments applied to common equity tier 1 (CET1)	**(13,350)**	(12,524)	**(13,350)**	(12,563)
Common equity tier 1 (CET1) capital	**29,284**	28,544	**29,284**	28,505
Additional tier 1 (AT1) capital: instruments				
Capital instruments and related share premium accounts	**5,320**	5,355	**5,320**	5,355
of which: classified as equity under applicable accounting standards	**5,320**	5,355	**5,320**	5,355
Amount of qualifying items referred to in Article 484 (4) of the CRR and the related share premium accounts subject to phase out from AT1	**592**	818	**–**	–
Qualifying Tier 1 capital included in consolidated AT1 capital (including minority interests not included in CET1) issued by subsidiaries and held by third parties	**2,714**	3,004	**–**	–
of which: instruments issued by subsidiaries subject to phase out	**2,714**	3,004	**–**	–
Additional tier 1 (AT1) capital before regulatory adjustments	**8,626**	9,177	**5,320**	5,355
Additional tier 1 (AT1) capital: regulatory adjustments				
Residual amounts deducted from AT1 capital with regard to deduction from Tier 2 capital during the transitional period pursuant to Article 475 of the CRR	**(1,329)**	(1,177)	**–**	–
of which: significant investments in Tier 2 instruments of other financial sector entities	**(1,329)**	(1,177)	**–**	–
Total regulatory adjustments applied to additional tier 1 (AT1) capital	**(1,329)**	(1,177)	**–**	–
Additional tier 1 (AT1) capital	**7,297**	8,000	**5,320**	5,355
Tier 1 capital	**36,581**	36,544	**34,604**	33,860

	Transitional rules		Fully loaded rules	
	At 31 Dec 2016 £m	At 31 Dec 2015[1] £m	**At 31 Dec 2016 £m**	At 31 Dec 2015[1] £m
Tier 2 (T2) capital: Instruments and provisions				
Capital instruments and related share premium accounts	**3,813**	2,134	**4,404**	2,952
Amount of qualifying items referred to in Article 484 (5) of the CRR and the related share premium accounts subject to phase out from T2	**10**	10	**–**	–
Qualifying own funds instruments included in consolidated T2 capital (including minority interests and AT1 instruments not included in CET1 or AT1) issued by subsidiaries and held by third parties	**7,104**	10,843	**3,328**	6,016
of which: instruments issued by subsidiaries subject to phase out	**3,711**	4,763	**–**	–
Credit risk adjustments	**186**	221	**186**	221
Tier 2 (T2) capital before regulatory adjustments	**11,113**	13,208	**7,918**	9,189
Tier (T2) capital: regulatory adjustments				
Direct and indirect holdings by the Group of the T2 instruments and subordinated loans of financial sector entities where the Group has a significant investment in those entities (net of eligible short positions)	**(1,571)**	(1,756)	**(2,900)**	(2,933)
Total regulatory adjustments applied to tier 2 (T2) capital	**(1,571)**	(1,756)	**(2,900)**	(2,933)
Tier 2 (T2) capital	**9,542**	11,452	**5,018**	6,256
Total capital	**46,123**	47,996	**39,622**	40,116
Total risk-weighted assets	**215,534**	222,845	**215,534**	222,747
Capital ratios and buffers				
Common Equity Tier 1 (as a percentage of risk exposure amount)	**13.6%**	12.8%	**13.6%**	12.8%
Tier 1 (as a percentage of risk exposure amount)	**17.0%**	16.4%	**16.1%**	15.2%
Total capital (as a percentage of risk exposure amount)	**21.4%**	21.5%	**18.4%**	18.0%
Institution specific buffer requirement (CET1 requirement in accordance with article 92 (1) (a) plus capital conservation and countercyclical buffer requirements, plus systemic risk buffer, plus the systemically important institution buffer (G-SII or O-SII buffer), expressed as a percentage of risk exposure amount)	**0.627%**	0.001%	**0.627%**	0.001%
of which: capital conservation buffer requirement[2]	**0.625%**	–	**0.625%**	–
of which: countercyclical buffer requirement	**0.002%**	0.001%	**0.002%**	0.001%
Common Equity Tier 1 available to meet buffers (as a percentage of risk exposure amount)[3]	**9.1%**	8.3%	**9.1%**	8.3%
Amounts below the threshold for deduction (before risk weighting)				
Direct and indirect holdings of the capital of financial sector entities where the Group does not have a significant investment in those entities (amount below 10% threshold and net of eligible short positions)	**1,040**	1,552	**1,040**	1,552
Direct and indirect holdings by the Group of the CET1 instruments of financial sector entities where the Group has a significant investment in those entities (amount below 10% threshold and net of eligible short positions)	**3,357**	3,127	**3,357**	3,127
Deferred tax assets arising from temporary differences (amount below 10% threshold, net of related tax liability where the conditions in 38 (3) are met)	**984**	1,188	**984**	1,188
Applicable caps on the inclusion of provisions in Tier 2				
Credit risk adjustments included in T2 in respect of exposures subject to internal ratings-based approach (prior to the application of the cap)	**186**	221	**186**	221
Cap on inclusion of credit risk adjustments in T2 under internal ratings-based approach	**932**	953	**932**	953
Capital instruments subject to phase-out arrangements (only applicable between 1 Jan 2013 and 1 Jan 2022)				
Current cap on AT1 instruments subject to phase out arrangements	**3,305**	3,856	**–**	–
Amount excluded from AT1 due to cap (excess over cap after redemptions and maturities)	**1,419**	671	**–**	–
Current cap on T2 instruments subject to phase out arrangements	**8,600**	10,034	**–**	–

[1] The presentation of the deconsolidation of the Group's insurance entities has been amended with comparative figures restated accordingly.
[2] The capital conservation buffer requirement is the percentage applicable at the reporting date. This will increase to 2.5 per cent by 2019.
[3] Excluding CET1 required to meet Pillar 2A requirements.

Appendix 1: Lloyds Banking Group continued

OWN FUNDS RECONCILIATION

The following table presents certain items from the Group's consolidated regulatory balance sheet (as presented on pages 7 and 8), for the year ended 31 December 2016, that are used to calculate own funds. Where necessary, the balance sheet components under the regulatory scope of consolidation have been expanded such that the components of the transitional own funds disclosure template appear separately.

Table 75: Lloyds Banking Group items extracted from the consolidated regulatory balance sheet and reconciliation of own funds items to audited financial statements

			Adjustments						
Lloyds Banking Group balance sheet category	Own funds description	Items extracted from the consolidated regulatory balance sheet (1) £m	Deferred tax £m	Threshold adjustments £m	Non-eligible instruments (12) £m	Amounts excluded from AT1 due to Cap (12) £m	Regulatory and other adjustments £m	Transitional own funds £m	Notes
	Common Equity Tier 1 (CET1) capital: instruments and reserves								
	Capital instruments and related share premium accounts	24,768	–	–	–	–	–	24,768	
Share capital	of which: called up share capital	7,146	–	–	–	–	–	7,146	
Share premium	of which: share premium	17,622	–	–	–	–	–	17,622	
Retained profits	Retained earnings	7,709	–	–	–	–	7	7,716	2
Other reserves	Accumulated other comprehensive income and other reserves (including unrealised gains and losses)	11,910	–	–	–	–	(192)	11,718	2
	Common equity tier 1 (CET1) capital: regulatory adjustments								
	Additional value adjustments	–	–	–	–	–	(630)	(630)	3
Goodwill and other intangible assets	Intangible assets (net of related tax liability)	(1,714)	91	–	–	–	–	(1,623)	4
Deferred tax assets	Deferred tax assets that rely on future profitability, excluding those arising from temporary differences (net of related tax liability where conditions in Article 38(3) of the CRR are met)	(3,645)	(906)	984	–	–	3	(3,564)	5
	Fair value reserves related to gains or losses on cash flow hedges	–	–	–	–	–	(2,136)	(2,136)	6
	Negative amounts resulting from the calculation of expected loss amounts	–	–	–	–	–	(602)	(602)	7
	Gains or losses on liabilities valued at fair value resulting from changes in own credit standing	–	–	–	–	–	(2)	(2)	8
Retirement benefit assets	Defined benefit pension fund assets	(342)	75	–	–	–	–	(267)	5
	Direct and indirect holding by the Group of own CET1 instruments	–	–	–	–	–	(27)	(27)	9
Investment in group undertakings	Direct and indirect holdings by the Group of CET1 instruments in financial sector entities where the Group has a significant investment in those entities (amounts above 10% threshold and net of eligible short positions)	(7,999)	–	3,357	–	–	360	(4,282)	10
	Exposures amount of the following items which qualify for a risk weight of 1,250%, where the Group has opted for the deduction alternative (securitisation positions)	–	–	–	–	–	(217)	(217)	11
	Foreseeable dividend	–	–	–	–	–	(1,568)	(1,568)	12
	Common Equity Tier 1 (CET1) capital	**30,687**	**(740)**	**4,341**	**–**	**–**	**(5,004)**	**29,284**	
	Additional Tier 1 (AT1) capital: instruments								
Other equity instruments	Capital instruments and the related share premium accounts	5,355	–	–	–	–	(35)	5,320	
Subordinated liabilities	Amount of qualifying items referred to in Article 484 (4) of the CRR and the related share premium accounts subject to phase out from AT1	864	–	–	–	(254)	(18)	592	13
Subordinated liabilities	Qualifying Tier 1 capital included in consolidated AT1 capital (including minority interests not included in CET1) issued by subsidiaries and held by third parties	4,148	–	–	(149)	(1,165)	(120)	2,714	13
	Additional Tier 1 (AT1) capital: regulatory adjustments								
Trading and other financial assets at fair value through profit or loss	Residual amounts deducted from AT1 capital with regard to deduction from T2 capital during the transitional period pursuant to article 475 of the CRR (significant investments)	(2,012)	–	–	–	–	683	(1,329)	14
	Additional Tier 1 (AT1) capital	**8,355**	**–**	**–**	**(149)**	**(1,419)**	**510**	**7,297**	
	Tier 1 capital	**39,042**	**(740)**	**4,341**	**(149)**	**(1,419)**	**(4,494)**	**36,581**	
	Tier 2 (T2) capital: instruments and provisions								
Subordinated liabilities	Capital instruments and related share premium accounts	3,587	–	–	–	254	(28)	3,813	13
Subordinated liabilities	Amount of qualifying items referred to in Article 484 (5) of the CRR and the related share premium accounts subject to phase out from T2	10	–	–	–	–	–	10	13
Subordinated liabilities	Qualifying own funds instruments included in consolidated T2 capital (including minority interests and AT1 instruments not included in CET1 or AT1) issued by subsidiaries and held by third parties	9,606	–	–	(68)	1,165	(3,599)	7,104	13
	Credit risk adjustments	–	–	–	–	–	186	186	15
	Tier 2 (T2) capital: regulatory adjustments								
Loans and receivables	Direct and indirect holdings by the Group of the T2 instruments and subordinated loans of financial sector entities where the Group has a significant investment in those entities (net of eligible short positions)	(578)	–	–	–	–	–	(578)	
Trading and other financial assets at fair value through profit or loss	Direct and indirect holdings by the Group of the T2 instruments and subordinated loans of financial sector entities where the Group has a significant investment in those entities (net of eligible short positions)	–	–	–	–	–	(993)	(993)	14
	Tier 2 (T2) capital	**12,625**	**–**	**–**	**(68)**	**1,419**	**(4,434)**	**9,542**	
	Total capital	**51,667**	**(740)**	**4,341**	**(217)**	**–**	**(8,928)**	**46,123**	

1 Assets on the regulatory balance sheet are presented as negative amounts, liabilities and equity are presented as positive amounts.

2. The regulatory definition of eligible items for inclusion in retained earnings differs from the statutory reporting definition. The aggregate of retained earnings and accumulated other comprehensive income and other reserves is comparable on both bases but the allocation between categories differs.

3. The additional value adjustments of £630m reflect the prudent valuation adjustment for all assets measured at fair value in accordance with Articles 34 and 105 of the CRR.

4. Own funds intangible assets of £1,714m extracted from the consolidated regulatory balance sheet comprise £194m of goodwill and £1,520m of intangible assets. CRD IV rules require the amount to be deducted from own funds to be reduced by the amount of the associated deferred tax liabilities.

5. The own funds deduction of £3,564m for deferred tax excludes the deferred tax balances relating to intangible assets, cash flow hedge and the defined benefit pension fund asset. Additionally, only the deferred tax amounts that rely on future profitability are required to be deducted from CET1, and may be reduced by associated deferred tax liabilities where conditions specified in Article 38 of CRR are met. £984m of the deferred tax assets relate to temporary differences that may be risk weighted instead of deducted from capital as presented in the threshold adjustments column.

6. Cash flow hedge reserve forms part of other reserves in the consolidated regulatory balance sheet. Please refer to note 42 Other Reserves in the 2016 Lloyds Banking Group plc Annual Report and Accounts.

7. In accordance with Articles 36, 62, 158 and 159 of the CRR the excess of expected losses over specific credit risk adjustments (SCRAs) and additional value adjustments of £602m are deducted from CET1. A comparison of regulatory expected losses to SCRAs on loans and receivables, in respect of credit risk exposures subject to the IRB Approach is presented on page 51.

8. CRD IV requires the removal of the impact of any gains or losses recorded on liabilities held at fair value through profit or loss or derivative liabilities due to changes in the credit spreads of Lloyds Bank plc.

9. The £27m deduction of holdings by the Group of its own CET1 instruments represents the regulatory adjustment required to remove the Group's investment in its own shares, excluding holdings through Open Ended Investment Companies (OEICs) as these shareholdings are held for third party investors through the Group's Insurance operations.

10. The investment in group undertakings of £7,999m extracted from the consolidated regulatory balance sheet represents the Group's total equity investment in Insurance subsidiaries as well as joint ventures and associates. The majority of the investment relates to the Group's investment in its Insurance operations headed by Scottish Widows Group. The own funds deduction of £4,282m reflects the regulatory requirement to deduct a portion of the Group's significant investments from CET1, above certain thresholds. In accordance with the CRD IV rules the cost of the Group's investment in the equity of the Insurance business is risk-weighted up to a limit based on the size of the Group's CET1 capital (as presented in the threshold adjustments column), with the remainder deducted from CET1.

11. The £217m deduction for securitisation positions reflects those positions that were rated below BB- or that are unrated.

12. The £1,568m foreseeable dividend is that recommended by the Board of Directors in respect of 2016 earnings.

13. A reconciliation of subordinated liabilities from the consolidated regulatory balance sheet to the amount recognised against each own funds description is presented in the table below.

Own funds description	Consolidated regulatory balance sheet total £m
Amount of qualifying items referred to in Article 484 (4) of the CRR and the related share premium accounts subject to phase out from AT1	**864**
Qualifying Tier 1 capital included in consolidated AT1 capital (including minority interests not included in CET1) issued by subsidiaries and held by third parties	**4,148**
Capital instruments and related share premium accounts	**3,587**
Amount of qualifying items referred to in Article 484 (5) of the CRR and the related share premium accounts subject to phase out from T2	**10**
Qualifying own funds instruments included in consolidated T2 capital (including minority interests and AT1 instruments not included in CET1 or AT1) issued by subsidiaries and held by third parties	**9,606**
Total subordinated liabilities as presented on the consolidated regulatory balance sheet, page 8	**18,215**

Adjustments required by regulatory rules to the value of subordinated liabilities presented within the regulatory and other adjustments column on the reconciliation include adjustments for accrued interest, amortisation and associated derivatives.

The non-eligible instruments column on the reconciliation represents instruments on the balance sheet that are not eligible for inclusion in regulatory capital.

Additional Tier 1 instruments presented in own funds reflect instruments issued by either Lloyds Banking Group plc or its subsidiaries and held by third parties that qualified as Tier 1 under regulation that preceded CRD IV, subject to certain restrictions, including a cap set at 60 per cent of the value of such instruments that were in issue at 31 December 2012 and net of interest. Any excess over the cap is included in Tier 2 instruments which have been issued in the same manner as Additional Tier 1 instruments and are net of interest and in some instances amortisation and associated derivatives.

14. The £2,012m extracted from the regulatory consolidated balance sheet reflects the Group's investment in the subordinated debt of Scottish Widows held at fair value through profit or loss. The Group's full investment in the subordinated debt of Scottish Widows is deducted from capital across AT1 and T2 in accordance with the transitional CRD IV rules. For 2016, 40% of the total investment is deducted equally from AT1 and T2, with the remainder deducted directly from AT1 or T2 in line with the classification of the underlying debt instrument.

15. Credit risk adjustments of £186m reflect the surplus provisions resulting from the calculation of excess expected loss amounts in accordance with Articles 158 and 159 of the CRR, subject to certain limits. A comparison of regulatory expected losses to SCRAs on loans and receivables, in respect of credit risk exposures subject to the IRB Approach is presented on page 51.

Appendix 1: Lloyds Banking Group continued

LEVERAGE DISCLOSURE TEMPLATE

Table 76: Lloyds Banking Group leverage ratio common disclosure

	At 31 Dec 2016 Fully loaded £m	At 31 Dec 2015 Fully loaded £m
On-balance sheet exposures (excluding derivatives and SFTs)		
On-balance sheet items (excluding derivatives, SFTs and fiduciary assets, but including collateral)	**596,415**	609,110
Asset amounts deducted in determining Tier 1 capital	**(9,128)**	(9,112)
Total on-balance sheet exposures (excluding derivatives, SFTs and fiduciary assets)	**587,287**	599,998
Derivative exposures		
Replacement cost associated with all derivatives transactions (ie net of eligible cash variation margin)	**7,863**	6,392
Add-on amounts for PFE associated with all derivatives transactions (mark-to-market method)	**13,188**	12,966
Gross-up for derivatives collateral provided where deducted from the balance sheet assets pursuant to the applicable accounting framework	**1,636**	2,371
Deductions of receivables assets for cash variation margin provided in derivatives transactions	**(4,686)**	(3,689)
Adjusted effective notional amount of written credit derivatives	**1,088**	813
Adjusted effective notional offsets and add-on deductions for written credit derivatives	**(389)**	(131)
Total derivative exposures	**18,700**	18,722
Securities financing transaction exposures		
Gross SFT assets (with no recognition of netting), after adjusting for sales accounting transactions	**44,617**	39,604
Netted amounts of cash payables and cash receivables of gross SFT assets	**(3,858)**	(5,909)
Counterparty credit risk exposure for SFT assets	**1,677**	3,361
Total securities financing transaction exposures	**42,436**	37,056
Other off-balance sheet exposures		
Off-balance sheet exposures at gross notional amount	**129,214**	129,491
Adjustments for conversion to credit equivalent amounts	**(70,529)**	(73,067)
Other off-balance sheet exposures	**58,685**	56,424
Capital and total exposure measure		
Tier 1 capital	**34,604**	33,860
Leverage ratio total exposure measure	**707,108**	712,200
Leverage ratio		
Leverage ratio	**4.9%**	4.8%

A description of the factors that had an impact on the leverage ratio during the year is discussed on page 23.

Table 77: Lloyds Banking Group summary reconciliation of accounting assets and leverage ratio exposures

	At 31 Dec 2016 Fully loaded £m	At 31 Dec 2015 Fully loaded £m
Total assets as per published financial statements	**817,793**	806,688
Adjustment for entities which are consolidated for accounting purposes but are outside the scope of regulatory consolidation	**(145,246)**	(135,926)
Adjustments for derivative financial instruments	**(15,035)**	(9,235)
Adjustments for securities financing transactions (SFTs)	**39**	3,361
Adjustment for off-balance sheet items (ie conversion to credit equivalent amounts of off-balance sheet exposures)	**58,685**	56,424
Other adjustments	**(9,128)**	(9,112)
Leverage ratio total exposure measure	**707,108**	712,200

Table 78: Lloyds Banking Group split-up of on balance sheet exposures (excluding derivatives, SFTs and exempted exposures)

	At 31 Dec 2016 Fully loaded £m	At 31 Dec 2015 Fully loaded £m
Total on-balance sheet exposures (excluding derivatives, SFTs, and exempted exposures), of which:	**596,415**	609,110
Trading book exposures	**12,174**	9,488
Banking book exposures, of which:	**584,241**	599,622
Covered bonds	**2,363**	3,944
Exposures treated as sovereigns	**98,799**	106,196
Exposures to regional governments, MDB, international organisations and PSE not treated as sovereigns	**2**	2
Institutions	**2,252**	1,776
Secured by mortgages of immovable properties	**325,290**	332,496
Retail exposures	**32,176**	30,591
Corporate	**77,679**	80,031
Exposures in default	**8,775**	9,995
Other exposures (eg equity, securitisations, and other non-credit obligation assets)	**36,905**	34,591

Description of the processes used to manage the risk of excessive leverage
Capital is actively managed and regulatory ratios, including leverage, are a key factor in the Group's internal risk appetite assessment, planning processes and stress analyses.

Capital plans include an assessment of leverage requirements over the forecast period, with capital adequacy in respect of both risk-based capital and leverage requirements subjected to a range of stress scenarios. Where relevant the scenarios consider the risk of excessive leverage and potential mitigating actions that could be undertaken in response.

The Group monitors its leverage position through a combination of actual and projected ratios, including those under stressed scenarios, ensuring that the ratio exceeds regulatory minimums and internal risk appetite and reports these on a regular basis to the Group Asset and Liability Committee, the Group Executive Committee, the Group Risk Committee, Board Risk Committee and the Board.

Further details on the process by which the Group manages its capital position in respect of both risk-based capital and leverage requirements is discussed in the Capital Risk section on pages 159 to 166 of the 2016 Lloyds Banking Group plc Annual Report and Accounts.

Appendix 1: Lloyds Banking Group continued

Table 79: Lloyds Banking Group geographical distribution of credit exposures relevant for the calculation of the countercyclical capital buffer

	2016 General credit exposures[2,3]		2016 Trading book exposures[2,4]		2016 Securitisation exposures[3]		2016 Own funds requirements					
Breakdown by Country	Exposure Value for STA £m	Exposure Value for IRB £m	Sum of long and short positions of trading book exposures for STA £m	Value of trading book exposures for internal models £m	Exposure Value for STA £m	Exposure Value for IRB £m	of which: General credit exposures[2,3] £m	of which: Trading book exposures[2,4] £m	of which: Securitisation exposures[3] £m	Total £m	2016 Own funds requirement weights %	2016 Countercyclical capital buffer rate %
Norway	10	308	–	–	–	–	12	–	–	12	0.09%	1.500%
Sweden	48	65	–	–	–	–	5	–	–	5	0.04%	1.500%
Hong Kong	234	28	–	–	–	–	10	–	–	10	0.08%	0.625%
i) Total[1]	**292**	**401**	**–**	**–**	**–**	**–**	**27**	**–**	**–**	**27**	**0.21%**	
United Kingdom	19,100	485,137	134	90	1,184	18,505	11,244	16	250	11,510	84.14%	n/a
United States of America	2,442	12,828	–	–	–	6,743	639	–	57	696	5.09%	n/a
Ireland	1,133	4,609	–	–	–	24	402	–	4	406	2.97%	n/a
Netherlands	740	6,771	–	–	–	20	187	–	–	187	1.37%	n/a
ii) Total[1]	**23,415**	**509,345**	**134**	**90**	**1,184**	**25,292**	**12,472**	**16**	**311**	**12,799**	**93.57%**	
iii) Rest of the World[1]	**3,408**	**15,985**	**–**	**–**	**–**	**1,117**	**838**	**–**	**16**	**854**	**6.22%**	
Total	**27,115**	**525,731**	**134**	**90**	**1,184**	**26,409**	**13,337**	**16**	**327**	**13,680**	**100.00%**	

Amount of institution specific countercyclical capital buffer	2016	2015
Total risk exposure amount	**£215,534m**	£222,845m
Institution specific countercyclical buffer rate	**0.002%**	0.001%
Institution specific countercyclical buffer requirement	**£5.0m**	£2.8m

[1] The breakdown by country is disclosed on the following basis:
i) those countries for which a countercyclical capital buffer rate has been set.
ii) those countries for which a countercyclical capital buffer rate has not been set and have an own funds requirement weighting of greater than or equal to one per cent, the threshold having been determined by the Group in accordance with the EBA guidelines on materiality for Pillar 3.
iii) the aggregate of all remaining countries for which a countercyclical buffer rate has not been set and individually have an own funds requirement weighting of less than one per cent.

[2] For the purposes of the calculation of the countercyclical capital buffer, general credit risk and trading book exposures exclude exposures to central governments, central banks, regional governments, local authorities, public sector entities, multilateral development banks, international organisations and institutions. In addition, trading book exposures are limited to those that are subject to the own funds requirement for specific risk or incremental default and migration risk.

[3] General credit and securitisation exposures include counterparty credit risk and are stated on a post CRM basis.

[4] Trading book exposures are allocated in full to the United Kingdom in accordance with the threshold criteria set out under the EBA Regulatory Technical Standard on the identification of the geographical location of the relevant credit exposures for the calculation of the countercyclical capital buffer.

Appendix 2: Lloyds Banking Group – Asset encumbrance

Table 80: Asset Encumbrance

	2016 Carrying amount of encumbered assets £m	2016 Fair Value of encumbered assets £m	2016 Carrying amount of unencumbered assets £m	2016 Fair value of unencumbered assets £m	2015 Carrying amount of encumbered assets £m	2015 Fair Value of encumbered assets £m	2015 Carrying amount of unencumbered assets £m	2015 Fair value of unencumbered assets £m
Assets[1]								
Total assets	**148,158**		**539,791**		143,482		543,626	
Equity instruments	**–**	**–**	**2,063**	**2,063**	–	–	1,950	1,950
Debt securities[2]	**33,233**	**33,233**	**47,793**	**47,793**	23,379	23,379	56,982	56,720
Other assets[3]	**114,745**		**489,639**		122,927		482,153	

Encumbered assets/collateral received and associated liabilities

	2016 Matching liabilities, contingent liabilities or securities lent £m	2016 Assets, collateral received and own debt securities issued other than covered bonds and ABSs encumbered £m	2015 Matching liabilities, contingent liabilities or securities lent £m	2015 Assets, collateral received and own debt securities issued other than covered bonds and ABSs encumbered £m
Carrying amount of selected financial liabilities[1]	**133,703**	**132,204**	131,680	150,534

[1] The reported values represent the median of the values reported to the regulator via supervisory returns over the period 31 December 2015 to 31 December 2016.

[2] Includes debt securities accounted for as trading and other financial assets at fair value through profit or loss, loans and receivables and AFS financial assets.

[3] All remaining regulatory balance sheet assets.

In accordance with the threshold criteria under PRA supervisory statement SS11/14 (CRD IV: Compliance with the EBA's Guidelines on the disclosure of encumbered and unencumbered assets) the Group is not required to report on the fair value of encumbered and unencumbered collateral received.

Monitoring and measurement of asset encumbrance

The Board and Group Asset & Liability Committee monitor and manage total balance sheet encumbrance via a number of risk appetite metrics. The amount of encumbered assets has been broadly stable over 2016. The vast majority of assets encumbered are in the UK banking entities, with the Group primarily encumbering mortgages, unsecured lending and credit card receivables through the issuance programmes (covered bonds and securitisation) and tradable securities through securities financing activity (repo and stock lending). The encumbered assets/collateral received and associated liabilities section demonstrates that in some transactions (i.e. covered bonds and securitisations) the Group will encumber assets in excess of the matching liabilities to provide greater security for investors. The Group also assesses what unencumbered assets are available to encumber and meet any future possible funding requirements, further details are included on pages 157 and 158 of the 2016 Lloyds Banking Group plc Annual Report and Accounts.

The Group provides collateralised security financing services to its clients, providing them with cash financing or specific securities. Collateralised security financing is also used to manage the Group's own short-term cash and collateral needs. For securities accepted as collateral, mandates are credit rating driven with appropriate notional limits per rating, asset and individual bond concentration. The vast majority of collateral the Group uses in repo/reverse repo and stock lending/stock borrowing transactions is investment grade government issued, primarily UK Government debt. The majority of repo/reverse repo and stock lending/stock borrowing transactions are short-term, having a residual maturity of less than three months.

Appendix 3: Lloyds Bank Group

OWN FUNDS DISCLOSURE TEMPLATE

Table 81: Lloyds Bank Group own funds template

	Transitional rules		Fully loaded rules	
	At 31 Dec 2016 £m	At 31 Dec 2015[1] £m	**At 31 Dec 2016 £m**	At 31 Dec 2015[1] £m
Common equity tier 1 (CET1) capital: instruments and reserves				
Capital instruments and related share premium accounts	**1,574**	37,107	**1,574**	37,107
of which: called up share capital	**1,574**	1,574	**1,574**	1,574
of which: share premium	**–**	35,533	**–**	35,533
Retained earnings[1]	**39,758**	6,109	**39,758**	6,109
Accumulated other comprehensive income and other reserves (including unrealised gains and losses)	**5,868**	4,325	**5,868**	4,325
Foreseeable dividend	**(1,568)**	(1,427)	**(1,568)**	(1,427)
Common equity tier 1 (CET1) capital before regulatory adjustments	**45,632**	46,114	**45,632**	46,114
Common equity tier 1 (CET1) capital: regulatory adjustments				
Additional value adjustments	**(630)**	(372)	**(630)**	(372)
Intangible assets (net of related tax liability)	**(1,623)**	(1,719)	**(1,623)**	(1,719)
Deferred tax assets that rely on future profitability, excluding those arising from temporary differences (net of related tax liability where the conditions in Article 38 (3) of the CRR are met)	**(3,536)**	(3,911)	**(3,536)**	(3,911)
Fair value reserves related to gains or losses on cash flow hedges	**(2,224)**	(915)	**(2,224)**	(915)
Negative amounts resulting from the calculation of expected loss amounts	**(602)**	(270)	**(602)**	(270)
Gains or losses on liabilities valued at fair value resulting from changes in own credit standing	**(3)**	5	**(3)**	5
Defined benefit pension fund assets	**(267)**	(721)	**(267)**	(721)
Direct, indirect and synthetic holdings by the Group of the CET1 instruments of financial sector entities where the Group has a significant investment in those entities (amount above 10% threshold and net of eligible short positions)[1]	**(3,986)**	(4,001)	**(3,986)**	(4,001)
Exposure amount of the following items which qualify for a risk weight of 1,250%, where the Group has opted for the deduction alternative	**(217)**	(169)	**(217)**	(169)
of which: securitisation positions	**(217)**	(169)	**(217)**	(169)
Total regulatory adjustments applied to common equity tier 1 (CET1)	**(13,088)**	(12,073)	**(13,088)**	(12,073)
Common equity tier 1 (CET1) capital	**32,544**	34,041	**32,544**	34,041
Additional tier 1 (AT1) capital: instruments				
Capital instruments and related share premium accounts	**3,182**	–	**3,182**	–
of which: classified as equity under applicable accounting standards	**3,182**	–	**3,182**	–
Amount of qualifying items referred to in Article 484 (4) of the CRR and the related share premium accounts subject to phase out from AT1	**2,380**	3,483	**–**	–
Qualifying Tier 1 capital included in consolidated AT1 capital (including minority interests not included in CET1) issued by subsidiaries and held by third parties	**1,499**	1,278	**–**	–
of which: instruments issued by subsidiaries subject to phase out	**1,499**	1,278	**–**	–
Additional tier 1 (AT1) capital before regulatory adjustments	**7,061**	4,761	**3,182**	–
Additional tier 1 (AT1) capital: regulatory adjustments				
Residual amounts deducted from AT1 capital with regard to deduction from Tier 2 capital during the transitional period pursuant to Article 475 of the CRR	**(1,329)**	(1,177)	**–**	–
of which: significant investments in Tier 2 instruments of other financial sector entities	**(1,329)**	(1,177)	**–**	–
Total regulatory adjustments applied to additional tier 1 (AT1) capital	**(1,329)**	(1,177)	**–**	–
Additional tier 1 (AT1) capital	**5,732**	3,584	**3,182**	–
Tier 1 capital	**38,276**	37,625	**35,726**	34,041

	Transitional rules		Fully loaded rules	
	At 31 Dec 2016 £m	At 31 Dec 2015[1] £m	**At 31 Dec 2016 £m**	At 31 Dec 2015[1] £m
Tier 2 (T2) capital: Instruments and provisions				
Capital instruments and related share premium accounts	**5,880**	9,410	**5,880**	11,057
Amount of qualifying items referred to in Article 484 (5) of the CRR and the related share premium accounts subject to phase out from T2	**685**	1,368	**–**	–
Qualifying own funds instruments included in consolidated T2 capital (including minority interests and AT1 instruments not included in CET1 or AT1) issued by subsidiaries and held by third parties	**2,355**	2,784	**495**	706
of which: instruments issued by subsidiaries subject to phase out	**1,860**	1,978	**–**	–
Credit risk adjustments	**186**	221	**186**	221
Tier 2 (T2) capital before regulatory adjustments	**9,106**	13,783	**6,561**	11,984
Tier (T2) capital: regulatory adjustments				
Direct and indirect holdings by the Group of the T2 instruments and subordinated loans of financial sector entities where the Group has a significant investment in those entities (net of eligible short positions)	**(1,571)**	(1,756)	**(2,900)**	(2,933)
Total regulatory adjustments applied to tier 2 (T2) capital	**(1,571)**	(1,756)	**(2,900)**	(2,933)
Tier 2 (T2) capital	**7,535**	12,027	**3,661**	9,051
Total capital	**45,811**	49,652	**39,387**	43,092
Total risk-weighted assets	**216,183**	224,020	**216,183**	224,020
Capital ratios and buffers				
Common Equity Tier 1 (as a percentage of risk exposure amount)	**15.1%**	15.2%	**15.1%**	15.2%
Tier 1 (as a percentage of risk exposure amount)	**17.7%**	16.8%	**16.5%**	15.2%
Total capital (as a percentage of risk exposure amount)	**21.2%**	22.2%	**18.2%**	19.2%
Institution specific buffer requirement (CET1 requirement in accordance with article 92 (1) (a) plus capital conservation and countercyclical buffer requirements, plus systemic risk buffer, plus the systemically important institution buffer (G-SII or O-SII buffer), expressed as a percentage of risk exposure amount)	**0.627%**	0.001%	**0.627%**	0.001%
of which: capital conservation buffer requirement[2]	**0.625%**	-	**0.625%**	-
of which: countercyclical buffer requirement	**0.002%**	0.001%	**0.002%**	0.001%
Common Equity Tier 1 available to meet buffers (as a percentage of risk exposure amount)[3]	**10.6%**	10.7%	**10.6%**	10.7%
Amounts below the threshold for deduction (before risk weighting)				
Direct and indirect holdings of the capital of financial sector entities where the Group does not have a significant investment in those entities (amount below 10% threshold and net of eligible short positions)	**1,040**	1,552	**1,040**	1,552
Direct and indirect holdings by the Group of the CET1 instruments of financial sector entities where the Group has a significant investment in those entities (amount below 10% threshold and net of eligible short positions)	**3,653**	3,626	**3,653**	3,626
Deferred tax assets arising from temporary differences (amount below 10% threshold, net of related tax liability where the conditions in 38 (3) of the CRR are met)	**947**	1,159	**947**	1,159
Applicable caps on the inclusion of provisions in Tier 2				
Credit risk adjustments included in T2 in respect of exposures subject to internal ratings-based approach (prior to the application of the cap)	**186**	221	**186**	221
Cap on inclusion of credit risk adjustments in T2 under internal ratings-based approach	**932**	953	**932**	953
Capital instruments subject to phase-out arrangements (only applicable between 1 Jan 2013 and 1 Jan 2022)				
Current cap on AT1 instruments subject to phase out arrangements	**4,081**	4,761	**–**	–
Amount excluded from AT1 due to cap (excess over cap after redemptions and maturities)	**–**	692	**–**	–
Current cap on T2 instruments subject to phase out arrangements	**3,974**	4,636	**–**	–

[1] The presentation of the deconsolidation of the Group's insurance entities has been amended with comparative figures restated accordingly.

[2] The capital conservation buffer requirement is the percentage applicable at the reporting date. This will increase to 2.5 per cent by 2019.

[3] Excluding CET1 required to meet Pillar 2A requirements.

Appendix 3: Lloyds Bank Group continued

OWN FUNDS RECONCILIATION

The following table presents certain items from the Lloyds Bank Group consolidated balance sheet on an accounting consolidation basis for the year ended 31 December 2016, that are used to calculate own funds. Where necessary, the balance sheet components have been expanded such that the components of the transitional own funds disclosure template appear separately.

Table 82: Lloyds Bank Group items extracted from the consolidated balance sheet on an accounting consolidation basis and reconciliation of own funds items to audited financial statements

			Adjustments							
Balance sheet category	Own funds description	Items extracted from the consolidated accounting balance sheet[1] £m	Deconsolidation and other adjustments[2]	Deferred tax £m	Threshold adjustments £m	Non-eligible instruments £m	Amounts excluded from AT1 due to Cap £m	Regulatory and other adjustments £m	Transitional own funds £m	Notes
	Common Equity Tier 1 (CET1) capital: instruments and reserves									
	Capital instruments and related share premium accounts	1,574	–	–	–	–	–	–	1,574	
Share capital	of which: called up share capital	1,574	–	–	–	–	–	–	1,574	
Retained profits	Retained earnings	36,231	3,541	–	–	–	–	(14)	39,758	3
Other reserves	Accumulated other comprehensive income and other reserves (including unrealised gains and losses)	8,484	(2,621)	–	–	–	–	5	5,868	3
	Common equity tier 1 (CET1) capital: regulatory adjustments									
	Additional value adjustments	–	–	–	–	–	–	(630)	(630)	4
Goodwill and other intangible assets	Intangible assets (net of related tax liability)	(1,700)	–	91	–	–	–	(14)	(1,623)	5
Deferred tax assets	Deferred tax assets that rely on future profitability, excluding those arising from temporary differences (net of related tax liability where conditions in Article 38(3) of the CRR are met	(3,603)	–	(881)	947	–	–	1	(3,536)	6
	Fair value reserves related to gains or losses on cash flow hedges	–	–	–	–	–	–	(2,224)	(2,224)	7
	Negative amounts resulting from the calculation of expected loss amounts	–	–	–	–	–	–	(602)	(602)	8
	Gains or losses on liabilities valued at fair value resulting from changes in own credit standing	–	–	–	–	–	–	(3)	(3)	9
Retirement benefit assets	Defined benefit pension fund assets	(342)	–	75	–	–	–	–	(267)	6
Investment in group undertakings	Direct and indirect holdings by the Group of CET1 instruments in financial sector entities where the Group has a significant investment in those entities (amounts above 10% threshold and net of eligible short positions)	–	(7,999)	–	3,653	–	–	360	(3,986)	10
	Exposures amount of the following items which qualify for a risk weight of 1,250%, where the Group has opted for the deduction alternative (securitisation positions)	–	–	–	–	–	–	(217)	(217)	11
	Foreseeable dividend	–	–	–	–	–	–	(1,568)	(1,568)	12
	Common Equity Tier 1 (CET1) capital	**40,644**	**(7,079)**	**(715)**	**4,600**	**–**	**–**	**(4,906)**	**32,544**	
	Additional Tier 1 (AT1) capital: instruments									
Other equity instruments	Capital instruments and the related share premium accounts	3,217	–	–	–	–	–	(35)	3,182	
Subordinated liabilities	Amount of qualifying items referred to in Article 484 (4) of the CRR and the related share premium accounts subject to phase out from AT1	3,091	–	–	–	(600)	–	(111)	2,380	13
Subordinated liabilities	Qualifying Tier 1 capital included in consolidated AT1 capital (including minority interests not included in CET1) issued by subsidiaries and held by third parties	1,656	–	–	–	(149)	–	(8)	1,499	13
	Additional Tier 1 (AT1) capital: regulatory adjustments									
Trading and other financial assets at fair value through profit or loss	Residual amounts deducted from AT1 capital with regard to deduction from T2 capital during the transitional period pursuant to Article 475 of the CRR: (significant investments)	(51,198)	49,792	–	–	–	–	77	(1,329)	14
	Additional Tier 1 (AT1) capital	**(43,234)**	**49,792**	**–**	**–**	**(749)**	**–**	**(77)**	**5,732**	
	Tier 1 capital	**(2,590)**	**42,713**	**(715)**	**4,600**	**(749)**	**–**	**(4,983)**	**38,276**	
	Tier 2 (T2) capital: instruments and provisions									
Subordinated liabilities	Capital instruments and related share premium accounts	6,729	–	–	–	–	–	(849)	5,880	13
Subordinated liabilities	Capital instruments and related share premium accounts	696	–	–	–	–	–	(11)	685	13
Subordinated liabilities	Qualifying own funds instruments included in consolidated T2 capital (including minority interests and AT1 instruments not included in CET1 or AT1) issued by subsidiaries and held by third parties	5,086	–	–	–	(68)	–	(2,663)	2,355	13
	Credit risk adjustments	–	–	–	–	–	–	186	186	15
	Tier 2 (T2) capital: regulatory adjustments									
Loans and receivables	Direct and indirect holdings by the Group of the T2 instruments and subordinated loans of financial sector entities where the Group has a significant investment in those entities (net of eligible short positions)	(3,397)	2,819	–	–	–	–	–	(578)	
Trading and other financial assets at fair value through profit or loss	Direct and indirect holdings by the Group of the T2 instruments and subordinated loans of financial sector entities where the Group has a significant investment in those entities (net of eligible short positions)	–	–	–	–	–	–	(993)	(993)	14
	Tier 2 (T2) capital	**9,114**	**2,819**	**–**	**–**	**(68)**	**–**	**(4,330)**	**7,535**	
	Total capital	**6,524**	**45,532**	**(715)**	**4,600**	**(817)**	**–**	**(9,313)**	**45,811**	

1. Assets extracted from the consolidated accounting balance sheet are presented as negative amounts, liabilities and equity are presented as positive amounts.
2. Deconsolidation and other adjustments primarily represent the removal of balances related to entities outside the regulatory scope of consolidation and the removal of assets subject to capital requirement rules.
3. The regulatory definition of eligible items for inclusion in retained earnings differs from the statutory reporting definition. The aggregate of retained earnings and accumulated other comprehensive income and other reserves is comparable on both bases but the allocation between categories differs.
4. The additional value adjustments of £630m reflect the prudent valuation adjustment for all assets measured at fair value in accordance with Articles 34 and 105 of the CRR.
5. Own funds intangible assets of £1,700m extracted from the consolidated accounting balance sheet representing £180m of goodwill and £1,520m of other intangible assets are net of the amount of associated deferred tax liabilities as required by CRD IV rules.
6. The own funds deduction of £3,536m for deferred tax excludes the deferred tax balances relating to intangible assets, cash flow hedge and the defined benefit pension fund asset. Additionally, only the deferred tax amounts that rely on future profitability are required to be deducted from CET1, and may be reduced by associated deferred tax liabilities where conditions specified in Article 38 of CRR are met. £947m of the deferred tax asset relating to temporary differences may be risk weighted instead of deducted from capital as presented in the threshold adjustments column.
7. Cash flow hedge reserve forms part of other reserves in the consolidated regulatory balance sheet.
8. In accordance with Articles 36, 62, 158 and 159 of the CRR the excess of expected losses over specific credit risk adjustments (SCRAs) and additional value adjustments of £602m are deducted from CET1.
9. CRD IV requires the removal of the impact of any gains or losses recorded on liabilities held at fair value through profit or loss or derivative liabilities due to changes in the credit spreads of Lloyds Bank plc.
10. The investment in group undertakings of £7,999m pre threshold and other adjustments represents the Group's total equity investment in Insurance subsidiaries as well as joint ventures and associates. The majority of the investment relates to the Group's investment in its Insurance operations headed by Scottish Widows Group. The own funds deduction of £3,986m reflects the regulatory requirement to deduct a portion of Lloyds Bank Group's significant investments from CET1, above certain thresholds. In accordance with the CRD IV rules the cost of Lloyds Bank Group's investment in the equity of the Insurance business is risk-weighted up to a limit based on the size of Lloyds Bank Group's CET1 capital with the remainder deducted from CET1.
11. The £217m deduction for securitisation positions reflects those positions that were rated below BB- or that are unrated.
12. The £1,568m foreseeable dividend is that recommended by the Board of Directors in respect of 2016 earnings.
13. A reconciliation of subordinated liabilities from the Lloyds Bank Group consolidated balance sheet to the amount recognised against each own funds description is presented in the table below.

Own funds description	Consolidated accounting balance sheet total £m
Amount of qualifying items referred to in Article 484 (4) of the CRR and the related share premium accounts subject to phase out from AT1	**3,091**
Qualifying Tier 1 capital included in consolidated AT1 capital (including minority interests not included in CET1) issued by subsidiaries and held by third parties	**1,656**
Capital instruments and related share premium accounts	**6,729**
Amount of qualifying items referred to in Article 484 (5) of the CRR and the related share premium accounts subject to phase out from T2	**696**
Qualifying own funds instruments included in consolidated T2 capital (including minority interests and AT1 instruments not included in CET1 or AT1) issued by subsidiaries and held by third parties	**5,086**
Total subordinated liabilities as presented on the Lloyds Bank Group consolidated balance sheet	**17,258**

Adjustments required by regulatory rules to the value of subordinated liabilities presented within the regulatory and other adjustments column on the reconciliation include adjustments for accrued interest, amortisation and associated derivatives.

The non-eligible instruments column on the reconciliation represents instruments on the balance sheet that are not eligible for inclusion in regulatory capital.

Additional Tier 1 instruments presented in own funds reflect instruments issued by either Lloyds Bank Group plc or its subsidiaries and held by third parties that qualified as Tier 1 under regulation that preceded CRD IV, subject to certain restrictions, including a cap set at 60% of the value of such instruments that were in issue at 31 December 2012 and net of interest. Any excess over the cap is included in Tier 2 instruments which have been issued in the same manner as Additional Tier 1 instruments and are net of interest and in some instances amortisation and associated derivatives.

14. The £51,198m extracted from the consolidated accounting balance sheet is adjusted for deconsolidation and other adjustments, primarily to remove balances to entities outside the regulatory scope of consolidation. The remaining balance represents the Group's investment in the subordinated debt of Scottish Widows. The Group's full investment in the subordinated debt of Scottish Widows is deducted from capital across AT1 and T2 in accordance with the transitional CRD IV rules. For 2016, 40% of the total investment is deducted equally from AT1 and T2, with the remainder deducted directly from AT1 or T2 in line with the classification of the underlying debt instrument.
15. Credit risk adjustments of £186m reflect the surplus provisions resulting from the calculation of excess expected loss amounts in accordance with Articles 158 and 159 of the CRR, subject to certain limits.

Appendix 3: Lloyds Bank Group continued

LEVERAGE DISCLOSURE TEMPLATE

Table 83: Lloyds Bank Group leverage ratio common disclosure

	At 31 Dec 2016 Fully loaded £m	At 31 Dec 2015[2] Fully loaded £m
On-balance sheet exposures (excluding derivatives and SFTs)		
On-balance sheet items (excluding derivatives, SFTs and fiduciary assets, but including collateral)	**599,273**	622,513
Asset amounts deducted in determining Tier 1 capital	**(9,187)**	(9,338)
Total on-balance sheet exposures (excluding derivatives, SFTs and fiduciary assets)	**590,086**	613,175
Derivative exposures		
Replacement cost associated with all derivatives transactions (ie net of eligible cash variation margin)	**7,863**	5,846
Add-on amounts for PFE associated with all derivatives transactions (mark-to-market method)	**13,188**	12,678
Gross-up for derivatives collateral provided where deducted from the balance sheet assets pursuant to the applicable accounting framework	**1,636**	2,371
Deductions of receivables assets for cash variation margin provided in derivatives transactions	**(4,686)**	(3,689)
Adjusted effective notional amount of written credit derivatives	**1,088**	813
Adjusted effective notional offsets and add-on deductions for written credit derivatives	**(389)**	(131)
Total derivative exposures	**18,700**	17,888
Securities financing transaction exposures		
Gross SFT assets (with no recognition of netting), after adjusting for sales accounting transactions	**44,617**	39,604
Netted amounts of cash payables and cash receivables of gross SFT assets	**(3,858)**	(5,909)
Counterparty credit risk exposure for SFT assets	**1,677**	3,361
Total securities financing transaction exposures	**42,436**	37,056
Other off-balance sheet exposures		
Off-balance sheet exposures at gross notional amount	**129,214**	129,491
Adjustments for conversion to credit equivalent amounts	**(70,529)**	(73,067)
Other off-balance sheet exposures	**58,685**	56,424
Exempted exposures in accordance with CRR Article 429 (7) (on and off balance sheet)		
Intragroup exposures exempted in accordance with Article 429(7) of Regulation (EU) No 575/2013 (on and off balance sheet)[1]	**(3,218)**	(11,639)
Capital and total exposure measure		
Tier 1 capital	**35,726**	34,041
Leverage ratio total exposure measure	**706,689**	712,904
Leverage ratio		
Leverage ratio	**5.1%**	4.8%

[1] Relates to exempted intragroup loans and receivables.

[2] Prior year comparatives have been restated to reflect the revised treatment of certain preference shares issued to the parent company, Lloyds Banking Group plc. Further details are available through the 2016 Lloyds Bank plc Annual Report and Accounts, Note 1 'Basis of preparation'.

Table 84: Lloyds Bank Group summary reconciliation of accounting assets and leverage ratio exposures

	At 31 Dec 2016 Fully loaded £m	At 31 Dec 2015[1] Fully loaded £m
Total assets as per the financial statements	**830,927**	818,489
Adjustment for entities which are consolidated for accounting purposes but are outside the scope of regulatory consolidation	**(155,522)**	(134,869)
Adjustments for derivative financial instruments	**(15,035)**	(9,524)
Adjustments for securities financing transactions (SFTs)	**39**	3,361
Adjustment for off-balance sheet items (ie conversion to credit equivalent amounts of off-balance sheet exposures)	**58,685**	56,424
Adjustment for intragroup exposures excluded from the leverage ratio total exposure measure in accordance with Article 429 (7) of Regulation (EU) No 575/2013	**(3,218)**	(11,639)
Other adjustments	**(9,187)**	(9,338)
Leverage ratio total exposure measure	**706,689**	712,904

[1] Prior year comparatives have been restated to reflect the revised treatment of certain preference shares issued to the parent company, Lloyds Banking Group plc. Further details are available through the 2016 Lloyds Bank plc Annual Report and Accounts, Note 1 'Basis of preparation'.

Table 85: Lloyds Bank Group geographical distribution of credit exposures relevant for the calculation of the countercyclical capital buffer

	2016 General credit exposures[2,3]		2016 Trading book exposures[2,4]		2016 Securitisation exposures[3]		2016 Own funds requirements					
Breakdown by Country	Exposure Value for STA £m	Exposure Value for IRB £m	Sum of long and short positions of trading book exposures for STA £m	Value of trading book exposures for internal models £m	Exposure Value for STA £m	Exposure Value for IRB £m	of which: General credit exposures[2,3] £m	of which: Trading book exposures[2,4] £m	of which: Securitisation exposures[3] £m	Total £m	2016 Own funds requirement weights %	2016 Countercyclical capital buffer rate %
Norway	10	308	–	–	–	–	12	–	–	12	0.09%	1.500%
Sweden	48	65	–	–	–	–	5	–	–	5	0.04%	1.500%
Hong Kong	234	28	–	–	–	–	10	–	–	10	0.08%	0.625%
i) Total[1]	292	401	–	–	–	–	27	–	–	27	0.21%	
United Kingdom	22,319	485,137	134	90	1,184	18,505	11,244	16	250	11,510	84.14%	n/a
United States of America	2,442	12,828	–	–	–	6,743	639	–	57	696	5.09%	n/a
Ireland	1,133	4,609	–	–	–	24	402	–	4	406	2.97%	n/a
Netherlands	740	6,771	–	–	–	20	187	–	–	187	1.37%	n/a
ii) Total[1]	26,634	509,345	134	90	1,184	25,292	12,472	16	311	12,799	93.57%	
iii) Rest of the World[1]	3,408	15,985	–	–	–	1,117	838	–	16	854	6.22%	
Total	30,334	525,731	134	90	1,184	26,409	13,337	16	327	13,680	100.00%	

Amount of institution specific countercyclical capital buffer	**2016**	2015
Total risk exposure amount	**£216,183m**	£224,020m
Institution specific countercyclical buffer rate	**0.002%**	0.001%
Institution specific countercyclical buffer requirement	**£5.0m**	£2.7m

[1] The breakdown by country is disclosed on the following basis:
i) those countries for which a countercyclical capital buffer rate has been set.
ii) those countries for which a countercyclical capital buffer rate has not been set and have an own funds requirement weighting of greater than or equal to one per cent, the threshold having been determined by the Group in accordance with the EBA guidelines on materiality for Pillar 3.
iii) the aggregate of all remaining countries for which a countercyclical buffer rate has not been set and individually have an own funds requirement weighting of less than one per cent.

[2] For the purposes of the calculation of the countercyclical capital buffer, general credit risk and trading book exposures exclude exposures to central governments, central banks, regional governments, local authorities, public sector entities, multilateral development banks, international organisations and institutions. In addition, trading book exposures are limited to those that are subject to the own funds requirement for specific risk or incremental default and migration risk.

[3] General credit and securitisation exposures include counterparty credit risk and are stated on a post CRM basis.

[4] Trading book exposures are allocated in full to the United Kingdom in accordance with the threshold criteria set out under the EBA Regulatory Technical Standard on the identification of the geographical location of the relevant credit exposures for the calculation of the countercyclical capital buffer.

Appendix 3: Lloyds Bank Group continued

CAPITAL REQUIREMENTS

LLOYDS BANK GROUP RISK-WEIGHTED ASSETS AND PILLAR 1 CAPITAL REQUIREMENTS

The risk-weighted assets and Pillar 1 capital requirements of Lloyds Bank Group as at 31 December 2016 are £216,183m (2015: £224,020m) and £17,295m (2015: £17,922m) respectively.

Table 86: Lloyds Bank Group overview of risk-weighted assets (OV1)

		2016 RWA £m	2015 RWA £m	2016 Minimum capital Requirements £m	2015 Minimum capital Requirements £m
1	**Credit risk (excluding counterparty credit risk)**	162,650	168,740	13,012	13,499
2	Of which standardised approach	18,688	20,443	1,495	1,635
3	Of which the foundation rating-based (FIRB) approach	51,438	54,596	4,115	4,368
4	Of which the retail IRB (RIRB) approach	64,970	63,912	5,198	5,113
	Of which corporates – specialised lending	13,469	14,394	1,077	1,152
	Of which non-credit obligation assets	6,427	5,502	514	440
5	Of which equity IRB under the simple risk -weight or the internal models approach	7,658	9,893	613	791
6	**Counterparty credit risk**	9,623	10,153	770	813
7	Of which marked to market	7,552	7,261	604	581
8	Of which original exposure	–	–	–	–
9	Of which the standardised approach	–	–	–	–
10	Of which internal ratings-based model method (IMM)	–	–	–	–
	Of which comprehensive approach for credit risk mitigation (for SFTs)	712	576	57	46
	Of which exposures to central counterparties (including trades, default fund contributions and initial margin)	495	632	40	51
12	Of which credit valuation adjustment (CVA)	864	1,684	69	135
13	**Settlement risk**	–	–	–	–
14	**Securitisation exposures in banking book**[1]	3,971	3,266	318	261
15	Of which IRB ratings-based approach (RBA)	2,878	2,379	231	190
16	Of which IRB supervisory formula approach (SFA)	–	–	–	–
17	Of which internal assessment approach (IAA)	825	887	66	71
18	Of which standardised approach	268	–	21	–
19	**Market risk**	3,147	3,775	252	302
20	Of which standardised approach	352	551	28	44
21	Of which internal model approaches	2,795	3,224	224	258
22	Large exposures	–	–	–	–
23	**Operational risk**	25,292	26,123	2,023	2,090
24	Of which basic indicator approach	–	–	–	–
25	Of which standardised approach	25,292	26,123	2,023	2,090
26	Of which advanced measurement approach	–	–	–	–
27	Amounts below the thresholds for deduction (subject to 250% risk weight)	11,500	11,963	920	957
28	Floor adjustment	–	–	–	–
29	**Total – transitional**	**216,183**	224,020	**17,295**	17,922

[1] Securitisations are shown separately within this table, however, are included within credit risk throughout the remainder of the disclosures.

ANALYSIS OF CREDIT RISK MITIGATION

The following table provides an analysis of credit risk exposures covered by eligible financial collateral, other eligible collateral, guarantees or credit derivatives.

The analysis excludes exposures covered by forms of credit risk mitigation that are not taken into consideration in the calculation of credit risk capital requirements.

Table 87: Lloyds Bank Group eligible financial collateral and other eligible collateral

	2016 Exposures covered by eligible financial collateral £m	2016 Exposures covered by other eligible collateral £m	2016 Total £m	2015 Exposures covered by eligible financial collateral £m	2015 Exposures covered by other eligible collateral £m	2015 Total £m
Exposures subject to the IRB approach						
Foundation IRB approach						
Corporate – main	1,225	8,970	10,195	1,244	8,698	9,942
Corporate – SME	8	7,363	7,371	9	7,422	7,431
Institutions	902	–	902	536	–	536
Other IRB approach						
Corporate – specialised lending	845	–	845	837	–	837
Total – IRB approach	2,980	16,333	19,313	2,626	16,120	18,746
Exposures subject to the standardised approach						
Corporates	855	5	860	937	4	941
Institutions	47	–	47	62	–	62
Exposures in default	–	6	6	–	10	10
Total – standardised approach	902	11	913	999	14	1,013
Total	3,882	16,344	20,226	3,625	16,134	19,759

Unfunded credit protection: Guarantees and credit derivatives

Protection provider	2016 Credit protection provided in the form of guarantees £m	2016 Credit protection provided in the form of credit derivatives £m	2016 Total £m	2015 Credit protection provided in the form of guarantees £m	2015 Credit protection provided in the form of credit derivatives £m	2015 Total £m
Exposures subject to the IRB approach						
Corporates	352	–	352	220	–	220
Central governments and central banks	–	–	–	–	–	–
Institutions	24	143	167	–	34	34
Total – IRB approach	376	143	519	220	34	254
Exposures subject to the standardised approach						
Corporates[1]	218	–	218	–	–	–
Central governments and central banks	280	–	280	90	–	90
Total – standardised approach	498	–	498	90	–	90
Total	874	143	1,017	310	34	344

[1] 2015 restated to exclude credit protection relevant to CCR exposures only.

Appendix 3: Lloyds Bank Group continued

ANALYSIS OF PAST DUE AND IMPAIRED LOANS AND ADVANCES TO CUSTOMERS

The analysis provided within this section has been presented on an accounting consolidation basis rather than a regulatory consolidation basis.

Analysis by industry

An analysis of past due but not impaired loans and advances to customers and impaired loans and advances to customers as at 31 December 2016, by major industrial sector, is provided in the table below.

Table 88: Lloyds Bank Group past due but not impaired and impaired loans and advances analysed by major industrial sector

	Past due but not impaired 2016		Impaired 2016		Past due but not impaired 2015		Impaired 2015	
	£m	As a % of credit risk exposure	£m	As a % of credit risk exposure	£m	As a % of credit risk exposure	£m	As a % of credit risk exposure
Agriculture, forestry and fishing	78	1.33%	141	2.41%	97	1.30%	123	1.65%
Energy and water supply	1	0.02%	4	0.08%	2	0.04%	134	2.35%
Manufacturing	17	0.10%	293	1.78%	31	0.20%	122	0.78%
Construction	22	0.45%	334	6.85%	39	0.84%	283	6.07%
Transport, distribution and hotels	93	0.42%	342	1.56%	131	0.59%	511	2.31%
Postal and communications	3	0.11%	5	0.18%	1	0.02%	296	6.49%
Property companies	81	0.25%	1,284	3.92%	189	0.57%	2,065	6.26%
Financial, business and other services	92	0.05%	784	0.44%	62	0.03%	985	0.51%
Personal: mortgages	7,340	2.21%	4,320	1.30%	8,233	2.43%	4,001	1.18%
Personal: other	201	0.43%	801	1.71%	227	0.48%	980	2.09%
Lease financing	–	–	–	–	–	–	13	0.38%
Hire purchase	103	0.90%	187	1.63%	77	0.82%	77	0.82%
Total	8,031	1.19%	8,495	1.26%	9,089	1.30%	9,590	1.37%

Analysis by geography

An analysis of past due but not impaired loans and advances to customers and impaired loans and advances to customers as at 31 December 2016, by geographical region, based on the country of residence of the customer, is provided in the table below.

Table 89: Lloyds Bank Group past due but not impaired and impaired loans and advances analysed by geographical region

	Past due but not impaired 2016		Impaired 2016		Past due but not impaired 2015		Impaired 2015	
	£m	As a % of credit risk exposure	£m	As a % of credit risk exposure	£m	As a % of credit risk exposure	£m	As a % of credit risk exposure
United Kingdom	7,641	1.33%	8,019	1.39%	8,761	1.46%	9,021	1.50%
Rest of Europe	389	0.97%	314	0.78%	299	0.73%	303	0.74%
United States of America	1	–	95	0.25%	–	–	108	0.30%
Asia-Pacific	–	–	13	0.65%	28	1.40%	93	4.63%
Other	–	–	54	0.95%	1	0.02%	65	1.25%
Total	8,031	1.19%	8,495	1.26%	9,089	1.30%	9,590	1.37%

ANALYSIS OF SPECIFIC CREDIT RISK ADJUSTMENTS IN RESPECT OF LOANS AND ADVANCES TO CUSTOMERS

The analysis provided within this section has been presented on an accounting consolidation basis rather than a regulatory consolidation basis.

The movement in impairment provisions, from 1 January 2016 to 31 December 2016, in respect of loans and advances to customers is provided below.

Table 90: Lloyds Bank Group movement in impairment provisions (loans and advances to customers)

	2016 £m	2015 £m
At 1 January	3,033	6,414
Exchange and other adjustments	69	(246)
Disposal of businesses	–	(82)
Advances written off	(2,111)	(4,204)
Recoveries of advances written off in previous years	861	764
Unwinding of discount	(32)	(56)
Charge (release) to the income statement	592	443
At 31 December	2,412	3,033

Table 91: Lloyds Bank Group movement in acquisition related fair value adjustments (loans and advances to customers)

	2016 £m	2015 £m
At 1 January	276	393
Fair value unwind[1]:		
in respect of impairment losses	(68)	(95)
other, including market liquidity	(31)	(22)
At 31 December	177	276

[1] The fair value adjustments relating to loans and advances were those required to reflect the HBOS assets in the Group's consolidated financial records at their fair value and took into account both the ELs and market liquidity at the date of acquisition. The unwind relating to future impairment losses requires significant management judgement to determine its timing which includes an assessment of whether the losses incurred in the current period were expected at the date of acquisition and assessing whether the remaining losses expected at the date of acquisition will still be incurred. The element related to market liquidity unwinds to the income statement over the estimated expected lives of the related assets although if an asset is written-off or suffers previously unexpected impairment then this element of the fair value will no longer be considered a timing difference (liquidity) but permanent (impairment). The fair value unwind in respect of impairment losses incurred for loans and advances to customers within portfolios applying the IRB Approach was £68m for the period ended 31 December 2016.

Analysis by industry

An analysis of closing impairment provisions, the net charge to the income statement and acquisition related fair value adjustments in respect of loans and advances to customers, by major industrial sector, is provided in the table below.

Table 92: Lloyds Bank Group Impairment provisions, net charge and acquisition related fair value adjustments analysed by major industrial sector

	2016 Impairment provisions[1] £m	2016 Net charge[1] £m	2016 Acquisition related fair value adjustments[2] £m	2015 Impairment provisions[1] £m	2015 Net charge[1] £m	2015 Acquisition related fair value adjustments[2] £m
Agriculture, forestry and fishing	13	3	–	15	1	–
Energy and water supply	6	(4)	–	20	35	–
Manufacturing	84	(48)	–	70	27	–
Construction	319	143	–	165	15	–
Transport, distribution and hotels	161	(35)	–	219	(77)	–
Postal and communications	5	191	–	4	(2)	–
Property companies	470	(166)	–	790	(91)	–
Financial, business and other services	312	6	–	811	96	–
Personal: mortgages	1,695	47	177	1,618	134	276
Personal: other	356	433	–	388	429	–
Lease financing	–	15	–	–	31	–
Hire purchase	110	72	–	72	23	–
	3,531	657	177	4,172	621	276
Fair value and other adjustments	(1,119)	(65)		(1,139)	(178)	
Total	2,412	592	177	3,033	443	276

[1] Analysis of closing impairment provisions and the net charge to the income statement in respect of loans and advances to customers, by major industrial sector, has been presented prior to the application of fair value and other adjustments.

[2] The acquisition related fair value adjustments represent SCRAs recognised in the calculation of EEL amounts for exposures subject to the IRB Approach (as presented in Table 91 above).

Appendix 3: Lloyds Bank Group continued

Analysis by geography

An analysis of closing impairment provisions, the net charge to the income statement and acquisition related fair value adjustments in respect of loans and advances to customers, by geographical region, based on the country of residence of the customer, is provided in the table below.

Table 93: Lloyds Bank Group Impairment provisions, net charge and acquisition related fair value adjustments analysed by geographical region

	2016			2015		
	Impairment provisions[1] £m	**Net charge[1] £m**	**Acquisition related fair value adjustments[2] £m**	Impairment provisions[1] £m	Net charge[1] £m	Acquisition related fair value adjustments[2] £m
United Kingdom	**3,189**	**727**	**177**	3,726	687	276
Rest of Europe	**270**	**(68)**	**–**	323	43	–
United States of America	**9**	**–**	**–**	74	(18)	–
Asia-Pacific	**9**	**–**	**–**	19	(4)	–
Other	**54**	**(2)**	**–**	30	(87)	–
	3,531	**657**	**177**	4,172	621	276
Fair value and other adjustments	**(1,119)**	**(65)**		(1,139)	(178)	
Total	**2,412**	**592**	**177**	3,033	443	276

[1] Analysis of closing impairment provisions, the net charge to the income statement and advances written off in respect of loans and advances to customers, by geographical region, has been presented prior to the application of fair value and other adjustments. Such adjustments are not analysed on a geographical basis within the business.

[2] The acquisition related fair value adjustments represent SCRAs recognised in the calculation of EEL amounts on IRB portfolios (as presented in Table 91).

ANALYSIS OF CREDIT RISK EXPOSURES

Table 94: Lloyds Bank Group credit risk exposures

Exposure class	2016 Credit risk exposure £m	2016 Risk-weighted assets £m	2016 Minimum capital requirements £m	2016 Average risk weight %	2016 Average credit risk exposure £m
Exposures subject to the IRB approach					
Foundation IRB approach					
Corporate – main	78,527	41,171	3,294	52%	80,060
Corporate – SME	11,981	7,880	630	66%	12,777
Corporate – specialised lending	2	2	–	137%	3
Central governments and central banks	15,153	1,430	114	9%	17,597
Institutions	6,011	957	77	16%	6,861
Retail IRB approach					
Retail mortgages	335,510	39,550	3,164	12%	338,097
of which: residential mortgages (SME)	10,211	2,662	213	26%	10,393
of which: residential mortgages (non-SME)	325,299	36,888	2,951	11%	327,704
Qualifying revolving retail exposures	36,984	12,073	966	33%	37,059
Other SME	2,445	1,728	138	71%	2,506
Other non-SME	16,026	11,618	930	72%	15,280
Other IRB approaches					
Corporate – specialised lending	18,814	13,467	1,077	72%	19,678
Equities – exchange traded	461	1,337	107	290%	737
Equities – private equity	2,583	4,909	393	190%	2,916
Equities – other	382	1,413	113	370%	432
Securitisation positions	26,066	3,703	296	14%	22,613
Non-credit obligation assets	10,890	6,427	514	59%	9,639
Total – IRB approach	561,835	147,665	11,813	26%	566,255
Exposures subject to the standardised approach					
Central governments and central banks	81,021	–	–	–	91,331
Regional governments or local authorities	–	–	–	–	1
Public sector entities	2	2	–	100%	2
Multilateral development banks	1,753	–	–	–	1,412
International organisations	–	–	–	–	–
Institutions	279	117	9	42%	193
Corporates	16,729	10,801	864	65%	21,095
Retail	4,114	2,761	221	67%	4,546
Secured by mortgages on immovable property	5,504	1,981	159	36%	5,703
of which: residential property	5,501	1,978	159	36%	5,684
of which: commercial property	3	3	–	100%	19
Exposures in default	789	883	71	112%	916
Exposures associated with particularly high risk	–	–	–	–	–
Securitisation positions	1,184	268	21	23%	237
Short term claims on institutions and corporates	–	–	–	–	–
Collective investment undertakings (CIUs)	224	45	4	20%	45
Other items	3,091	2,098	168	68%	3,372
Total – standardised approach	114,690	18,956	1,517	17%	128,853
Total credit risk	676,525	166,621	13,330	25%	695,108
Threshold – significant investments	3,653	9,133	731	250%	3,631
Threshold – deferred tax	947	2,367	189	250%	1,144
Total credit risk	681,125	178,121	14,250	26%	699,883

Appendix 3: Lloyds Bank Group continued

Exposure class	2015 Credit risk exposure £m	2015 Risk-weighted assets £m	2015 Minimum capital requirements £m	2015 Average risk weight %	2015 Average credit risk exposure £m
Exposures subject to the IRB approach					
Foundation IRB approach					
Corporate – main	80,629	43,005	3,441	53%	79,610
Corporate – SME	12,964	8,814	705	68%	13,350
Corporate – specialised lending	6	8	1	120%	60
Central governments and central banks	15,716	1,347	108	9%	21,395
Institutions	7,364	1,430	114	19%	7,421
Retail IRB approach					
Retail mortgages	341,807	38,252	3,060	11%	347,021
of which: residential mortgages (SME)	10,517	3,214	257	31%	10,867
of which: residential mortgages (non-SME)	331,290	35,038	2,803	11%	336,155
Qualifying revolving retail exposures	36,975	12,501	1,000	34%	37,400
Other SME	2,661	1,807	145	68%	2,618
Other non-SME	14,331	11,352	908	79%	14,373
Other IRB approaches					
Corporate – specialised lending	19,887	14,386	1,151	72%	21,293
Equities – exchange traded	978	2,837	227	290%	904
Equities – private equity	2,981	5,664	453	190%	3,068
Equities – other	376	1,392	111	370%	102
Securitisation positions	22,125	3,266	261	15%	18,162
Non-credit obligation assets	9,228	5,502	440	60%	8,624
Total – IRB approach	568,028	151,563	12,125	27%	575,401
Exposures subject to the standardised approach					
Central governments and central banks	88,415	–	–	–	96,082
Regional governments or local authorities	1	–	–	20%	–
Public sector entities	2	2	–	100%	8
Multilateral development banks	997	–	–	–	77
International organisations	–	–	–	–	–
Institutions	170	24	2	14%	175
Corporates	26,102	11,921	954	46%	27,077
Retail	4,438	2,880	230	65%	3,837
Secured by mortgages on immovable property	5,840	2,109	168	36%	7,098
of which: residential property	5,809	2,078	166	36%	7,075
of which: commercial property	31	31	2	100%	23
Exposures in default	1,005	1,198	96	119%	1,120
Exposures associated with particularly high risk	–	–	–	–	–
Securitisation positions	–	–	–	–	–
Short term claims on institutions and corporates	–	–	–	–	–
Collective investment undertakings (CIUs)	–	–	–	–	–
Other items	3,204	2,309	185	72%	4,500
Total – standardised approach	130,174	20,443	1,635	16%	139,974
Total credit risk	698,202	172,006	13,760	25%	715,375
Threshold – significant investments	3,626	9,066	725	250%	3,808
Threshold – deferred tax	1,159	2,897	232	250%	938
Total credit risk	702,987	183,969	14,717	26%	720,121

ANALYSIS OF CREDIT RISK EXPOSURES BY INDUSTRY

Credit risk exposures as at 31 December 2016, analysed by major industrial sector, are provided in the table below.

Table 95: Lloyds Bank Group credit risk exposures analysed by major industrial sector

	2016 Agriculture, forestry and fishing £m	2016 Energy and water supply £m	2016 Manufacturing £m	2016 Construction £m	2016 Transport, distribution and hotels £m	2016 Postal and comms £m	2016 Property companies £m	2016 Financial, business and other services £m	2016 Personal: mortgages £m	2016 Personal: other £m	2016 Lease financing £m	2016 Hire purchase £m	2016 Total £m
Exposures subject to the IRB approach													
Foundation IRB approach													
Corporate – main	213	3,387	12,187	3,229	12,605	2,066	9,744	30,477	–	–	2,221	2,398	78,527
Corporate – SME	1,265	44	1,371	462	2,706	43	2,110	3,613	–	–	39	328	11,981
Corporate – specialised lending	–	–	–	–	–	–	2	–	–	–	–	–	2
Central governments and central banks	–	–	–	–	–	–	–	15,153	–	–	–	–	15,153
Institutions	–	3	–	10	–	–	–	5,901	–	–	55	42	6,011
Retail IRB approach													
Retail mortgages	1,512	7	346	321	1,707	32	4,324	1,960	325,299	2	–	–	335,510
of which: residential mortgages (SME)	1,512	7	346	321	1,707	32	4,324	1,960	–	2	–	–	10,211
of which: residential mortgages (non-SME)	–	–	–	–	–	–	–	–	325,299	–	–	–	325,299
Qualifying revolving retail exposures	–	–	–	–	–	–	–	–	–	36,984	–	–	36,984
Other SME	217	3	180	314	562	15	333	818	–	3	–	–	2,445
Other non-SME	–	–	–	–	–	–	–	–	–	7,816	–	8,210	16,026
Other IRB approaches													
Corporate – specialised lending	–	1,067	325	254	995	32	14,853	570	–	–	718	–	18,814
Equities – exchange traded	–	–	–	–	–	–	–	461	–	–	–	–	461
Equities – private equity	–	84	223	145	320	474	43	1,294	–	–	–	–	2,583
Equities – other	–	–	–	–	–	–	–	382	–	–	–	–	382
Securitisation positions	–	–	–	–	–	–	–	26,066	–	–	–	–	26,066
Total – IRB approach	3,207	4,595	14,632	4,735	18,895	2,662	31,409	86,695	325,299	44,805	3,033	10,978	550,945
Exposures subject to the standardised approach													
Central governments and central banks	–	–	–	–	–	–	–	81,021	–	–	–	–	81,021
Regional governments or local authorities	–	–	–	–	–	–	–	–	–	–	–	–	–
Public sector entities	–	–	–	–	–	–	–	2	–	–	–	–	2
Multilateral development banks	–	–	–	–	–	–	–	1,753	–	–	–	–	1,753
International organisations	–	–	–	–	–	–	–	–	–	–	–	–	–
Institutions	–	–	–	–	–	–	–	271	–	–	8	–	279
Corporates	1,565	322	1,791	103	2,862	103	1,022	7,395	96	948	475	47	16,729
Retail	1,060	3	23	20	148	1	225	176	977	1,040	–	441	4,114
Secured by mortgages on immovable property	–	–	1	–	–	–	1	253	5,249	1	–	–	5,504
of which: residential property	–	–	1	–	–	–	1	253	5,246	1	–	–	5,501
of which: commercial property	–	–	–	–	–	–	–	–	3	–	–	–	3
Exposures in default	13	–	6	15	25	–	136	33	476	82	1	2	789
Exposures associated with particularly high risk	–	–	–	–	–	–	–	–	–	–	–	–	–
Covered bonds	–	–	–	–	–	–	–	–	–	–	–	–	–
Securitisation positions	–	–	–	–	–	–	–	1,184	–	–	–	–	1,184
Short term claims on institutions and corporates	–	–	–	–	–	–	–	–	–	–	–	–	–
Collective investment undertakings (CIUs)	–	–	–	–	–	–	–	224	–	–	–	–	224
Equity Exposures	–	–	–	–	–	–	–	–	–	–	–	–	–
Total – standardised approach	2,638	325	1,821	138	3,035	104	1,383	92,312	6,798	2,071	484	490	111,599
Total	5,845	4,920	16,453	4,873	21,930	2,766	32,792	179,007	332,097	46,876	3,517	11,468	662,544
Other items													3,091
Non-credit obligation assets													10,890
Total credit risk exposure													676,525

Appendix 3: Lloyds Bank Group continued

	2015 Agriculture, forestry and fishing £m	2015 Energy and water supply £m	2015 Manufacturing £m	2015 Construction £m	2015 Transport, distribution and hotels £m	2015 Postal and comms £m	2015 Property companies £m	2015 Financial, business and other services £m	2015 Personal: mortgages £m	2015 Personal: other £m	2015 Lease financing £m	2015 Hire purchase £m	2015 Total £m
Exposures subject to the IRB approach													
Foundation IRB approach													
Corporate – main	219	4,050	11,291	2,835	12,347	3,743	9,697	31,944	–	3	2,235	2,265	80,629
Corporate – SME	1,383	53	1,672	450	2,919	40	1,902	4,197	–	–	43	305	12,964
Corporate – specialised lending	–	–	–	–	–	–	4	2	–	–	–	–	6
Central governments and central banks	–	–	–	–	–	–	–	15,716	–	–	–	–	15,716
Institutions	–	3	–	8	–	–	–	7,268	–	–	53	32	7,364
Retail IRB approach													
Retail mortgages	1,500	7	359	350	1,827	34	4,440	1,998	331,290	2	–	–	341,807
of which: residential mortgages (SME)	1,500	7	359	350	1,827	34	4,440	1,998	–	2	–	–	10,517
of which: residential mortgages (non-SME)	–	–	–	–	–	–	–	–	331,290	–	–	–	331,290
Qualifying revolving retail exposures	–	–	–	–	–	–	–	–	–	36,975	–	–	36,975
Other SME	241	2	190	303	595	16	441	870	–	3	–	–	2,661
Other non-SME	–	–	–	–	–	–	–	–	–	7,890	–	6,441	14,331
Other IRB approaches													
Corporate – specialised lending	–	1,298	345	346	1,039	167	14,861	1,127	–	–	704	–	19,887
Equities – exchange traded	–	–	–	–	–	–	92	886	–	–	–	–	978
Equities – private equity	–	102	296	136	430	547	87	1,383	–	–	–	–	2,981
Equities – other	–	–	–	–	–	–	–	376	–	–	–	–	376
Securitisation positions[1]	–	–	–	–	–	–	–	22,125	–	–	–	–	22,125
Total – IRB approach	3,343	5,515	14,153	4,428	19,157	4,547	31,524	87,892	331,290	44,873	3,035	9,043	558,800
Exposures subject to the standardised approach													
Central governments and central banks	–	–	–	–	–	–	–	88,415	–	–	–	–	88,415
Regional governments or local authorities	–	–	–	–	–	–	–	1	–	–	–	–	1
Public sector entities	–	–	–	–	–	–	–	2	–	–	–	–	2
Multilateral development banks	–	–	–	–	–	–	–	997	–	–	–	–	997
International organisations	–	–	–	–	–	–	–	–	–	–	–	–	–
Institutions	–	–	–	–	–	–	–	165	–	–	5	–	170
Corporates	2,293	190	1,419	139	2,701	11	1,163	16,729	98	956	360	42	26,102
Retail	1,795	2	22	23	146	2	203	171	862	894	–	318	4,438
Secured by mortgages on immovable property	–	–	1	–	–	–	6	163	5,669	1	–	–	5,840
of which: residential property	–	–	1	–	–	–	6	135	5,666	1	–	–	5,809
of which: commercial property	–	–	–	–	–	–	–	28	3	–	–	–	31
Exposures in default	15	–	7	70	130	–	73	159	446	102	2	1	1,005
Exposures associated with particularly high risk	–	–	–	–	–	–	–	–	–	–	–	–	–
Covered bonds	–	–	–	–	–	–	–	–	–	–	–	–	–
Securitisation positions	–	–	–	–	–	–	–	–	–	–	–	–	–
Short term claims on institutions and corporates	–	–	–	–	–	–	–	–	–	–	–	–	–
Collective investment undertakings (CIUs)	–	–	–	–	–	–	–	–	–	–	–	–	–
Equity Exposures	–	–	–	–	–	–	–	–	–	–	–	–	–
Total – standardised approach	4,103	192	1,449	232	2,977	13	1,445	106,802	7,075	1,953	367	361	126,970
Total	7,446	5,707	15,602	4,660	22,134	4,560	32,969	194,694	338,365	46,826	3,402	9,404	685,770
Other items													3,204
Non-credit obligation assets													9,228
Total credit risk exposure													698,202

ANALYSIS OF CREDIT RISK EXPOSURES BY GEOGRAPHY

Credit risk exposures as at 31 December 2016, analysed by major geographical region, based on the country of residence/incorporation of the customer, are provided in the table below.

Table 96: Lloyds Bank Group credit risk exposures analysed by geographical region

	2016 United Kingdom £m	2016 Rest of Europe £m	2016 United States of America £m	2016 Asia-Pacific £m	2016 Other £m	2016 Total £m	2015 United Kingdom £m	2015 Rest of Europe £m	2015 United States of America £m	2015 Asia-Pacific £m	2015 Other £m	2015 Total £m
Exposures subject to the IRB approach												
Foundation IRB approach												
Corporate – main	**54,852**	**8,821**	**11,641**	**627**	**2,586**	**78,527**	57,356	8,518	11,603	703	2,449	80,629
Corporate – SME	**11,887**	**33**	**–**	**–**	**61**	**11,981**	12,936	18	–	–	10	12,964
Corporate – specialised lending	**2**	**–**	**–**	**–**	**–**	**2**	6	–	–	–	–	6
Central governments and central banks	**–**	**156**	**14,779**	**–**	**218**	**15,153**	–	27	15,552	–	137	15,716
Institutions	**1,793**	**2,039**	**1,252**	**424**	**503**	**6,011**	1,896	3,139	1,362	139	828	7,364
Retail IRB approach												
Retail mortgages	**326,000**	**9,504**	**–**	**1**	**5**	**335,510**	333,799	8,003	–	1	4	341,807
of which: residential mortgages (SME)	**10,201**	**4**	**–**	**1**	**5**	**10,211**	10,508	4	–	1	4	10,517
of which: residential mortgages (non-SME)	**315,799**	**9,500**	**–**	**–**	**–**	**325,299**	323,291	7,999	–	–	–	331,290
Qualifying revolving retail exposures	**36,984**	**–**	**–**	**–**	**–**	**36,984**	36,975	–	–	–	–	36,975
Other SME	**2,444**	**–**	**–**	**–**	**1**	**2,445**	2,661	–	–	–	–	2,661
Other non-SME	**15,974**	**52**	**–**	**–**	**–**	**16,026**	14,248	83	–	–	–	14,331
Other IRB approaches												
Corporate – specialised lending	**14,389**	**2,818**	**569**	**114**	**924**	**18,814**	14,855	3,327	646	209	850	19,887
Equities – exchange traded	**361**	**100**	**–**	**–**	**–**	**461**	876	102	–	–	–	978
Equities – private equity	**2,465**	**56**	**60**	**2**	**–**	**2,583**	2,759	81	82	17	42	2,981
Equities – other	**382**	**–**	**–**	**–**	**–**	**382**	370	6	–	–	–	376
Securitisation positions[1]	**17,776**	**1,366**	**6,734**	**–**	**190**	**26,066**	16,946	423	4,730	–	26	22,125
Total – IRB approach	**485,309**	**24,945**	**35,035**	**1,168**	**4,488**	**550,945**	495,683	23,727	33,975	1,069	4,346	558,800
Exposures subject to the standardised approach												
Central governments and central banks	**69,957**	**11,064**	**–**	**–**	**–**	**81,021**	75,315	13,100	–	–	–	88,415
Regional governments or local authorities	**–**	**–**	**–**	**–**	**–**	**–**	1	–	–	–	–	1
Public sector entities	**2**	**–**	**–**	**–**	**–**	**2**	2	–	–	–	–	2
Multilateral development banks	**41**	**397**	**1,283**	**32**	**–**	**1,753**	–	426	571	–	–	997
International organisations	**–**	**–**	**–**	**–**	**–**	**–**	–	–	–	–	–	–
Institutions	**90**	**101**	**87**	**1**	**–**	**279**	18	88	61	3	–	170
Corporates	**11,275**	**1,940**	**2,193**	**284**	**1,037**	**16,729**	20,855	2,355	1,838	389	665	26,102
Retail	**2,755**	**1,339**	**2**	**9**	**9**	**4,114**	3,485	935	2	6	10	4,438
Secured by mortgages on immovable property	**4,479**	**276**	**100**	**501**	**148**	**5,504**	4,776	286	92	526	160	5,840
of which: residential property	**4,476**	**276**	**100**	**501**	**148**	**5,501**	4,772	259	92	526	160	5,809
of which: commercial property	**3**	**–**	**–**	**–**	**–**	**3**	3	28	–	–	–	31
Exposures in default	**707**	**48**	**6**	**10**	**18**	**789**	845	108	5	14	33	1,005
Exposures associated with particularly high risk	**–**	**–**	**–**	**–**	**–**	**–**	–	–	–	–	–	–
Covered bonds	**–**	**–**	**–**	**–**	**–**	**–**	–	–	–	–	–	–
Securitisation positions	**1,184**	**–**	**–**	**–**	**–**	**1,184**	–	–	–	–	–	–
Short term claims on institutions and corporates	**–**	**–**	**–**	**–**	**–**	**–**	–	–	–	–	–	–
Collective investment undertakings (CIUs)	**224**	**–**	**–**	**–**	**–**	**224**	–	–	–	–	–	–
Equity exposures	**–**	**–**	**–**	**–**	**–**	**–**	–	–	–	–	–	–
Total – standardised approach	**90,714**	**15,165**	**3,671**	**837**	**1,212**	**111,599**	105,297	17,298	2,569	938	868	126,970
Total	**576,023**	**40,110**	**38,706**	**2,005**	**5,700**	**662,544**	600,980	41,025	36,544	2,007	5,214	685,770
Other items						**3,091**						3,204
Non-credit obligation assets						**10,890**						9,228
Total credit risk exposure						**676,525**						698,202

Appendix 3: Lloyds Bank Group continued

ANALYSIS OF CREDIT RISK EXPOSURES BY RESIDUAL MATURITY

Credit risk exposures as at 31 December 2016, analysed by residual contractual maturity, are provided in the table below.

Table 97: Lloyds Bank Group credit risk exposures analysed by residual contractual maturity

	2016 On demand £m	2016 Repayable in 3 months or less £m	2016 Repayable between 3 months and 1 year £m	2016 Repayable between 1 and 5 years £m	2016 Repayable over 5 years or undated £m	2016 Total £m	2015 On demand £m	2015 Repayable in 3 months or less £m	2015 Repayable between 3 months and 1 year £m	2015 Repayable between 1 and 5 years £m	2015 Repayable over 5 years or undated £m	2015 Total £m
Exposures subject to the IRB approach												
Foundation IRB approach												
Corporate – main	7,074	5,691	13,879	41,334	10,549	78,527	6,110	4,555	16,343	42,504	11,117	80,629
Corporate – SME	930	618	3,307	2,629	4,497	11,981	888	546	3,357	3,104	5,069	12,964
Corporate – specialised lending	–	–	–	–	2	2	1	–	–	–	5	6
Central governments and central banks	–	6,017	–	5,025	4,111	15,153	–	8,549	99	3,252	3,816	15,716
Institutions	245	1,298	1,690	2,382	396	6,011	181	1,345	1,394	3,364	1,080	7,364
Retail IRB approach												
Retail mortgages	1,427	1,195	13,504	19,063	300,321	335,510	1,171	1,171	12,719	19,393	307,353	341,807
of which: residential mortgages (SME)	217	531	1,008	1,211	7,244	10,211	242	551	983	1,329	7,412	10,517
of which: residential mortgages (non-SME)	1,210	664	12,496	17,852	293,077	325,299	929	620	11,736	18,064	299,941	331,290
Qualifying revolving retail exposures	36,984	–	–	–	–	36,984	36,975	–	–	–	–	36,975
Other SME	105	338	776	338	888	2,445	110	341	780	356	1,074	2,661
Other non-SME	18	274	1,365	13,396	973	16,026	26	250	1,184	11,950	921	14,331
Other IRB approaches												
Corporate – specialised lending	297	866	2,294	8,713	6,644	18,814	238	924	1,755	8,476	8,494	19,887
Equities – exchange traded	–	–	–	–	461	461	–	–	–	–	978	978
Equities – private equity	–	–	–	–	2,583	2,583	–	–	–	–	2,981	2,981
Equities – other	–	–	–	–	382	382	–	–	–	–	376	376
Securitisation positions[1]	–	2,191	9,231	7,370	7,274	26,066	–	1,195	4,685	8,766	7,479	22,125
Total – IRB approach	47,080	18,488	46,046	100,250	339,081	550,945	45,700	18,876	42,316	101,165	350,743	558,800
Exposures subject to the standardised approach												
Central governments and central banks	29,220	8,995	549	10,251	32,006	81,021	35,304	11,602	374	5,785	35,350	88,415
Regional governments or local authorities	–	–	–	–	–	–	–	–	–	–	1	1
Public sector entities	–	–	–	–	2	2	–	–	–	–	2	2
Multilateral development banks	–	24	61	1,265	403	1,753	–	–	27	608	362	997
International organisations	–	–	–	–	–	–	–	–	–	–	–	–
Institutions	11	103	56	2	107	279	11	90	62	1	6	170
Corporates	807	822	1,984	3,954	9,162	16,729	1,020	880	1,621	4,106	18,475	26,102
Retail	198	43	117	1,312	2,444	4,114	232	44	108	1,050	3,004	4,438
Secured by mortgages on immovable property	666	35	122	496	4,185	5,504	559	34	134	598	4,515	5,840
of which: residential property	666	35	122	496	4,182	5,501	558	34	134	570	4,513	5,809
of which: commercial property	–	–	–	–	3	3	1	–	–	28	2	31
Exposures in default	55	12	42	177	503	789	83	18	136	111	657	1,005
Exposures associated with particularly high risk	–	–	–	–	–	–	–	–	–	–	–	–
Covered bonds	–	–	–	–	–	–	–	–	–	–	–	–
Securitisation positions	–	–	–	–	1,184	1,184	–	–	–	–	–	–
Short term claims on institutions and corporates	–	–	–	–	–	–	–	–	–	–	–	–
Collective investment undertakings (CIUs)	–	–	–	–	224	224	–	–	–	–	–	–
Equity exposures	–	–	–	–	–	–	–	–	–	–	–	–
Total – standardised approach	30,957	10,034	2,931	17,457	50,220	111,599	37,209	12,668	2,462	12,259	62,372	126,970
Total	78,037	28,522	48,977	117,707	389,301	662,544	82,909	31,544	44,778	113,424	413,114	685,770
Other items						3,091						3,204
Non-credit obligation assets						10,890						9,228
Total credit risk exposure						676,525						698,202

Appendix 4: Bank of Scotland Group

OWN FUNDS DISCLOSURE TEMPLATE

Table 98: Bank of Scotland Group own funds template

	Transitional rules		Fully loaded rules	
	At 31 Dec 2016 £m	At 31 Dec 2015 £m	**At 31 Dec 2016 £m**	At 31 Dec 2015 £m
Common equity tier 1 (CET1) capital: instruments and reserves				
Capital instruments and related share premium accounts	**5,847**	5,847	**5,847**	5,847
of which: called up share capital	**5,847**	5,847	**5,847**	5,847
Retained earnings	**4,243**	5,496	**4,243**	5,496
Accumulated other comprehensive income and other reserves (including unrealised gains and losses)	**2,165**	2,268	**2,165**	2,268
Foreseeable dividend	**(500)**	(2,000)	**(500)**	(2,000)
Common equity tier 1 (CET1) capital before regulatory adjustments	**11,755**	11,611	**11,755**	11,611
Common equity tier 1 (CET1) capital: regulatory adjustments				
Additional value adjustments	**(165)**	(63)	**(165)**	(63)
Intangible assets (net of related tax liability)	**(424)**	(425)	**(424)**	(425)
Deferred tax assets that rely on future profitability, excluding those arising from temporary differences (net of related tax liability where the conditions in Article 38 (3) of the CRR are met)	**(1,650)**	(1,569)	**(1,650)**	(1,569)
Fair value reserves related to gains or losses on cash flow hedges	**(90)**	(170)	**(90)**	(170)
Negative amounts resulting from the calculation of expected loss amounts	**(132)**	(175)	**(132)**	(175)
Gains or losses on liabilities valued at fair value resulting from changes in own credit standing	**(11)**	(8)	**(11)**	(8)
Exposure amount of the following items which qualify for a risk weight of 1,250%, where the Group has opted for the deduction alternative	**(186)**	(166)	**(186)**	(166)
of which: securitisation positions	**(186)**	(166)	**(186)**	(166)
Total regulatory adjustments applied to common equity tier 1 (CET1)	**(2,658)**	(2,576)	**(2,658)**	(2,576)
Common equity tier 1 (CET1) capital	**9,097**	9,035	**9,097**	9,035
Additional tier 1 (AT1) capital: instruments				
Capital instruments and related share premium accounts	**1,500**	1,500	**1,500**	1,500
of which: classified as equity under applicable accounting standards	**1,500**	1,500	**1,500**	1,500
Amount of qualifying items referred to in Article 484 (4) of the CRR and the related share premium accounts subject to phase out from AT1	**177**	316	**–**	–
Qualifying Tier 1 capital included in consolidated AT1 capital (including minority interests not included in CET1) issued by subsidiaries and held by third parties	**150**	150	**–**	–
of which: instruments issued by subsidiaries subject to phase out	**150**	150	**–**	–
Additional tier 1 (AT1) capital	**1,827**	1,966	**1,500**	1,500
Tier 1 capital	**10,924**	11,001	**10,597**	10,535
Tier 2 (T2) capital: Instruments and provisions				
Capital instruments and related share premium accounts	**3,216**	3,332	**3,216**	3,332
Amount of qualifying items referred to in Article 484 (5) of the CRR and the related share premium accounts subject to phase out from T2	**3,052**	2,381	**–**	–
Credit risk adjustments	**304**	307	**304**	307
Tier 2 (T2) capital	**6,572**	6,020	**3,520**	3,639
Total capital	**17,496**	17,021	**14,117**	14,174
Total risk-weighted assets	**75,561**	76,054	**75,561**	76,054

Appendix 4: Bank of Scotland Group continued

	Transitional rules		Fully loaded rules	
	At 31 Dec 2016 £m	At 31 Dec 2015 £m	**At 31 Dec 2016 £m**	At 31 Dec 2015 £m
Capital ratios and buffers				
Common Equity Tier 1 (as a percentage of risk exposure amount)	**12.0%**	11.9%	**12.0%**	11.9%
Tier 1 (as a percentage of risk exposure amount)	**14.5%**	14.5%	**14.0%**	13.9%
Total capital (as a percentage of risk exposure amount)	**23.2%**	22.4%	**18.7%**	18.6%
Institution specific buffer requirement (CET1 requirement in accordance with article 92 (1) (a) plus capital conservation and countercyclical buffer requirements, plus systemic risk buffer, plus the systemically important institution buffer (G-SII or O-SII buffer), expressed as a percentage of risk exposure amount)	**0.627%**	0.0005%	**0.627%**	0.0005%
of which: capital conservation buffer requirement[1]	**0.625%**	–	**0.625%**	–
of which: countercyclical buffer requirement	**0.002%**	0.0005%	**0.002%**	0.0005%
Common Equity Tier 1 available to meet buffers (as a percentage of risk exposure amount)[2]	**7.5%**	7.4%	**7.5%**	7.4%
Amounts below the threshold for deduction (before risk-weighting)				
Direct and indirect holdings of the capital of financial sector entities where the Group does not have a significant investment in those entities (amount below 10% threshold and net of eligible short positions)	**133**	56	**133**	56
Direct and indirect holdings by the institution of the CET1 instruments of financial sector entities where the institution has a significant investment in those entities (amount below 10% threshold and net of eligible short positions)	**2**	–	**2**	–
Deferred tax assets arising from temporary differences (amount below 10% threshold, net of related tax liability where the conditions in 38 (3) of the CRR are met)	**323**	455	**323**	455
Applicable caps on the inclusion of provisions in Tier 2				
Credit risk adjustments included in T2 in respect of exposures subject to internal ratings-based approach (prior to the application of the cap)	**392**	383	**392**	383
Cap on inclusion of credit risk adjustments in T2 under internal ratings-based approach	**304**	307	**304**	307
Capital instruments subject to phase-out arrangements (only applicable between 1 Jan 2013 and 1 Jan 2022)				
Current cap on AT1 instruments subject to phase out arrangements	**427**	498	**–**	–
Current cap on T2 instruments subject to phase out arrangements	**5,316**	6,202	**–**	–

[1] The capital conservation buffer requirement is the percentage applicable at the reporting date. This will increase to 2.5 per cent by 2019.

[2] Excluding CET1 required to meet Pillar 2A requirements.

OWN FUNDS RECONCILIATION

The following table presents certain items from the Bank of Scotland Group consolidated balance sheet on an accounting consolidation basis for the year ended 31 December 2016, that are used to calculate own funds. Where necessary, the balance sheet components have been expanded such that the components of the transitional own funds disclosure template appear separately.

Table 99: Bank of Scotland Group items extracted from the consolidated balance sheet on an accounting consolidation basis and reconciliation of own funds items to audited financial statements

			Adjustments						
Balance sheet category	**Own funds description**	**Items extracted from the consolidated accounting balance sheet (1) £m**	**Deferred tax £m**	**Threshold adjustments £m**	**Non-eligible instruments £m**	**Amounts excluded from AT1 due to Cap £m**	**Regulatory and other adjustments £m**	**Transitional own funds £m**	**Notes**
	Common Equity Tier 1 (CET1) capital: instruments and reserves								
	Capital instruments and related share premium accounts	5,847	–	–	–	–	–	5,847	
Share capital	of which: called up share capital	5,847	–	–	–	–	–	5,847	
Retained profits	Retained earnings	4,243	–	–	–	–	–	4,243	
Other reserves	Accumulated other comprehensive income and other reserves (including unrealised gains and losses)	2,165	–	–	–	–	–	2,165	
	Common equity tier 1 (CET1) capital: regulatory adjustments								
	Additional value adjustments	–	–	–	–	–	(165)	(165)	2
Goodwill and other intangible assets	Intangible assets (net of related tax liability)	(425)	1	–	–	–	–	(424)	3
Deferred tax assets	Deferred tax assets that rely on future profitability, excluding those arising from temporary differences (net of related tax liability where conditions in Article 38(3) of the CRR are met)	(1,941)	(32)	323	–	–	–	(1,650)	4
	Fair value reserves related to gains or losses on cash flow hedges	–	–	–	–	–	(90)	(90)	5
	Negative amounts resulting from the calculation of expected loss amounts	–	–	–	–	–	(132)	(132)	6
	Gains or losses on liabilities valued at fair value resulting from changes in own credit standing	–	–	–	–	–	(11)	(11)	7
	Exposures amount of the following items which qualify for a risk weight of 1,250%, where the Group has opted for the deduction alternative (securitisation positions)	–	–	–	–	–	(186)	(186)	8
	Foreseeable dividend	–	–	–	–	–	(500)	(500)	9
	Common Equity Tier 1 (CET1) capital	9,889	(31)	323	–	–	(1,084)	9,097	
	Additional Tier 1 (AT1) capital: instruments								
Subordinated liabilities	Capital instruments and the related share premium accounts	1,500	–	–	–	–	–	1,500	
Subordinated liabilities	Amount of qualifying items referred to in Article 484 (4) of the CRR and the related share premium accounts subject to phase out from AT1	178	–	–	–	–	(1)	177	10
Subordinated liabilities	Qualifying Tier 1 capital included in consolidated AT1 capital (including minority interests not included in CET1) issued by subsidiaries and held by third parties	151	–	–	–	–	(1)	150	10
	Additional Tier 1 (AT1) capital	1,829	–	–	–	–	(2)	1,827	
	Tier 1 capital	11,718	(31)	323	–	–	(1,086)	10,924	
	Tier 2 (T2) capital: instruments and provisions								
Subordinated liabilities	Capital instruments and related share premium accounts	3,660	–	–	(32)	–	(412)	3,216	10
Subordinated liabilities	Amount of qualifying items referred to in Article 484 (5) of the CRR and the related share premium accounts subject to phase out from T2	3,095	–	–	–	–	(43)	3,052	10
	Credit risk adjustments	–	–	–	–	–	304	304	11
	Tier 2 (T2) capital	6,755	–	–	(32)	–	(151)	6,572	
	Total capital	18,473	(31)	323	(32)	–	(1,237)	17,496	

Appendix 4: Bank of Scotland Group continued

1. Assets extracted from the consolidated accounting balance sheet are presented as negative amounts, liabilities and equity are presented as positive amounts.
2. The adjustment of £165m reflects the prudent valuation adjustment for all assets measured at fair value in accordance with Articles 34 and 105 of the CRR.
3. Own funds intangible assets of £425m extracted from the consolidated balance sheet comprise £325m of goodwill and £100m of other intangible assets. CRD IV rules require the amount to be deducted from own funds to be reduced by the amount of the associated deferred tax liabilities.
4. The own funds deduction of £1,941m for deferred tax excludes the deferred tax balances relating to intangible assets and the cash flow hedge. Additionally, only the deferred tax amounts that rely on future profitability are required to be deducted from CET1, and may be reduced by associated deferred tax liabilities where conditions specified in Article 38 of CRR are met. £323m of the deferred tax asset relating to the temporary differences may be risk weighted instead of deducted from capital as presented in the threshold adjustments column.
5. Cash flow hedge reserve forms part of other reserves in the consolidated regulatory balance sheet.
6. In accordance with Articles 36, 62, 158 and 159 of the CRR the excess of expected losses over specific credit risk adjustments (SCRAs) and additional value adjustments of £132m are deducted from CET1.
7. CRD IV requires the removal of the impact of any gains or losses recorded on liabilities held at fair value through profit or loss or derivative liabilities due to changes in the credit spreads of Bank of Scotland plc.
8. The £186m deduction for securitisation positions reflects those positions that were rated below BB- or that are unrated.
9. The £500m foreseeable dividend is that recommended by the Board of Directors in respect of 2016 earnings.
10. A reconciliation of subordinated liabilities from the Bank of Scotland Group's consolidated balance sheet to the amount recognised against each own funds description is presented in the table below.

Own funds description	Consolidated accounting balance sheet total £m
Amount of qualifying items referred to in Article 484 (4) of the CRR and the related share premium accounts subject to phase out from AT1	178
Qualifying Tier 1 capital included in consolidated AT1 capital (including minority interests not included in CET1) issued by subsidiaries and held by third parties	151
Capital instruments and related share premium accounts	3,660
Amount of qualifying items referred to in Article 484 (5) of the CRR and the related share premium accounts subject to phase out from T2	3,095
Total subordinated liabilities as presented on the Bank of Scotland Group's consolidated balance sheet	**7,084**

Adjustments required by regulatory rules to the value of subordinated liabilities presented within the regulatory and other adjustments column on the reconciliation include adjustments for accrued interest, amortisation and associated derivatives.

The non-eligible instruments column on the reconciliation represents instruments on the balance sheet that are not eligible for inclusion in regulatory capital.

Additional Tier 1 instruments presented in own funds reflect instruments issued by either Bank of Scotland Group plc or its subsidiaries and held by third parties that qualified as Tier 1 under regulation that preceded CRD IV, subject to certain restrictions, including a cap set at 60% of the value of such instruments that were in issue at 31 December 2012 and net of interest. Any excess over the cap is included in Tier 2 instruments which have been issued in the same manner as Additional Tier 1 instruments and are net of interest and in some instances amortisation and associated derivatives.

11. Credit risk adjustments of £304m reflect the surplus provisions resulting from the calculation of excess expected loss amounts in accordance with Articles 158 and 159 of the CRR, subject to certain limits.

LEVERAGE DISCLOSURE TEMPLATE

Table 100: Bank of Scotland Group leverage ratio common disclosure

	At 31 Dec 2016 Fully loaded £m	At 31 Dec 2015 Fully loaded £m
On-balance sheet exposures (excluding derivatives and SFTs)		
On-balance sheet items (excluding derivatives, SFTs and fiduciary assets, but including collateral)	**333,075**	322,175
Asset amounts deducted in determining Tier 1 capital	**(2,658)**	(2,577)
Total on-balance sheet exposures (excluding derivatives, SFTs and fiduciary assets)	**330,417**	319,598
Derivative exposures[1]		
Replacement cost associated with all derivatives transactions (ie net of eligible cash variation margin)	**2,296**	2,016
Add-on amounts for PFE associated with all derivatives transactions (mark-to-market method)	**318**	492
Deductions of receivables assets for cash variation margin provided in derivatives transactions	**(602)**	(413)
Total derivative exposures	**2,012**	2,095
Securities financing transaction exposures[2]		
Gross SFT assets (with no recognition of netting), after adjusting for sales accounting transactions	**–**	–
Netted amounts of cash payables and cash receivables of gross SFT assets	**–**	–
Counterparty credit risk exposure for SFT assets	**–**	5
Total securities financing transaction exposures	**–**	5
Other off-balance sheet exposures		
Off-balance sheet exposures at gross notional amount	**37,061**	37,380
Adjustments for conversion to credit equivalent amounts	**(21,553)**	(20,641)
Other off-balance sheet exposures	**15,508**	16,739
Exempted exposures in accordance with CRR Article 429 (7) (on and off balance sheet)		
Intragroup exposures exempted in accordance with Article 429(7) of Regulation (EU) No 575/2013 (on and off balance sheet)[3]	**(50,933)**	(38,023)
Capital and total exposure measure		
Tier 1 capital	**10,597**	10,535
Leverage ratio total exposure measure	**297,004**	300,414
Leverage ratio		
Leverage ratio	**3.6%**	3.5%

[1] Excludes intragroup derivative assets amounting to £8,468m (2015: £9,178m) exempted in accordance with CRR Article 429(7).

[2] Excludes intragroup SFT assets amounting to £946m (2015: £4,233m) exempted in accordance with CRR Article 429(7).

[3] Relates to exempted intragroup loans and receivables. Total intragroup exposures exempted in accordance with CRR Article 429(7), including derivatives and SFTs, amounted to £60,347m (2015: £51,434m).

Table 101: Bank of Scotland Group summary reconciliation of accounting assets and leverage ratio exposures

	At 31 Dec 2016 Fully loaded £m	At 31 Dec 2015 Fully loaded £m
Total assets as per the financial statements	**348,685**	341,333
Adjustment for entities which are consolidated for accounting purposes but are outside the scope of regulatory consolidation	**–**	–
Adjustments for derivative financial instruments	**(4,184)**	(3,652)
Adjustments for securities financing transactions (SFTs)	**–**	5
Adjustment for off-balance sheet items (ie conversion to credit equivalent amounts of off-balance sheet exposures)	**15,508**	16,739
Adjustment for intragroup exposures excluded from the leverage ratio total exposure measure in accordance with Article 429 (7) of Regulation (EU) No 575/2013	**(60,347)**	(51,434)
Other adjustments	**(2,658)**	(2,577)
Leverage ratio total exposure measure	**297,004**	300,414

Appendix 4: Bank of Scotland Group continued

Table 102: Bank of Scotland Group geographical distribution of credit exposures relevant for the calculation of countercyclical capital buffer

Breakdown by Country	2016 General credit exposures[2,3] Exposure Value for STA £m	Exposure Value for IRB £m	2016 Trading book exposures[2,4] Sum of long and short positions of trading book exposures for STA £m	Value of trading book exposures for internal models £m	2016 Securitisation exposures[3] Exposure Value for STA £m	Exposure Value for IRB £m	2016 Own funds requirements of which: General credit exposures[2,3] £m	of which: Trading book exposures[2,4] £m	of which: Securitisation exposures[3] £m	Total £m	2016 Own funds requirement weights %	2016 Countercyclical capital buffer rate %
Norway	–	26	–	–	–	–	5	–	–	5	0.11%	1.500%
Sweden	–	–	–	–	–	–	–	–	–	–	–	1.500%
Hong Kong	–	–	–	–	–	–	–	–	–	–	–	0.625%
i) Total[1]	–	26	–	–	–	–	5	–	–	5	0.11%	
United Kingdom	16,075	290,020	–	–	–	1,673	4,124	–	14	4,138	86.28%	n/a
Ireland	900	3,781	–	–	–	–	351	–	–	351	7.32%	n/a
Netherlands	216	5,853	–	–	–	–	117	–	–	117	2.44%	n/a
British Virgin Islands	770	33	–	–	–	–	63	–	–	63	1.32%	n/a
ii) Total[1]	17,961	299,687	–	–	–	1,673	4,655	–	14	4,669	97.36%	
iii) Rest of the World[1]	691	873	–	–	–	1,238	112	–	10	122	2.53%	
Total	18,652	300,586	–	–	–	2,911	4,772	–	24	4,796	100.00%	

Amount of institution specific countercyclical capital buffer	2016	2015
Total risk exposure amount	£75,561m	£76,054m
Institution specific countercyclical buffer rate	0.002%	0.001%
Institution specific countercyclical buffer requirement	£1.3m	£0.4m

[1] The breakdown by country is disclosed on the following basis:
i) those countries for which a countercyclical capital buffer rate has been set.
ii) those countries for which a countercyclical capital buffer rate has not been set and have an own funds requirement weighting of greater than or equal to one per cent, the threshold having been determined by the Group in accordance with the EBA guidelines on materiality for Pillar 3.
iii) the aggregate of all remaining countries for which a countercyclical buffer rate has not been set and individually have an own funds requirement weighting of less than one per cent.

[2] For the purposes of the calculation of the countercyclical capital buffer, general credit risk and trading book exposures exclude exposures to central governments, central banks, regional governments, local authorities, public sector entities, multilateral development banks, international organisations and institutions. In addition, trading book exposures are limited to those that are subject to the own funds requirement for specific risk or incremental default and migration risk.

[3] General credit and securitisation exposures include counterparty credit risk and are stated on a post CRM basis.

[4] Trading book exposures are allocated in full to the United Kingdom in accordance with the threshold criteria set out under the EBA Regulatory Technical Standard on the identification of the geographical location of the relevant credit exposures for the calculation of the countercyclical capital buffer.

CAPITAL REQUIREMENTS

BANK OF SCOTLAND GROUP RISK-WEIGHTED ASSETS AND PILLAR 1 CAPITAL REQUIREMENTS

The risk-weighted assets and Pillar 1 capital requirements of BOS Group as at 31 December 2016 are £75,561m (2015: £76,054m) and £6,045m (2015: £6,084m).

Table 103: Bank of Scotland Group overview of risk-weighted assets (OV1)

		2016 RWA £m	2015 RWA £m	2016 Minimum capital Requirements £m	2015 Minimum capital Requirements £m
1	**Credit risk (excluding counterparty credit risk)**	**58,597**	59,466	**4,688**	4,757
2	Of which standardised approach	**8,150**	8,651	**652**	692
3	Of which the foundation rating-based (FIRB) approach	**4,459**	6,428	**357**	514
4	Of which the retail IRB (RIRB) approach	**40,295**	37,626	**3,224**	3,010
	Of which corporates – specialised lending	**3,167**	4,028	**253**	322
	Of which non-credit obligation assets	**1,030**	1,013	**82**	81
5	Of which equity IRB under the simple risk -weight or the internal models approach	**1,496**	1,720	**120**	138
6	**Counterparty credit risk**	**1,816**	2,099	**145**	168
7	Of which marked to market	**1,574**	1,785	**126**	143
8	Of which original exposure	**–**	–	**–**	–
9	Of which the standardised approach	**–**	–	**–**	–
10	Of which internal ratings-based model method (IMM)	**–**	–	**–**	–
	Of which comprehensive approach for credit risk mitigation (for SFTs)	**–**	–	**–**	–
	Of which exposures to central counterparties (including trades, default fund contributions and initial margin)	**–**	1	**–**	–
12	Of which credit valuation adjustment (CVA)	**242**	313	**19**	25
13	**Settlement risk**	**–**	–	**–**	–
14	**Securitisation exposures in banking book[1]**	**296**	395	**24**	32
15	Of which IRB ratings-based approach (RBA)	**66**	102	**5**	8
16	Of which IRB supervisory formula approach (SFA)	**–**	–	**–**	–
17	Of which internal assessment approach (IAA)	**230**	293	**19**	24
18	Of which standardised approach	**–**	–	**–**	–
19	**Market risk**	**1,980**	1,579	**158**	126
20	Of which standardised approach	**253**	152	**20**	12
21	Of which internal model approaches	**1,727**	1,427	**138**	114
22	Large exposures	**–**	–	**–**	–
23	**Operational risk**	**12,059**	11,379	**965**	910
24	Of which basic indicator approach	**–**	–	**–**	–
25	Of which standardised approach	**12,059**	11,379	**965**	910
26	Of which advanced measurement approach	**–**	–	**–**	–
27	Amounts below the thresholds for deduction (subject to 250% risk weight)	**813**	1,136	**65**	91
28	Floor adjustment	**–**	–	**–**	–
29	**Total – transitional**	**75,561**	76,054	**6,045**	6,084

[1] Securitisations are shown separately within this table, however, are included within credit risk throughout the remainder of the disclosures.

Appendix 4: Bank of Scotland Group continued

ANALYSIS OF CREDIT RISK MITIGATION

The following table provides an analysis of credit risk exposures covered by eligible financial collateral and other eligible collateral.

The analysis excludes exposures covered by forms of credit risk mitigation that are not taken into consideration in the calculation of credit risk capital requirements.

Table 104: Bank of Scotland Group eligible financial collateral and other eligible collateral

	2016			2015		
	Exposures covered by eligible financial collateral £m	Exposures covered by other eligible collateral £m	Total £m	Exposures covered by eligible financial collateral £m	Exposures covered by other eligible collateral £m	Total £m
Exposures subject to the IRB approach						
Foundation IRB approach						
Corporate – main	4	3,001	3,005	3	3,140	3,143
Corporate – SME	7	1,436	1,443	9	1,738	1,747
Total – IRB approach	11	4,437	4,448	12	4,878	4,890
Exposures subject to the standardised approach						
Corporates	834	–	834	765	–	765
Institutions	1	–	1	1	–	1
Exposures in default	–	6	6	–	10	10
Total – Standardised approach	835	6	841	766	10	776
Total	846	4,443	5,289	778	4,888	5,666

ANALYSIS OF PAST DUE AND IMPAIRED LOANS AND ADVANCES TO CUSTOMERS

The analysis provided within this section has been presented on an accounting consolidation basis rather than a regulatory consolidation basis.

Analysis by industry

An analysis of past due but not impaired loans and advances to customers and impaired loans and advances to customers as at 31 December 2016, by major industrial sector, is provided in the table below.

Table 105: Bank of Scotland Group past due but not impaired and impaired loans and advances analysed by major industrial sector

	Past due but not impaired 2016		Impaired 2016		Past due but not impaired 2015		Impaired 2015	
	£m	As a % of credit risk exposure	£m	As a % of credit risk exposure	£m	As a % of credit risk exposure	£m	As a % of credit risk exposure
Agriculture, forestry and fishing	18	2.58%	15	2.15%	23	3.51%	19	2.90%
Energy and water supply	1	0.41%	2	0.81%	1	0.31%	32	9.88%
Manufacturing	5	0.81%	11	1.78%	10	0.84%	22	1.85%
Construction	4	0.32%	236	19.00%	17	1.31%	130	10.04%
Transport, distribution and hotels	22	0.61%	111	3.06%	28	0.68%	209	5.11%
Postal and communications	1	5.00%	1	5.00%	–	–	1	3.45%
Property companies	30	0.41%	720	9.85%	47	0.57%	1,246	14.98%
Financial, business and other services	28	0.05%	427	0.71%	43	0.08%	438	0.85%
Personal: mortgages	6,358	2.39%	3,785	1.42%	7,022	2.64%	3,522	1.32%
Personal: other	99	0.42%	369	1.57%	110	0.45%	434	1.79%
Lease financing	–	–	–	–	–	–	–	–
Hire purchase	–	–	82	100.00%	–	–	–	–
Total	6,566	1.78%	5,759	1.56%	7,301	2.02%	6,053	1.67%

Analysis by geography

An analysis of past due but not impaired loans and advances to customers and impaired loans and advances to customers as at 31 December 2016, by geographical region, based on the country of residence of the customer, is provided in the table below.

Table 106: Bank of Scotland Group past due but not impaired and impaired loans and advances analysed by geographical region

	Past due but not impaired		Impaired		Past due but not impaired		Impaired	
	2016		2016		2015		2015	
	£m	As a % of credit risk exposure	£m	As a % of credit risk exposure	£m	As a % of credit risk exposure	£m	As a % of credit risk exposure
United Kingdom	6,177	1.78%	5,442	1.57%	7,004	2.05%	5,602	1.64%
Rest of Europe	388	2.90%	226	1.69%	296	2.27%	360	2.77%
United States of America	1	0.07%	81	5.77%	–	–	72	2.86%
Asia-Pacific	–	–	–	–	–	–	–	–
Other	–	–	10	0.88%	1	0.07%	19	1.42%
Total	6,566	1.78%	5,759	1.56%	7,301	2.02%	6,053	1.67%

ANALYSIS OF SPECIFIC CREDIT RISK ADJUSTMENTS IN RESPECT OF LOANS AND ADVANCES TO CUSTOMERS

The analysis provided within this section has been presented on an accounting consolidation basis rather than a regulatory consolidation basis.

The movement in impairment provisions, from 1 January 2016 to 31 December 2016, in respect of loans and advances to customers is provided below.

Table 107: Bank of Scotland Group movement in impairment provisions (loans and advances to customers)

	2016 £m	2015 £m
At 1 January	2,810	5,683
Exchange and other adjustments	23	(214)
Disposal of businesses	–	–
Advances written off	(1,154)	(3,517)
Recoveries of advances written off in previous years	479	622
Unwinding of discount	11	19
Charge (release) to the income statement	216	217
At 31 December	2,385	2,810

Analysis by industry

An analysis of closing impairment provisions and the net charge to the income statement in respect of loans and advances to customers, by major industrial sector, is provided in the table below.

Table 108: Bank of Scotland Group Impairment provisions and net charge analysed by major industrial sector

	2016		2015	
	Impairment provisions £m	Net charge £m	Impairment provisions £m	Net charge £m
Agriculture, forestry and fishing	2	2	5	1
Energy and water supply	1	7	7	25
Manufacturing	44	(35)	21	–
Construction	66	9	89	2
Transport, distribution and hotels	60	(26)	94	(80)
Postal and communications	1	–	1	–
Property companies	308	(133)	533	(125)
Financial, business and other services	144	139	389	73
Personal: mortgages	1,575	53	1,479	170
Personal: other	184	200	192	151
Lease financing	–	–	–	–
Hire purchase	–	–	–	–
Total	2,385	216	2,810	217

Appendix 4: Bank of Scotland Group continued

Analysis by geography

An analysis of closing impairment provisions and the net charge to the income statement in respect of loans and advances to customers, by geographical region, based on the country of residence of the customer, is provided in the table below.

Table 109: Bank of Scotland Group impairment provisions and net charges analysed by geographical region

	2016		2015	
	Impairment provisions £m	Net charge £m	Impairment provisions £m	Net charge £m
United Kingdom	**2,155**	**306**	2,548	354
Rest of Europe	**216**	**(87)**	231	(11)
United States of America	**2**	**(1)**	20	(29)
Asia-Pacific	**2**	**–**	2	(6)
Other	**10**	**(2)**	9	(91)
Total	**2,385**	**216**	2,810	217

ANALYSIS OF CREDIT RISK EXPOSURES

Table 110: Bank of Scotland Group credit risk exposures

Exposure class	2016 Credit risk exposure £m	2016 Risk-weighted assets £m	2016 Minimum capital requirements £m	2016 Average risk weight %	2016 Average credit risk exposure £m
Exposures subject to the IRB approach					
Foundation IRB approach					
Corporate – main	5,236	2,970	237	57%	6,184
Corporate – SME	2,090	1,280	102	61%	2,544
Corporate – specialised lending	–	–	–	–	–
Central governments and central banks	–	–	–	–	–
Institutions	2,409	209	17	9%	3,381
Retail IRB approach					
Retail mortgages	261,213	30,972	2,478	12%	260,618
of which: residential mortgages (SME)	–	–	–	–	–
of which: residential mortgages (non-SME)	261,213	30,972	2,478	12%	260,618
Qualifying revolving retail exposures	18,556	6,000	480	32%	19,200
Other SME	–	–	–	–	–
Other non-SME	3,059	3,323	266	109%	2,919
Other IRB approaches					
Corporate – specialised lending	4,290	3,167	253	74%	4,835
Equities – exchange traded	–	1	–	290%	19
Equities – private equity	611	1,160	93	190%	646
Equities – other	90	335	27	370%	79
Securitisation positions	2,911	296	24	10%	3,402
Non-credit obligation assets	3,817	1,030	82	27%	3,390
Total – IRB approach	304,282	50,743	4,059	17%	307,217
Exposures subject to the standardised approach					
Central governments and central banks	207	–	–	–	174
Regional governments or local authorities	–	–	–	–	1
Public sector entities	2	2	–	100%	2
Multilateral development banks	61	–	–	–	54
International organisations	–	–	–	–	–
Institutions	44,597	30	2	–	34,635
Corporates	11,583	3,951	316	34%	12,327
Retail	2,735	1,912	153	70%	2,638
Secured by mortgages on immovable property	3,322	1,163	93	35%	3,555
of which: residential property	3,322	1,163	93	35%	3,539
of which: commercial property	–	–	–	–	16
Exposures in default	633	709	57	112%	719
Exposures associated with particularly high risk	–	–	–	–	–
Securitisation positions	–	–	–	–	–
Short term claims on institutions and corporates	–	–	–	–	–
Collective investment undertakings (CIUs)	–	–	–	–	–
Other items[3]	628	383	31	61%	758
Total – standardised approach	63,768	8,150	652	13%	54,863
Total credit risk	368,050	58,893	4,711	16%	362,080
Threshold – significant investments	2	6	–	286%	–
Threshold – deferred tax	323	807	65	250%	349
Total credit risk	368,375	59,706	4,776	16%	362,429

Appendix 4: Bank of Scotland Group continued

Exposure class	2015 Credit risk exposure £m	2015 Risk-weighted assets £m	2015 Minimum capital requirements £m	2015 Average risk weight %	2015 Average credit risk exposure £m
Exposures subject to the IRB approach					
Foundation IRB approach					
Corporate – main	6,793	3,834	307	56%	7,584
Corporate – SME	3,152	2,140	171	68%	3,236
Corporate – specialised lending	–	–	–	–	2
Central governments and central banks	–	–	–	–	1,740
Institutions	4,149	455	36	11%	4,087
Retail IRB approach					
Retail mortgages	261,093	28,269	2,261	11%	257,003
of which: residential mortgages (SME)	–	–	–	–	–
of which: residential mortgages (non-SME)	261,093	28,269	2,261	11%	257,003
Qualifying revolving retail exposures	19,585	6,323	506	32%	18,776
Other SME	–	–	–	–	–
Other non-SME	2,774	3,034	243	109%	2,889
Other IRB approaches					
Corporate – specialised lending	5,269	4,028	322	76%	7,641
Equities – exchange traded	93	269	22	290%	49
Equities – private equity	676	1,285	103	190%	725
Equities – other	45	165	13	370%	39
Securitisation positions	3,653	395	32	11%	3,870
Non-credit obligation assets	3,391	1,013	81	30%	3,312
Total – IRB approach	310,673	51,210	4,097	16%	310,953
Exposures subject to the standardised approach					
Central governments and central banks	168	–	–	–	313
Regional governments or local authorities	1	–	–	20%	–
Public sector entities	2	2	–	100%	8
Multilateral development banks	52	–	–	–	10
International organisations	–	–	–	–	–
Institutions	30,255	27	2	–	39,525
Corporates	13,162	4,171	334	32%	13,697
Retail	2,444	1,697	136	69%	1,673
Secured by mortgages on immovable property	3,791	1,345	107	35%	4,011
of which: residential property	3,763	1,317	105	35%	3,990
of which: commercial property	28	28	2	100%	21
Exposures in default	747	895	72	120%	886
Exposures associated with particularly high risk	–	–	–	–	–
Securitisation positions	–	–	–	–	–
Short term claims on institutions and corporates	–	–	–	–	–
Collective investment undertakings (CIUs)	–	–	–	–	–
Other items[3]	800	514	41	64%	1,594
Total – standardised approach	51,422	8,651	692	17%	61,717
Total credit risk	362,095	59,861	4,789	17%	372,670
Threshold – significant investments	–	–	–	–	–
Threshold – deferred tax	455	1,136	91	250%	381
Total credit risk	362,549	60,997	4,880	17%	373,051

ANALYSIS OF CREDIT RISK EXPOSURES BY INDUSTRY

Credit risk exposures as at 31 December 2016, analysed by major industrial sector, are provided in the table below.

Table 111: Bank of Scotland Group credit risk exposure analysed by major industrial sector

	2016 Agriculture, forestry and fishing £m	2016 Energy and water supply £m	2016 Manufacturing £m	2016 Construction £m	2016 Transport, distribution and hotels £m	2016 Postal and comms £m	2016 Property companies £m	2016 Financial, business and other services £m	2016 Personal: mortgages £m	2016 Personal: other £m	2016 Lease financing £m	2016 Hire purchase £m	2016 Total £m
Exposures subject to the IRB approach													
Foundation IRB approach													
Corporate – main	54	115	352	965	969	13	2,052	716	–	–	–	–	5,236
Corporate – SME	16	4	105	141	522	1	803	498	–	–	–	–	2,090
Corporate – specialised lending	–	–	–	–	–	–	–	–	–	–	–	–	–
Central governments and central banks	–	–	–	–	–	–	–	–	–	–	–	–	–
Institutions	–	–	–	–	–	–	–	2,409	–	–	–	–	2,409
Retail IRB approach	–	–	–	–	–	–	–	–	–	–	–	–	–
Retail mortgages	–	–	–	–	–	–	–	–	261,213	–	–	–	261,213
of which: residential mortgages (SME)	–	–	–	–	–	–	–	–	–	–	–	–	–
of which: residential mortgages (non-SME)	–	–	–	–	–	–	–	–	261,213	–	–	–	261,213
Qualifying revolving retail exposures	–	–	–	–	–	–	–	–	–	18,556	–	–	18,556
Other SME	–	–	–	–	–	–	–	–	–	–	–	–	–
Other non-SME	–	–	–	–	–	–	–	–	–	3,059	–	–	3,059
Other IRB approaches	–	–	–	–	–	–	–	–	–	–	–	–	–
Corporate – specialised lending	–	104	50	36	240	–	3,743	117	–	–	–	–	4,290
Equities – exchange traded	–	–	–	–	–	–	–	–	–	–	–	–	–
Equities – private equity	–	–	–	–	30	–	35	546	–	–	–	–	611
Equities – other	–	–	–	–	–	–	–	90	–	–	–	–	90
Securitisation positions	–	–	–	–	–	–	–	2,911	–	–	–	–	2,911
Total – IRB approach	70	223	507	1,142	1,761	14	6,633	7,287	261,213	21,615	–	–	300,465
Exposures subject to the standardised approach													
Central governments and central banks	–	–	–	–	–	–	–	207	–	–	–	–	207
Regional governments or local authorities	–	–	–	–	–	–	–	–	–	–	–	–	–
Public sector entities	–	–	–	–	–	–	–	2	–	–	–	–	2
Multilateral development banks	–	–	–	–	–	–	–	61	–	–	–	–	61
International organisations	–	–	–	–	–	–	–	–	–	–	–	–	–
Institutions	–	–	–	–	–	–	–	44,597	–	–	–	–	44,597
Corporates	349	20	83	65	1,691	5	405	7,989	70	897	9	–	11,583
Retail	268	3	23	19	148	1	225	175	883	908	–	82	2,735
Secured by mortgages on immovable property	–	–	–	–	–	–	–	–	3,322	–	–	–	3,322
of which: residential property	–	–	–	–	–	–	–	–	3,322	–	–	–	3,322
of which: commercial property	–	–	–	–	–	–	–	–	–	–	–	–	–
Exposures in default	11	–	5	15	24	–	50	15	432	81	–	–	633
Exposures associated with particularly high risk	–	–	–	–	–	–	–	–	–	–	–	–	–
Covered bonds	–	–	–	–	–	–	–	–	–	–	–	–	–
Securitisation positions	–	–	–	–	–	–	–	–	–	–	–	–	–
Short term claims on institutions and corporates	–	–	–	–	–	–	–	–	–	–	–	–	–
Collective investment undertakings (CIUs)	–	–	–	–	–	–	–	–	–	–	–	–	–
Equity Exposures	–	–	–	–	–	–	–	–	–	–	–	–	–
Total – standardised approach	628	23	111	99	1,863	6	680	53,046	4,707	1,886	9	82	63,140
Total	698	246	618	1,241	3,624	20	7,313	60,333	265,920	23,501	9	82	363,605
Other items													628
Non-credit obligation assets													3,817
Total credit risk exposure													368,050

Appendix 4: Bank of Scotland Group continued

	2015 Agriculture, forestry and fishing £m	2015 Energy and water supply £m	2015 Manufacturing £m	2015 Construction £m	2015 Transport, distribution and hotels £m	2015 Postal and comms £m	2015 Property companies £m	2015 Financial, business and other services £m	2015 Personal: mortgages £m	2015 Personal: other £m	2015 Lease financing £m	2015 Hire purchase £m	2015 Total £m
Exposures subject to the IRB approach													
Foundation IRB approach													
Corporate – main	11	111	499	971	1,017	21	2,200	1,960	–	3	–	–	6,793
Corporate – SME	17	10	437	125	880	1	945	737	–	–	–	–	3,152
Corporate – specialised lending	–	–	–	–	–	–	–	–	–	–	–	–	–
Central governments and central banks	–	–	–	–	–	–	–	–	–	–	–	–	–
Institutions	–	–	–	–	–	–	–	4,149	–	–	–	–	4,149
Retail IRB approach													
Retail mortgages	–	–	–	–	–	–	–	–	261,093	–	–	–	261,093
of which: residential mortgages (SME)	–	–	–	–	–	–	–	–	–	–	–	–	–
of which: residential mortgages (non-SME)	–	–	–	–	–	–	–	–	261,093	–	–	–	261,093
Qualifying revolving retail exposures	–	–	–	–	–	–	–	–	–	19,585	–	–	19,585
Other SME	–	–	–	–	–	–	–	–	–	–	–	–	–
Other non-SME	–	–	–	–	–	–	–	–	–	2,774	–	–	2,774
Other IRB approaches													
Corporate – specialised lending	–	191	63	77	322	–	4,345	270	–	–	–	–	5,269
Equities – exchange traded	–	–	–	–	–	–	93	–	–	–	–	–	93
Equities – private equity	–	–	–	–	31	–	79	566	–	–	–	–	676
Equities – other	–	–	–	–	–	–	–	45	–	–	–	–	45
Securitisation positions	–	–	–	–	–	–	–	3,653	–	–	–	–	3,653
Total – IRB approach	28	312	999	1,173	2,250	22	7,662	11,380	261,093	22,362	–	–	307,282
Exposures subject to the standardised approach													
Central governments and central banks	–	–	–	–	–	–	–	168	–	–	–	–	168
Regional governments or local authorities	–	–	–	–	–	–	–	1	–	–	–	–	1
Public sector entities	–	–	–	–	–	–	–	2	–	–	–	–	2
Multilateral development banks	–	–	–	–	–	–	–	52	–	–	–	–	52
International organisations	–	–	–	–	–	–	–	–	–	–	–	–	–
Institutions	–	–	–	–	–	–	–	30,255	–	–	–	–	30,255
Corporates	357	10	160	85	1,565	5	396	9,538	82	949	7	8	13,162
Retail	257	2	22	23	146	2	202	168	789	795	–	38	2,444
Secured by mortgages on immovable property	–	–	–	–	–	–	–	28	3,763	–	–	–	3,791
of which: residential property	–	–	–	–	–	–	–	–	3,763	–	–	–	3,763
of which: commercial property	–	–	–	–	–	–	–	28	–	–	–	–	28
Exposures in default	13	–	6	14	128	–	56	27	399	102	1	1	747
Exposures associated with particularly high risk	–	–	–	–	–	–	–	–	–	–	–	–	–
Covered bonds	–	–	–	–	–	–	–	–	–	–	–	–	–
Securitisation positions	–	–	–	–	–	–	–	–	–	–	–	–	–
Short term claims on institutions and corporates	–	–	–	–	–	–	–	–	–	–	–	–	–
Collective investment undertakings (CIUs)	–	–	–	–	–	–	–	–	–	–	–	–	–
Equity Exposures	–	–	–	–	–	–	–	–	–	–	–	–	–
Total – standardised approach	627	12	188	122	1,839	7	654	40,239	5,033	1,846	8	47	50,622
Total	655	324	1,187	1,295	4,089	29	8,316	51,619	266,126	24,208	8	47	357,904
Other items													800
Non-credit obligation assets													3,391
Total credit risk exposure													362,095

ANALYSIS OF CREDIT RISK EXPOSURES BY GEOGRAPHY

Credit risk exposures as at 31 December 2016, analysed by major geographical region, based on the country of residence/incorporation of the customer, are provided in the table below.

Table 112: Bank of Scotland Group credit risk exposures analysed by geographical region

	2016 United Kingdom £m	2016 Rest of Europe £m	2016 United States of America £m	2016 Asia-Pacific £m	2016 Other £m	2016 Total £m	2015 United Kingdom £m	2015 Rest of Europe £m	2015 United States of America £m	2015 Asia-Pacific £m	2015 Other £m	2015 Total £m
Exposures subject to the IRB approach												
Foundation IRB approach												
Corporate – main	5,098	82	22	–	34	5,236	5,541	86	1,011	–	155	6,793
Corporate – SME	2,054	27	–	–	9	2,090	3,135	10	–	–	7	3,152
Corporate – specialised lending	–	–	–	–	–	–	–	–	–	–	–	–
Central governments and central banks	–	–	–	–	–	–	–	–	–	–	–	–
Institutions	1,098	1,293	16	1	1	2,409	1,322	2,385	15	–	427	4,149
Retail IRB approach												
Retail mortgages	251,713	9,500	–	–	–	261,213	253,109	7,984	–	–	–	261,093
of which: residential mortgages (SME)	–	–	–	–	–	–	–	–	–	–	–	–
of which: residential mortgages (non-SME)	251,713	9,500	–	–	–	261,213	253,109	7,984	–	–	–	261,093
Qualifying revolving retail exposures	18,556	–	–	–	–	18,556	19,585	–	–	–	–	19,585
Other SME	–	–	–	–	–	–	–	–	–	–	–	–
Other non-SME	3,059	–	–	–	–	3,059	2,774	–	–	–	–	2,774
Other IRB approaches												
Corporate – specialised lending	3,604	401	56	42	187	4,290	4,268	724	56	40	181	5,269
Equities – exchange traded	–	–	–	–	–	–	93	–	–	–	–	93
Equities – private equity	496	56	56	3	–	611	525	54	50	5	42	676
Equities – other	90	–	–	–	–	90	39	6	–	–	–	45
Securitisation positions1	1,644	110	1,157	–	–	2,911	2,286	150	1,217	–	–	3,653
Total – IRB approach	287,412	11,469	1,307	46	231	300,465	292,677	11,399	2,349	45	812	307,282
Exposures subject to the standardised approach												
Central governments and central banks	114	93	–	–	–	207	70	98	–	–	–	168
Regional governments or local authorities	–	–	–	–	–	–	1	–	–	–	–	1
Public sector entities	2	–	–	–	–	2	2	–	–	–	–	2
Multilateral development banks	–	61	–	–	–	61	–	52	–	–	–	52
International organisations	–	–	–	–	–	–	–	–	–	–	–	–
Institutions	44,495	102	–	–	–	44,597	30,167	88	–	–	–	30,255
Corporates	10,429	160	97	2	895	11,583	12,197	248	170	31	516	13,162
Retail	1,450	1,278	1	–	6	2,735	1,523	912	1	–	8	2,444
Secured by mortgages on immovable property	3,157	165	–	–	–	3,322	3,613	178	–	–	–	3,791
of which: residential property	3,157	165	–	–	–	3,322	3,613	150	–	–	–	3,763
of which: commercial property	–	–	–	–	–	–	–	28	–	–	–	28
Exposures in default	599	34	–	–	–	633	705	42	–	–	–	747
Exposures associated with particularly high risk	–	–	–	–	–	–	–	–	–	–	–	–
Covered bonds	–	–	–	–	–	–	–	–	–	–	–	–
Securitisation positions	–	–	–	–	–	–	–	–	–	–	–	–
Short term claims on institutions and corporates	–	–	–	–	–	–	–	–	–	–	–	–
Collective investment undertakings (CIUs)	–	–	–	–	–	–	–	–	–	–	–	–
Equity exposures	–	–	–	–	–	–	–	–	–	–	–	–
Total – standardised approach	60,246	1,893	98	2	901	63,140	48,278	1,618	171	31	524	50,622
Total	347,658	13,362	1,405	48	1,132	363,605	340,955	13,017	2,520	76	1,336	357,904
Other items						628						800
Non-credit obligation assets						3,817						3,391
Total credit risk exposure						368,050						362,095

Appendix 4: Bank of Scotland Group continued

ANALYSIS OF CREDIT RISK EXPOSURES BY RESIDUAL MATURITY

Credit risk exposures as at 31 December 2016, analysed by residual contractual maturity, are provided in the table below

Table 113: Bank of Scotland credit risk exposures analysed by residual contractual maturity

	2016 On demand £m	2016 Repayable in 3 months or less £m	2016 Repayable between 3 months and 1 year £m	2016 Repayable between 1 and 5 years £m	2016 Repayable over 5 years or undated £m	2016 Total £m	2015 On demand £m	2015 Repayable in 3 months or less £m	2015 Repayable between 3 months and 1 year £m	2015 Repayable between 1 and 5 years £m	2015 Repayable over 5 years or undated £m	2015 Total £m
Exposures subject to the IRB approach												
Foundation IRB approach												
Corporate – main	**153**	**301**	**521**	**1,937**	**2,324**	**5,236**	70	232	1,528	2,549	2,414	6,793
Corporate – SME	**24**	**144**	**350**	**738**	**834**	**2,090**	20	122	752	1,185	1,073	3,152
Corporate – specialised lending	**–**	**–**	**–**	**–**	**–**	**–**	–	–	–	–	–	–
Central governments and central banks	**–**	**–**	**–**	**–**	**–**	**–**	–	–	–	–	–	–
Institutions	**–**	**92**	**286**	**1,635**	**396**	**2,409**	–	60	308	2,702	1,079	4,149
Retail IRB approach												
Retail mortgages	**972**	**467**	**11,173**	**12,671**	**235,930**	**261,213**	736	471	10,410	12,808	236,668	261,093
of which: residential mortgages (SME)	**–**	**–**	**–**	**–**	**–**	**–**	–	–	–	–	–	–
of which: residential mortgages (non-SME)	**972**	**467**	**11,173**	**12,671**	**235,930**	**261,213**	736	471	10,410	12,808	236,668	261,093
Qualifying revolving retail exposures	**18,556**	**–**	**–**	**–**	**–**	**18,556**	19,585	–	–	–	–	19,585
Other SME	**–**	**–**	**–**	**–**	**–**	**–**	–	–	–	–	–	–
Other non-SME	**–**	**63**	**353**	**2,315**	**328**	**3,059**	–	50	282	2,122	320	2,774
Other IRB approaches												
Corporate – specialised lending	**65**	**341**	**618**	**1,374**	**1,892**	**4,290**	24	317	544	1,831	2,553	5,269
Equities – exchange traded	**–**	**–**	**–**	**–**	**–**	**–**	–	–	–	–	93	93
Equities – private equity	**–**	**–**	**–**	**–**	**611**	**611**	–	–	–	–	676	676
Equities – other	**–**	**–**	**–**	**–**	**90**	**90**	–	–	–	–	45	45
Securitisation positions	**–**	**747**	**1,507**	**280**	**377**	**2,911**	–	237	917	2,091	408	3,653
Total – IRB approach	**19,770**	**2,155**	**14,808**	**20,950**	**242,782**	**300,465**	20,435	1,489	14,741	25,288	245,329	307,282
Exposures subject to the standardised approach												
Central governments and central banks	**93**	**–**	**–**	**–**	**114**	**207**	97	–	–	–	71	168
Regional governments or local authorities	**–**	**–**	**–**	**–**	**–**	**–**	–	–	–	–	1	1
Public sector entities	**–**	**–**	**–**	**–**	**2**	**2**	–	–	–	–	2	2
Multilateral development banks	**–**	**–**	**–**	**61**	**–**	**61**	–	–	–	–	52	52
International organisations	**–**	**–**	**–**	**–**	**–**	**–**	–	–	–	–	–	–
Institutions	**6**	**96**	**–**	**–**	**44,495**	**44,597**	5	83	–	–	30,167	30,255
Corporates	**–**	**106**	**940**	**731**	**9,806**	**11,583**	–	95	719	726	11,622	13,162
Retail	**76**	**28**	**62**	**790**	**1,779**	**2,735**	93	32	60	538	1,721	2,444
Secured by mortgages on immovable property	**18**	**27**	**103**	**359**	**2,815**	**3,322**	16	29	107	405	3,234	3,791
of which: residential property	**18**	**27**	**103**	**359**	**2,815**	**3,322**	16	29	107	377	3,234	3,763
of which: commercial property	**–**	**–**	**–**	**–**	**–**	**–**	–	–	–	28	–	28
Exposures in default	**40**	**12**	**42**	**81**	**458**	**633**	41	18	39	90	559	747
Exposures associated with particularly high risk	**–**	**–**	**–**	**–**	**–**	**–**	–	–	–	–	–	–
Covered bonds	**–**	**–**	**–**	**–**	**–**	**–**	–	–	–	–	–	–
Securitisation positions	**–**	**–**	**–**	**–**	**–**	**–**	–	–	–	–	–	–
Short term claims on institutions and corporates	**–**	**–**	**–**	**–**	**–**	**–**	–	–	–	–	–	–
Collective investment undertakings (CIUs)	**–**	**–**	**–**	**–**	**–**	**–**	–	–	–	–	–	–
Equity exposures	**–**	**–**	**–**	**–**	**–**	**–**	–	–	–	–	–	–
Total – standardised approach	**233**	**269**	**1,147**	**2,022**	**59,469**	**63,140**	252	257	925	1,759	47,429	50,622
Total	**20,003**	**2,424**	**15,955**	**22,972**	**302,251**	**363,605**	20,687	1,746	15,666	27,047	292,758	357,904
Other items						**628**						800
Non-credit obligation assets						**3,817**						3,391
Total credit risk exposure						**368,050**						362,095

Appendix 5: EBA early adoption tables

Listed below is a summary of those EBA templates which the Group has early adopted for 2016 year end reporting.

Risk-weighted assets flow statements of CCR exposures under the Internal Model Method (CCR7) is not applicable for the Group, however, a full risk-weighted assets flow table for CCR exposures has been presented on page 88.

Appendix 6: CRR mapping

CRR ref	High-level summary	Compliance reference
Scope of disclosure requirements		
431 (1)	Requirement to publish Pillar 3 disclosures.	Lloyds Banking Group publishes Pillar 3 disclosures.
431 (2)	Firms with permission to use specific operational risk methodologies must disclose operational risk information.	ARA – Pages 152-153 (Operational Risk) The Group's operational risk systems, mitigation and approach to capital requirements are disclosed in ARA Risk Management Section
431 (3)	Institution must have a policy covering frequency of disclosures, their verification, comprehensiveness and appropriateness. Institution must also have policies for assessing whether their disclosures convey their risk profile comprehensively to market participants.	Pillar 3 – Page 4 (Disclosure Policy) Lloyds Banking Group has a Pillar 3 Policy Pillar 3 – Page 10 (The Group's Approach to Risk)
431 (4)	Explanation of ratings decision upon request.	Not applicable
Non-material, proprietary or confidential information		
432 (1)	Institutions may omit information that is not material if certain conditions are respected.	Pillar 3 – Page 4 (Basis of Preparation) Limited disclosure on Trading Book securitisations given its relative materiality.
432 (2)	Institutions may omit information that is proprietary or confidential if certain conditions are respected	Not applicable
432 (3)	Where 432 (2) applies this must be stated in the disclosures, and more general information must be disclosed.	Not applicable
432 (4)	Use of 432 (1), (2) or (3) is without prejudice to scope of liability for failure to disclose material information.	Not applicable
Frequency of disclosure		
433	Disclosures must be published once a year at a minimum and more frequently if necessary	Pillar 3 – Page 4 (Frequency, media and location)
Means of disclosure		
434 (1)	To include all disclosures in one appropriate medium, or provide clear cross-references.	Pillar 3 – Page 4 (Frequency, media and location) Most disclosures are contained within this document.
434 (2)	Disclosures made under other requirements (e.g. accounting) can be used to satisfy Pillar 3 if appropriate.	Any cross-references to accounting or other disclosures are clearly signposted in this document where appropriate.
Risk management objectives and policies		
435 (1)	Disclose information on:	
435 (1) (a)	The strategies and processes to manage risks	ARA – Pages 115-169 (Risk Management Section)
435 (1) (b)	Structure and organisation of risk management function	ARA – Page 119 (How Risk is managed in Lloyds Banking Group)
435 (1) (c)	Risk reporting and measurement systems	ARA – Pages 115-169 (Risk Management Section)
435 (1) (d)	Hedging and mitigating risk – policies and processes	ARA – Pages 115-169 (Risk Management Section)
435 (1) (e)	A declaration of adequacy of risk management arrangements approved by the Board	ARA – Pages 67 (Corporate Governance) Reference to this is made on page 4 of the Pillar 3 disclosures (Introduction)
435 (1) (f)	Concise risk statement approved by the Board.	
435 (2)	Information on governance arrangements, including information on Board composition and recruitment and risk committees.	ARA – Pages 60-80 (Corporate Governance) ARA – Page 121 (Risk Governance)
435 (2) (a)	Number of directorships held by Board members	ARA – Pages 54-57 (Board of Directors)
435 (2) (b)	Recruitment policy for selection of Board members, their actual knowledge, skills and expertise.	ARA – Pages 54-57 & 60 (Corporate Governance)
435 (2) (c)	Policy on diversity of Board membership and results against targets.	ARA – Page 70 (Corporate Governance)
435 (2) (d)	Disclosure of whether a dedicated risk committee is in place, and number of meeting in the year.	ARA – Page 76 (Board Risk Committee Report)
435 (2) (e)	Description of information flow on risk to Board	ARA – Page 63 (Corporate Governance)
Scope of application		
436 (a)	Name of institution.	Pillar 3 – Page 3 (Introduction)
436 (b)	Difference in basis of consolidation for accounting and prudential purposes, describing entities that are:	Pillar 3 – Page 5 (Scope of Consolidation) Details of the scope of consolidation applied to Lloyds Banking Group are outlined in the diagram referred to on Page 6.
436 (b) (i)	Fully consolidated;	
436 (b) (ii)	Proportionally consolidated;	
436 (b) (iii)	Deducted from own funds;	
436 (b) (iv)	Neither consolidated nor deducted.	
436 (c)	Impediments to transfer of own funds between parent and subsidiaries.	Not applicable

CRR ref	High-level summary	Compliance reference
436 (d)	Capital shortfalls in any subsidiaries outside the scope of consolidation.	ARA – Pages 159-166 (Capital Risk) The Group actively manages the capital of its subsidiaries to ensure these remain appropriately capitalised.
436 (e)	Making use of articles on derogations from a) prudential requirements or b) liquidity requirements for individual subsidiaries/entities.	Pillar 3 – Page 5 (Scope of Consolidation) LBG makes use of these provisions according to its waiver from the PRA.
Own funds		
437 (1)	Disclose the following information regarding own funds:	
437 (1) (a)	a full reconciliation of Common Equity Tier 1 items, Additional Tier 1 items, Tier 2 items and filters and deductions applied pursuant to Articles 32 to 35, 36, 56, 66 and 79 to own funds of the institution and the balance sheet in the audited financial statements of the institution;	Pillar 3 – Page 116 (Table 75: Lloyds Banking Group Own Funds Reconciliation) Pillar 3 – Page 124 (Table 82: Lloyds Bank Group Own Funds Reconciliation) Pillar 3 – Page 141 (Table 99: Bank of Scotland Group Own Funds Reconciliation)
437 (1) (b)	a description of the main features of the Common Equity Tier 1 and Additional Tier 1 instruments and Tier 2 instruments issued by the institution;	Pillar 3 Capital Instruments Disclosure separately disclosed on Group website http://www.lloydsbankinggroup.com/investors/financial-performance/other-disclosures/
437 (1) (c)	the full terms and conditions of all Common Equity Tier 1, Additional Tier 1 and Tier 2 instruments;	Separately disclosed on Group website http://www.lloydsbankinggroup.com/investors/financial-performance/other-disclosures/
437 (1) (d)	disclosure of the nature and amounts of the following:	Pillar 3 – Page 116 (Table 75: Lloyds Banking Group Own Funds Reconciliation) Pillar 3 – Page 124 (Table 82: Lloyds Bank Group Own Funds Reconciliation) Pillar 3 – Page 141 (Table 99: Bank of Scotland Group Own Funds Reconciliation)
437 (1) (d) (i)		
437 (1) (d) (ii)	each deduction made pursuant to Articles 36, 56 and 66;	
437 (1) (d) (iii)	items not deducted in accordance with Articles 47, 48, 56, 66 and 79;	
437 (1) (e)	a description of all restrictions applied to the calculation of own funds in accordance with this Regulation and the instruments, prudential filters and deductions to which those restrictions apply;	
437 (1) (f)	where institutions disclose capital ratios calculated using elements of own funds determined on a different basis	Not applicable
Capital requirements		
438 (a)	Summary of institution's approach to assessing adequacy of capital levels.	Pillar 3 – Page 19 (The Group's approach to Capital Risk)
438 (b)	Result of ICAAP on demand from authorities.	Not applicable
438 (c)	Capital requirements for each Standardised approach credit risk exposure class.	Pillar 3 – Page 53 and Page 54 (Table 22: Credit risk exposures)
438 (d)	Capital requirements for each Internal Ratings Based Approach credit risk exposure class.	
438 (e)	Capital requirements for market risk or settlement risk.	Pillar 3 – Page 98 (Table 61: Market risk own funds requirements)
438 (f)	Capital requirements for operational risk, separately for the Basic Indicator Approach, the Standardised Approach, and the Advanced Measurement Approaches as applicable.	Pillar 3 – Page 107 (Operational Risk)
438 (endnote)	Requirement to disclose specialised lending exposures and equity exposures in the banking book falling under the simple risk weight approach.	Pillar 3 – Page 67 (Table 34A: IRB (Specialised lending (CR10) and Page 68 (Table 34B: Equity exposures subject to the simple risk weight method (CR10)
Exposure to counterparty credit risk (CCR)		
439 (a)	Description of process to assign internal capital and credit limits to CCR exposures.	Pillar 3 – Page 89 (Internal capital and credit limits)
439 (b)	Discussion of policies for securing collateral and establishing credit reserves.	Pillar 3 – Page 89 (Securing collateral and establishing credit reserves)
439 (c)	Discussion of management of wrong-way risk exposures.	Pillar 3 – Page 89 (Correlation (Wrong Way) Risk)
439 (d)	Disclosure of collateral to be provided (outflows) in the event of a ratings downgrade.	Pillar 3 – Page 89 (Collateral requirements in the event of a downgrade in credit rating)
439 (e)	Derivation of net derivative credit exposure.	Pillar 3 – Page 97 (Table 59: Net derivatives credit exposures)
439 (f)	Exposure values for mark-to-market, original exposure, standardised and internal model methods.	Pillar 3 – Page 90 (Table 50: CCR: analysis by measurement approach)
439 (g)	Notional value of credit derivative hedges and current credit exposure by type of exposure.	Pillar 3 – Page 97 (Table 60: Notional value of credit derivative transactions)
439 (h)	Notional amounts of credit derivative transactions.	
439 (i)	Estimate of alpha, if applicable.	Not applicable

Appendix 6: CRR mapping continued

CRR ref	High-level summary	Compliance reference
Capital buffers		
440 (1) (a)	Geographical distribution of relevant credit exposures for calculation of countercyclical capital buffer.	Pillar 3 – Page 120 (Table 79: Lloyds Banking Group Countercyclical capital buffer) Pillar 3 – Page 127 (Table 85: Lloyds Bank Group Countercyclical capital buffer) Pillar 3 – Page 144 (Table 102: Bank of Scotland Group Countercyclical capital buffer)
440 (1) (b)	Amount of the institution specific countercyclical capital buffer.	
Indicators of global systemic importance		
441 (1)	Disclosure of the indicators of global systemic importance.	The Group's G-SIB metrics are separately disclosed on the Group's website. http://www.lloydsbankinggroup.com/investors/financial-performance/other-disclosures/
Credit risk adjustments		
442 (a)	Disclosure of bank's definitions of past due and impaired.	Pillar 3 – Page 46 (Past due exposures, impaired exposures and impairment provisions)
442 (b)	Approaches for calculating specific and general credit risk adjustments.	Pillar 3 – Page 46 to Page 49 (Past due exposures, impaired exposures and impairment provisions)
442 (c)	Disclosure of pre-CRM EAD by exposure class.	Pillar 3 – Page 53 (Table 22: Credit risk exposures)
442 (d)	Disclosure of pre-CRM EAD by geography and exposure class	Pillar 3 – Page 74 (Table 39: Credit risk exposures analysed by geographical region)
442 (e)	Disclosure of pre-CRM EAD by industry and exposure class.	Pillar 3 – Page 72 (Table 38: Credit risk exposures analysed by major industrial sector)
442 (f)	Disclosure of pre-CRM EAD by residual maturity and exposure class.	Pillar 3 – Page 77 (Table 41: Credit risk exposures analysed by residual contractual maturity)
442 (g) (i), (ii), (iii)	Breakdown of impaired, past due, specific and general credit risk adjustments, and impairment charges for the period, by industry.	Pillar 3 – Page 47 (Table 15: Past due exposures by industry) Pillar 3 – Page 49 (Table 19: Impairment provisions by industry)
442 (h)	Impaired, past due exposures, by geographical area, and amounts of specific and general impairment for each geography.	Pillar 3 – Page 47 (Table 16: Past due exposures by geography) Pillar 3 – Page 49 (Table 20: Impairment provisions by geography)
442 (i), (ii), (iii), (iv), (v)	Reconciliation of changes in specific and general credit risk adjustments for impaired exposures.	Pillar 3 – Page 48 (Table 17: Movement in impairment provisions) and Page 48 (Table 18: Movement in acquisition related fair value adjustments, loans and advances to customers)
442 (endnote)	Specific credit risk adjustments recorded to income statement are disclosed separately.	
Unencumbered assets		
443	Disclosures on unencumbered assets.	Pillar 3 – Page 121 (Appendix 2: Asset Encumbrance)
Use of ECAIs		
444 (a)	Names of the ECAIs used in the calculation of Standardised approach risk-weighted assets and reasons for any changes.	Pillar 3 – Page 35 (Exposures subject to the Standardised Approach)
444 (b)	Exposure classes associated with each ECAI.	
444 (c)	Description of the process used to transfer credit assessments to non-trading book items.	
444 (d)	Mapping of external rating to CQS.	Not applicable The Group complies with the standard association published on the EBA website
444 (e)	Exposure value pre and post-credit risk mitigation, by CQS.	Pillar 3 – Page 70 (Table 36: Standardised credit risk exposures) Pillar 3 – Page 71 (Table 37: Standardised credit risk exposures by asset class and risk weight)
Exposure to market risk		
445	Disclosure of position risk, large exposures exceeding limits, FX, settlement and commodities risk.	Pillar 3 – Page 98-106 (Market risk)
Operational risk		
446	Scope of approaches used to calculate operational risk.	Pillar 3 – Page 13 (Pillar 1 capital requirements: approaches by risk type)

CRR ref	High-level summary	Compliance reference
Exposure in equities not included in the trading book		
447 (a)	Differentiation of exposures based on objectives and an overview of accounting techniques and valuation methodologies.	Pillar 3 – Page 69 (Non-Trading Book exposures in equities) This outlines the appropriate cross referencing to the ARA.
447 (b)	The balance sheet value, the fair value and, for those exchange-traded, a comparison to the market price where it is materially different from the fair value.	Pillar 3 – Page 69 (Table 35: Analysis of non-trading book exposures in equities)
447 (c)	The types, nature and amounts of exchange-traded exposures, private equity exposures in sufficiently diversified portfolios, and other exposures.	Pillar 3 – Page 69 (Non-Trading Book exposures in equities)
447 (d)	Realised gains or losses arising from sales and liquidations in the period.	Pillar 3 – Page 69 (Analysis of non-trading book exposures in equities)
447 (e)	Total unrealised gains or losses, the total latent revaluation gains or losses, and any of these amounts included in the original or additional own funds.	Pillar 3 – Page 69 (Analysis of non-trading book exposures in equities)
Exposure to interest rate risk on positions not included in the trading book		
448 (a)	Nature of the interest rate risk and the key assumptions, and frequency of measurement of the interest rate risk.	ARA – Pages 148 and 149 (Banking activities)
448 (b)	Variation in earnings, economic value or other relevant measure used by the bank for upward and downward rate shocks according to the banks method for measuring the interest rate risk, broken down by currency.	
Exposure to securitisation positions		
449 (a)	Objectives in relation to securitisation activity.	Pillar 3 – Page 80 (Banking book securitisation strategy and roles)
449 (b)	Nature of other risks in securitised assets, including liquidity.	Pillar 3 – Page 80 (Trading book securitisation strategy and roles) & Page 81 (Risks inherent in banking book securitised assets)
449 (c)	Risks in re-securitisation activity stemming from seniority of underlying securitisations and ultimate underlying assets.	Not applicable
449 (d)	The roles played by the institution in the securitisation process.	Pillar 3 – Page 80 (Banking book securitisation strategy and roles)
449 (e)	Indication of the extent of involvement in roles.	Pillar 3 – Page 81 (Table 42: Summary of securitisation exposures and capital requirements)
449 (f)	Processes in place to monitor changes in credit and market risks of securitisation exposures, and how the processes differ for re-securitisation exposures.	Pillar 3 – Page 82 (Monitoring changes in the credit risk of securitised exposures) & (Monitoring changes in the credit risk of ABS portfolios)
449 (g)	Description of the institution's policies with respect to hedging and unfunded protection, and identification of material hedge counterparties.	Pillar 3 – Page 85 (Use of credit derivatives and guarantees)
449 (h)	Approaches to the calculation of risk-weighted assets for securitisations mapped to types of exposures.	Pillar 3 – Page 81 (Table 42: Summary of securitisation exposures and capital requirements)
449 (i)	Types of SSPEs used to securitise third-party exposures as a sponsor.	Pillar 3 – Page 85 (Sponsored and invested securitisations)
449 (j) (i-vi)	Summary of accounting policies for securitisations.	Pillar 3 – Page 84 (Accounting treatment)
449 (k)	Names of ECAIs used for securitisations and type.	Pillar 3 – Page 83 (Originated securitisations – regulatory treatment) Pillar 3 – Page 86 (Sponsored and invested securitisations – capital assessment)
449 (l)	Full description of Internal Assessment Approach.	Pillar 3 – Page 86 (Capital assessment)
449 (m)	Explanation of significant changes in quantitative disclosures.	Key movements explained where applicable under relevant tables
449 (n)	As appropriate, separately for the Banking and trading book securitisation exposures:	
449 (n) (i)	Amount of outstanding exposures securitised;	Pillar 3 – Page 81 (Table 42: Summary of securitisation exposures and capital requirements)
449 (n) (ii)	On balance sheet securitisation retained or purchased, and off balance sheet exposures;	Pillar 3 – Page 83 and 84 (Table 45 and Table 46: Analysis of originated positions by risk weight category) Pillar 3 – Page 86 (Table 47: Analysis of sponsored positions by risk weight category) Pillar 3 – Page 87 (Table 48: Analysis of invested positions by risk weight category)
449 (n) (iii)	Amount of assets awaiting securitisation;	Pillar 3 – Page 85 (Assets awaiting securitisation)
449 (n) (iv)	Early amortisation treatment; aggregate drawn exposures, capital requirements.	Not applicable

Appendix 6: CRR mapping continued

CRR ref	High-level summary	Compliance reference
449 (n) (v)	Deducted or 1,250%-weighted securitisation positions.	Pillar 3 – Page 81 (Table 42: Summary of securitisation exposures and capital requirements)
449 (n) (vi)	Securitisation activity including the amount of exposures securitised and recognised gains or losses on sales;	Pillar 3 – Page 81 (Securitisation programmes and activity)
449 (o)	Banking and trading book securitisations.	Pillar 3 – Page 83 and Page 84 (Table 45 and Table 46: Analysis of originated positions by risk weight category) Pillar 3 – Page 86 (Table 47: Analysis of sponsored positions by risk weight category) Pillar 3 – Page 87 (Table 48: Analysis of invested positions by risk weight category)
449 (o) (i)	Retained and purchased positions and associated capital requirements, broken down by risk-weight bands.	
449 (o) (ii)	Retained and purchased re-securitisation positions before and after hedging and insurance; exposure to financial guarantors broken down by guarantor credit worthiness.	Not applicable
449 (p)	Impaired assets and recognised losses related to banking book securitisations, by exposure type.	Pillar 3 – Page 83 (Table 44: Analysis of gross securitised exposures on a regulatory basis)
449 (q)	Exposure and capital requirements for trading book securitisations, separated into traditional and synthetic.	Pillar 3 – Page 82 (Table 43: Value of exposures of retained and purchased positions in the banking and trading book by exposure type)
449 (r)	Whether the institution has provided non-contractual financial support to securitisation vehicles.	Not applicable
Remuneration disclosure		
450	Remuneration disclosures (Material Risk Takers).	Pillar 3 – Page 108-113 (Remuneration disclosures) contain the remuneration awards made to the Group's Material Risk Takers. Refer to the Directors' Remuneration Report of the 2016 Lloyds Banking Group ARA for other remuneration disclosures
Leverage		
451 (1) (a) 451 (1) (b) 451 (1) (c)	Leverage ratio, and breakdown of total exposure measure, including reconciliation to financial statements, and derecognised fiduciary items.	Pillar 3 – Table 5, Table 76 to Table 78 for Lloyds Banking Group Pillar 3 – Table 83 and Table 84 for Lloyds Bank Group Pillar 3 – Table 100 and Table 101 for Bank of Scotland Group
451 (1) (d) 451 (1) (e)	Description of the processes used to manage the risk of excessive leverage, and factors that impacted the leverage ratio during the year.	Pillar 3 – Page 119 (Description of the processes used to manage the risk of excessive leverage)
Use of the IRB approach to credit risk		
452 (a)	Permission for use of the IRB approach from the competent authority.	Pillar 3 – Page 37 (Scope of the IRB permission)
452 (b)	Explanation of:	
452 (b) (i)	Internal rating scales, mapped to external ratings;	Pillar 3 – Page 36 (Internal Ratings Scales)
452 (b) (ii)	Use of internal ratings for purposes other than capital requirement calculations;	Pillar 3 – Page 39 (Other application of IRB model outputs)
452 (b) (iii)	Management and recognition of credit risk mitigation;	Pillar 3 – Page 32 to Page 34 (Credit risk mitigation)
452 (b) (iv)	Controls around ratings systems.	Pillar 3 – Page 38 (Internal development and monitoring of IRB models)
452 (c) (i)-(v)	Description of ratings processes for each IRB asset class, provided separately.	Pillar 3 – Page 37 and Page 38 (Scope of the IRB permission and Internal development and monitoring of IRB models)
452 (d)	Exposure values by IRB exposure class, separately for Advanced and Foundation IRB.	Pillar 3 – Page 53 and Page 54 (Table 22: Credit risk exposures). This is also shown in other tables throughout the document.
452 (e)-(f)	For each exposure class, disclosed separately by obligor grade: Total exposure, separating loans and undrawn exposures where applicable, and exposure-weighted average risk weight.	Pillar 3 – Page 57 to Page 66 (Analysis of Credit Risk Exposures by PD grade, including Table 24 to Table 29 and Table 31 to Table 33)
452 (g)	Actual specific risk adjustments for the period and explanation of changes.	Pillar 3 – Page 50 (Comparison of Expected Losses to SCRAs)
452 (h)	Commentary on drivers of losses in preceding period.	Pillar 3 – Page 50 (Factors impacting loss experience)
452 (i)	Estimates against actual losses for sufficient period, and historical analysis to help assess the performance of the rating system over a sufficient period.	Pillar 3 – Page 39 to Page 45 (Model Performance) Including quantified analysis in Table 13: Model Performance
452 (j)	For all IRB exposure classes:	
452 (j) (i)-(ii)	Where applicable, PD and LGD by each country where the bank operates.	Pillar 3 – Page 76 (Table 40: IRB exposures by geographical region)

CRR ref	High-level summary	Compliance reference
Use of credit risk mitigation techniques		
453 (a)	Use of on and off-balance sheet netting.	Pillar 3 – Page 32 to Page 34 (Credit risk mitigation) Please note additional information with regards to balance sheet netting and derivatives is included in Counterparty Credit Risk section of Pillar 3 (Page 89)
453 (b)	How collateral valuation is managed.	
453 (c)	Description of types of collateral used by the institution	
453 (d)	Main types of guarantor and credit derivative counterparty, creditworthiness.	
453 (e)	Market or credit risk concentrations within risk mitigation exposures.	ARA – Pages 124-125 (Credit Risk)
453 (f)	Standardised or Foundation IRB Approach, exposure value covered by eligible collateral.	Pillar 3 – Page 34 (Table 10: Eligible financial collateral and other eligible collateral)
453 (g)	Exposures covered by guarantees or credit derivatives.	
Use of the Advanced Measurement Approaches to Operational Risk		
454	Description of the use of insurance or other risk transfer mechanisms to mitigate operational risk.	Not applicable
Use of Internal Market Risk Models		
455 (a) (i)	Disclosure of the characteristics of the market risk models.	Pillar 3 – Page 101 (Key characteristics of market risk models)
455 (a) (ii)	Disclosure of the methodologies used to measure incremental default and migration risk.	Pillar 3 – Page 101 (Review of internal models)
455 (a) (iii)	Descriptions of stress tests applied to the portfolios.	Pillar 3 – Page 102 (Stress Testing)
455 (a) (iv)	Methodology for back-testing and validating the models.	Pillar 3 – Page 102 (Back testing of VaR models)
455 (b)	Scope of permission for use of the models.	Pillar 3 – Page 101 (Review of internal models)
455 (c)	Policies and processes to determine trading book classification, and to comply with prudential valuation requirements.	Pillar 3 – Page 103 (Valuation principles)
455 (d) (i)-(iii)	High/Low/Mean values over the year of VaR, SVaR and incremental risk charge.	ARA – Page 151 (Table 1.39: Trading portfolios: VaR (1-day 95 per cent confidence level) Pillar 3 – Page 104 (Table 66: IMA values for trading portfolios)
455 (e)	The elements of the own fund calculation.	Pillar 3 – Page 98 (Table 61: Market risk own funds requirement)
455 (f)	Weighted average liquidity horizons of portfolios covered by models.	Pillar 3 – Page 101 (Review of internal models)
455 (g)	Comparison of end-of-day VaR measures compared with one-day changes in the portfolio's value.	Pillar 3 – Page 103 (Comparison of VaR to hypothetical profit and loss)

Abbreviations

Abbreviation	Brief description
A	
ABCP	Asset-backed commercial paper
ABS	Asset-backed securities
AFS	Available-for-sale
AIRB	Advanced Internal Ratings-Based Approach
ALRB	Additional Leverage Ratio Buffer
AMA	Advanced Measurement Approach
AT1	Additional Tier 1 capital
B	
BCBS	Basel Committee on Banking Supervision
BEEL	Best estimate of expected losses
BRC	Board Risk Committee
C	
CCB	Capital Conservation Buffer
CCF	Credit conversion factor
CCLB	Countercyclical Leverage Buffer
CCP	Central counterparty
CCR	Counterparty credit risk
CCyB	Countercyclical Capital Buffer
CDS	Credit default swap
CET1	Common equity tier 1 capital
CIU	Collective investment undertaking
CLN	Credit linked notes
CP	Commercial paper
CRD IV	Capital Requirements Directive & Regulation
CRM	Credit risk mitigation
CRR	Capital Requirements Regulation
CSA	Credit support annex
CVA	Credit valuation adjustment
D	
DVA	Debit valuation adjustment
E	
EAD	Exposure at default
EBA	European Banking Authority
ECAI	External Credit Assessment Institutions
ECNs	Enhanced Capital Notes
EEL	Excess expected loss
EL	Expected loss
EU	European Union
F	
FCA	Financial Conduct Authority (UK)
FCCM	Financial Collateral Comprehensive Method
FII	Financial Institutions Interconnectedness
FIRB	Foundation Internal Ratings-Based Approach
Fitch	Fitch Ratings
FPC	Financial Policy Committee (UK)
FRTB	Fundamental review of the trading book (BCBS)
FSB	Financial Stability Board
G	
GALCO	Group Asset and Liability Committee
GEC	Group Executive Committee
GENPRU	The PRA's rules, as set out in the General Prudential Sourcebook
GRC	Group Risk Committee
Group	Lloyds Banking Group plc together with its subsidiary undertakings on a consolidated basis
G-SIB	Global Systemically Important Bank
H	
HPI	House price index
I	
IAA	Internal Assessment Approach
IAS	International Accounting Standard
ICAAP	Internal Capital Adequacy Assessment Process
ICG	Individual Capital Guidance
IFRS	International Financial Reporting Standards
IMM	Internal Model Method
IRB	Internal Ratings-Based Approach
IRRBB	Interest rate risk in the banking book
IRC	Incremental risk charge
ISDA	International Swaps and Derivatives Association
L	
LCR	Liquidity coverage ratio
LGD	Loss given default
LIBOR	London Interbank Offer Rate
LTIP	Long-term incentive plan
LTV	Loan-to-value
M	
MGC	Model Governance Committee
Moody's	Moody's Investors Service
MTM	Mark-to-market
O	
OTC	Over-the-counter
P	
PD	Probability of default
PFE	Potential future exposure
PFI	Private finance initiative
PIT	Point-in-time
PPI	Payment protection insurance product
PRA	Prudential Regulation Authority (UK)
PRR	Position risk requirement
PVA	Prudent valuation adjustment
Q	
QRRE	Qualifying revolving retail exposure
R	
RBA	Ratings Based Approach
Retail IRB	Retail Internal Ratings Based Approach
RMBS	Residential mortgage-backed security
RNIV	Risks not in VaR

S	
STA	Standardised Approach
S&P	Standard and Poor's
SCRA	Specific credit risk adjustment
SE	Structured entity
SFTs	Securities financing transactions
SME	Small and medium-sized enterprise
SRB	Systemic risk buffer
SRT	Significant risk transfer
T	
TTC	Through-the-cycle
T1	Tier 1 capital
T2	Tier 2 capital
U	
UK	United Kingdom
US	United States of America
V	
VaR	Value-at-risk

Glossary

Additional Tier 1 Capital (AT1)	Additional tier 1 capital instruments are non-cumulative perpetual securities containing a specific provision to write down the security or convert it to equity should the CET1 ratio fall to a defined trigger limit. The Group's current AT1 securities contain a trigger limit of 7 per cent.
Asset-Backed Commercial Paper (ABCP)	See **Commercial paper**
Asset-Backed Securities (ABS)	Asset-Backed Securities are securities that represent an interest in an underlying pool of referenced assets. The referenced pool can comprise any assets which attract a set of associated cash flows but are commonly pools of residential or commercial mortgages but could also include leases, credit card receivables, motor vehicles and student loans.
Backtesting	Application of an analytical method where historical data is used to determine how accurately the model has predicted actual results.
Basel III Framework	The initial capital reforms and introduction of a global liquidity standard proposed by the Basel Committee on Banking Supervision in 2010 that are being phased in through CRD IV. Remaining reforms under the Framework are expected to be finalised in 2017.
Basel III Leverage Ratio	A capital leverage measure, introduced under the Basel III reforms, that is defined as the ratio of tier 1 capital to total exposures, where total exposures equal the adjusted sum of all on balance sheet assets and off-balance sheet items not deducted in determining tier 1 capital. The leverage ratio is intended to reinforce risk based capital requirements with a simple, non-risk based 'backstop' measure.
Basis point	One hundredth of a per cent (0.01 per cent). 100 basis points is 1 per cent. Used in quoting movements in interest rates or yields on securities.
Buy-to-let mortgages	Buy-to-let mortgages are those mortgages offered to customers purchasing residential property as a retail investment.
Capital resources	Eligible capital held by the Group in order to satisfy its capital requirements.
Central Counterparty (CCP)	An institution mediating between the buyer and seller in a financial transaction, such as a derivative contract or repurchase agreement. Where a CCP is used, a single bilateral contract between the buyer and the seller is replaced with two contracts, one between the buyer and the CCP and one between the CCP seller.
Collateralised guarantees	A guarantee which is backed by assets pledged to the bank to provide additional comfort around the value of protection offered by the guarantee.
Collectively assessed loan impairment provision	A provision established following an impairment assessment on a collective basis for homogeneous groups of loans, such as credit card receivables and personal loans, that are not considered individually significant and for loan losses that have been incurred but not separately identified at the balance sheet date.
Commercial paper (CP)	Commercial paper is an unsecured promissory note issued to finance short-term credit needs. It specifies the face amount paid to investors on the maturity date. Commercial paper can be issued as an unsecured obligation of the Group or, for example when issued by the Group's conduit, as an asset-backed obligation (in such a case it is referred to as **Asset-Backed Commercial Paper**). Commercial paper is usually issued for periods from as little as a week up to nine months.
Commercial real estate	Commercial real estate includes office buildings, industrial properties, medical centres, hotels, malls, retail stores, shopping centres, farm land, multifamily housing buildings, warehouses, garages, and industrial properties.
Common equity tier 1 capital (CET1)	The highest quality form of regulatory capital under CRD IV that comprises common shares issued and related share premium, retained earnings and other reserves excluding the cash flow hedging reserve, less specified regulatory adjustments.
Conduits	A financial vehicle that holds asset-backed securities which are financed with short-term deposits (generally **commercial paper**) that use the asset backed securities as collateral. The conduit will often have a liquidity line provided by a bank that it can draw down on in the event that it is unable to issue funding to the market.
Contractual maturities	Contractual maturity refers to the final payment date of a loan or other financial instrument, at which point all the remaining outstanding principal will be repaid and interest is due to be paid.
Countercyclical capital buffer	The countercyclical capital buffer is time-varying and designed to require banks to hold additional capital to remove or reduce the build-up of systemic risk in times of credit boom, providing additional loss absorbing capacity and acting as an incentive for banks to constrain further credit growth.
Counterparty credit risk	Counterparty credit risk is the risk that the counterparty to a transaction could default before the final settlement of the transaction's cash flows. Such transactions relate to contracts for financial instruments and may include derivative contracts and repo contracts.
CRD IV	On 27 June 2013, the European Commission published, through the Official Journal of the European Union, its legislation for a Capital Requirements Directive (CRD) and Capital Requirements Regulation (CRR), which together form the CRD IV package. Amendments published on 30 November 2013 were made to the Regulation. The package implements the initial Basel III reforms in addition to the inclusion of new proposals on sanctions for non-compliance with prudential rules, corporate governance and remuneration. CRD IV rules apply from 1 January 2014 onwards, with certain requirements phased in over time.
Credit quality step	A step in the PRA's credit quality assessment scale which is based on the credit ratings applied by ECAIs. The scale is used to assign risk weights to exposures under the Standardised Approach.
Credit Conversion Factor (CCF)	Credit conversion factors (CCF) are used in determining the exposure at default (EAD) in relation to a credit risk exposure. The CCF is an estimate of the proportion of undrawn commitments expected to be drawn down at the point of default.

Credit Default Swaps (CDS)	A credit default swap is a type of credit derivative. It is an arrangement whereby the credit risk of an asset (the reference asset) is transferred from the buyer to the seller of protection. The entity selling protection receives premium or interest-related payments in return for contracting to make payments to the protection buyer upon a defined credit event. Credit events normally include bankruptcy, payment default on a reference asset or assets, or downgrades by a rating agency.
Credit derivatives	A credit derivative is a financial instrument that derives its value from the credit rating of an underlying instrument carrying the credit risk of the issuing entity. The principal type of credit derivatives are credit default swaps, which are used by the Group as part of its trading activity and to manage its own exposure to credit risk.
Credit Linked Note (CLN)	A credit linked note is a type of credit derivative. It is an arrangement whereby the protection buyer will issue a bond or note which is linked to the creditworthiness of an obligor and backed by certain collateral. The bond or note is purchased by the protection seller and the investor will receive a coupon on the bond or note (market rate and spread). If a credit event occurs in either the obligor or the collateral, the bond or note is redeemed by the protection buyer with the recovery being the redemption amount. If no credit event occurs, the bond or note will be redeemed at par by the protection buyer.
Credit risk	The risk that parties with whom the Group has contracted fail to meet their obligations (both on and off-balance sheet).
Credit risk mitigation	A technique used to reduce the credit risk associated with an exposure (which continues to be held) by application of credit risk mitigants such as collateral, guarantees and credit protection.
Credit risk spread (or credit spread)	The credit spread is the yield spread between securities with the same currency and maturity structure but with different associated credit risks, with the yield spread rising as the credit rating worsens. It is the premium over the benchmark or risk-free rate required by the market to take on a lower credit quality.
Credit Valuation Adjustments (CVA)	These are adjustments to the fair values of derivative assets to reflect the creditworthiness of the counterparty.
CVA capital charge	A capital charge for CVA is applied under CRD IV requirements. The charge is based on the mid-market valuation of the portfolio of transactions with a counterparty and reflects the current market value of the credit risk of the counterparty to the institution, but does not reflect the current market value of the credit risk of the institution to the counterparty.
Debit Valuation Adjustment (DVA)	An adjustment to the measurement of derivative liabilities to reflect default risk of the entity.
Debt securities	Debt securities are assets held by the Group representing certificates of indebtedness of credit institutions, public bodies or other undertakings, excluding those issued by Central Banks.
Debt securities in issue	These are unsubordinated debt securities issued by the Group. They include commercial paper, certificates of deposit, bonds and medium-term notes.
Default fund contributions (CCPs)	Contributions to the default fund of a central counterparty (CCP) are made by clearing members to protect the CCP and its members in the event that losses incurred by the CCP, following the default of a member, are greater than the other defences employed by the CCP.
Enhanced Capital Notes (ECNs)	Subordinated notes formerly issued by the Group that contained an embedded equity conversion feature. All remaining series of ECNs were redeemed during 2016.
Equity risk	The financial risk involved in holding equity in a particular investment.
Expected Loss (EL)	A regulatory measure under Internal Ratings Based approaches of the expected loss on a credit risk exposure over a 12 month time horizon. It is determined by multiplying the **Probability of Default** by the **Loss Given Default** by the **Exposure of Default.** The EL rates under the Supervisory Slotting Approach and Simple Risk Weight Method are set by the CRD IV rules.
Export Credit Agencies	These agencies are defined as state or government sponsored, owned or controlled organisations or multi-lateral agencies that promote a country's exports of goods and services by enabling the exporter or the importer to obtain financing on terms that would not be otherwise available commercially. Such agencies can provide risk mitigation in the form of a guarantee (typically up to 85 per cent – 95 per cent of a contract value) providing cover and guarantee of payment in relation to commercial and political risk, thereby enabling lenders to support customers by offering financing on terms and for periods which might otherwise not be available in certain jurisdictions.
Exposure	An asset, off-balance sheet item or position which carries a risk of financial loss.
Exposure at default (EAD)	An estimate of the amount expected to be owed by a customer at the time of the customer's default.
External Credit Assessment Institutions (ECAI)	External Credit Assessment Institutions (ECAIs) include external credit rating agencies such as Standard & Poor's, Moody's and Fitch.
Fair value adjustment	Fair value adjustments arise on acquisition when assets and liabilities are acquired at fair values that are different from the carrying values in the acquired company. In respect of the Group's acquisition of HBOS the principal adjustments were write-downs in respect of loans and advances to customers and debt issued.
Financial Institutions Interconnectedness (FII)	Loans to other financial sector entities (FSEs) may require additional capital to be held through an adjustment to risk-weighted assets. In particular this additional capital applies to large FSEs and unregulated FSEs and is reflective of the additional risk created through the correlation of interbank lending.

Glossary continued

Foundation Internal Ratings Based (FIRB) Approach	Application of the Foundation Internal Ratings Based (FIRB) Approach allows internal estimates of PD to be used by the Group in determining credit risk capital requirements for wholesale portfolios. However, LGD and EAD under the Foundation IRB Approach are determined in accordance with standard parameters set by the regulator rather than on the basis of internal estimates. The FIRB Approach cannot be applied to retail portfolios.
Guarantees	A guarantee is a contract whereby a third party guarantor promises to recompense the lender in the event of failure by a customer to meet their obligations.
Impaired loans	Impaired loans are loans where the Group does not expect to collect all the contractual cash flows or to collect them when they are contractually due.
Impairment allowances	Impairment allowances are a provision held on the balance sheet as a result of the raising of a charge against profit for the incurred loss inherent in the lending book. An impairment allowance may either be individual or collective.
Impairment losses	An impairment loss is the reduction in value that arises following an impairment review of an asset that determines that the asset's value is lower than it's carrying value. For impaired financial assets measured at amortised cost, impairment losses are the difference between the carrying value and the present value of estimated future cash flows, discounted at the asset's original effective interest rate.
Individually/collectively assessed	Impairment is measured individually for assets that are individually significant, and collectively where a portfolio comprises homogenous assets and where appropriate statistical techniques are available.
Individually assessed loan impairment provisions	Impairment loss provisions for individually significant impaired loans are assessed on a case-by-case basis, taking into account the financial condition of the counterparty, any guarantor and the realisable value of any collateral held.
Interest rate risk (IRR)	Interest rate risk in arises from the different repricing characteristics of the Group's non-trading assets, liabilities and off-balance sheet positions of the Group. IRR arises predominantly from the mismatch between interest rate sensitive assets and liabilities, but also to the investment term of capital and reserves, and the need to minimise income volatility.
Internal Assessment Approach (IAA)	The Internal Assessment Approach is an IRB approach for securitisations whereby a firm applies its internal assessment of the credit quality of the positions in the risk-weighted asset calculations. A firm must apply to the PRA for permission to use this approach and must satisfy the PRA of its internal assessment processes. The IAA may only be applied to exposures arising from asset backed commercial paper programmes.
Internal Capital Adequacy Assessment Process (ICAAP)	The Group's own assessment, based on CRD IV and PRA requirements, of the levels of capital that it needs to hold in addition to its Pillar 1 capital requirement to capture risks not covered or not fully covered under Pillar 1. This includes stress events as they apply on a solo level and on a consolidated level.
Internal Model Method (IMM)	The Internal Model Method is one of three methods available to calculate exposure values for counterparty credit risk. A firm can only apply the IMM if it has permission from the PRA to do so.
Investment grade	This refers to the highest range of credit ratings, from 'AAA' to 'BBB' as measured by external credit rating agencies.
International Swaps and Derivatives Association master agreement (ISDA)	A standardised contract developed by ISDA which is used as an umbrella contract for bilateral derivative contracts.
Loan-to-value Ratio (LTV)	The loan-to-value ratio is a mathematical calculation which expresses the amount of a mortgage balance outstanding as a percentage of the total appraised value of the property.
Loans past due	Loans are past due when a counterparty has failed to make a payment when contractually due.
Loss Given Default (LGD)	The estimated loss that will arise if a customer defaults. It is calculated after taking account of credit risk mitigation and includes the cost of recovery.
Mark-to-Market (MTM) Approach	The Mark-to-Market Approach is one of three methods available to calculate exposure values for counterparty credit risk. The method adjusts daily to account for profits and losses in the value of related assets and liabilities.
Market risk	The risk that unfavourable market moves (including changes in and increased volatility of interest rates, market-implied inflation rates, credit spreads and bond prices, foreign exchange rates, equity, property and commodity prices and other instruments) lead to reductions in earnings and/or value.
Master netting agreement	An agreement between two counterparties that have multiple derivative contracts with each other that provides for the net settlement of all contracts through a single payment, in a single currency, in the event of default on, or termination of, any one contract.
Minimum capital requirement	The minimum regulatory capital that must be held in accordance with Pillar 1 requirements for credit, market and operational risk.
Model validation	The process of assessing and providing evidence that the bank's models perform as planned and adequately reflect the risk profile of the business, and that there are no material misstatements of the capital requirement. See also Backtesting.
Mortgage related assets	Assets which are referenced to underlying mortgages.
Multilateral Development Banks	Institutions created by groups of countries to provide finance and professional advice for development.
Operational risk	The risk of loss resulting from inadequate or failed internal processes, people and systems or from external events.

Over-the-counter derivatives (OTC)	Over-the-counter derivatives are derivatives for which the terms and conditions can be freely negotiated by the counterparties involved, unlike exchange traded derivatives which have standardised terms.
Past due items	An exposure class under the Standardised Approach that recognises exposures that are more than 90 days past due.
Pillar 1	The first pillar of the Basel III framework sets out the minimum regulatory capital requirements for credit, operational and market risks.
Pillar 2	The second pillar of the Basel III framework is known as the Supervisory Review Process, and sets out the review process for a banks capital adequacy; the process under which the supervisors evaluate how well financial institutions are assessing their risks and the actions taken as a result of these assessments.
Pillar 3	The third pillar of the Basel III framework aims to encourage market discipline by setting out disclosure requirements for bank's on their capital, risk exposures and risk assessment processes. These disclosures are aimed at improving the information made available to the market.
Potential Future Exposure (PFE)	An additional measure of counterparty credit risk over and above the current replacement cost of the derivative contract. It is defined as the maximum potential credit exposure of a derivative contract representing the additional amount by which the exposure could increase over the remaining life of the contract with a given level of confidence.
Private equity investments	Private equity is equity securities in operating companies not quoted on a public exchange. Investment in private equity often involves the investment of capital in private companies or the acquisition of a public company that results in the delisting of public equity. Capital for private equity investment is raised by retail or institutional investors and used to fund investment strategies such as leveraged buyouts, venture capital, growth capital, distressed investments and mezzanine capital.
Prudent Valuation Adjustment (PVA)	A regulatory deduction applied to CRD IV common equity tier 1 capital based upon the difference between the prudent value of trading book assets or other financial assets measured at fair value with the fair values recognised for these assets in the financial statements.
Point-in-Time (PIT)	Estimates of PD (or other measures) made on a Point-in-Time basis generally cover a short time horizon (usually a 12 month period) and are sensitive to changes in the economic cycle. This differs from a Through-the-Cycle (TTC) basis which uses long run average economic and risk data to reduce such sensitivity.
Probability of Default (PD)	The likelihood that a customer will default on their obligation within the next year.
Qualifying Revolving Retail Exposure (QRRE)	Qualifying Revolving Retail Exposures relate to revolving, unsecured retail exposures that, to the extent they are not drawn, are immediately and unconditionally cancellable. Such exposures include credit cards and overdraft facilities.
Ratings Based Approach (RBA)	The Ratings Based Approach is an IRB approach for securitisations applied to rated securitisation and re-securitisation positions. The approach applies risk weightings to positions based on a combination of ECAI ratings, the granularity of the underlying pool, the seniority of the position and whether the position is a re-securitisation position.
Regulatory capital	The amount of capital that the Group holds, determined in accordance with rules established by the PRA for the consolidated Group and by local regulators for individual Group companies.
Re-securitisations	A securitisation where the risk associated with an underlying pool of exposures is tranched and at least one of the underlying exposures is a securitisation position.
Repurchase agreements or 'repos'	Short-term funding agreements which allow a borrower to sell a financial asset, such as ABS or Government bonds as collateral for cash. As part of the agreement the borrower agrees to repurchase the security at some later date, usually less than 30 days, repaying the proceeds of the loan.
Residential Mortgaged-Backed Securities (RMBS)	Residential Mortgage-Backed Securities are a category of ABS. They are securities that represent interests in a group of residential mortgages. Investors in these securities have the right to cash received from future mortgage payments (interest and/or principal).
Residual maturity	The length of time remaining from present date until the maturity of the exposure.
Retail Internal Ratings Based (Retail IRB) Approach	The Retail Internal Ratings Based (Retail IRB) Approach allows internal estimates of PD, LGD and EAD to be used in determining credit risk capital requirements for retail portfolios.
Retail loans	Money loaned to individuals rather than institutions. These include both secured and unsecured loans such as mortgages and credit card balances.
Risk appetite	The amount and type of risk that the Group is prepared to seek, accept or tolerate.
Risk-weighted assets (RWAs)	A measure of a bank's assets adjusted for their associated risks. Risk weightings are established in accordance with CRD IV requirements.
Securities financing transactions (SFTs)	Securities financing transactions are repurchase and reverse repurchase agreements, buy/sell backs and securities lending. For the lender (seller) of the securities it is usually a way to raise funds to finance the securities positions. For the borrower (buyer) of the securities it is a way to invest short–term funds or to cover short (bond) positions.

Glossary continued

Securitisation	Securitisation is a process by which a group of assets, usually loans, are aggregated into a pool, which is used to back the issuance of new securities. Securitisation is the process by which ABS are created. A company sells assets to a structured entity which then issues securities backed by the assets. This allows the credit quality of the assets to be separated from the credit rating of the original company and transfers risk to external investors. Assets used in securitisations include mortgages to create mortgage-backed securities or Residential Mortgage-Backed Securities (RMBS) as well as Commercial Mortgage Backed Securities (CMBS). The Group has established several securitisation structures as part of its funding and capital management activities. These generally use mortgages, corporate loans and credit cards as asset pools.
Securitisation position	A retained or purchased position (exposure) in the notes issued by a securitisation.
Sovereign exposures	Exposures to central governments and central government departments, central banks and entities owned or guaranteed by the aforementioned.
Specific credit risk adjustment (SCRAs)	Specific credit risk adjustments comprise of accounting impairment provisions and fair value adjustments that reflect losses exclusively related to credit risk. The criteria for recognition and applications under CRD IV are governed by the EBA Regulatory Technical Standard on the calculation of specific and general credit risk adjustments.
Standardised Approach	The Standardised Approach to calculating credit risk capital requirements requires the use of a standard set of risk weights prescribed by the regulator. Use may be made of external credit ratings supplied by ECAIs to assign risk weights to exposures. Standardised approaches, following prescribed methodologies, also exist for calculating market risk and operational risk capital requirements.
Stressed VaR (SVaR)	Stressed VaR is a one year forward looking measure of VaR where certain parameters of the portfolio are calculated under a period of stress.
Stress testing	Stress and scenario testing is the term used to describe techniques where plausible events are considered as vulnerabilities to ascertain how this will impact the capital resources which are required to be held.
Structured entities (SEs)	SEs are entities that have been designed so that voting or similar rights are not the dominant factor in determining who controls the entity, such as when voting rights relate to administrative tasks only and the relevant activities are directed by means of contractual arrangements. SEs often have specific restrictions around their ongoing activities and are created to accomplish a narrow and well-defined objective.
Subordinated liabilities	Liabilities which, in the event of insolvency or liquidation of the issuer, are subordinated to the claims of depositors and other creditors of the issuer.
The Standardised Approach (TSA)	A standardised measure for calculating operational risk capital requirements based on the three year average of the aggregate risk-weighted relevant indicators of the underlying business. The relevant indicators are derived from total income.
Through-the-cycle (TTC)	See Point-in-time (PIT)
Tier 1 capital ratio	Tier 1 capital as a percentage of risk-weighted assets.
Tier 2 capital	A component of regulatory capital mainly comprising certain subordinated debt securities that do not qualify as AT1 capital. Such securities must have an original term of at least 5 years and cannot normally be redeemed within their first 5 years.
Total Return Swap	A total return swap is a type of credit derivative. It is an arrangement whereby the protection buyer will pass on to the seller all payments it receives in return for an interest related payment (market rate and spread), plus any decrease in the market value of the credit obligation. Where net payments received from the swap are recorded as net income but any offsetting deterioration in the value of the asset that is protected is not recorded (either through reductions in fair value or by an addition to reserves), the credit protection must not be recognised as eligible.
Trading book	Positions in financial instruments and commodities held for trading purposes or to hedge other elements of the trading book.
Value-at-Risk (VaR)	Value-at-Risk is an estimate of the potential loss in earnings which might arise from market movements under normal market conditions, if the current positions were to be held unchanged for one business day. It is measured to specified level of confidence, often 95 per cent or 99 per cent.
Write downs	The depreciation or lowering of the value of an asset in the books to reflect a decline in their value, or expected cash flows.
Write-off	The reduction of the value of an asset to zero, reflecting the inability to recover any residual value.
Wrong way risk	The risk that arises from the correlation between a counterparty exposure and the credit quality of the counterparty. It is therefore the risk that the probability of default of the counterparty increases with the exposure.

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