Lloyds Bank Corporate Markets plc

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Table Of Contents

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Major Rating Factors

Global Scale Ratings
Issuer Credit Rating
A/Stable/A-1
Resolution Counterparty Rating
A+/--/A-1

Strengths:	Weaknesses
• Highly strategic subsidiary of Lloyds Banking Group plc. • Solid capital ratios and additional loss-absorbing capacity.	• Business activity is weighted toward corporate and institutional clients, which brings a certain degree of cyclicality and complexity.

Outlook

S&P Global Ratings' stable outlook on Lloyds Bank Corporate Markets plc (LBCM) mirrors that on ultimate parent Lloyds Banking Group plc (Lloyds). Our base-case expectation is that Lloyds' statutory profitability will improve toward management's targets, and continued dividends and share buybacks will maintain our risk-adjusted capital ratio in the 7.5%-8.0% range over our two-year outlook horizon. We project that Lloyds' credit losses will gradually normalize from the current low level, but asset quality will remain sound assuming an orderly Brexit process.

Upside scenario

A positive rating action on LBCM would follow a similar action on Lloyds. It is unlikely in the next 12-18 months while we continue to see potential downside risks to the U.K. economy and banking system from a disruptive Brexit process.

Alternatively, we could raise the ratings on LBCM if its strategic importance to Lloyds increases and we classify it as a core subsidiary. This outcome would depend on it becoming a much more material and integral part of the group, which we do not expect.

Downside scenario

We could lower the ratings on Lloyds--and therefore LBCM--if the group's performance appears likely to significantly undershoot our current earnings and capital expectations.

We could lower the ratings on LBCM independently of a rating action on Lloyds if we saw LBCM becoming less integral to the group's strategy, which we do not expect. We could also lower the ratings if we expected the group's additional loss-absorbing capacity (ALAC) to fall materially, which is not a likely scenario in view of regulatory requirements.

Rationale

The ratings on U.K.-incorporated LBCM reflect our view that it is a highly strategic subsidiary of Lloyds. This classification takes into account LBCM's materiality, important role in Lloyds' strategy, and close link to the group's brand and reputation. We see LBCM as highly strategic rather than core (which is a stronger assessment) because we consider it has higher business risk and less diversification than the group's ring-fenced activities. As a result of LBCM's highly strategic status, the 'A' long-term issuer credit rating stands one notch below the 'a+' group credit profile, which includes a two-notch ALAC uplift. Due to LBCM's close integration with the group, we do not assign a stand-alone credit profile to it.

LBCM was established in response to U.K. ring fencing rules, which took effect in January 2019. The objective of the ring fencing regime is to protect critical banking functions, and we think parental support for non-ring fenced entities might be marginally weaker in a stress scenario than for ring-fenced banks (see "Rearranged And Ready: U.K. Banks

Are On Track For Ring-Fencing," published on Aug. 15, 2018). LBCM's balance sheet includes certain capital market activities and financial institution business that are not permitted within the ring-fenced subgroup headed by sister entity Lloyds Bank plc (A+/Stable/A-1). LBCM also owns non-U.K. entities including Jersey-incorporated Lloyds Bank International Ltd. (LBIL; A/Stable/A-1), which provides retail and commercial banking services in the U.K. crown dependencies.

Although much smaller than the ring-fenced business, we see LBCM as a material entity and integral to the group's commercial banking strategy. In preparation for ring fencing, Lloyds transferred various assets, liabilities, and legal entities to LBCM between May and December 2018. At year-end 2018, LBCM's consolidated balance sheet represented 10% of Lloyds' consolidated risk-weighted assets (RWAs) and the same proportion of the group's total assets. LBCM's common equity tier 1 ratio was 13.7% at year-end 2018, and we expect it will remain around that level.

LBCM's balance sheet profile reflects its focus on commercial banking and capital markets. Its £78.5 billion consolidated assets at year-end 2018 included £20.7 billion of customer loans (mostly to commercial clients), £15.9 billion of derivatives, £11.9 billion of reverse repurchase (repo) agreements, £5.3 billion of other fair-valued financial assets, and £14.4 billion of central bank balances. It had no level 3 fair-valued assets, which indicates its trading inventory was reasonably liquid, and 1.5% of its customer loans were classified as credit-impaired.

LBCM's 2018 statutory earnings are not representative of its potential due to the staggered business transfers during the year. It reported a £190 million statutory pretax profit for 2018. If LBCM had existed in its current form for the full year, its carve-out financial statements indicate it would have generated a £426 million pretax profit and a 53% cost-to-income ratio. We anticipate that LBCM will be solidly profitable over the medium term, but it may exhibit higher earnings volatility than Lloyds' commercial banking division due to its narrower scope of business. The commercial banking division's £2.2 billion underlying pretax profit in 2018 represented 27% of Lloyds' earnings.

We view LBCM's funding and liquidity profiles as satisfactory. It held £26.9 billion of customer deposits at year-end 2018, of which LBIL contributed about one-half. Debt securities and repos are also material funding sources, and LBCM recently finalized a euro medium-term note program to complement its existing euro commercial paper and certificate of deposit program. It plans to issue about £2 billion of term senior unsecured debt in 2019. LBCM holds material central bank balances and government securities to cover potential liquidity outflows.

We include ALAC uplift in the ratings on LBCM because, through internal downstreaming, we believe its senior creditors benefit from Lloyds' substantial ALAC buffer. At year-end 2018, LBCM's regulatory capital included £1.4 billion of Additional Tier 1 and Tier 2 securities downstreamed by Lloyds, and its outstanding debt securities included £6.4 billion issued to other group entities.

Related Criteria

- Criteria - Financial Institutions - General: Methodology For Assigning Financial Institution Resolution Counterparty Ratings, April 19, 2018
- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017

- General Criteria: Guarantee Criteria, Oct. 21, 2016
- Criteria | Financial Institutions | Banks: Bank Rating Methodology And Assumptions: Additional Loss-Absorbing Capacity, April 27, 2015
- Criteria | Financial Institutions | Banks: Bank Hybrid Capital And Nondeferrable Subordinated Debt Methodology And Assumptions, Jan. 29, 2015
- General Criteria: Principles For Rating Debt Issues Based On Imputed Promises, Dec. 19, 2014
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- Criteria | Financial Institutions | Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Criteria | Financial Institutions | Banks: Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Criteria | Financial Institutions | Banks: Commercial Paper I: Banks, March 23, 2004

Related Research

- Lloyds Banking Group plc, June 21, 2019
- U.K. Banks: Looking At The Facts Rather Than Received Wisdom, March 4, 2019
- Countdown To Brexit: Rating Implications Of A No-Deal Brexit, Feb. 6, 2019
- The 2019 Outlook For U.K. Banks Hinges On Brexit, Jan. 10, 2019
- Banking Industry Country Risk Assessment: United Kingdom, Nov. 5, 2018
- Rearranged And Ready: U.K. Banks Are On Track For Ring-Fencing, Aug. 15, 2018
- Lloyds Banking Entities Upgraded On Strengthened Bail-In Buffer And Improving Profitability; Outlook Stable, May 8, 2018
- Lloyds Bank Corporate Markets plc And Lloyds Bank International Ltd. Assigned 'A-/A-2' Ratings; Outlook Positive, April 24, 2018

Ratings Detail (As Of June 27, 2019)*	
Lloyds Bank Corporate Markets PLC	
Issuer Credit Rating	A/Stable/A-1
Resolution Counterparty Rating	A+/--/A-1
Commercial Paper	A-1
Issuer Credit Ratings History	
08-May-2018	A/Stable/A-1
24-Apr-2018	A-/Positive/A-2

Ratings Detail (As Of June 27, 2019)*(cont.)	
Sovereign Rating	
United Kingdom	AA/Negative/A-1+
Related Entities	
Bank of Scotland Capital Funding L.P.	
Preferred Stock	BB+
Bank of Scotland PLC	
Issuer Credit Rating	A+/Stable/A-1
Resolution Counterparty Rating	AA-/--/A-1+
Junior Subordinated	BB+
Junior Subordinated	BBB-
Senior Secured	AAA/Stable
Senior Unsecured	A+
Subordinated	BBB
HBOS PLC	
Issuer Credit Rating	BBB+/Stable/A-2
Junior Subordinated	BB+
Senior Unsecured	BBB+
Short-Term Debt	A-2
Subordinated	BBB
Subordinated	BBB-
LBG Capital No. 1 PLC	
Junior Subordinated	BB+
Subordinated	BBB-
LBG Capital No. 2 PLC	
Junior Subordinated	BB+
Subordinated	BB+
Lloyds Banking Group PLC	
Issuer Credit Rating	BBB+/Stable/A-2
Junior Subordinated	BB-
Preference Stock	BB
Senior Unsecured	BBB+
Short-Term Debt	A-2
Subordinated	BBB-
Lloyds Bank International Ltd.	
Issuer Credit Rating	A/Stable/A-1
Lloyds Bank PLC	
Issuer Credit Rating	A+/Stable/A-1
Resolution Counterparty Rating	AA-/--/A-1+
Commercial Paper	A-1
Junior Subordinated	BB+
Junior Subordinated	BBB-
Senior Unsecured	A+
Short-Term Debt	A-1
Subordinated	BBB

Ratings Detail (As Of June 27, 2019)*(cont.)
*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.