MOODY'S
INVESTORS SERVICE

CREDIT OPINION
28 July 2022

Update

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RATINGS

Lloyds Bank plc

Domicile	London, United Kingdom
Long Term CRR	Aa3
Type	LT Counterparty Risk Rating - Fgn Curr
Outlook	Not Assigned
Long Term Debt	A1
Type	Senior Unsecured - Fgn Curr
Outlook	Stable
Long Term Deposit	A1
Type	LT Bank Deposits - Fgn Curr
Outlook	Stable

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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Lloyds Bank plc

Update following rating action

Summary

We assign a rating of A1 to the long-term deposit and senior unsecured debt of Lloyds Bank plc (LB), the ring-fenced bank of the Lloyds Banking Group plc (LBG, senior unsecured rating A3 Stable).

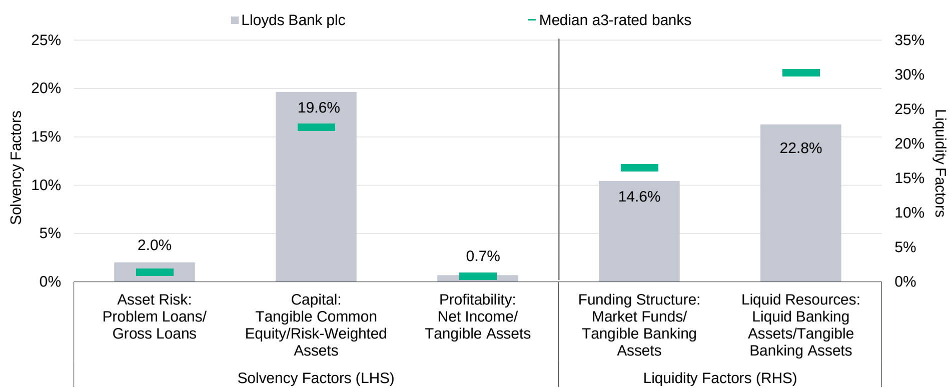
On 19 July 2022, we affirmed LB's senior unsecured debt ratings at A1 with a stable outlook and downgraded by one notch its subordinated debt ratings to Baa1 from A3 and its junior subordinated debt ratings to Baa2(hyb) from Baa1(hyb). The action only focused on the results from our Advanced Loss Given Failure (LGF) analysis.

LB's A1 long-term deposit and senior unsecured ratings reflects (1) the bank's standalone creditworthiness, expressed in an a3 Baseline Credit Assessment (BCA); (2) low loss-given-failure, which provides one notch of uplift under our Advanced Loss Given Failure (LGF) analysis; and (3) our assessment of a moderate probability of support from the Government of the United Kingdom (Aa3 stable), which provides one notch of uplift.

LB's a3 BCA reflects its strong capital, good asset quality, stable retail funding and ample liquidity, and its improving levels of profitability as revenues recover and rates rises support net interest income.

We align the ratings of HBOS plc and Bank of Scotland plc subsidiaries to those of LB, to reflect their high integration with LB.

Exhibit 1
Rating Scorecard - Key financial ratios



Source: Moody's Investors Service

Credit strengths

» Strong capital

» Low asset risk

» Stable retail funding and ample liquidity

Credit challenges

» Profitability will Improve on the back of increases in volumes and margins, while the cost of risk will remain low; however, inflationary pressures, if they persist, will constrain household incomes and debt servicing capacity and impact business and consumer confidence, weakening credit demand

Outlook

The stable outlook on LB's ratings reflects our view that the combined solvency and liquidity metrics will on a forward-looking basis remain in line with our current assessment, as its asset quality normalises and its profitability stabilizes, following the pandemic-induced deterioration in 2020, and taking into account tail winds from rising interest rates and headwinds from current macroeconomic pressures.

Factors that could lead to an upgrade of the ratings

LB's BCA could be upgraded if the bank's profitability and liquidity buffers improve. An upgrade of the BCA could lead to an upgrade of all long-term ratings of LB, with the exclusion of its senior unsecured debt, as government support would decrease to zero notches from one notch. LB's junior debt rating could also be upgraded following a significant increase in the stock of subordinated debt issued by LB.

Factors that could lead to a downgrade of the ratings

LB's BCA could be downgraded following (1) a deterioration of the UK operating environment beyond our current expectations, or (2) a material decline in the group's capital metrics. A one notch downgrade of the bank's BCA would lead to a downgrade of all its ratings.

Key indicators

Exhibit 2

Lloyds Bank plc (Consolidated Financials) [1]

	12-21[2]	12-20[2]	12-19[2]	12-18[2]	12-17[2]	CAGR/Avg.[3]
Total Assets (GBP Billion)	602.8	590.5	567.8	578.8	786.4	(6.4)[4]
Total Assets (USD Billion)	813.6	807.2	752.2	737.2	1,063.8	(6.5)[4]
Tangible Common Equity (GBP Billion)	31.7	29.6	33.5	35.4	46.3	(9.0)[4]
Tangible Common Equity (USD Billion)	42.8	40.4	44.4	45.0	62.6	(9.0)[4]
Problem Loans / Gross Loans (%)	2.0	2.1	2.0	2.1	1.7	2.0[5]
Tangible Common Equity / Risk Weighted Assets (%)	19.6	17.3	19.5	20.3	22.5	19.8[6]
Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%)	24.4	25.6	22.9	23.1	16.0	22.4[5]
Net Interest Margin (%)	1.8	1.8	2.2	2.1	1.9	2.0[5]
PPI / Average RWA (%)	3.2	3.2	4.4	3.4	3.7	3.6[6]
Net Income / Tangible Assets (%)	0.7	1.0	0.9	0.5	0.7	0.7[5]
Cost / Income Ratio (%)	63.0	62.3	53.5	60.2	54.4	58.7[5]
Market Funds / Tangible Banking Assets (%)	14.6	16.2	17.2	19.5	17.7	17.0[5]
Liquid Banking Assets / Tangible Banking Assets (%)	22.8	23.5	21.4	21.6	21.1	22.1[5]
Gross Loans / Due to Customers (%)	96.7	100.6	106.0	108.4	105.3	103.4[5]

[-] Further to the publication of our revised methodology in July 2021, only ratios from annual 2020 onwards included in this report reflect the change in analytical treatment of the "high-trigger" Additional Tier 1 instruments. [1] All figures and ratios are adjusted using Moody's standard adjustments. [2] Basel III - fully loaded or transitional phase-in; IFRS. [3] May include

rounding differences because of the scale of reported amounts. [4] Compound annual growth rate (%) based on the periods for the latest accounting regime. [5] Simple average of periods for the latest accounting regime. [6] Simple average of Basel III periods.
Sources: Moody's Investors Service and company filings

Profile

LB is the ring-fenced bank of Lloyds Banking Group plc (LBG), a leading UK-based financial services group providing a wide range of banking and financial services, focused on retail and commercial customers. LB operates also through other brands, mainly Halifax and Bank of Scotland. The bank retains most of the group's banking businesses, including more than 95% of loans and most of the retail, small and medium-sized enterprise, and corporate deposits.

Besides LB, LBG's other main subsidiaries are the insurer Scottish Widows Limited (Scottish Widows, IFRS A2 stable), and the non-ring-fenced bank Lloyds Bank Corporate Markets plc (LBCM, A1/A1 stable), holding capital markets activities, business outside of the European Economic Area and lending to financial institutions.

Detailed credit considerations

The financial data in the following sections are sourced from LB's consolidated financial statements, unless otherwise stated.

Low asset risk

We assign an a3 Asset Risk score, one notch below the Macro-Adjusted score, reflecting our expectation that Stage 3 loans will moderately increase and then stabilize at just above 2% of loans. We calculate that IFRS9 Stage 3 loans were 2.0% of gross loans at end-2021 (end-2020: 2.0%) and that Stage 2 loans were around 7% (end-2020: 14%).

LB's lending book includes high exposure to lower-risk retail mortgages (64%), followed by unsecured and auto lending (8%), and commercial lending (14%) at end-2021. LB classifies 10% of its loan book as "Other".

Underwriting standards in the mortgage book are higher than the market's average. The bank remains focused on the prime UK residential mortgage business, a segment with low risks. Riskier mortgages with high loan-to-values of above 90% accounted for 0.5% of gross lending at end-2021, lower than the 4% market average. Within UK residential mortgages, 17% are buy-to-let loans, which represents a higher proportion than for some of its peers.

Strong capital

We assign an aa3 Capital score as we expect capital levels to decrease in 2021 and beyond. Our tangible common equity (TCE) ratio was 19.6% at end-2021.

LB reported a high Common Equity Tier 1 (CET1) capital ratio of 15.2% at end-June 2022 (16.7% at end-2021), with a significant headroom over c.11% regulatory requirement. We expect regulatory capital will decrease, reflecting capital distributions and regulatory changes.

Profitability will significantly improve in 2022; however, long-term trends are uncertain

We assign a baa3 Profitability score, reflecting our expectation that LB's net income will stabilize around £4-4.5 billion in the medium-term, reflecting improved revenue supported by higher net interest margin in both 2021 and 2022, and an increase in the cost of risk in 2023 from a low base.

In H1 2022, LB reported profit after tax of £2.4 billion (from £3.7 billion in H1 2021). The decrease largely reflects an impairment charge of £364 million, most of which related to revisions around the economic outlook including additional risks from a higher inflation and interest rate environment, versus a £677 million impairment reversal in H1 2021. Revenue increased by 10% yoy reflecting higher net interest income and net fee and commission income; operating costs decreased by 3% yoy.

Stable retail funding and ample liquidity

We assign an a3 Combined Liquidity score, reflecting an a3 Funding Structure score and a baa1 Liquid Resources score. LB's Combined Liquidity score is one notch above LBG's, reflecting lower market funding and higher liquidity.

LB benefits from its stable and granular retail deposit base: its market share in the UK for personal current accounts was 24% at end-2021, the highest in the country.

LB's reliance on wholesale funding is moderate, representing 15% of tangible banking assets at end-2021.

In 2020, LBG replaced all Term Funding Scheme (TFS) balances and Funding for Lending Scheme (FLS) drawings with £13.7 billion borrowings under the Term Funding Scheme with additional incentives for SMEs (TFSME), which allows banks to borrow at an interest close to the Bank Rate for a period of four years. In 2021, LB made net drawings of £16.3 billion from TFSME, taking the total outstanding amount to £30 billion as of end-2021.

ESG Considerations

In line with our general view for the banking sector, LB has a low exposure to Environmental risks and moderate exposure to Social risks. See our Environmental risks heatmap and Social risks heatmap for further information.

Our assessment of moderate Social risk for LB considers its exposure to the coronavirus-induced economic shock. Despite LB incurred substantial provisions related to Payment Protection Insurance mis-selling in the past, we expect any further charges to be marginal, as the deadline for UK consumers to claim compensation elapsed in August 2019.

Governance is highly relevant for LB, as it is to all banks. Corporate governance weaknesses can lead to a deterioration in a company's credit quality, while governance strengths can benefit its credit profile. Governance risks are largely internal rather than externally driven, and for LB we do not have any particular governance concern. Nonetheless, corporate governance remains a key credit consideration and requires ongoing monitoring.

As a ring-fenced bank LB is subject to separate governance arrangements than LBG: LB has its own board, which acts independently from the group and prioritises the interests of LB over those of LBG.

Support and structural considerations

Affiliate support

We expect a very high probability of support from LBG, based on the size and importance of LB within the group. Our assumptions do not lead to any uplift, because LBG and LB have the same BCA.

Loss Given Failure analysis

We apply our advanced LGF analysis to LB because the bank is incorporated in the UK, which we consider to be an operational resolution regime.

Following the implementation of ring-fencing in the UK, we believe that LB would be resolved separately from its non ring-fenced sister bank, LBCM. As such our LGF analysis for LB reflects the entity's own liability structure.

Our LGF analysis assumes residual TCE of 3%, post-failure losses of 8% of tangible banking assets, a 25% runoff in junior wholesale deposits and a 5% runoff in preferred deposits, and it assigns a 25% probability to deposits being preferred to senior unsecured debt. These assumptions are in line with our standard assumptions. We also assume that the junior proportion of LB's deposits is 26%. These are in line with our standard assumptions.

Our LGF analysis indicates that LB's deposits and senior unsecured debt are likely to face a very low and low loss-given-failure respectively because of the loss absorption provided by subordinated debt (including the debt down-streamed from LBG), and the volume of deposits and senior debt themselves. This results in a two-notch uplift for the long-term deposit and a one-notch uplift to the senior unsecured debt ratings from the BCA.

Government support considerations

Given LB's systemic importance to the UK economy, reflecting its large national market share of residential mortgages and deposits, we incorporate a moderate probability of government support for deposits and senior unsecured debt, which leads to no uplift for the long-term deposit and a one-notch uplift for the senior unsecured debt ratings.

We believe that potential government support is low for LB's subordinated liabilities, which does not result in any uplift.

Counterparty Risk (CR) Assessments and Counterparty Risk Ratings (CRRs)

LB's CR Assessments are Aa3(cr)/Prime-1(cr). The long-term CR Assessments, before government support, are three notches above the bank's standalone BCAs of a3. The uplift results from the buffer against default provided to the operating obligations by substantial bail-in-able debt and deposits. A moderate probability of government support results in no additional notch of uplift.

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About Moody's Bank scorecard

Our scorecard is designed to capture, express and explain in summary form our Rating Committee's judgement. When read in conjunction with our research, a fulsome presentation of our judgement is expressed. As a result, the output of our scorecard may materially differ from that suggested by raw data alone (though it has been calibrated to avoid the frequent need for strong divergence). The scorecard output and the individual scores are discussed in rating committees and may be adjusted up or down to reflect conditions specific to each rated entity.

Rating methodology and scorecard factors

Exhibit 3

Lloyds Bank plc

Macro Factors		
Weighted Macro Profile	**Strong +**	**100%**

Factor	**Historic Ratio**	**Initial Score**	**Expected Trend**	**Assigned Score**	**Key driver #1**	**Key driver #2**
Solvency						
Asset Risk						
Problem Loans / Gross Loans	2.0%	a2	↔	a3	Sector concentration	
Capital						
Tangible Common Equity / Risk Weighted Assets (Basel III - fully loaded)	19.6%	aa2	↔	aa3	Expected trend	
Profitability						
Net Income / Tangible Assets	0.7%	baa2	↔	baa3	Expected trend	
Combined Solvency Score		a2		a3		
Liquidity						
Funding Structure						
Market Funds / Tangible Banking Assets	14.6%	a2	↔	a3		
Liquid Resources						
Liquid Banking Assets / Tangible Banking Assets	22.8%	baa1	↔	baa1		
Combined Liquidity Score		a3		a3		
Financial Profile				a3		
Qualitative Adjustments				Adjustment		
Business Diversification				0		
Opacity and Complexity				0		
Corporate Behavior				0		
Total Qualitative Adjustments				0		
Sovereign or Affiliate constraint				Aa3		
BCA Scorecard-indicated Outcome - Range				a2 - baa1		
Assigned BCA				a3		
Affiliate Support notching				0		
Adjusted BCA				a3		

Balance Sheet	**in-scope (GBP Million)**	**% in-scope**	**at-failure (GBP Million)**	**% at-failure**
Other liabilities	93,932	15.7%	139,798	23.4%
Deposits	449,663	75.2%	403,797	67.5%
Preferred deposits	332,751	55.6%	316,113	52.8%
Junior deposits	116,912	19.5%	87,684	14.7%
Senior unsecured bank debt	5,859	1.0%	5,859	1.0%
Junior senior unsecured bank debt	17,775	3.0%	17,775	3.0%
Dated subordinated bank debt	7,183	1.2%	7,183	1.2%
Junior subordinated bank debt	169	0.0%	169	0.0%
Preference shares (bank)	5,707	1.0%	5,707	1.0%
Equity	17,947	3.0%	17,947	3.0%
Total Tangible Banking Assets	598,235	100.0%	598,235	100.0%

Debt Class	De Jure waterfall		De Facto waterfall		Notching		LGF Notching Guidance vs. Adjusted BCA	Assigned LGF notching	Additional Notching	Preliminary Rating Assessment
	Instrument volume + subordination	Sub-ordination	Instrument volume + subordination	Sub-ordination	De Jure	De Facto				
Counterparty Risk Rating	23.8%	23.8%	23.8%	23.8%	3	3	3	3	0	aa3
Counterparty Risk Assessment	23.8%	23.8%	23.8%	23.8%	3	3	3	3	0	aa3 (cr)
Deposits	23.8%	8.2%	23.8%	9.1%	3	3	3	2	0	a1
Senior unsecured bank debt	23.8%	8.2%	9.1%	8.2%	3	1	2	1	0	a2
Dated subordinated bank debt	5.2%	4.0%	5.2%	4.0%	-1	-1	-1	-1	0	baa1
Junior subordinated bank debt	4.0%	4.0%	4.0%	4.0%	-1	-1	-1	-1	-1	baa2

Instrument Class	Loss Given Failure notching	Additional notching	Preliminary Rating Assessment	Government Support notching	Local Currency Rating	Foreign Currency Rating
Counterparty Risk Rating	3	0	aa3	0	Aa3	Aa3
Counterparty Risk Assessment	3	0	aa3 (cr)	0	Aa3(cr)	
Deposits	2	0	a1	0	A1	A1
Senior unsecured bank debt	1	0	a2	1	A1	A1
Dated subordinated bank debt	-1	0	baa1	0	Baa1	(P)Baa1
Junior subordinated bank debt	-1	-1	baa2	0	Baa2 (hyb)	

[1] Where dashes are shown for a particular factor (or sub-factor), the score is based on non-public information.
Source: Moody's Investors Service

Ratings

Exhibit 4

Category	Moody's Rating
LLOYDS BANK PLC	
Outlook	Stable
Counterparty Risk Rating	Aa3/P-1
Bank Deposits	A1/P-1
Baseline Credit Assessment	a3
Adjusted Baseline Credit Assessment	a3
Counterparty Risk Assessment	Aa3(cr)/P-1(cr)
Senior Unsecured	A1
Subordinate -Dom Curr	Baa1
Jr Subordinate -Dom Curr	Baa2 (hyb)
Commercial Paper	P-1
Other Short Term -Dom Curr	(P)P-1
PARENT: LLOYDS BANKING GROUP PLC	
Outlook	Stable
Baseline Credit Assessment	a3
Adjusted Baseline Credit Assessment	a3
Senior Unsecured	A3
Subordinate	Baa1
Bkd Jr Subordinate -Dom Curr	Baa2 (hyb)
Pref. Stock Non-cumulative	Baa3 (hyb)
Other Short Term -Dom Curr	(P)P-2
BANK OF SCOTLAND PLC	
Outlook	Stable
Counterparty Risk Rating	Aa3/P-1
Bank Deposits	A1/P-1
Baseline Credit Assessment	a3
Adjusted Baseline Credit Assessment	a3
Counterparty Risk Assessment	Aa3(cr)/P-1(cr)
Issuer Rating	A1
Bkd Senior Unsecured	A1
Jr Subordinate -Dom Curr	Baa2 (hyb)
Pref. Stock Non-cumulative -Dom Curr	Baa3 (hyb)
HBOS PLC	
Outlook	Stable
Counterparty Risk Rating	Aa3/P-1
Counterparty Risk Assessment	Aa3(cr)/P-1(cr)
Issuer Rating	A1
Subordinate	Baa1
Jr Subordinate -Dom Curr	Baa2 (hyb)
ST Issuer Rating	P-1

Source: Moody's Investors Service

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