Lloyds TSB Group plc – Interims 2008

The Plaisterers Hall, London – Wednesday 30th July 2008

Sir Victor Blank – Chairman

Ladies and gentlemen good morning and welcome to the Lloyds TSB results for the first half of 2008. With me on the platform this morning are Eric Daniels, our Group Chief Executive and Tim Tookey, the Acting Group Finance Director, and they will both join me in making some prepared comments, first of all and then we will take questions from the floor.

As you might possibly have noticed, the first half of 2008 has been a period of considerable turbulence in the financial services sector and with the marked slow down in the UK economy as a whole, this is impacting in both consumer and corporate confidence.

Whilst no bank can be completely immune from market turbulence, the impact on Lloyds TSB has been relatively limited. We have been able to focus on growing our business and we have put in a very good underlying operating and financial performance in the first half of the year. This continues a succession of good results as Eric and his team have put the Group on a solid footing and really driven forward the business to where we are today.

Our success is based on building a strong, well thought through business model. We are able to add real, consistent value to our individual and our corporate customers with the full range of banking, insurance and life products that they need to manage their personal lives and their businesses effectively. The result is that our model produces lower risk and higher quality earnings.

Looking at the results overall, there are two things that strike me in particular. Firstly it is important to note that there continues to be really strong momentum in our core businesses. We have plenty of headroom to continue growing, particularly through cross sales of products as more and more of our customers buy from us an ever greater range of products and services, and secondly, particularly important, is that there is quality and prudence built into our portfolio. For example, over the last few years we have foregone the apparently high margins in some of the more exotic and higher risk areas of lending and instead ensured that our exposures are conservatively managed. We have good security and cash coverage for our loans, providing a good level of protection from falling revaluations. Our actions over the past few years have prepared us well for any slow down.

Now Tim and Eric will cover these areas in more detail and will give you evidence as to why we believe that we have a differentiated and a proven business model that can not only withstand a lower growth environment, but one which is a model which positions us to capture share and to increase profitability at the same time. We will not be immune from any slowdown but we believe that the strength of our business

model means that we are pretty well positioned. So in the light of this, the board has decided to increase the interim dividend by 2% to 11.4 pence per share.

On that note, I will now hand you over to Tim Tookey – thank you.

Tim Tookey – Acting Group Finance Director

Thank you Victor – good morning everyone.

This morning I'm pleased to be presenting a robust set of results which once again demonstrate the underlying momentum we have established in our business, and the benefits of our lower risk, more conservative operating model. During the first half of the year, we have delivered an excellent underlying performance, driven by our core relationship businesses.

Before moving my focus onto the strong relationship business performance, it is appropriate to touch on some of the facts that affected our statutory earnings.

Whilst Insurance volatility was a significant feature in the first quarter of the year, I am pleased to say that we only saw modest further impact in the second quarter. I would just remind you that whilst policyholder interests volatility is a debit above the line, there is a corresponding credit in the tax line where you will see in the news release a significant reduction in our tax charge.

The other items here have all been previously disclosed. Adjusting for these items you can see our continuing businesses profit down 19%. Adjusting also then for market dislocation we get to the strong underlying performance of our key relationship focused businesses that have delivered 11% profit growth. Relative to many of our peers the impact of market dislocation has clearly been limited, nevertheless we have had a combination of mark-to-market adjustments and impairment charges that totalled £585 million in the first half. I will go through these in some detail later.

On an underlying basis, we see the continued execution of our growth strategy delivering improved income growth of 9%. At the same time we have continued to maintain excellent cost control, achieving strong positive jaws whilst ensuring that we continue to make ongoing investments in the business. As a result, our trading surplus grew strongly, up 14%.

We have highlighted several times within recent announcements that corporate impairment levels have been unsustainably low in recent years and we are now seeing the expected increase as the economy slows, and this is the dominant factor behind our 18% increase in impairments.

Overall profit before tax grew by 11%, with earnings per share and economic profit growth of 5% and 7% respectively, and as you can see, we also continued to deliver a high return on equity. We have made fundamental improvements to the business in each of the last 3 to 4 years and the results are evident on each line of the P&L.

Firstly, the good income growth is a result of building customer relationships and balancing growth across assets and liabilities. In addition, our margin outlook has started to improve with increases across virtually all products.

We continue to focus on sustainable cost reduction that then creates headroom for further investment in the business, and our strong productivity programme has once again delivered strong benefits and we will deliver, on track, net cost benefits of £250 million this year, even after reinvestment. Our asset quality remains satisfactory and we have actually seen an improvement in the quality of our retail book.

Alongside this, we have continued our work on capital efficiency and as you know we transitioned well from Basel II. Our capital position remains robust with a total capital ratio of 11.3% and a core tier 1 ratio of 6.2%. Finally, the robustness of our model, including our strong customer deposit base, has meant that we have continued to fund very successfully, and at market leading rates, despite the recent market turmoil.

Turning now to the drivers of income growth. In Retail, asset growth was 8% driven primarily by mortgage balances, where we achieved a 24% share of net new lending in the first half, while unsecured retail lending was broadly flat in a slightly declining market.

We have seen very good growth on the liability side of the balance sheet, and our savings growth has been particularly strong. Retail deposits increased by 10%, including strong growth in wealth management. Over the last 12 months, savings balances have increased by some £8 billion.

In the Wholesale Bank, we continue to lend to good quality customers throughout the more challenging conditions, benefiting from our strong liquidity position and excellent liability growth of 16%, and this liability growth was achieved across our Corporate and Commercial customer bases as well as within our international businesses. So we are delivering good growth on both sides of the balance sheet.

Turning now to margin. Half on half product margins have begun to increase and more than offset the mix effect. In particular, margins have widened in the Corporate book, and margins on mortgage allocations have improved significantly. Our margins have of course benefited from our more favourable position in the current competitive environment.

Turning now to the individual divisions and looking specifically at the drivers of income growth in the retail bank – this is now a familiar picture. Once again we have seen the liability side of the balance sheet making the greatest contribution to overall income growth, and this remains important in terms of income sustainability because liability-led earnings tend to be more recurring.

We continue to make good progress in driving income from both savings and investments. Our focus has been very much on growing core savings deposits. These relationship balances are the more profitable areas of our savings book and are also important from a liquidity perspective because they tend to be more 'sticky'. On the asset side, we saw continued income growth from lending as we particularly benefited from

our strong mortgage performance, although this has been offset by lower commissions from creditor insurance products, reflecting a decrease in the proportion of sales through the branch network.

Turning now to the Wholesale division where, excluding market dislocation, income is up 18% cent year-on-year. Most of this growth came from our two key relationship businesses – Corporate Markets and Commercial Banking, although both Asset Finance and International Banking income have also delivered improving trends. Commercial Banking income increased by 9% reflecting disciplined growth in both lending and deposit balances, and an increased focus on the more valuable higher turnover customers where their needs are greater.

In Corporate Markets, we have continued to develop our businesses across our core corporate customer base. This long term relationship strategy, as well as the development of new product capabilities, has enabled us to deliver very strong growth in cross-selling income, up 64% in the first half of the year notably from interest rate and currency derivative products. The most important dynamic of this slide is the significant bias of our income growth towards relationship based sales.

The significant turbulence in global financial markets over the last 12 months has clearly affected all banks. However, Lloyds TSB's limited exposures in the key areas of contagion means that we are relatively well positioned. In our news release we have been as transparent as possible and split the impact of market dislocation into its different components.

The first point to note is that we have no direct exposure to US sub-prime ABS – we've broken out our CDOs, held as part of our structuring business. In terms of the unhedged positions, we have written down a further £62 million leaving limited residual exposure amounting to some £70 million which relates to super senior high grade notes of 2005 vintage, and with no underlying asset defaults.

We also have a holding of CDO super senior notes which is fully hedged with a CDS from a monoline insurer. During the first half of the year, the Group has written down the value of this protection by £170 million, following a further rating agency downgrade to the Guarantor. The gross value of the position stands at £297 million.

At the half-year, the reliance we placed on the swap was £121 million (down from £155 million at year end). In addition, we have approximately £1.4 billion of CDOs, down from £1.9 billion at the year end, hedged by leading financial institutions with our exposure fully cash collateralised. The risk here therefore is effectively global bank counterparty risk.

We have limited SIV capital note holdings. All of these SIVs are fully funded – although the costs of funding have clearly increased. This, combined with some uncertainty over future funding has led us to write down the value of our SIV assets by £46 million. And as you can see, this leaves us with only a small residual exposure. In addition, we had a further £85 million of SIV liquidity backstops. During July, these liquidity backstops have reduced further to a single drawn facility of £22 million. Looking back, it is pleasing to see

that we have considerably reduced these exposures from £370 million at the year end, to just £22 million now.

We've also provided details of the impact on our trading portfolio, and we're aware that not every bank has done this but we wanted to continue to ensure that we provide clear disclosure. We have seen mark to market falls in parts of our trading book which reflects the marketwide repricing of credit so our liquidity and, to a lesser extent, credit.

The greatest writedown at £170 million represents a variety of mark-to-market adjustments against high quality assets; primarily high quality senior European and US Bank Bonds and investment grade corporates. We are confident in the underlying quality of these assets, and expect a recovery in values over time.

In addition, we have seen a writedown through reserves of £630 million in our AFS book. Pleasingly, this is an improvement of about £100 million from the position as detailed in the May Interim Management Statement. Over two thirds of the writedown relates to the ABS assets held in Cancara, our conduit, where over 90% of all the ABS bonds remain AAA rated and in which there has never been a default on any asset since its inception 6 years ago. In addition, there is no exposure either directly or indirectly to sub prime US mortgages, and only very limited Alt-A exposure.

Throughout the first half of the year Cancara has of course continued to fund well. The remaining AFS writedowns are split between US Government backed student loans and major bank senior paper and high quality ABS, of which more than 95% is AAA rated. So as we have said before, while no financial institution is left unaffected by the recent market dislocation, the impact on the Group is relatively low.

Turning now to Insurance & Investments where we have seen a resilient performance against the backdrop of difficult equity markets.

Through rigorous cost control our investment management operation SWIP has maintained its profitability despite the effect of falling markets on its income. In General Insurance, profit growth of £63 million is predominantly due to the welcome lack of severe flood claims this year. Scottish Widows has increased its IFRS profits by 15% as a result of an improved mix of protection sales and an increase in Corporate pensions business.

On an EEV basis, Scottish Widows profits were up 4%, after adjusting for surplus capital repatriation. Scottish Widows delivered a good sales performance, growing market share in a difficult market, with sales through the more profitable bancassurance channel up 8%, reflecting good protection sales and strong growth in OEICs through our wealth management business. The new business margin remained strong by industry standards at 3%, but includes the impact of a change in sales mix.

Existing business profit remained robust with weaker persistency in life and pensions being offset by a favourable experience in the OEICs business. The expected return on shareholder funds reduced as a result of lower levels of free assets.

As well as growth, return is an important metric throughout the Group, and improved Widows capital efficiency, combined with the capital repatriation programme, means that our return on embedded value has again increased and now stands at 11.7%.

Turning now to costs. As you would expect, tight cost control continues to be a priority, all our divisions have once again delivered a strong cost performance – notwithstanding the continued investments we are making in the business. All divisions have also once again delivered income growth ahead of cost growth. As a result, our Group cost:income ratio continues to improve significantly and now stands at 46.6%, down a full 2 percentage points.

Moving on to impairment. The Group charge for impairment losses grew by 22% excluding the impact of last year's corporation tax rate change, and market dislocation. In the Retail Bank, we indicated earlier in the year that we did not expect the impairment charge to be significantly higher in the first half of this year, compared to the first half of last year – and indeed our expectations have been realised with the charge increasing by only 4%.

Asset quality trends across the retail portfolios remain broadly stable and the quality of new lending continues to be strong. Looking at the unsecured portfolios, the asset quality ratios for both personal loans and credit cards have improved, and we have reduced the overall level of arrears. In the mortgage business, arrears have remained broadly stable – up 3% over the last year reflecting a slight uptick in the last couple of months.

£36 million of the increase in the mortgage impairment charge relates to the impact of the first half fall in the house price index. This is where falling house prices increased the 'loss given default' in our impairment calculations. Looking forward, our view is full year house price falls could be between 10% and 15%, by way of illustration, were prices to fall 12.5% this year we might expect the HPI impact on our impairment charge in the second half of the year to be approximately £100 million.

We have historically used dynamic delinquency charts to demonstrate the quality of our new business. I won't dwell on these detailed charts, but you will see from the loans chart here that the quality of new business remains strong, and within cards the trend is similar, with later vintages showing improved stable trends. These charts continue to highlight the strength of our loan books and that recent lending in both our loan and card books continues to perform well.

We have an excellent UKRB mortgage portfolio with an average indexed loan to value of 47%. In addition, the average LTV for new business was unchanged at 63%. The full breakdown of our portfolio shown here clearly emphasises the conservative nature of our book.

Though, as I highlighted earlier, we have seen increased impairment in the mortgage book largely as a result of the falls in HPI, our arrears profile remains strong compared to our peers. I have used some CML data here to bring out some comparative indicators that demonstrate the high quality of our mortgage book,

compared to widely available industry data – albeit some of the industry data is only available a quarter in arrears.

Looking at 3 months in arrears data, C&G arrears have increased by only 3% over the last 12 months, compared to an industry average of a 27% rise in the 12 months to March 2008. Our new repossessions rate, as a percentage of total mortgages in 2007, was just half that of the industry average. Looking further at properties in possession, we tend to operate at about half of the industry average and our share of properties in possession is less than half our implied natural market share.

Turning now to look at our W&IB impairments. As expected, the underlying impairment charge increased, reflecting a modest increase as a result of the economic slowdown in the UK, growth in the book and a small number of specific provisions in the Corporate Book. Impairments in Asset Finance followed a similar strong trend to the unsecured retail book, increasing only slightly half on half.

Asset quality in the SME book continues to be strong, reflecting in part our strategy of focusing on secured lending although we are seeing some early warning indicators starting to turn. The increase in the first half charge predominantly relates to one specific case within the Commercial Finance portfolio. So whilst overall asset quality in Wholesale remains satisfactory we are seeing the expected increase in charges compared to recent periods.

In the past there have been some questions about our property lending – particularly given the recent growth in the book so I thought it helpful to share with you some facts which set out why we are confident in the quality of our portfolio.

At the end of June lending to property companies amounted to £20.9 billion, or about 20% of our overall Wholesale lending. The portfolio splits approximately one third residential and two thirds commercial property. Of the residential lending, over half is to local authority backed public housing. Within the commercial property portfolio, 88% is investment or, effectively, corporate credit lending. The balance is development lending and is subject to strict lending criteria. For example, we require that the interest expense is fully covered by pre-let income, and that the overall level of lending does not exceed 60% of the gross development value. Our geographic spread is consistent with the market as a whole – although we don't have any direct development lending in either the City or Docklands. Our loan to value on the commercial portfolio as a whole is around 60%.

The new lending this year is predominantly investment business and has met our risk appetite criteria – offering lower LTVs, higher interest cover and the normal full set of covenant protections. With pricing having lifted materially and the attractive profile of LTVs on new business, which has averaged 54%, these transactions have been highly remunerative. We have also avoided lending at over 75% LTV.

By way of example, the two largest commercial property deals done this half, had LTVs of 39% and 34% respectively with good quality covenants in place. This highlights our stance of lending to cash flows rather than purely to property values.

There has been a great deal written about the scale of the slowdown in the UK and the knock-on impact on impairments. So I thought that this would be a good time to pause for thought and reflect on some of the key factors behind our impairment outlook. In terms of the economy as a whole, consumer confidence is low but despite recent months increases unemployment levels remain at a relatively low level. Overall corporate liquidity remains satisfactory but again confidence is much lower than a year ago. Against this backdrop, we continue to lend cautiously, focused on the increasing number of profitable opportunities and lending to customers that fit our relationship model.

In terms of unsecured lending, our asset quality remains good and our current arrears performance remains satisfactory. As a result, we do not expect the retail unsecured impairment charge in 2008 to significantly exceed the unsecured impairment charge in 2007. However, in the context of the uncertain UK economic environment and the potential for increased consumer insolvencies, we are continuing to enhance our underwriting, collections and fraud prevention procedures. So, whilst the outlook remains uncertain, we are well placed to deal with the economic headwinds before us.

I have already spoken about the good income and profit momentum in the business, however this growth has not come at the expense of returns. Our return on equity is high and stable, and we have continued to increase our economic profit. This reflects well on the underlying performance of the business.

Turning now to risk weighted assets and capital. I have already commented on the strong earnings growth in our core relationship businesses. This has been achieved through targeted asset growth across our business franchises, benefiting from our robust capital position and strong funding capability. This growth has been achieved at attractive margins despite the increased cost of funding to the Group.

Risk-weighted asset growth of 8% over the last 6 months includes approximately £2 billion of increased weightings as a result of the house price index reducing. We have taken a significant proportion of net new mortgage lending in the first half and at better margins than we have seen for some time, as well as growing our corporate and commercial banking books.

Our capital position shows a total capital ratio of 11.3% and a core tier 1 ratio of 6.2%. On this basis, our capital position remains robust despite having had to absorb the impacts of mark-to-market adjustments from dislocated assets and insurance volatility in the first half.

When considering the appropriateness of our capital base, we start with an understanding of the Group's strategy and risk appetite. Our lower risk business model is generating strong earnings and we have had only modest write-downs from dislocated assets. Our balance sheet reflects many years of prudent business growth based upon through-the-cycle relationship banking and although we won't be immune from the impact of an economic downturn, we are comfortable that our capital position remains robust.

Before I finish, I'd just like to touch on the liquidity position of the Group. Throughout the crisis we've continued to fund well – and at market leading rates. There are a number of factors behind this, I've already mentioned not just the absolute size, but also the growth that we have seen in our customer deposit base.

As a result, we have a conservative wholesale funding profile. Our strong funding position is evidenced by our 'triple A' Moody's credit rating – which was reaffirmed earlier this year. Finally, not only have we maintained a consistent market presence leveraging our long term relationships, but we have always ensured that we maintain significant funding headroom.

Our high, and growing, customer funding base is a key part of our funding model. We currently have over £162 billion of customer deposits, the majority of which are 'sticky' relationship deposits, this includes nearly £47 billion of current account balances. As a result of the strength of our relationship customer funding base, our overall wholesale funding requirement is significantly lower than our peers. Overall, this translates into a funding advantage for the Bank such that during the recent period of market turbulence our funding operations continued to fund on a business as usual basis.

In summary then, in the first half of 2008 we have achieved a strong set of underlying results, notwithstanding the challenging market conditions, building momentum across our high quality, balanced set of businesses and maintaining satisfactory asset quality.

Cost management remains strong and we have again delivered wide and positive jaws. Once again we have substantially improved our cost:income ratio and we continue to both grow the business and maintain our high returns. Finally, we have a robust capital position.

The Board's decision to increase the dividend by 2% balances our confidence in the Group's future earnings capability with a level of caution reflecting the slowing UK economic environment.

And with that, I will hand over to Eric who will take you through a further review of our progress.

Eric Daniels – Group Chief Executive

Thanks Tim – good morning and thanks very much for coming,

You heard from Victor and Tim about the good set of results we achieved during the first half of the year. Our statutory profits were clearly impacted by the market dislocation charge and the effect of insurance volatility, however, to get a better view of what is going on in the business, our prospects looking forward, it is appropriate to look at the core business performance. All of my subsequent slides are prepared on that basis.

I would like to spend the next few minutes giving you my perspective and some context around the results.

Over the past 5 years, we have been executing against a strategy and business model that was designed to build strong customer franchises and generate high quality earnings throughout the cycle. I am pleased to report that this latest set of earnings continues the trajectory that we have established and gives another data point in our strong track record of delivery. All 3 of our divisions have good momentum on both leading and lagging indicators.

However, we are entering a different part of the cycle where we, along with the rest of the market, predict lower economic growth for the next several periods. We believe that while we will not be immune to the slowdown, the organisation is well positioned. We have a robust business model and will benefit from the measures we have taken over the years to strengthen our core disciplines and lower volatility.

We enjoy a good capital and liquidity position and a funding cost advantage, which allows us to capture market share at better margins. All in, while our first half results were impacted by the market dislocation, our core business performance reflects the strength of our business model and demonstrates our successful execution against that model.

Let me remind you briefly of the strategy and our business model – our objective is to build strong customer franchises. We believe that a sustainable, long term franchise must be built around the customer. In pursuit of our strategy, we identified a series of key disciplines where we wanted to establish clear, advantaged capability.

First, we wanted to be better than our peers at acquiring and deepening relationships. We measure our success by looking at indicators such as sales volumes, new customer share and share of customer wallet; and the result is sustainable growth on the income line. This provides stable annuity-like revenue streams and high future value as customers give us more of their business.

The second set of disciplines centre on being an increasingly efficient and effective organisation. This is not just about reducing costs, but structurally changing the organisation to consistently serve our customers better, make it easier for our staff to be more productive and to free up capacity for investment in future growth. The result is a consistent improvement in the cost:income ratio and enhanced customer satisfaction scores.

The third set of disciplines is around the effective use of resources and deals with how we set risk appetite and allocate risk capacity and capital. Our relationship approach means that we have a consistent posture towards our customers. We set our risk policies to go through the cycle. We are more conservative in the expansionary periods, but we are still there for our customers in the slower parts of the cycle. We manage our balance sheet and funding conservatively. Our risk appetite is set with a view that we will maintain our standards in the good and less good times, and this will result in:

– robust capital ratios
– more predictable earnings
– consistent growth
– and high returns

With that backdrop in mind, let me walk you through our trajectory over last several years. I will give you a progress update on each of the divisions and show you how we are positioned for the next several periods.

Our underlying income was up 9% for the first half, with each division growing well. The pleasing thing about the income growth is that it is solidly based, as it is derived from an increase in the number of customers,

improved sales, and growth in market share. Also pleasing is the fact that we have been growing while raising our already high, risk standards. Given the momentum we have in acquiring and deepening relationships we expect to be able to continue to grow.

In the first half of the year, we continue to improve our productivity, with a full two percentage point gain and we maintained the trajectory we established some years ago. The programmes in procurement, Group manufacturing and straight through processing are well embedded. Given our successes to date, and our ongoing focus on productivity, we expect to be able to further improve our cost: income ratio.

As I mentioned earlier, our growth has been achieved without compromising our high standards for risk. The asset quality ratio has been consistent over the past several years, as we have improved our portfolio quality. We have not chased share at the expense of greater risk, and we have often sacrificed margin in exchange for lower risk. For example, we allowed market share in IFA introduced mortgages to fluctuate, when we couldn't get adequate terms and conditions. Within our corporate portfolios we never went covenant lite and our leveraged loan exposure is limited.

Over the years, in Commercial lending we moved more of our book to a secured basis, which now represents some 87% of our portfolio. We have a high quality asset portfolio and we are well positioned for the future.

We have seen good progress on the income line. We have managed down our cost:income ratio consistently while funding major investment programmes. Our portfolio is in good shape and our risk is well managed – the sum of these efforts has led to an 11% growth in core business profits for the half, continuing the double digit growth trend established several years ago. We have built momentum through our unremitting execution against the disciplines underpinning our business model and that gives us confidence as we look forward.

We enjoy some of the highest returns in the industry, in no small part due to our focus on economic profit. When we set the strategy, we looked to achieve both growth and returns for our shareholders and we are delivering.

Let me now turn to the divisions. In the Retail Bank, Helen and her team have delivered excellent profit growth of 15%, led by income growth of up 6%. As a result of improving and leveraging our terrific retail franchise, we have established market leading new business flows across the majority of our key business lines.

We are:

- – number one in new current accounts and added value accounts
- – number one in credit card issuance
- – number two in mortgage lending
- – number one in personal loans
- – and, number three in savings

We have seen continued good growth in sales volumes, with each of our channels reporting strong progress.

– branch sales are up 7%

– telephone sales up 27%

– and internet sales up 49%

This has flowed through to growth in market share and all products show good progress over the period. Our momentum in acquiring new customers and deepening relationships with our franchise customers means we are able to continue to grow, although we will only do so where we can have appropriate returns and at a suitable risk profile.

As importantly as attracting new customers, we are growing cross-sales as we deepen relationships with customers – this is key to customer retention and building annuity like revenue streams. The scale and breadth of our customer franchise supports better lending decisions and offers a lower cost for incremental sales.

The top graph shows the number of additional products that we sell at account opening. The number of products sold at initiation has almost doubled from 2 years ago, we are continuing to deepen the relationship with our customers over time. The bottom graph shows the increase in products sold to customers who joined us in June 2006. As you can see we consistently improve our product penetration which rises from 1.6 to 2.5 products and we have much more opportunity for future growth.

We have real momentum in acquiring and deepening customer relations in the retail bank and when we overlay that with good risk management, a focus on deposit growth and our drive for sustained productivity improvement, we are well positioned for the future. Over the past several years we have increasingly concentrated on lending to franchise customers, where we have experience with the customer and superior information that allows us to make better credit decisions. 99% of our personal loans and 90% of our credit cards are to franchise customers.

Over the past 2 years, we have put in place improved collections systems which have boosted collector productivity by over 50% and we have actually increased the number of collectors by 15%. Our mortgage arrears have been stable and Tim showed you that our more recent vintages in unsecured have better arrears performance.

Turning now to Insurance & Investments. We have delivered another strong growth with profits up 31%, or 11% excluding the extraordinary claims impact from the floods last year. Archie and his team continue to deliver good results, despite the challenging equity markets which have resulted in a move towards cash based products.

Scottish Widows has improved market share and is a leading provider of life and pensions products. We saw an 8% increase in bancassurance sales which is our more profitable channel.

In the IFA channel we saw an overall reduction in sales of 5%, in line with the fall in the market although we did see strong sales in pensions during the period. We are targeting the more attractive business lines, and a more select number of IFAs, to ensure we generate the appropriate returns.

Particularly pleasing has been the fact that we have improved the overall level of sales while maintaining returns, which continues the trajectory that we have seen in recent periods. As with the other businesses, an excellent cost performance contributed to the results and Scottish Widows and we now benchmark as one of the most efficient life and pensions providers. This is exactly where we want to be as we face into more difficult market conditions. In our General Insurance business, we see excellent opportunity to grow the bancassurance performance as we continue to cross-sell into customer need across our business franchises.

Moving now to look at the Wholesale Bank, Truett and his team put in a very strong performance, with profits up 22%, excluding the market dislocation charge. This performance is driven by the investment that we have made over the years in new teams and in new products. We also are using our access to liquidity to support our customers at a time when market conditions have changed and this reflects the strength of Lloyds TSB's balance sheet and the prudent manner in which we manage the business.

In the mid Corporate sector, we have seen excellent progress in our market share which has risen from 12% to 14% and we have achieved this without reducing our asset quality. We have also seen success in terms of winning a greater share of our customers spend, and our cross-sales have risen by 64% in comparison with prior period.

In Commercial Banking, we have also seen great progress. We achieved increases in market share in our target markets, as our account managers continue to be very successful in attracting the profitable, high turnover customers 'switching' from other financial services providers. In addition, as a result of our strong partnership with the retail bank, we also retained the leading position for business start-ups. The strong 9% income growth reflects the success in acquiring and deepening customer relations.

In the Wholesale Bank, we have taken a through the cycle approach to risk. We have maintained our high standards though the more expansionary period and we have not slackened in terms of covenants, coverage ratios and security. As Tim showed you, our lending in commercial real estate is well thought through and errs on the side of prudence.

We showed you at the full year results that our portfolio quality has actually improved over the last couple of years. We have taken higher impairments in Wholesale in this half and we are approaching more normalised loss ratios, but we believe that the portfolios will hold up well in a slower growth market. We also believe we are well positioned with our limited exposures to some of the more problematic areas such as leveraged lending and lending to hedge funds.

One of the drivers underpinning our results and our confidence in our future is that we have invested in the business to support growth and we are seeing the benefits flowing through. We have increased our

investment sharply over the past several years, as you can see from the chart, which includes revenue, capital expense and marketing. These figures do not include the investment in new people, where for example, we have seen a 19% increase in front office staff in products and markets over the last eighteen months to support business lines. In Large Corporate we have seen a 17% increase in relationship managers, and in the Retail bank we have increased front line branch sales staff by 500.

So let me summarise my comments – in the first half of 2008, we have clearly been impacted by the market dislocation and insurance volatility but when we look to the core business results, we once again delivered a strong operating and financial performance. We have consistently executed against our customer focused model. We have established market leading positions. We have good momentum and good opportunity to grow. Our customer based business model, our through the cycle approach to risk, and our focus on efficiency, position us well for the slowdown in the economy.

When combined with our robust capital and liquidity, we believe we can continue to grow and capture share in future periods. Thank you.

Sir Victor Blank

Thank you Eric and Tim. We are happy to take questions now – if you could give us a name and your house and then we'll decide among us who is going to take the question. I will start over there on the third row.

Question & Answer Session

Question 1 : HPI Issues - Jonathan Pierce, Credit Suisse

Thank you very much, it is Jonathan Pierce from Credit Suisse. Can I ask 3 questions – they are all on house price related issues – I suppose all 3 really are for Tim.

The first is on which house price index you are using in these calculations?

The second question is really on the impairment impact as house prices come down because clearly the distribution the LTV implies is going to be a non linear increase in impairment as prices fall, and that is kind of confirmed by your suggestion that in the first half there is a £36 million impact. And for about the same impact on house prices in H2, that is rising to £100 million. So I am just wondering whether you have run the numbers or the impact for a further 12½% fall? Will it be the sum multiple of the 136 that we are looking at for this year?

The final question is on risk weighted assets, I am assuming the non linear relationship again applies here, so can you give us a feel for, on your 12 ½% fall in HPI this year, what the risk weighted assets will do in the second half of the year. We have obviously seen £2.3 billion in H1, will it be a multiple of that in H2? Thank you.

Answer : Tim Tookey

I think I have caught all 3 of your questions Jon, let me take it in turn. We use a blend of the publically available house price indices rather than rely on any particular one, so we certainly take into account Nationwide, the Halifax and obviously the RICS data in forming our own view. And as you can see, using that data, we are giving likely outcomes for the full year, rather than taking guidance on any particular one over the others. We use those to inform our views on house prices, and how they are likely to behave in the second half of the year.

On the second part of your question to do with impairment charges, you are right to observe its non linear impact. We would all expect that to be the case. In terms of have we run the numbers on a further 12½%, well as you would expect we run all sorts of different stress scenarios on our models, looking at both the profit as well as the pure impairment impact. If you were to take a further increase in house price falls beyond that 12½%, then yes you would expect to see a further movement in impairment. The impact does actually flatten out as you go beyond it, it is not right to assume that it is infinitely geared. Let's remember that the impairment calculation is actually looking at your loss given default and the impact of HPI on that, so you actually have to take a view on what level of defaults and repossessions you are going to have. So that is as much driven by the actual quality of the book and how one is managing that. Whereas of course the impairment aspect is purely looking at those people who are in default or repossession. So I would guide you against assuming that you would take a multiple if you wanted to write a hypothetical 25% fall.

The same is true also on the balance sheet side. As you rightly observe, there has been a £2.3 billion impact in the first half. I would expect there to be a broadly similar impact in the second half in line with the illustrative 12½% guidance on the mid point in the range on HPI for the full year.

Question 2 : Balance Sheet: corporate loan growth, Credit loss reserves, Deposit growth - Ian Smillie, ABN Amro

Thanks, good morning, it's Ian Smillie from RBS and 3 questions as well please – all on the balance sheet on the first half of the year relative to the December numbers that you had given us.

Firstly in terms of the corporate loan growth, something like £12 billion, could you give us some sense how much of that would relate to new lending which you commissioned in the period and how much of that would reflect the draw down of commitments which had been put in place before the credit crisis had started?

The second question is on the credit loss reserves coverage, given your cautious outlook for the economy. Can you explain to us why the credit loss reserves coverage to compared assets fell in the period from something like 45% to 43% and what would need to happen for you to move to rebuild that ratio, which is what we would anticipate in the slowing economic environment?

And then the third question on deposits – a sharp slowdown in the increase of deposits generated in the first half of the year, something like £5 billion which is less than half the run rate from the second half of last year. So could you give us some forward looking indication as to whether that is the new level we should get used to? And if so, will the loan to deposit ratio for the Group continue to rise? Or is that a ratio which you are explicitly managing?

Answer : Tim Tookey

Again I will break it down into three and if I miss one please remind me, I am sure you will. On draws versus new lending, the vast majority of the increase in lending in the corporate business is actual new lending rather than draws on existing facilities. Yes of course there are some draws on existing, but the vast majority of it is new lending where, because of our strong liquidity position, the bank is able to take advantage of the significant number of quite profitable opportunities that are being brought to us and to a degree cherry pick the kind of clients that we wish to take on. I made reference from the podium earlier to making sure that we are growing with those kinds of customers who fit with our relationship model, and that's where the majority of that corporate lending has come from and we are very pleased with it.

You ask about credit loss reserves coverage. I congratulate you on getting to the numbers, you found them in two different halves of the book and I agree with your 43/45. If you had also done the figure of June of last year you would have found it was 44%, and actually the move between 43% and 44% in a year or 2% in a year is really very modest and we are quite comfortable with the level of impairment provisions that we are covering against our impaired assets. The overall credit quality of the books remains very satisfactory indeed.

Your third question was about deposits and I am not quite sure that I followed all the numbers. There has been a small increase in the loans deposit ratio during the first half, I think that probably reflects to some degree our standing back from offering some of the highest deposit and savings rate balances that some of our competitors are having to. And I think what that reflects is that we can still grow our deposit balances, our deposit balances are up by 12% over a year. To be able to do that in an environment where we are not offering the best rates, I think actually is a very creditable performance, and shows the level of attraction to customers to come to the bank by offering those kind of rates. What you really get is the hot money, and the hot money that disappears as soon as somebody else goes and posts another special offer rate. So actually we are very comfortable and very pleased actually with our level of deposit growth.

Further Question

Could you just give some sense as to where you expect the loan to deposit ratio to go over time please? Will it continue to rise or is that a ratio you are explicitly managing?

Answer

I would not be surprised to see a small further increase in the loans deposit ratio. But if you look at the mix of our funding, you will see that we have maintained a constant balance between deposit based income and our reliance on the wholesale markets. So keeping that balance in check is very important. That is a core part of our overall management of the balance sheet.

Question 3 : Capital ratios and RWA growth - Peter Toeman, HSBC

Peter Toeman from HSBC. I wonder if you could provide some more colour on the movement in the equity Tier 1 ratio which has gone down from 7.4 to 6.2? I appreciate the expansion of risk weighted assets is a big driver of that and £2bn has come from the revised risk weighting of mortgages, but the underlying growth of RWA's is still 7% for the half year. So I wonder if you could tell us what your expectation is for RWA growth going forward.

Answer : Tim Tookey

Yes you are right. It has come down from 7.4% to 6.2% at the year end. Let's also remember that the core Tier 1 ratio during the first half of the year has to bear a disproportionate proportion of the whole year dividend. So that is actually a factor of some of the phasing of how the dividend comes off reserves and therefore the capital within core Tier 1 impacts on the headline ratio itself. Also during the first half of the year, we have had an unusual combination of the insurance volatility as well as the significant (relative to zero) impact of mark-to-market adjustments on our dislocated assets. And we would not expect that kind of a cocktail of insurance volatility market dislocation to repeat itself going forward to the same scale.

Question 4 : Capital and growth - Alastair Ryan, UBS

Development on a theme really, Alastair Ryan from UBS. You put on £20bn of lending and £5bn of deposits in the first half and your shareholder equity has fallen by a billion and a half sterling. I mean you are the only bank that I have come across that is going to be putting up those sort of metrics, a rising loan deposit ratio, falling capitalisation. I mean, how long does the market have to stay bad before you have to stop doing that as well?

Answer : Eric Daniels

I think that we have been very clear that we are content with our level of capital. We think that we are one of the best capitalised banks in the marketplace. Because we have managed prudently through the cycle on both a capital and liquidity basis, this is really somewhere where we can continue to grow our business, even though others have withdrawn from the market. As Tim mentioned, we are being very selective in terms of the new deals we are putting on. We are very happy with them. Any time that you can do commercial real estate deals at 39% and 34% loan to values with very good names, strong governance and good cashflows, and very, very good margins, we should do it. We should continue to expand because we can. So we don't feel at all uncomfortable with our present posture.

Question 5 : Sustainable Return on Equity, Impaired Loans - Manus Costello, Merrill Lynch

You made much in the presentation of the improvement in return of equity which in part has to be said was driven by lower equity. But given that 27% level in the first half and given that most of your competitors in both the UK and indeed internationally would say that ROEs are reducing, would you encourage us to think about that 27% as a sustainable level of return of equity for Lloyds going forward?

And my second question was just on disclosure. At the full year stage you gave us a very useful breakdown of impaired loans by division and in particular we noticed the impaired loans in the corporate division which were about £850 million, just over that I think at the year end stage. Do you have the similar number for the half year stage please within corporate?

Answer : Eric Daniels

In terms of return on equity, if you saw the chart, we have been absolutely consistent in terms of our focus on both growth and returns. If you recall in the not too distant past, about 5 years ago when we set the strategy, we enjoyed some of the highest returns on the market and the question by analysts at that time was, how can you possibly achieve growth and maintain the returns? Something has got to give. Well over the past 5 years we have consistently maintained or improved our returns and at the same time we have achieved growth. It comes from leveraging the franchise in building on those core disciplines that I spoke about: acquiring and deepening customers, focus on productivity and focus on being an effective organisation. And so we see no change in terms of our focus on the same core disciplines. We expect that we will achieve and continue to achieve both growth and returns. In terms of the impairments let me turn it over to Tim and Tim if you have another comment about ROE as well?

Answer : Tim Tookey

No nothing to add on ROE Eric, but on the impaired loans, we haven't broken it out in the news release between the different divisions. But the majority of the increase in impaired loans across the half actually does relate to the Wholesale and International Banking Division.

Question 6 : Write down projections, Mortgage volumes - James Invine, Dresdner Kleinwort

Hi good morning, it's James Invine here from Dresdner Kleinwort. I just wanted to ask Tim, when you are thinking about capital for the year ahead, what are you thinking about with regard to the write downs that you have made on your dislocated assets? I mean I guess you would say that some of those are definitely gone forever now, but are you assuming that you are going to write any of that back this year? Or in fact are you assuming further write downs in the second half of the year?

Answer : Tim Tookey

Thanks for the question James. Very difficult one to call what is going to happen in these markets going forward. We certainly don't plan or assume for a level of write backs to happen in the rest of the year. That may of course happen and I think what that reflects is the fact that a proportion of the marks that one take, are actually liquidity related rather than being credit related. And various commentators have tried to gauge the rough split between what may be a timing difference ie, liquidity mark versus credit. That is very difficult to do, but we are not dependent on those marks coming back in the second half.

Further question

Can I have a second on mortgage volumes. Clearly your mortgage volumes have gone up pretty strongly versus last year. And I was just wondering should we expect that to increase quite a bit further in the second half of the year, given your Northern Rock agreement?

Answer : Eric Daniels

What we have done and we have always been very, very clear about is that we will let the IFA introduced mortgages float in terms of can we get the appropriate margins and can we get the appropriate terms and conditions. As we are well capitalised, we can in fact let that share grow and wane depending on where the market is. We don't really have a forward looking projection and we don't set forward targets on that basis. It will depend on what the market can bring. The difference between the IFA introduced and our own mortgages is that we jealously guard the share that is originated by Lloyds TSB. Those are customers, they are deep relationships and we treasure that relationship with the customer. The Northern Rock deal is clearly something that we believe will be an important source of origination for us but again it is very difficult to call that in isolation with the rest of the market. We will simply have to see what conditions are permitted.

Question 7 : Capital ratios, Net interest margin outlook, PPI - Michael Helsby, Morgan Stanley

I have just got three unrelated questions if that is okay.

Firstly following on from the ROE and the capital question, I mean one of the reasons why your ROE is a lot higher than peers is that you use a lot of the insurance division's capital within the banking book. And certainly if we reduce your core equity Tier 1 by the deduction that you are going to have to do in 2012, then your core equity ratio is about 4.9% which is clearly given the recent capital increases, a lot lower than peers. So I was wondering if you could tell me a couple of things. Firstly, what do you see as an appropriate level of what we would call a banking core equity Tier 1 or a core equity Tier 1 as you measure it? And secondly, if plan B or sorry plan A doesn't come through, ie the economy is a lot worse, what is your plan B to that in terms of dividend, capital increase etc?

The second point is on margin. I note your net interest margin clearly went up versus the first half of last year, but it was flat versus the second half of last year. So I was just wondering if you could give us a steer in terms of what you think the outlook for the second half of this year is. I know there are a lot of moving parts.

And lastly on PPI, looks like you had about 13% of your underlying profits in the first half of the year coming from PPI. Clearly there has been a big discussion paper from the competition commission. I was just wondering what your response to that is and whether you see that profit as being at risk. Thanks.

Sir Victor Blank

Eric is going to start with the comment on Capital and then I will pass it over to Tim.

Answer : Eric Daniels

Thanks Victor. We basically are very comfortable with our capital position and I think Tim will amplify further. The Core Tier 1 ratio is an interesting ratio and something that we certainly look at. It is not the primary regulatory ratio, that is the total capital ratio where as you know we stand at a very robust 11.3%. Again Tim will have more comments. Turning very quickly to margin. What we have seen over the past several periods and we would expect to continue to see, is that we have a funding cost which contributes to our margin where what we have seen over the past several periods, and we would expect to continue to see, is that we have a funding cost advantage which contributes to our margin. We are also getting better pricing virtually across the board in virtually every product category. However, despite those two favourable pieces, we also have a different mix impact. We are growing our corporate book and our mortgage books faster than some of the other area, personal lending or credit cards for example. And so while you are watching product margins increase, you are seeing a mixed impact dampen some of that increase. We would expect to see some of that same factor going forward.

Finally on PPI, what we believe and we have certainly seen from comments, we follow it with great interest, is that we offer an absolutely superior product. Our pricing is more or less in the middle of the range. We have a more benefits rich product than our competitors. We think we offer good value for customers and our independent research tells us that customers value the product. So we will have to see what eventually is going to come from that. Tim.

Answer : Tim Tookey

Thank you. I agree with everything you said on capital. I don't agree it is right to look at one particular ratio or focus on one. Moreover I think it is appropriate to look at all of: our capital position, our risk appetite and our strategy and in that sense one would set ones appetite for the right level of capital commensurate with a broader capital analysis that takes into account the risk profile and the asset quality of the bank. And in that regard I think it is worth remembering that the balance sheet has got many years of prudent lending based upon through the cycle criteria. And that leaves the balance sheet in pretty good shape. You know, on top of that our risk appetite has been low for some time. So although we would not be immune from anything that is coming to us in terms of an economic downturn, our overall risk level and therefore capital strength to us, leaves us in a very robust and comfortable position.

Question 8 : US charge, Dividend - Tim Sykes, Execution

Thank you it is Tim Sykes from Execution. Two questions, slightly unrelated if I can.

The first one is about the US charge. I note you have mentioned this before and I note the very carefully worded statement. But I also note that OFAK are involved where fines can be scaleable relative to extent of the misdemeanour. Can you comment on whether or not this is a once and for all charge or would there be further charges to come from the US exposure?

Answer : Eric Daniels

We think we have taken a prudent position in terms of reserving for this. We obviously don't comment on the conversations with our Regulators.

Further question

And the dividend is really the most important question. You are clearly much more cautious than you were six months ago about the outlook for the UK economy. Can you just comment on why you bothered to increase the dividend by 2% and what you think about where that position is going forward? And also comment on your thoughts on the coverage ratio looking into next year?

Answer: Sir Victor Blank

Let's just deal with the present for the moment. We are comfortable, as you have heard us talk about, with our capital position. And we are very confident in the growth of our businesses, each of which, if you look at underlying performance, have performed very strongly in the first half. And we felt that we wanted therefore to indicate that degree of confidence both in our own financial position and in the prospects of growth and signal that with a small increase in dividend for our shareholders. So I think that is the background to the dividend and increase.

Further question

And your thoughts on coverage?

Answer: Sir Victor Blank

I don't think there is anything to add on coverage.

Question 9: Credit cards - Derek Chambers, Standard & Poor's

Derek Chambers from Standard & Poor's Equity Research. Can I ask a couple of questions on the credit card area. One is could you comment on the changing dynamics of that business where you seem to be moving towards a more transactional customer base? So how does that impact the income statement? Secondly, you passed over rather rapidly arrears performance by vintage on credit cards. But it looks as if it is not quite as straightforward as on the loans. So could you just take us through what you are seeing there? Because it doesn't seem quite as an improving trend as it is in loans?

Answer : Tim Tookey

Yes I will happily take the second part of the question on trends. I am sorry if I skipped through the graph a bit quick Derek. I think what the chart shows there is the blobs and I have put blobs on the end of the recent vintages. This shows that recent vintages by quarter are performing in the middle of the pack and better than that, if one compares it against the vintages which I believe go back on the chart several years. So I think we would be comfortable in the current vintage and the way that it is performing in terms of the profile of the book.

Further answer: Eric Daniels

What I would add, and I completely agree with, is that we don't run our card business to minimise losses. We run it to maximise the risk reward ratio. And so what you are seeing is our fine tuning and you will see each vintage has a slightly different performance. As we judge the market and as we basically direct our sales to more and more segmented parts of the portfolio, you will see some variants. Broadly we are very comfortable with our arrears levels on the cards. Now we are seeing some changes you have noted between what we would call transactors and revolvers. And as we launched our Duo card which has been enormously successful, we are attracting in more transactors as of late. Now we are very comfortable doing that because the fees that we get from that card and the merchant discount is in fact an attractive proposition.

Question 10 : Capital ratios, GDP forecast - Michael Helsby, Morgan Stanley

Michael Helsby from Morgan Stanley. I don't like to go on, but I hear what you are saying about the total capital ratio and I fully take that on board, but a lot of your peers have given us a target tier 1 and I think most investors within the market, be it UK, Europe or US certainly put a lot more focus on core equity Tier 1 when looking at capital ratios. So I was just wondering again if you could maybe give us a view on what you think is an appropriate level of core equity and I have just got a slight follow up question as well.

Answer : Eric Daniels

Again I will give a quick comment and turn it over to Tim. But Michael I think that we are in a slightly different position than many of the other banks around the circuit. We are well capitalised, if you look at our capital ratios today on virtually any measure, we are extremely well capitalised and what I think is happening is other banks are capitalising up to our ratios. So we are very comfortable. We don't, and we haven't given any further guidance. In fact we never provided guidance in terms of what minimums we were shooting for on a total capital basis, nevermind any other ratios. So I think that what you can do is look to our track record of handling capital extremely prudently and we will basically continue to manage in a fashion where we will run very healthy capital ratios. Tim.

Answer : Tim Tookey

That's fine. I have nothing particular to add.

Further question

Sorry one quick follow up question. It is just I noted at the IMS Statement that you had an expectation that the economy was going to improve in 2009 versus 2008, based on at the time, I think that was what you

said. But I was just wondering if you have told us what your GDP forecast is. I would be interested in knowing what you are planning purpose is for growth for next year?

Answer : Eric Daniels

No, I think at the Interims we said that we were expecting 1.6 – 1.8% growth this year and about 1.3 next year, I think that was our statement. We would expect that we are going to be slightly towards the higher end this year, as the economy is doing slightly better than we predicted, around closer to the 1.8 than the 1.6. And we expect that it is going to be slightly lower than the 1.3 that we called out at the Interims. So we don't see any huge tectonic changes. What we do see however as the economy continues to evolve, is that the chances of recession are higher than they were when we last looked or when we last reported. But our base case is still for positive growth, albeit at lower levels. Tim?

Answer : Tim Tookey

That's fine.

Question 11 : Impairment - Sandy Chen, Panmure Gordon

Just two related questions just on impairment charges. I just want to make sure that I heard this correctly. The guidance for retail unsecured impairment charges was flat '08 versus '07. I am trying to put that together with the growth in the actual unsecured personal loans. And as well, just the relatively negative outlook in terms of arrears trends. How do those two things go together? And also on a broader point, just given your leading market shares in several key areas, in customer loans, and I appreciate that your arrears performance is significantly better than the peers, can you give us some guidance in terms of your peak arrears expectations? Maybe in reference to what happened in the early '90s?

Answer : Tim Tookey

Let me deal with the first part of that and perhaps Eric would take the second part. On the guidance given, I think you misheard me. I didn't actually say flat. What I said was that we would not expect the retail unsecured impairment charge in '08 to significantly exceed the unsecured impairment charge in '07. So Sandy if you don't mind, that is a slight refinement on how you have played it back to us from the floor.

Further question

And peak arrears?

Answer : Eric Daniels

In terms of peak arrears, we are clearly looking at what has happened during the last several cycles and what we do is we model the base case and then we stress test those and have more extreme scenarios. I think that I would not give any particular guidance other than saying that you know very clearly, we are comfortable with our portfolios. We have given you guidance that we think that we are going to be able to continue to grow and that our portfolios are well positioned and so that is a statement of confidence in terms of what we have been doing over the last several years. So I think that is about as much guidance as we give.

Question 12 : Arrears - Mike Trippitt, Oriel Securities

Thank you. It's Mike Trippitt at Oriel Securities. It is a bit of a follow up on that actually. On the guidance you have given for the impairment charge, you know the suggestion of the 12½% price fall, £100m impairment. I suppose the question I have got is actually on the arrears level underlying that. As far as I can see you have given I think some data on repossessions. You have also said that arrears are up I think 3%. I am not sure if you are disclosing actually what the arrears are on the mortgage book at the moment either as a percentage, three month plus or three to six month or whatever? And in the £100m in the second half, are you assuming any increase in arrears or is it at the current arrears level?

Answer : Tim Tookey

Let me just see Mike what I have got here for you. Yes, you are right, we haven't given an arrears figure on three months plus in the presentation. What I can tell you from my notes here is that our arrears numbers are lower than the CML average and in fact the arrears numbers on our three months plus arrears book on our buy to let portfolio are significantly better. I mean they are a fraction of the CML and that reflects the fact that a lot of our buy to let exposure is actually to our core customers and therefore it is core relationship business where actually the profile of it is much stronger. I can't remember, what is the second part of your question?

Further question

The £100m charge is that assuming the current level of arrears run rate? Or are you expecting deterioration?

Answer : Tim Tookey

No that is based upon our estimate of where arrears will trend to over the rest of the year.

Question 13 : Impairment, Capital ratios - Leigh Goodwin, Fox-Pitt Kelton

Just a couple of follow up questions actually to previous ones. Firstly on the impairment point and secondly on capital again. Just on this impairment point. I mean the relationship isn't linear as you say quite rightly because one would expect in fact that arrears and defaults will actually rise as house prices fall. So as well as loss given default rising, more people who get into difficulty will be unable to trade their way out of their difficulties or to refinance. So one would expect there to be this non linear relationship and I don't really see how it flattens off as you described. But I would like to think ahead to next year and assuming that we get 12 ½ % for this year and assuming we do get a further decline next year and maybe more modest than 12 ½%, should we be thinking about some multiple of £100m for each half as the impairment charge for next year? Sorry that is my first question. I have got an unrelated question on capital. I will come back to.

Answer : Tim Tookey

I mean it is not linear but there does come a point at which it levels off because you start to look at the quality of your book and the likelihood of people getting into arrears. I think the big dynamic for us that could really change it is actually if there is a significant spike in UK unemployment. It is actually unemployment that is the biggest driver of people then moving into arrears and then that gives you the issue where your loss

given default impact can come through and result in a direct impairment charge. So I would actually think that unemployment is probably the bigger issue as far as ’09 is concerned.

Further question

But if we assumed say 5%, I don’t know, house price decline next year on top of 12 ½ we are looking for something significantly more than £100m for each half next year?

Answer : Tim Tookey

As you are in sort of theoretical modelling form floor to podium, why don’t we have a chat afterwards and I will talk you through it.

Further question

Okay fine, but you will appreciate this is a very important question and this is what we are grappling with at the moment. The second issue on capital, just to come back to this point about core Tier 1 ratios. I mean I think it is absolutely correct as some of my counterparts have said, that there is a focus on this in the market, so it would be helpful for you to give us a little more idea about where you are targeting and I think, the other point is, I know we have moved from Basel I to Basel II now. Some of your competitors are still reporting on Basel I. I wondered if you could give us some indication of where the ratio might have been under Basel I. At the end of last year just to help you out it was one percentage point lower than the Basel II capital ratio, which would therefore suggest a Basel I ratio of 5.1% if we applied the same thing crudely. If you are not going to do that could you give us an indication of where the Pillar 2 charge is please?

Answer : Tim Tookey

Leigh there are three questions in there. Firstly, no we are not going to comment on Pillar 2, that was the last point. The middle point of your question was related to Basel I. Actually we don’t look at it, we don’t even calculate it under Basel I any more. Basel II is the basis upon which we measure and manage the business. It is the way we are regulated so it is entirely appropriate that that should be the way we looked at it. In terms of the first part of your question, look please don’t apologise for keep asking the question, but please don’t be offended if I bat it straight back and say, we have given a full answer on where we stand on capital. We don’t really focus on any one measure. Moreover you have to do a full capital analysis that looks at the risk appetite in the business and exactly what you have got on your balance sheet. And I think if you do that for Lloyds TSB, you would be hard pushed to disagree that our capital position is robust.

Sir Victor Blank

One last question.

<u>Question 13: Wholesale funding - Alastair Ryan, UBS</u>

Thanks. It’s Alastair Ryan at UBS again. Can I just ask on the term of your wholesale funding. What the sort of less than one year proportion would be and whether there has been a big shift in that over the last twelve months please?

Answer : Tim Tookey

Yes we haven't broken out the less than or more than, but what I can tell you is that the average term is slightly longer than it was at June of last year.

Sir Victor Blank

Alright. Thank you all very, very much for coming and for joining us. Thank you.

End of Presentation