LLOYDS BANKING GROUP

97/09 3 November 2009

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PROPOSED ALTERNATIVE TO THE GOVERNMENT ASSET PROTECTION SCHEME COMPRISING A RIGHTS ISSUE AND LIABILITY MANAGEMENT EXERCISE BY WAY OF EXCHANGE OFFERS

Lloyds Banking Group plc ('Lloyds Banking Group') today announces proposals intended to meet its current and long-term capital requirements which, if approved by shareholders, will mean that the Group will not participate in the Government Asset Protection Scheme ('GAPS').

- Fully underwritten Proposals to generate at least £21 billion of core capital[1], comprising:
  - £13.5 billion rights issue. HM Treasury, advised by UKFI, has undertaken to subscribe in full for its 43 per cent entitlement
  - Exchange Offers to generate at least £7.5 billion of contingent core tier 1 and/or core tier 1 capital (core tier 1 capital capped at £1.5 billion)
- High quality, robust and efficient capital structure:
  - Immediate 230bps increase in core tier 1 capital ratio from 6.3 per cent to 8.6 per cent[2]
  - Significant contingent core tier 1 capital – equates to additional core tier 1 capital of 1.6 per cent[3] if the Group's published core tier 1 capital ratio falls below 5 per cent
  - Reinforces the Group's capital ratios in stress conditions and meets FSA's stress test
  - Higher quality capital compared to GAPS where capital benefit reduces over time
- Significantly more attractive for shareholders than GAPS:
  - Expected to make no claims under GAPS on basis of current performance expectations
  - Expected claims less than £15.6 billion GAPS fee under the FSA's stress test scenario
  - EPS and Return on Equity enhancing relative to GAPS
- Expected EU State Aid remedies not materially negative to the Group and less onerous than anticipated under GAPS:
  - Disposal of a retail banking business with a 4.6 per cent current account market share and c.19 per cent of the Group's mortgage balances
  - £180 billion non-core asset run-down (consistent with half year announcement)
  - Prohibition on discretionary coupon payments and calls for 2 years
  - Consequent prohibition on ordinary share dividends for a similar period
  - Prohibition on making certain acquisitions for a period of 3 to 4 years
  - Group will pay £2.5 billion to HM Treasury for the benefit to the Group's trading operations as a result of HM Treasury proposing to make GAPS available to the Group
  - Continue to expect cost synergies of over £1.5 billion per annum by 2011
- Third quarter IMS released today: Group on track to deliver in line with expectations:
  - Good revenue performance with margins stabilising
  - Impairment run rate has slowed: continued confidence that overall impairments peaked in first half 2009

[1] Core tier 1 and contingent core tier 1 capital; before transaction expenses and the payment of the fee to HM Treasury for the benefit to the Group's trading operations as a result of HM Treasury proposing to make GAPS available to the Group.
[2] Pro-forma as at 30 June 2009, after expenses and GAPS payment.
[3] Pro-forma as at 30 June 2009 using the Group's actual risk-weighted assets at that date.

Sir Winfried Bischoff, Chairman of Lloyds Banking Group, said:
"These Proposals provide a significantly more attractive, market-based alternative to participating in GAPS and offer superior economic value to shareholders. We believe that this represents a significant step towards meeting our, and the Government's, objective that the Group operates as a wholly privately-owned, self supporting commercial enterprise."

A letter from Sir Winfried Bischoff to Lloyds Banking Group shareholders is included in the circular, a copy of which is being sent to shareholders today. This letter is reproduced in full below.

Availability of the Circular, Prospectus and Exchange Offer Memorandums
The Circular, including a notice convening a general meeting of Lloyds Banking Group to be held at 11.00 a.m. on 26 November 2009 at Hall 12, The Atrium, National Exhibition Centre, Birmingham B40 1NT, will be posted to shareholders today.

Copies of the Prospectus and the Exchange Offer Memorandums will be available on request in hard copy free of charge from the Lloyds Banking Group's registered office (Henry Duncan House, 120 George Street, Edinburgh EH2 4LH) or by calling 0871 384 2990 and on the Lloyds Banking Group website at www.lloydsbankinggroup.com.

Copies of each of the Prospectus, the Circular and the Exchange Offer Memorandums will also shortly be available (subject to certain restrictions including, but not limited to, restrictions on access to such documents in certain jurisdictions) on the Lloyds Banking Group website at www.lloydsbankinggroup.com/investors. The implications of the information contained in the Prospectus, the Circular and the Exchange Offer Memorandums for Overseas Shareholders may be affected by the laws of the relevant jurisdiction. Such Overseas Shareholders should inform themselves about and observe any applicable legal requirements.

The Prospectus, the Circular and the Exchange Offer Memorandums will shortly be available for inspection at the UKLA's Document Viewing Facility which is situated at:
Financial Services Authority
25 The North Colonnade
Canary Wharf
London E14 5HS

Investor meeting
A meeting for analysts and investors will be held today at 10.00 a.m. (GMT) in the King Edward Hall, Merrill Lynch Financial Centre, 2 King Edward Street, London EC1A 1HQ. This meeting will be webcast live on the Group's website www.lloydsbankinggroup.com.

Merrill Lynch International ('Merrill Lynch') and UBS Limited ("'UBS") are acting as joint sponsors, joint financial advisers, joint global co-ordinators and joint bookrunners. Citigroup Global Markets U.K. Equity Limited ("Citi") is acting as joint global co-ordinator and joint bookrunner. The Rights Issue is fully underwritten by Merrill Lynch, UBS, Citi, Goldman Sachs International ("Goldman Sachs"), HSBC Bank plc ("HSBC"), J.P. Morgan Cazenove Limited ("JPMorgan Cazenove") and others. Lloyds TSB Corporate Markets is acting as Co-Bookrunner. Credit Suisse Securities (Europe) Limited and Deutsche Bank AG are each acting as financial advisor for HM Treasury and UKFI.

This summary should be read in conjunction with the full text of this announcement and the prospectuses which are being made available today and it is not a prospectus or a prospectus "equivalent" document. Any investment decision in relation to the Proposals must only be made on the basis of information contained in and incorporated by reference in the relevant prospectuses. Qualifying Shareholders should also read, in full, the risk factors set out in the prospectus published by the Company relating to the Rights Issue dated the date of this announcement. Unless otherwise defined, capitalised terms used in this announcement have the same meaning as in the Circular.

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Shareholder enquiries
If you have questions in relation to the Proposals, please telephone the Shareholder Helpline on the numbers set out below.
UK: 0871 384 2990
Overseas: +44 (0) 208 495 4630

LETTER FROM SIR WINFRIED BISCHOFF, CHAIRMAN OF LLOYDS BANKING GROUP PLC

Directors:
Sir Winfried Bischoff (Chairman)
Lord Leitch (Deputy Chairman)
J Eric Daniels (Group Chief Executive)
Archie G Kane
G Truett Tate
Tim J W Tookey
Helen A Weir CBE
Dr. Wolfgang C G Berndt
Sir Julian Horn-Smith
Carolyn J McCall OBE
T Timothy Ryan, Jr.
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Registered Office:
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3 November 2009

Dear Shareholder,

PROPOSED ALTERNATIVE TO THE GOVERNMENT ASSET PROTECTION SCHEME COMPRISING A RIGHTS ISSUE AND LIABILITY MANAGEMENT EXERCISE BY WAY OF EXCHANGE OFFERS TOGETHER WITH THE HMT TRANSACTIONS AND SHARE SUBDIVISION

1 Introduction

Today, Lloyds Banking Group plc has announced proposals intended to meet its current and long-term capital requirements. If you, our shareholders, approve these proposals, it will mean that the Group will not participate in the Government Asset Protection Scheme ("GAPS").

The Group has also released a trading update today. This reinforces the Group's views expressed in its Interim Results News Release in August that the economic environment in the UK has begun to stabilise. Group margins are also beginning to stabilise, cost reductions for the Group remain on track and overall Group impairments have peaked. Based on the Group's trading performance during the year to date, the Board now has increased confidence in the Group's ability to deliver a strongly improving business performance in 2010 and 2011. Further details on the Group's trading update can be found in paragraph 12 of this letter.

Under the Proposals, which are fully underwritten pursuant to the Underwriting Agreements and the HMT Undertaking to Subscribe, the Group will, subject to Ordinary Shareholder approval: (i) raise £13.5 billion (£13 billion net of expenses of the Proposals) by way of a Rights Issue; and (ii) generate at least £7.5 billion in core tier 1 and/or nominal value of contingent core tier 1 capital through the Exchange Offers and/or the related underwriting arrangements. The Board believes that the Proposals provide a significantly more attractive alternative to participating in GAPS and offer superior economic value to shareholders.

HM Treasury, which holds a 43.4 per cent. holding in Lloyds Banking Group, has undertaken to the Company, pursuant to the HMT Undertaking to Subscribe, to procure that the Solicitor for the Affairs of Her Majesty's Treasury (as nominee for HM Treasury) will vote in favour of the Resolutions which are being put before Ordinary Shareholders to implement the Proposals and on which it is entitled to vote. HM Treasury has also undertaken to participate in full in respect of its rights in the Rights Issue. The Board welcomes HM Treasury's support. In addition, all the Directors intend to participate in respect of their rights in the Rights Issue.

Alongside the Proposals the Group has agreed, subject to shareholder approval (excluding HM Treasury), to pay to HM Treasury a fee of £2.5 billion for the benefit to the Group's trading operations arising as a result of HM Treasury proposing to make GAPS available to the Group (the "GAPS Payment") and the HMT Commitment Commission, being a commission of up to £143.7 million in consideration, *inter alia*, of HM Treasury's pre-launch commitment to participate in full in respect of its entitlements under the Rights Issue. Payment of a fee in relation to the benefit to the Group's trading operations as described above is also required by the European Commission as part of the expected state aid remedies. The Group has also agreed to reaffirm the lending commitments that it gave to HM Treasury in March 2009 and to maintain in the 12 months commencing 1 March 2010 similar overall levels of lending as in the 12 months commencing 1 March 2009.

Over the past few months, HM Treasury and the Group have been involved in detailed negotiations with the European Commission in relation to the terms of a restructuring plan which is required in the context of a review resulting from the state aid which has been received by the Group. The Group, together with HM Treasury, has now finalised negotiations with the European Commission around the terms of the restructuring plan and the Group expects to receive a formal decision from the Commission on the state aid position and the restructuring plan by the end of 2009. The Group is confident that the final terms of the restructuring plan will not have a materially negative impact on the Group. However, the Company expects to be prevented from paying dividends on Ordinary Shares for so long as it is prohibited from making coupon payments on certain of its other securities (which is expected to be between 31 January 2010 and 31 January 2012) as a result of the restrictions expected to be required by the European Commission as part of the restructuring plan. Further details on the current state aid position are set out in paragraph 5 of this letter.

2 The Proposals

The Proposals comprise:

(i) an equity raising of £13.5 billion (£13 billion net of the expenses of the Proposals) by way of a Rights Issue. The Rights Issue is fully underwritten pursuant to the Rights Issue Underwriting Agreement and the HMT Undertaking to Subscribe. The Issue Price at which Qualifying Shareholders will be invited to subscribe for New Shares will be determined by the Company and the Joint Bookrunners in advance of the General Meeting and will be at a discount to the Theoretical Ex-Rights Price (“TERP”), taking account of market conditions and other relevant factors; and

(ii) two separate Exchange Offers. Under the Exchange Offers, eligible holders of Existing Securities will be invited to offer to exchange such Existing Securities for either: (a) new lower tier 2 capital qualifying bonds which will be guaranteed by either the Company and/or Lloyds TSB Bank (“Enhanced Capital Notes” or “ECNs”) and which will convert into Ordinary Shares if the Group's published consolidated core tier 1 capital ratio falls to less than 5 per cent.; or (b) in the Non-US Exchange Offer only, an Exchange Consideration Amount which shall be settled in new Ordinary Shares or, at the election of the Company, cash or, in certain circumstances, ECNs. The Exchange Offers, and/or the underwriting arrangements related thereto, will create at least £7.5 billion in core tier 1 and/or nominal value of contingent core tier 1 capital. While the Exchange Offers are underwritten up to £7.5 billion, to the extent that the Exchange Offers are successful and that a market develops in ECNs, the Directors believe it is in the best interests of the Company to have the flexibility to issue further ECNs to satisfy demand.

The Proposals are fully underwritten, pursuant to the Underwriting Agreement and the HMT Undertaking to subscribe, as discussed further in paragraph 8 of this letter and sections 8.5 and 8.6 of Part XX (“Additional Information”) of the Rights Issue Prospectus. Each element of the Proposals is conditional on the approval by the Ordinary Shareholders of the Proposals Resolutions which include the HMT Transactions and the Share Subdivision).

A more detailed summary of the terms of the Exchange Offers is set out in paragraph 8 and Part A of the Appendix to this the Chairman’s Letter in the Circular. **No offer of Nil Paid Rights, Fully Paid Rights, New Shares or ECNs is being made by means of this announcement or the Circular.** Full details of the Rights Issue and the Exchange Offers, as the case may be, will be made available to eligible investors or holders in the Rights Issue Prospectus and PALS and the Exchange Offer Memoranda, respectively.

3 Rationale and key benefits of the Proposals

Rationale

As discussed further in paragraph 7 of this letter, the Board believes that the economic environment in the UK has begun to stabilise and that the UK economy is now expected to return to growth in 2010. This represents a significantly more positive environment for the Group than the conditions prevailing when the FSA Stress Test was carried out in March 2009, the time at which the Group announced its intended participation in GAPS. As previously announced, the Board continues to expect that the Group's overall impairments in the second half of the year will be significantly lower than those incurred in the first half, with progressive reductions expected thereafter.

Claims under GAPS could only be made after the First Loss (as defined in paragraph 6 of this letter) had been exceeded. However, based on the Board's view of the economic outlook for the UK, the Group does not expect that its overall impairments will be high enough to justify entering into GAPS. On this basis the Group would not expect to make any claim were it to participate in GAPS, but would nevertheless still incur significant costs. Even if the UK economy were to deteriorate to the level assumed in the FSA Stress Test, which the Board considers to be unlikely, the Board believes that the net amounts that the Group would have received under GAPS would have been less than the £15.6 billion participation fee which it would have been required to pay to participate in GAPS on the terms announced in March.

Accordingly, the Board is of the view that an alternative approach to meeting its current and long-term capital commitments, in the form of the Proposals, is in the best interests of the Group and its shareholders. The Proposals have been structured in consultation with the FSA. The Board is therefore confident that the Proposals, together with other management actions which the Board considers to be readily actionable, will generate sufficient capital to ensure that the Group no longer requires the asset protection which it would have obtained through participation in GAPS, even if the severe scenario envisaged by the FSA Stress Test were to occur. The Board believes that the Proposals represent a significant step in meeting its long-term objective: that the Group operates as a wholly privately-owned, self-supporting commercial enterprise.

The Board is pleased that it is now able to offer a market-based solution to meet its capital requirements. Such a solution was not available to the Group at the time of the announcement of the Group's intended participation in GAPS in March 2009.

Key benefits

Were it to participate in GAPS, the Group would benefit from certain loss and regulatory capital relief (as set out in more detail in paragraph 6 of this letter). However, the Board believes that the Proposals offer substantial benefits to shareholders, both on their own merits and as a significantly more attractive option in comparison to GAPS, for the reasons described in more detail below. The Board believes that the Proposals, after taking into account the GAPS Payment, will enhance both earnings per share and returns on equity for the Company relative to GAPS, even if the UK economy deteriorates to the level implied by the FSA Stress Test, which the Board considers to be unlikely.

Substantial increase in non-amortising core tier 1 equity capital: The Rights Issue will raise a total of £13.5 billion of immediately available and non-amortising core tier 1 capital, before expenses of the Proposals. Had the Rights Issue been completed as at 30 June 2009, the Group would have had a *pro forma* core tier 1 capital ratio of approximately 8.6 per cent., after taking into account expenses of the Proposals and the GAPS Payment. The Board considers that this implied level of core tier 1 capital represents a strong capital foundation to support the future stability and success of the Group.

Moreover, the core tier 1 capital raised by the Rights Issue will be available to absorb potential losses across all of the Group's assets, as opposed to GAPS which would only protect against losses on those particular assets covered by the scheme. The core tier 1 capital which would be created on conversion of the ECNs (if and when they were to convert) would also be available to absorb potential losses across all the Group's assets.

By contrast, based on the terms announced in March 2009, GAPS would have created an initial £15.6 billion of core tier 1 capital through the subscription by HM Treasury, using the GAPS participation fee, for B Shares. However, the core tier 1 capital benefit of £15.6 billion from the issue of the B Shares would have been largely offset over the subsequent seven-year period by the GAPS participation fee which would have been amortised through the Group's income statement. After taking tax into consideration, this would have reduced core tier 1 capital by £11.2 billion. Furthermore, although GAPS would offer an additional core tier 1 capital benefit by providing capital relief on the risk-weighted assets that would initially have been included in the scheme, this benefit would have reduced significantly as the assets within GAPS matured or otherwise ceased to be covered by GAPS in the short-to-medium term.

Improved capital efficiency and lower shareholder dilution: The ECNs to be issued pursuant to the Exchange Offers have been designed to provide capital to the Group without being dilutive to shareholders at the time of their issue. The ECNs will qualify at the time of their issue as lower tier 2 capital and automatically convert into Ordinary Shares if the Group's published consolidated core tier 1 capital ratio falls to less than 5 per cent. thereby increasing the Group's core tier 1 capital at such time. In the event of a conversion pursuant to this feature, up to £7.5 billion of core tier 1 capital would be generated. This provides protection against unexpected deterioration in the UK economy and the effect that such deterioration would have on the Group's capital ratios. Conversion of the ECNs, and the resulting dilution of Ordinary Shareholders, would only occur if the Group's results (in particular impairments) were significantly worse than the Board currently expects.

By contrast, under GAPS, the B Shares to be issued to HM Treasury, at a cost to HM Treasury of £15.6 billion, would have been available for conversion at HM Treasury's option into 13.6 billion Ordinary Shares, and would have converted automatically if the volume weighted average trading price of the Ordinary Shares equalled or exceeded 150 pence per Ordinary Share for 20 complete trading days in any 30 trading day period. Upon such conversion, HM Treasury's ownership of the Company would have increased to approximately 62.3 per cent. from its current level of 43.4 per cent. This substantial dilution to Ordinary Shareholders (other than HM Treasury) would, therefore, have occurred in the event that the Company's share price increased to such levels or if HM Treasury exercised its option to convert to Ordinary Shares.

Cost effective: By implementing the Proposals, although the Group will be required to make the GAPS Payment, the Group will not have to pay the £15.6 billion GAPS participation fee to HM Treasury. In addition, the Company will not issue any B Shares and, accordingly, will not have to pay HM Treasury the proposed annual dividend on the B Shares of at least £1.1 billion, subject to the Company having sufficient distributable reserves.

Improved EU state aid position relative to GAPS: Based on discussions with HM Treasury and the European Commission, the Board believes that, should shareholders adopt the Proposals, the total amount of state aid received by the Group will be significantly lower than would have been expected to be the case had the Group participated in GAPS. The Board believes that this will significantly reduce the severity of the final terms of the restructuring plan required by the European Commission to limit distortions of competition resulting from the state aid received by the Group. An update on the Group's current state aid position is set out in paragraph 5 of this letter.

No additional administrative and operational burden: Participation in GAPS would have required the Group to create an additional administrative and reporting infrastructure that would have been costly, both from a financial perspective and in terms of management time. This would have inhibited the Group's operational and commercial efficiency and flexibility and absorbed substantial Group resources.

Further detailed information on the background to GAPS and the Proposals, including the reasons for the Board concluding that not participating in GAPS is preferable to renegotiating an amended scheme, is set out in the remaining paragraphs of this letter.

4 GAPS Withdrawal Deed; HMT Undertaking to Subscribe

GAPS Withdrawal Deed

Alongside the Proposals, the Company has entered into the GAPS Withdrawal Deed. This agreement sets out the various commitments and terms agreed with HM Treasury including with respect to the implementation of the expected state aid remedies (for further detail, see paragraph 5 of this letter).

The GAPS Withdrawal Deed provides that the Group shall, subject to state aid approval being obtained and to Resolution 4 being approved by the Ordinary Shareholders (excluding HM Treasury) at the General Meeting, make the GAPS Payment. This is a fee which the Group is proposing to pay to HM Treasury for the benefit to the Group's trading operations arising as a result of HM Treasury proposing to make GAPS available to the Group from the time of the Group's announcement of its intention to participate in GAPS in March 2009 until the announcement of the Proposals. Payment of a fee is also required by the European Commission as part of the expected state aid remedies.

Had the Group not reached agreement with HM Treasury on the amount of the GAPS Payment, the Group would not be able to pursue and implement the Proposals since payment of an agreed fee is a pre-requisite to finalising negotiations with the European Commission in respect of the remedies to address the state aid the Group has received, as described further in paragraph 5 of this letter.

The terms announced in March in connection with the Group's intended participation in GAPS did not address whether a fee should be paid by the Group if it did not ultimately accede to GAPS. Therefore there is no contractual measure by which the Group can determine the level of such fee. Furthermore, whilst the European Commission has required that a commercially appropriate fee be paid, they have not prescribed the amount. The GAPS Payment has been negotiated between the Company and HM Treasury and is expected to be approved by the European Commission.

In order to determine what level of fee it would be appropriate to pay, the Group sought to quantify the benefit to the Group's trading operations arising as a result of HM Treasury making GAPS available to the Group.

The benefit to the Group has been calculated based on an estimate of the cost of capital for the Group equal to the amount of regulatory capital benefit which the Directors consider would have been received by or generated for the Group through GAPS for the period from the announcement of the Group's intention to participate in GAPS until today's date. Had GAPS not been available to the Group it would have needed to raise further capital. The calculation is difficult and, in some material respects, relies upon subjective judgements of some complexity and uncertainty. However, the amount of such regulatory capital benefit is based on: (i) the reduction of risk-weighted assets which would have arisen by virtue of GAPS; and (ii) the issuance of the B Shares. In order to determine the cost of capital for the Group, a range of outcomes can be derived from long-term historical data as well as relevant market transactions during the period. However, in this case, the Board took into account the fact that, in March 2009, the capital markets were under severe stress and the cost of capital for the Group would have been correspondingly materially higher than might have been available were only long-term historical data being used.

There are several other reasonable and supportable bases on which one can seek to quantify the benefit to the Group, and therefore the appropriate amount of the GAPS Payment. Before coming to an agreement with HM Treasury on the amount of the GAPS Payment based on the cost of capital for the Group, the Group carried out a number of analyses, in addition to the analysis referenced above, and determined a range of amounts which the Board believes reflect the amount of benefit received by the Group. The amount of the GAPS Payment negotiated and agreed with HM Treasury falls within the range of such appropriate amounts, albeit at the high end of that range. However, the Board believes that the GAPS Payment is a proportionate fee and reflects the amount of benefit received by the Group's trading operations.

The Board, having assessed carefully the amount of the GAPS Payment and the substantial benefits of the Proposals, believes that the Proposals, after taking into account the GAPS Payment, will enhance earnings per share and returns on equity for the Company relative to GAPS and, therefore, represent superior economic value to shareholders.

The GAPS Withdrawal Deed also includes undertakings by the Company in respect of certain other matters. In particular, with respect to remuneration, the Company has acknowledged its commitment to the principle that, from 2010, it should be at the leading edge of implementing the G20 principles, the FSA code on remuneration and any remuneration provisions accepted by the Government from the Walker Review, provided that this principle shall always allow the Group to operate on a level playing field with its competitors. In addition, the Company has agreed with HM Treasury the specific deferral and clawback terms which will apply to any bonuses in respect of the 2009 performance year.

Furthermore, under the GAPS Withdrawal Deed, the Group has agreed to reaffirm the lending commitments which were originally given in the Lending Commitments Deed entered into by the Group on 6 March 2009 in connection with the Group's then proposed participation in GAPS. Under those lending commitments, the Company agreed to increase lending by approximately £14 billion in the 12 months commencing 1 March 2009 to support UK businesses (£11 billion) and homeowners (£3 billion). The Group has agreed to maintain similar levels of lending in the 12 months commencing 1 March 2010, subject to adjustment of the funding commitments by agreement with HM Treasury, the Department for Business, Innovation and Skills and the Department for Communities and Local Government to reflect circumstances at the start of the 12-month period commencing 1 March 2010.

This additional lending in 2009 and 2010 is expressed to be subject to the Group's prevailing commercial terms and conditions (including pricing and risk assessment) and, in relation to mortgage lending, the Group's standard credit and other acceptance criteria (see the summary of the terms of the Lending Commitments Deed in section 8.2 of Part XX ("Additional Information") of the Rights Issue Prospectus). This lending commitment is part of the Group's ongoing support for UK businesses and homeowners.

The Group has additionally pledged its support for various Government schemes designed to provide additional funding for small businesses, and has also published charters for its small business customers making a range of pledges to help firms through the downturn.

HMT Undertaking to Subscribe

Under the HMT Undertaking to Subscribe, subject to certain terms and conditions, HM Treasury has irrevocably undertaken to procure that the Solicitor for the Affairs of Her Majesty's Treasury (as nominee for HM Treasury) (i) votes in favour of all of the Resolutions in accordance with the recommendation of the Board (except for the related party transaction resolution (Resolution 4) approving the HMT Transactions) and (ii) takes up its rights to subscribe for all of the New Shares to which it is entitled under the Rights Issue. The HMT Undertaking to Subscribe is conditional upon, among other things, the passing of Resolution 4 approving the HMT Transactions. Conditional upon (ii) above and the receipt by the Company of the aggregate subscription proceeds payable by HM Treasury, the Company has agreed to pay to HM Treasury (or to such other person as HM Treasury may direct) the HMT Commitment Commission. If HM Treasury had not committed to participate in full in respect of its entitlements under the Rights Issue, then the Group would have sought to ensure that HM Treasury's entitlement under the Rights Issue would have been covered by the underwriting commitments given by the Underwriters in which case an amount similar to that to be paid to HM Treasury would have been expected to have been paid instead to the Underwriters. Further details of the HMT Undertaking to Subscribe are set out in section 7.2 of Part XX ("Additional Information") of the Rights Issue Prospectus.

Related Party Transaction

As HM Treasury holds more than 10 per cent. of the voting rights in the Company, HM Treasury is a "related party" for the purposes of the Listing Rules. Making the GAPS Payment and payment of the HMT Commitment Commission (together the "HMT Transactions") are each "related party transactions" (as defined in the Listing Rules). The HMT Transactions must, pursuant to the Listing Rules, each be approved by the Ordinary Shareholders other than the related party, that is HM Treasury. Resolution 4 seeks approval for the HMT Transactions. However, HM Treasury shall not be entitled to vote on such Resolution. HM Treasury has further undertaken, as required by the Listing Rules, to take all reasonable steps to ensure that its associates, if any, will not vote on that Resolution.

5 State Aid

The Group has previously announced that, as a result of HM Treasury's investment in the Company in the context of the placing and open offer undertaken by the Company in November 2008 and the Group's participation in the Credit Guarantee Scheme, the Group has been required to work with HM Treasury to submit a restructuring plan to the European Commission in the context of a state aid review. Any such plan is required to contain measures to limit any competition distortions resulting from the state aid received by the Group.

The European Commission has made it clear that it will require the Group to divest a standalone UK banking business as a condition of obtaining state aid approval and may also require behavioural restrictions as part of the restructuring plan. Accordingly, over the past few months, HM Treasury and the Group have been involved in detailed negotiations with the European Commission in relation to the terms of the restructuring plan (including the ultimate compensatory measures) in order to reach a mutually acceptable solution.

The ultimate decision regarding the approval of the UK Government's state measures, including the terms of the final restructuring plan, will be taken by the College of Commissioners (which the Board expects to occur before the end of 2009), and therefore at this stage there can be no certainty as to the outcome of the state aid proceedings and the content of the final restructuring plan. See the risk factor described in section 1.3 of Part II ("Risk Factors") of the Rights Issue Prospectus for further discussion of the risks relating to the state aid proceedings. The Board expects, however, based on the outcome of its negotiations with HM Treasury and the European Commission, that the final restructuring plan will consist of the following principal elements:

(i) the disposal of a retail banking business with at least 600 branches, a 4.6 per cent share of the personal current accounts market in the UK and approximately 19 per cent of the Group's mortgage assets. The business would consist of:

- the TSB brand;
- the branches, savings accounts and branch based mortgages of Cheltenham & Gloucester;
- the branches and Branch Based Customers of Lloyds TSB Scotland and a related banking licence;
- additional Lloyds TSB branches in England and Wales, with Branch Based Customers; and
- Intelligent Finance,

and would need to be disposed of within four years;

(ii) an asset reduction programme to achieve a £181 billion reduction in a specified pool of assets by 31 December 2014; and

(iii) behavioural commitments, including commitments:

- not to make certain acquisitions for approximately three to four years; and
- not to make discretionary payments of coupons or to exercise voluntary call options on hybrid securities from 31 January 2010 until 31 January 2012, which will prevent the Group from paying dividends on its ordinary shares for the same duration.

The assets and liabilities, and associated income and expenses, of the business to be divested (referred to in sub-paragraph (i) above) cannot be determined with precision until nearer the date of sale. However, the Company estimates that, as at 31 December 2008 and after aggregating the elements relating to Lloyds TSB and HBOS, the business to be divested comprised approximately £70 billion of customer lending and £30 billion of customer deposits and, on this basis, approximately £18 billion of risk-weighted assets. For the year ended 31 December 2008, the Board estimates that the business to be divested generated income of approximately £1.4 billion and, after associated direct expenses of approximately £600 million and impairment charges of £300 million, contributed approximately £500 million of profit before tax to the Group.

The Board believes that the restructuring plan as described above is sufficient to obtain approval from the European Commission for the state aid the Group has received, including to the extent that HM Treasury's participation in the placing and compensatory open offer in June 2009 and in the Rights Issue might constitute state aid, as well as any commercial benefit received by the Group following the Group's announcement in March 2009 of its intention to participate in GAPS. The Board is confident that this restructuring plan will not have a materially negative impact on the Group.

The Company has agreed with HM Treasury in the GAPS Withdrawal Deed that the Company will comply with the terms of the European Commission's final decision (see section 7.1 of Part XX

("Additional Information") of the Rights Issue Prospectus for a summary of the GAPS Withdrawal Deed).

6 Background to GAPS

Given the extremely uncertain outlook for the UK economy at the end of 2008 and into 2009, the Group worked with the FSA to identify and analyse the potential impact of an extended and severe UK recession on the Group's regulatory capital ratios. Due to the significant uncertainty at that time over the length and depth of the recession, the Group was tested against the FSA Stress Test.

The FSA has stated that the assumptions underlying the FSA Stress Test were not intended to be a forecast of what was likely to happen, but were designed to be a severe economic scenario. These assumptions included a peak-to-trough fall in UK GDP of over 6 per cent., with growth not returning until 2011 and only returning to trend-rate growth in 2012. They also included assumptions that unemployment would rise to just over 12 per cent, that the UK would experience a 50 per cent peak-to-trough fall in house prices and that there would be a 60 per cent peak-to-trough fall in commercial property prices.[1]

The conclusion from this exercise was that the Group would need additional capital to enable it to absorb the future impairments anticipated in such a severe scenario.

As a result, on 7 March 2009, the Group announced its intention to participate in GAPS in respect of certain assets with an aggregate par value of approximately £260 billion. This announcement was made, in part, on the basis of the term sheet published by HM Treasury on 26 February 2009, which set out the expected key terms, conditions and operational principles of GAPS.

As consideration for entering into GAPS, it was expected that the Group would pay a participation fee to HM Treasury of £15.6 billion, to be amortised over an estimated seven-year period. The proceeds of this fee would have been applied by HM Treasury in subscribing for an issue of B Shares by the Company. In addition to the participation fee, the Group would also have had to assume 100 per cent of the losses relating to the first £35 billion of impairments (including historical impairments and write-downs) relating to the assets covered by GAPS (the "First Loss") and a further 10 per cent of cumulative losses in the whole portfolio of assets thereafter, up until the date specified as the maturity date of each covered asset.

The £15.6 billion of B Shares would have carried an annual dividend to be paid to HM Treasury (subject to the availability of distributable reserves and any restriction on payment of dividends that might have been required by the European Commission) of the greater of 7 per cent of the issue price of the B Shares and 125 per cent. of any dividend on Ordinary Shares for each period. It was expected that the dividend payable on the B Shares would have been at least £1.1 billion per annum, subject to the availability of distributable reserves.

The entry into GAPS was intended to provide two key benefits to the Group. First, loss relief, particularly in a scenario of severe economic stress such as would be implied by the FSA Stress Test. Once the First Loss had been utilised the Group would not have been exposed to the full amount of losses it might otherwise have incurred in respect of non-performing assets covered by the scheme. Second, the entry into GAPS was intended to provide regulatory capital relief (or an increase in the Group's core tier 1 capital ratio), arising from a reduction in the Group's risk-weighted assets as well as the generation of new core tier 1 capital through the issuance of the B Shares.

As explained in paragraph 7 of this letter, however, the Board no longer believes that the entry into GAPS, either on the terms announced in March 2009 or on any such revised terms which the Board believes may currently be available to the Group, is in the best economic interests of its shareholders.

[1] Source: FSA statement on its use of stress tests, FSA/PN/068/2009.

7 Background to the Proposals

The Group accepts and agrees with the merits of severe stress testing of regulatory capital, and the Proposals, together with other management actions which the Board considers to be readily actionable, are specifically designed to provide the capital enhancement that the Board believes is necessary to meet the capital requirements of the FSA Stress Test. The Board believes that, since commencing the negotiation of the terms of GAPS, the UK economy has begun to stabilise and is now expected to return to growth in 2010. Accordingly, the Board believes that the likelihood of the UK economy deteriorating to the levels implied by the FSA Stress Test, the assumptions behind which remain unchanged, is now materially lower than was the case in March 2009.

Since March 2009, the Group's core business has proved to be resilient despite the difficult economic circumstances under which it has had to operate.

In addition, the Group has completed detailed credit reviews of the Group's asset portfolio in accordance with the Group's risk management approach, including, most importantly, the legacy HBOS portfolio and file-level credit reviews of the Group's wholesale portfolio. This analysis, in conjunction with management's view of the economic outlook for the UK, underpins the Board's belief that the Group's overall impairments peaked in the first half of the current year, and that overall impairments in the second half of the year will be lower than in the first half. It also gives the Board a high level of confidence both in the adequacy of the substantial impairments which it has already taken against these assets (including with respect to the Group's commercial and residential property exposures) and in the scale and timing of expected future impairments. Further detail on Group impairments by division is set out below, and in the Interim Management Statement (set out in full in the appendix to Part IX ("Information on the Group") of the Rights Issue Prospectus).

Impairments

A significant proportion of the Group's impairments to date have originated in the Group's Wholesale division, primarily reflecting the significant and rapid decline in commercial property prices and reducing levels of corporate cash flow. The Group's impairments were also impacted by the exposures in certain legacy HBOS portfolios, which were more sensitive to the downturn in the economic environment. Having analysed the portfolio of wholesale assets, the Board expects a significant overall reduction in the Wholesale impairment charge in the second half of 2009, with a further improving trend in 2010.

In the Retail division, the Company has experienced a change in the mix of impairments in the first half of 2009, as the relative weighting between secured and unsecured impairments returned to a more normal pattern. This change has been more positive than expected due to a variety of factors, including: (i) a stabilising outlook for house prices (which has had a positive impact, primarily on the secured portfolio); (ii) increasing levels of unemployment (which has had a negative impact, primarily on the unsecured portfolio); and (iii) lower than previously expected house repossessions as customers benefit from the low interest rate environment and therefore lower mortgage payments (which has had a positive impact, primarily on the secured portfolio). In light of these trends, and management's expectations with regard to the UK economic outlook, the Board believes that Retail impairments will peak in the second half of 2009, with an improving trend expected in 2010.

In the Wealth and International division, the impairment charge increased in the first half of 2009 reflecting significant provisions against the Group's Irish and Australian commercial real estate portfolios. The Group continues to have ongoing concerns with regard to the outlook for the Irish economy and expects the high level of impairments to continue throughout 2009 and in 2010.

In conclusion, given its view of the economic outlook for the UK, the Board believes that, at the Group, level the overall impairment charge has now peaked and that the overall impairment charge in the second half of 2009 will be significantly lower than the overall impairment charge in the first half of 2009, with a significantly improving trend thereafter.

GAPS

Since 7 March 2009, the Company has been working closely with HM Treasury to finalise the terms and conditions and operational mechanics of the Group's participation in GAPS. However, as these terms and conditions were being negotiated, it became clear that the benefits of GAPS to the Group would have been materially less extensive and that the costs to the Group of participating in the scheme, both financially and in terms of management time, would have been materially higher (and the impact on the Group materially more onerous) than was anticipated by the Board at the time its intended participation in GAPS was announced. The following issues in particular are relevant:

Capital Relief: The capital relief arising as a result of the large reduction in risk-weighted assets would have been much lower than had been anticipated by the Board in March 2009. This is due to various factors, including the fact that: (i) in March 2009 significant benefit was expected to arise in respect of the Group's Treasury assets (however, the Group has (with FSA approval) successfully resecuritised those assets and thereby reduced the risk-weighting of the assets); and (ii) updated, more accurate forecasting has changed the Group's expectations of its quantum of risk-weighted assets. Further, it has become clear to the Board that the operation of GAPS, as it would apply to the Group, would serve to remove certain assets from coverage within a short period after commencement of the scheme which would mean the risk-weighted asset relief afforded by GAPS would reduce more quickly than had been anticipated by the Board in March.

GAPS Rules: The development of the detailed scheme rules for GAPS since the GAPS term sheet was published in February 2009 has meant that in many areas the scheme rules are more disadvantageous for the Group than the position which had been anticipated by the Board when it announced its initial intention to participate. In practice, the Board believes it is highly likely that the operation of GAPS would have been economically unsatisfactory for the Group. For example, although it is expected that under GAPS losses relating to restructuring events would be covered, the Group may not have benefitted from full coverage for certain restructuring and refinancing activities.

Consideration of alternative solutions

These circumstances and improved economic conditions caused the Board to consider alternative solutions that might provide superior economic value to shareholders than entry into GAPS. These potential alternative solutions included:

- renegotiating the commercial terms of GAPS, the type and quantum of assets covered by the scheme and the scheme rules;
- not entering into GAPS at all and instead raising sufficient additional capital on the public capital markets; or
- a combination of either of the above options.

Over the past few months, the Board has had negotiations with HM Treasury and discussions with other relevant authorities in relation to these potential alternatives. The Board gave careful consideration to possible alternative formulations of GAPS, including a possible combination of a smaller version of GAPS with elements of the Proposals. The Board concluded it would not be in the best interests of its shareholders to pursue these alternative formulations for the reasons set out below:

- **State aid**: The alternative formulations of GAPS would, in the view of the Board, constitute additional state aid, which would likely require more severe compensatory measures than is expected to be the case if the Proposals are implemented;
- **Uncertainty of outcome and potential delay**: There was no agreement between the Group and HM Treasury either on the general outline of any specific alternative formulation of GAPS or on the precise commercial terms on which any alternative formulation would have been made available to the Group. While the Board believes that, had negotiations continued, they would have been conducted in good faith, it had no certainty as to the outcome of such negotiations or whether or when such negotiations would have been concluded to the parties' mutual satisfaction, whereas the Proposals can be implemented immediately;
- **Shareholder dilution**: The issue of any B Shares in connection with a renegotiated or reduced form of GAPS would still have resulted in dilution for Ordinary Shareholders (other than HM Treasury) and would have increased the percentage holding of HM Treasury in the Company, thereby potentially delaying and making more difficult any eventual orderly exit by HM Treasury from its shareholding;

- **Non-market-based solution**: The Board's aim is that the Group returns to being a self-standing, wholly privately-financed institution as soon as practicable. The Board believes that the Proposals advance this objective more quickly and effectively than would have been the case had the Group participated in GAPS. At the same time, the Proposals improve the quality of the Group's capital structure in a way that is to the long-term benefit of the Group; and
- **Cost and complexity:** The alternative formulations of GAPS would have involved additional administrative and reporting structures which would, in the Board's view, have inhibited the Group's operational and commercial flexibility.

8 Principal terms of the Proposals

Rights Issue

The Group is proposing to raise £13.5 billion by way of the Rights Issue.

The Rights Issue is fully underwritten pursuant to the Rights Issue Underwriting Agreement and the HMT Undertaking to Subscribe. The Issue Price at which Qualifying Shareholders will be invited to subscribe for New Shares will be determined by the Company and the Underwriters in advance of the General Meeting and will be at a discount to TERP. The Issue Price is expected to be announced on 24 November 2009, two days before the General Meeting.

Under the Rights Issue, the New Shares will be offered by way of rights to all Qualifying Shareholders (other than, subject to certain exceptions as set out in section 2.5 of Part VIII ("Terms and Conditions of the Rights Issue") of the Rights Issue Prospectus, Qualifying Shareholders with a registered address or resident in the United States or any other Restricted Jurisdictions).

Entitlements to New Shares will be rounded down to the nearest whole number and fractions of New Shares will not be allotted to Qualifying Shareholders but will be aggregated and the resulting New Shares will be issued to subscribers in the market for the benefit of the Company. Holdings of Existing Qualifying Shares in certificated and uncertificated form will be treated as separate holdings for the purpose of calculating entitlements under the Rights Issue, as will holdings under different designations and in different accounts.

The New Shares, when issued and fully paid, will rank *pari passu* in all respects with the Existing Ordinary Shares, including the right to receive dividends or distributions made, paid or declared (if any) after Admission of such New Shares, as described below.

Applications will be made to the UK Listing Authority for the New Shares to be admitted to the Official List and to the London Stock Exchange for the New Shares to be admitted to trading on the London Stock Exchange's main market for listed securities.

It is expected that Admission will occur, and that dealings in the New Shares on the London Stock Exchange will commence at 8.00 a.m. on 27 November 2009.

Some questions and answers, together with details of further terms and conditions of the Rights Issue including the procedure for application and payment, are set out in Parts VII ("Some Questions and Answers about the Rights Issue") and VIII ("Terms and Conditions of the Rights Issue") of the Rights Issue Prospectus and, for Qualifying Non-CREST Shareholders, will also be set out in the Provisional Allotment Letters and the Shareholder Guide.

Exchange Offers

The Group will generate at least £7.5 billion of core tier 1 and/or nominal value of contingent core tier 1 capital through the Exchange Offers and/or the related underwriting arrangements.

The Exchange Offers comprise two separate offers in respect of Existing Securities issued by various members of the Group, as follows:

(i) an offer to be conducted in certain countries outside the United States and will be available only to non-US persons with respect to 52 series of Existing Securities, comprising upper tier 2 capital securities in an aggregate principal amount of £2.52 billion, innovative tier 1 securities in an aggregate principal amount of £7.68 billion and preference shares (or equivalents) in an aggregate liquidation preference/principal amount of £4.09 billion; and

(ii) a separate offer to the holders of six series of Existing Securities, comprising upper tier 2 capital securities in an aggregate principal amount of £1.74 billion and tier 1 securities in an aggregate principal amount of £0.46 billion, which is being made in certain countries outside the United States and to certain sophisticated holders in the United States who are "qualified institutional buyers" as defined in Rule 144A of the Securities Act.

Certain eligible holders of the Existing Securities will be invited to offer to exchange their Existing Securities for either: (i) Enhanced Capital Notes on a par-for-par basis; or (ii) (in the Non-US Exchange Offer only) an Exchange Consideration Amount (up to a limit of £1.5 billion) which shall be settled in Ordinary Shares or, at the election of the Company, cash or, in certain circumstances ECNs.

Eligible holders of those Existing Securities which are accepted for exchange into the relevant Exchange Consideration Amount will receive, following a delayed settlement period of 90 days, such Exchange Consideration Amount in the form of Ordinary Shares or, at the election of the Company, cash (or, in the limited circumstances described below, ECNs). The number of Ordinary Shares to be delivered in satisfaction of such Exchange Consideration Amount shall be based on the higher of (i) the arithmetic average of the volume-weighted average trading price of the Ordinary Shares to be determined over a five trading day period towards the end of the delayed settlement period (the "VWAP") and (ii) 90 per cent. of the Ordinary Share closing price on 11 February 2010. The Company may satisfy some or all of the Exchange Consideration Amount (being an amount up to £1.5 billion) in either cash or Ordinary Shares, provided that the maximum number of Ordinary Shares to be issued for this purpose will not exceed a number, the value of which is equal to £1.5 billion (or, if the total Exchange Consideration Amount is less than £1.5 billion, such lesser amount) divided by 75 per cent. of the Unadjusted Conversion Price, subject to adjustment for the impact of the Rights Issue. To the extent that the value of all such Ordinary Shares is less than £1.5 billion, holders will, on the delayed settlement date, receive ECNs on the same par-for-par basis as described above to satisfy any such short fall.

The Exchange Offers described above are not being made by means of this announcement or the Circular. The Non-US Exchange Offer is not being made available to U.S. persons. The Non-US Exchange Offer is not being made, directly or indirectly in or into, or by use of the mail of, or by any means or instrumentality or foreign commerce of, or of any facilities of a national securities exchange of, the United States as defined under Regulation S of the Securities Act, or for the account or benefit of, U.S. persons.

The Exchange Offers have not been registered under the Securities Act. Securities offered pursuant thereto may not be offered or sold within the United States absent registration or an applicable exemption from the registration requirement of the Securities Act.

Underwriting

The Proposals are being fully underwritten pursuant to the Underwriting Agreements.

Rights Issue

The Rights Issue is fully underwritten pursuant to the Rights Issue Underwriting Agreement and the HMT Undertaking to Subscribe. The New Shares will be issued at price equal to the higher of (i) 15 pence per New Share and (ii) a price which is within a range of 38 per cent. to 42 per cent. discount to TERP, taking account of market conditions and other relevant factors. Sufficient New Shares will be issued to ensure that the gross proceeds of the Rights Issue receivable by the Company, including pursuant to the HMT Undertaking to Subscribe, are not less than £13.5 billion. To the extent that any New Shares are not subscribed for or are otherwise deemed not to be taken up or placed within the Rump Placing, the Joint Bookrunners, the Senior Co - Lead Managers and the Co-Lead Managers will severally subscribe for such number of New Shares (excluding any New Shares to be subscribed by HM Treasury pursuant to the HMT Undertaking to Subscribe) at the Issue Price as is required to ensure that the gross proceeds of the Rights Issue received by the Company, including pursuant to the HMT Undertaking to Subscribe, are not less than £13.5 billion.

A summary of the principal terms and conditions of the Rights Issue Underwriting Agreement is set out in section 8.5 of Part XX ("Additional Information") of the Rights Issue Prospectus.

Exchange Offers
The Exchange Offers are also fully underwritten pursuant to the Additional ECN Issues Underwriting Agreement. This means that, to the extent that the Exchange Offers, together with any other liability management transactions that might be undertaken by the Group (acting reasonably and in consultation with the Underwriters) prior to 30 April 2010, do not generate £7.5 billion or more of core tier 1 capital and/or nominal value of contingent core tier 1 capital, the Additional ECN Underwriters will underwrite one or more further issues of additional ECNs in an aggregate amount sufficient to reduce such shortfall to zero.

A summary of the principal terms and conditions of the Additional ECN Issues Underwriting Agreement is set out in section 8.6 of Part XX ("Additional Information") of the Rights Issue Prospectus.

Once the Resolutions relating to the Proposals have been approved, each of the Proposals shall proceed independently of one another.

9 Impact of conversion

The ECNs will convert into Ordinary Shares in certain circumstances. This could have the effect of materially diluting the interests of Ordinary Shareholders at the time of any conversion. **For further details on how such dilution might impact Ordinary Shareholders, please refer to Part C of the Appendix to the Chairman's Letter in the Circular.**

10 Share Subdivision

Under the Companies Act, it is not permissible for a company to issue shares at a discount to their nominal value, which, in respect of the Existing Ordinary Shares is currently 25 pence per share. It is proposed that the Company carries out the Share Subdivision which will reduce the nominal value to 10 pence per share. This provides the Company and the Joint Bookrunners with greater certainty that the Issue Price will be able to be set at a 38 per cent. to 42 per cent. discount to TERP irrespective of market conditions. The Board believes that the Share Subdivision also provides the Company access to the best available underwriting structure and terms. Although no decision has currently been made as to the Issue Price, in no circumstances will the Issue Price be below 15 pence. As noted in paragraph 8 of this letter, the Issue Price is expected to be announced on 24 November 2009, two days before the General Meeting. The Proposals are conditional on, amongst other things, the completion of the Share Subdivision.

It is proposed that, pursuant to the Share Subdivision, each existing Ordinary Share of 25 pence in issue at the close of business on the date of the General Meeting will be subdivided into one ordinary share of 10 pence in the capital of the Company (a "10p Ordinary Share") and one deferred share of 15 pence in the capital of the company (a "Deferred Share"). The purpose of the issue of Deferred Shares is to ensure that the reduction in the nominal value of the Ordinary Shares does not result in a reduction in the capital of the Company.

Each Ordinary Shareholder's proportionate interest in the Company's issued ordinary share capital will remain unchanged as a result of the Share Subdivision. Aside from the change in nominal value, the rights attaching to 10p Ordinary Shares (including voting and dividend rights and rights on a return of capital) will be identical in all respects to those of existing Ordinary Shares. No new share certificates will be issued in respect of the 10p Ordinary Shares as existing share certificates for existing Ordinary Shares will remain valid in respect of the same number of 10p Ordinary Shares arising from the Share Subdivision. The number of Ordinary Shares of the Company listed on the Official List and admitted to trading on the London Stock Exchange's main market for listed securities shall not change as a result of the Share Subdivision. The Share Subdivision will not affect the Group's or the Company's net assets. Consequently, the market price of a 10p Ordinary Share immediately after completion of the Share Subdivision should, theoretically, be the same as the market price of an Ordinary Share immediately prior to the Share Subdivision.

In addition, it is proposed that, pursuant to the Share Subdivision and as required by Article 3.1.4(i) of the Articles of Association, each existing Limited Voting Share of 25 pence in issue at the close of business on the date of the General Meeting will be subdivided into one limited voting share of 10 pence (a "10p Limited Voting Share") and one Deferred Share. Aside from the change in nominal value, the rights attaching to 10p Limited Voting Shares will be identical in all respects to those of existing Limited Voting Shares. No new share certificates will be issued in respect of the 10p Limited Voting Shares as existing share certificates for existing Limited Voting Shares will remain valid in respect of the same number of 10p Limited Voting Shares arising from the Share Subdivision.

The Deferred Shares created on the Share Subdivision becoming effective will have no voting or dividend rights and, on a return of capital on a winding up of the Company, will have the right to receive the amount paid up thereon only after Ordinary Shareholders have received, in aggregate, any amounts paid up thereon plus £10 million per Ordinary Share.

No share certificates will be issued in respect of the Deferred Shares, nor will CREST accounts of shareholders be credited in respect of any entitlement to Deferred Shares, nor will they be admitted to the Official List or to trading on the London Stock Exchange or any other investment exchange. The Deferred Shares shall not be transferable at any time, other than with the prior written consent of the Directors. The rights attaching to, and restrictions upon, the Deferred Shares are set out in Resolution 6.

At the appropriate time, the Company may repurchase the Deferred Shares, make an application to the High Court for the Deferred Shares to be cancelled, or cancel, or seek the surrender of the Deferred Shares using such other lawful means as the Directors may determine.

11 Integration of HBOS and synergies update

The Group has completed the planning of its key integration activities and the execution of a broad range of over 100 integration programmes is well underway just over nine months after the acquisition of HBOS. The Board is pleased with the progress made so far and remains confident that the Group will meet its commitment to deliver cost synergies and other operating efficiencies from the Acquisition of greater than £1.5 billion per annum by the end of 2011, notwithstanding the business impact of the expected state aid remedies as referred to in paragraph 5 of this letter. The Company's unaudited interim results announcement on 5 August 2009 highlighted that over £100 million of cost synergies were realised by the Group in the first half of 2009. On the basis of first half initiatives and programmes to be implemented during the second half of the financial year, the Group expects to finish 2009 with annualised run-rate cost savings of £750 million.

The integration of such a large enterprise as HBOS inevitably takes time, but once the full extent of the benefits of such integration are realised, particularly in light of the Group's view that the economic environment in the UK has begun to stabilise, the Board believes the Group will be in a strong position to create significant value for you, our shareholders.

12 Current trading, trends and prospects

On 5 August 2009, Lloyds Banking Group announced its interim results for the half year ended 30 June 2009. Despite the significant impairments which were announced at that time, the Group was able to demonstrate the continued resilience of its core business.

As announced in the Interim Management Statement, the Group has continued to deliver a good revenue performance in the third quarter of 2009, with similar trends, excluding gains on liability management, to those delivered in the first half of the year. The Group's banking net interest margin has shown clear signs of stabilising in the third quarter of 2009, compared to the first half of the year. The Group continues to deliver a strong cost performance and, in addition, the Board feels that excellent progress has continued to be made on the integration of the enlarged Group, with the achievement of a higher run-rate of cost synergies than those previously announced. The overall run-rate of impairments has slowed in the third quarter of the year. As a result, the Group continues to expect impairments to fall significantly in the second half of 2009, compared to the first half of the year. As previously announced, the Group continues to expect to report a loss before tax for 2009, excluding the impact of the £11.2 billion credit relating to negative goodwill.

As reported in the Interim Results News Release, the Group has identified approximately £300 billion of assets associated with non-relationship lending and investments, including business which is outside its current risk appetite, which may have been earmarked for GAPS protection were the Group to participate in the scheme. The Group's approach to managing these assets would be the same whether or not it moves forward with the Proposals or participates in GAPS. It is the Group's intention to manage such assets for value and run them down over time given the current economic climate. Over the next five years, the Group expects to achieve a reduction in such assets of approximately £200 billion, which equates to approximately 20 per cent of the Group's total balance sheet assets as at 30 June 2009. The impact of running down those assets is not expected to have a materially negative impact on the Group's income over the five year period.

The full text of the Interim Management Statement is set out on pages 109 to 111 of the Rights Issue Prospectus.

13 Group capital and liquidity policies

In September 2008, the Group set out a target that its core tier 1 capital ratio be in the range of 6 to 7 per cent. Reflecting the increase in expected levels of core tier 1 capital across the industry since that time, the Board's target has now been increased to be more than 7 per cent.

As discussed above, the Rights Issue will raise a total of £13.5 billion of core tier 1 capital before expenses of the Proposals and before the making of the GAPS Payment. Had the Rights Issue been completed as at 30 June 2009, this would have resulted in a pro forma core tier 1 capital ratio for the Group of approximately 8.6 per cent. after expenses of the Proposals and the GAPS Payment. Further details on the Group's capital resources and liquidity can be found in Part XV ("Capital Resources") of the Rights Issue Prospectus.

14 Working Capital

The Company is of the opinion that, after taking into account existing available bank and other facilities, the Exchange Offers and the net proceeds of the Rights Issue, the Group has sufficient working capital for its present requirements, that is, for at least the next 12 months from the date of this announcment.

15 Dividends and dividend policy

As a result of the expected state aid remedies referred to in paragraph 5 of this letter, the Company expects to be prevented from making discretionary (contractually deferrable or waivable) coupon and dividend payments on hybrid capital securities or making voluntary calls on such securities from 31 January 2010 until 31 January 2012. Should the Group be prevented from making such payments, the Company will be restricted by the terms of such hybrid capital securities from paying dividends on its Ordinary Shares for the duration of such restrictions. However, the Board intends to resume dividend payments on its Ordinary Shares as soon as market conditions and the financial position of the Group permit, subject to the expiry of the restrictions outlined above. See also the risk factor described in section 1.5 of Part II ("Risk Factors") of the Rights Issue Prospectus.

16 Lloyds Banking Group General Meeting

The Proposals are conditional upon the approval of the Proposals Resolutions by the Ordinary Shareholders at the General Meeting. These Resolutions, together with other Resolutions intended to update the Directors' authorities to allot shares generally and on a non-pre-emptive basis, to effect a capitalisation issue for holders of Limited Voting Shares as required by the Articles, and to buy back certain 6.3673 per cent. preference shares in order to simplify the Group's capital structure, are set out in the notice convening a General Meeting of the Company to be held on 26 November 2009 at Hall 12, The Atrium, National Exhibition Centre, Birmingham B40 1NT at 11:00 a.m., which is set out at the end of the Circular. Further details of the Resolutions proposed to be passed at the General Meeting are set out in the notice. The purpose of the General Meeting is to consider and, if thought fit, pass the Resolutions, a summary of which is set out in Part B of the Appendix to the Chairman's Letter in the Circular.

As mentioned in paragraph 4 above, since the HMT Transactions involve Lloyds Banking Group's substantial shareholder, HM Treasury (which at 30 October 2009, (being the last practicable date prior to the date of the Circular) indirectly held 11,798,531,471 Ordinary Shares, representing approximately 43.4 per cent. of the issued ordinary share capital of the Company), they are related party transactions for the purposes of the Listing Rules. Therefore, as required by the Listing

Rules, the HMT Transactions are conditional on the approval of Resolution 4 by the Ordinary Shareholders (other than HM Treasury, which, in accordance with the Listing Rules, may not vote on Resolution 4 and has agreed to take all reasonable steps to ensure that its associates, if any, do not vote on Resolution 4).

17 Use of proceeds

The primary motive behind the Proposals is to raise core tier 1 and contingent core tier 1 capital, and as such any net cash proceeds will be used in the day-to-day operations of the Group. The proceeds raised and/or capital generated from the Rights Issue are expected to, in aggregate, increase the Group's core tier 1 capital ratio by approximately 230 basis points to around 8.6 per cent on a *pro forma* basis as at 30 June 2009 taking into account expenses of the Proposals and the GAPS Payment.

18 Action to be taken by Ordinary Shareholders

A Form of Proxy is enclosed which covers the Resolutions to be proposed at the General Meeting and which is for use by the holders of Ordinary Shares. If you are a person nominated under section 146 of the 2006 Act to enjoy information rights, please read Note 2 to the Notice of General Meeting.

Completed Forms of Proxy should be returned in accordance with the instructions printed on them as soon as possible, but in any event no later than 11.00 a.m. on 24 November 2009. In addition, it is possible to appoint and instruct your proxy electronically by following the instructions on the enclosed Form of Proxy. Completion of a Form of Proxy will not prevent you from attending and voting at the General Meeting if you so wish. To appoint more than one proxy (each of whom must be appointed to exercise rights attached to the different shares held by you), see Note 3(b) on the reverse of the Form of Proxy.

At the General Meeting, the Company will disclose, for each Resolution, the total of the proxy votes received and any votes cast at the meeting, the proportion for and against each Resolution, and the number of votes withheld. Votes withheld will not be counted in the calculation of the proportion of votes `for' and `against' a Resolution.

Voting at the General Meeting in respect of each Resolution will be conducted by way of a poll. The Directors believe it is important that the intentions of all members who register a vote are fully taken into account. Voting on a poll is more transparent and equitable, since it allows the votes of all shareholders who wish to vote to be taken into account, and it reflects evolving best practice. Ordinary Shareholders who attend the meeting will still be able to ask questions relevant to the business of the meeting prior to voting on the Resolutions.

19 Fees and Expenses relating to the Proposals

Fees and expenses relating to the Proposals are expected to be approximately £500 million.

20 Further information

Your attention is drawn to the further information set out in Parts A, B and C of the Appendix to the Chairman’s Letter in the Circular. You should read the whole of the Circular and not rely solely on the information set out in this announcement or the Chairman’s Letter in the Circular.

21 Consents

Merrill Lynch, whose address is Merrill Lynch Financial Centre, 2 King Edward Street, London EC1A 1HQ, has given and has not withdrawn its written consent to the inclusion in the Circular of references to its name in the form and context in which they appear.

UBS, whose address is 1 Finsbury Avenue, London EC2M 2PP, has given and has not withdrawn its written consent to the inclusion in the Circular of references to its name in the form and context in which they appear.

J.P. Morgan Cazenove, whose address is 20 Moorgate, London EC2R 6DA, has given and has not withdrawn its written consent to the inclusion in the Circular of references to its name in the form and context in which they appear.

22 Importance of the Vote

The Board believes that the Proposals provide a more attractive alternative to participating in GAPS and offer superior economic value to shareholders. Should any of the Proposals Resolutions (which include the resolution to approve the HMT Transactions) not be approved by the relevant Ordinary Shareholders, the Proposals will not proceed. Should the Proposals not proceed, the Group may not be able to meet the regulatory capital ratios required to be maintained by the FSA in the medium and long term and, should that be the case, will need to raise additional capital. For the avoidance of doubt, should any of Resolutions 3, 5, 10 and 12 not be approved by Ordinary Shareholders, the Proposals may still proceed.

The options available to the Board in such circumstances are not yet clear. However, it is highly likely that the Group would need to reopen discussions with HM Treasury regarding its possible participation in GAPS or approach the UK Government for alternative support, although there can be no assurance that the Group would be permitted to enter into GAPS, or what form any alternative UK Government support may take. Furthermore, there can be no certainty that any such participation by the Group in GAPS would not be on terms which are more onerous to the Company than the terms announced in March 2009. In addition, such participation or alternative support could require additional state aid remedies. If the Group were permitted to participate in GAPS in these circumstances, it would seek to finalise the terms of its participation as soon as practicable, although there can be no assurance that it would be possible to do so in the near future.

23 Directors' Recommendation

The Board, which has been so advised by Merrill Lynch and UBS, considers that the HMT Commitment Commission payable in relation to HM Treasury's entry into the HMT Undertaking to Subscribe (proposed in Resolution 4 and which is a related party transaction for the purposes of the Listing Rules) is fair and reasonable so far as shareholders are concerned. In providing their advice, Merrill Lynch and UBS have taken into account the Board's commercial assessments.

The Board, which has been so advised by J.P. Morgan Cazenove, considers that the GAPS Payment (proposed in Resolution 4 and which is a related party transaction for the purposes of the Listing Rules) is fair and reasonable so far as shareholders are concerned. In providing their advice, J.P. Morgan Cazenove has taken into account the Board's commercial assessments.

Shareholders are reminded of the importance of the disclosure contained in paragraph 4 above.

The Board considers that the Resolutions are in the best interests of Ordinary Shareholders taken as a whole and accordingly unanimously recommends that Ordinary Shareholders vote in favour of the Resolutions to be put to the General Meeting as they intend to do, or procure, in respect of their own beneficial holdings at the time of the General Meeting.

Yours faithfully,

Sir Winfried Bischoff
Chairman

Expected timetable of principal events

(Each of the times and dates in the table below is indicative only and may be subject to change)

Record Date for entitlement under the Rights Issue for Qualifying CREST Shareholders and Qualifying Non-CREST Shareholders and for holders of Limited Voting Shares for the LVS Capitalisation Issue	close of business on 20 November 2009
Announcement of Issue Price and entitlements of Qualifying Shareholders	7.00 a.m. on 24 November 2009
Latest time and date for receipt of Forms of Proxy for the General Meeting	11.00 a.m. on 24 November 2009
General Meeting	11.00 a.m. on 26 November 2009
Share Subdivision becomes effective	4.30 p.m. on 26 November 2009
LVS Record Date for entitlement under the Rights Issue for Qualifying LV Shareholders	4.30 p.m. on 26 November 2009
Despatch of Provisional Allotment Letters (to Qualifying Non-CREST Shareholders only)	26 November 2009
Start of subscription period	26 November 2009
Admission	8.00 a.m. on 27 November 2009
Dealings in New Shares, nil paid, commence on the London Stock Exchange	8.00 a.m. on 27 November 2009
Existing Ordinary Shares marked “ex-rights” by the London Stock Exchange	8.00 a.m. on 27 November 2009
Nil Paid Rights credited to stock accounts in CREST (Qualifying CREST Shareholders only)	8.00 a.m. on 27 November 2009
Nil Paid Rights and Fully Paid Rights enabled in CREST	8.00 a.m. on 27 November 2009
Recommended latest time for requesting withdrawal of Nil Paid Rights and Fully Paid Rights from CREST (i.e. if your Nil Paid Rights and Fully Paid Rights are in CREST and you wish to convert them to certificated form)	3.00 p.m. on 4 December 2009
Latest time for depositing renounced Provisional Allotment Letters, nil or fully paid, into CREST or for dematerialising Nil Paid Rights or Fully Paid Rights into a CREST stock account (i.e. if your Nil Paid Rights and Fully Paid Rights are represented by a Provisional Allotment Letter and you wish to convert them to uncertificated form)	3.00 p.m. on 8 December 2009
Latest time and date for splitting Provisional Allotment Letters, nil or fully paid	3.00 p.m. on 9 December 2009
Latest time and date for acceptance, payment in full and registration or renunciation of Provisional Allotment Letters	11.00 a.m. on 11 December 2009
Dealings in New Shares, fully paid, commence on the London Stock Exchange	8.00 a.m. on 14 December 2009
New Shares credited to CREST accounts	by 14 December 2009
Despatch of definitive share certificates for the New Shares in certificated form	by 29 December 2009

Notes:

(1) The ability to participate in the Rights Issue is subject to certain restrictions relating to Ordinary Shareholders with registered addresses outside the United Kingdom, details of which are set out in Part VIII ("Terms and Conditions of the Rights Issue") of the Rights Issue Prospectus.

(2) The above times and dates are indicative only. The times and dates set out in the expected timetable of principal events above and mentioned throughout this document may be adjusted, in which event details of the new times and dates will be notified to the FSA, the London Stock Exchange and, where appropriate, Qualifying Shareholders.

(3) If you hold your Existing Ordinary Shares through one of the Lloyds Banking Group Employee Share Plans or a CREST nominee, please note that certain of the latest dates set out in the timetable above may not be applicable to you. Where this is the case, the latest such dates which are applicable to you will be set out in your Provisional Allotment Letter or advice from your service provider.

(4) References to times in this announcement are to London times unless otherwise stated.

The Lloyds Banking Group Directors accept responsibility for the information contained in this announcement. To the best of the knowledge and belief of the Lloyds Banking Group Directors (who have taken all reasonable care to ensure that such is the case) the information contained in this announcement is in accordance with the facts and does not omit anything likely to affect the import of such information.

This announcement does not constitute an offer to sell, or a solicitation of an offer to subscribe for, the securities being issued in any jurisdiction in which such offer or solicitation is unlawful.

This announcement is not for distribution, directly or indirectly, in or into the United States, Hong Kong, Israel, Japan, Thailand or any other state or jurisdiction in which it would be unlawful to do so. This announcement does not constitute or form a part of any offer or solicitation to purchase or subscribe for securities in the United States. The securities mentioned herein (the "Securities") have not been, and will not be, registered under the United States Securities Act of 1933 (the "Securities Act"). The Securities may not be offered or sold in the United States absent registration or an applicable exemption from the registration requirements of the Securities Act. There will be no public offer of the Securities in the United States, and the Securities have not been approved or disapproved by the US Securities and Exchange Commission, any state securities commission in the United States, or any US regulatory authority, nor have any of the foregoing authorities passed upon or endorsed the merits of the offering or the Securities or the accuracy or adequacy of any of the documents or other information contained therein.

One of the exchange offers referred to herein is not being made, and will not be made, directly or indirectly, in or into, or by use of the mail of, or by any means or instrumentality of interstate or foreign commerce of or of any facilities of a national securities exchange of, the United States or to, or for the account or benefit of, U.S. persons. This includes, but is not limited to, facsimile transmission, electronic mail, telex, telephone and the internet. Accordingly, copies of this announcement and any other documents or materials relating to such exchange offer are not being, and must not be, directly or indirectly, mailed or otherwise transmitted, distributed or forwarded (including, without limitation, by custodians, nominees or trustees) in or into the United States or to U.S. persons.

This announcement does not constitute a prospectus or prospectus equivalent document. Nothing in this announcement should be interpreted as a term or condition of any of the Proposals. Prospectuses relating to the Rights Issue and the Exchange Offers will be prepared and made available in accordance with EU Directive 2003/71/EC and/or Part VI of the Financial Services and Markets Act 2000. Any decision to invest in Lloyds Banking Group under the Proposals must be made only on the basis of the information contained in and incorporated by reference into the prospectuses. The prospectuses, when published, will be available on the website of Lloyds Banking Group (www.lloydsbankinggroup.com) and in hard copy from the Lloyds Banking Group's registered office or by calling 0871 384 2990.

Neither the content of Lloyds Banking Group's website nor any website accessible by hyperlinks on Lloyds Banking Group's website is incorporated in, or forms part of, this announcement.

The distribution of this announcement and/or any other documents related to any offering of securities or the transfer or offering of securities into jurisdictions other than the United Kingdom ('UK') may be restricted by law. Persons into whose possession this announcement comes should inform themselves about and observe any such restrictions. Any failure to comply with these restrictions may constitute a violation of the securities laws of any such jurisdiction.

This announcement has been prepared for the purposes of complying with applicable law and regulation in the UK and the information disclosed may not be the same as that which would have been disclosed if this announcement had been prepared in accordance with the laws and regulations of any jurisdiction outside of the UK.

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

Examples of such forward-looking statements include, but are not limited to, projections or expectations of profit attributable to shareholders, provisions, economic profit, dividends, capital structure or any other financial items or ratios; statements of plans, objectives or goals of the Group or its management; statements about the future trends in interest rates, foreign exchange rates, stock market levels and demographic trends and any impact on the Group; statements concerning any future UK or other economic environment or performance including in particular any such statements included in this announcement or its annual report; statements about strategic goals, competition, regulation, disposals and consolidation or technological developments in the financial services industry; and statements of assumptions underlying such statements.

Factors that could cause actual results to differ materially from the plans, objectives, expectations, estimates and intentions expressed in such forward-looking statements made by the Group or on the Group's behalf include, but are not limited to, general economic conditions in the UK and internationally; inflation, deflation, interest rates, policies of the Bank of England and other G8 central banks, exchange rate, market and monetary fluctuations; changing demographic developments including mortality and changing customer behaviour including consumer spending, saving and borrowing habits, borrower credit quality, technological changes, natural and other disasters, adverse weather and similar contingencies outside the Group's control; inadequate or failed internal or external processes, people and systems; terrorist acts, other acts of war, geopolitical, pandemic or other such events; changes in laws, regulations, taxation, government policies or accounting standards or practices, exposure to regulatory scrutiny, legal proceedings or complaints, changes in competition and pricing environments; the inability to hedge certain risks economically; the adequacy of loss reserves; the ability to secure new customers and develop more business from existing customers; the ability to achieve value-creating mergers and/or acquisitions at the appropriate time and prices and the success of the Group in managing the risks of the foregoing; the ability to derive cost saving and other benefits as well as to mitigate exposures from the HBOS acquisition.

The Group may also make or disclose written and/or oral forward-looking statements in reports filed with or furnished to the SEC, the Company's annual reviews, half yearly announcements, proxy statements, offering circulars, prospectuses, press releases and other written materials and in oral statements made by the directors, officers or employees of the Group to third parties, including financial analysts.

Except as required by the FSA, the London Stock Exchange, the Listing Rules, the Prospectus Rules, the Disclosure and Transparency Rules or any other applicable law or regulation, the forward-looking statements in this announcement are made as of the date hereof, and the Company expressly disclaims any obligations or undertaking to release publicly any updates or revisions to any forward-looking statements contained in this announcement or incorporated by reference into this announcement to reflect any change in the Company's expectations with regard thereto or any change in events, conditions or circumstances on which any such statement is based.

Merrill Lynch, UBS, Citi, Goldman Sachs, HSBC and J.P. Morgan Cazenove are each acting for Lloyds Banking Group in connection with the Proposals and no-one else and will not be responsible to anyone other than Lloyds Banking Group for providing the protections afforded to their respective clients nor for providing advice in relation to the Proposals and/or any other matter referred to in this announcement. Credit Suisse Securities (Europe) Limited and Deutsche Bank AG are acting as financial advisor for HM Treasury and UKFI in connection with the Proposals and will not be responsible to anyone other than HM Treasury and UKFI for providing advice in relation to the Proposals and/or any other matter referred to in this announcement.