LLOYDS BANKING GROUP PLC – 2014 STRATEGIC UPDATE

TUESDAY 28 OCTOBER 2014

Lord Blackwell, Chairman

Before António outlines the key components of the Strategy Update, I would like to provide some brief context.

Lloyds Banking Group, we believe, enters this next phase of its strategic journey from a position of strength, having substantially delivered against its key strategic priorities over the last three years. This has reshaped the Group to focus on the UK and returned the balance sheet to full strength with a much reduced funding requirement, while generating a significant improvement in underlying profitability. In the light of these achievements, and as evidence of our rehabilitation, the UK Government as you know has started the process of selling down its stake in Lloyds Banking Group.

While we are all proud of these achievements, the Board recognises that this is just a staging post, not the end of the strategic journey. There are significant changes in the environment that the Group needs to address in the next phase of our development.

We have therefore spent a significant amount of time discussing how we can take the business forward, recognising the impact that the evolving regulatory and competitive environment as well as customers' changing needs in an increasingly digitised world are having on our UK retail and commercial banking focused business model.

As we look ahead, we recognise that the digital transformation in particular will be fundamental. And together with the external factors of competition and regulation are expected to result in a pace of change across the UK financial services sector that is unprecedented, with more fundamental change occurring over the next ten years than has happened over the past two hundred years.

Alongside this strategic challenge, our other priority is rebuilding trust. The UK financial services sector as a whole faces a major challenge of " rebuilding trust" with key stakeholders, including customers, regulators and politicians, following the significant long-term damage that was caused by the financial crisis. Regaining this Trust, which is a business imperative rather than a "nice to have", will take time, however Lloyds Banking Group is completely committed to achieving this by enshrining the highest standards of integrity to serve our customers.

The new strategy that António will now outline, has been fully debated by, and endorsed by, the Board. I am confident that it is the right one in the current environment and capitalises on the Group's unique assets including its franchise and its capabilities. It is also consistent with our prudent risk appetite.

Focusing on the best outcome for our customers will continue to be a core objective for the Group, alongside and supporting our commitment to become the best bank for our shareholders. Through these commitments, Lloyds Banking Group will continue to support the UK economic recovery and be an employer that our colleagues are proud to work for.

I would now like to hand over to António to provide you with a deeper insight into the Group's strategic focus over the next three years.

Over to you António.

António Horta-Osório, Group Chief Executive

Thank you Chairman, and good morning everyone. I am delighted to be introducing the next phase of our strategic journey to you today.

Over the last three years, we have succeeded in simplifying and reshaping the Group to become a low cost, low risk customer focused, retail and commercial bank. This business model remains unchanged, with the combination of our multi-brand strategy, through our iconic brands, multi-channel approach and leading cost position continuing to be a key differentiator versus our major UK peers.

Our focus on the UK, where we now have more than ninety five per cent of our assets, means we are based in a Triple A rated country, without the complexities, regulations and costs of multiple jurisdictions. Similarly our simple Retail and Commercial specialisation means we don't have the exposure to, or increased risk weightings from, volatile investment banking activities.

Our low operating and financial leverage, coupled with the significant reduction in our non-core assets, reinforce the low risk characteristics of our business model.

And this low risk business model is increasingly reflected in our low cost of equity. In a world where higher capital requirements are the norm, having a low cost of equity is fundamental in helping deliver competitive advantage and superior and sustainable economic returns for our shareholders.

Customers are at the heart of our strategy, with our strong relationships and insight, commitment to service, customer focused people, and multi brand / multi-channel approach integral to our business model.

At the beginning of the year we also launched our Helping Britain Prosper plan, designed to support our UK customers and businesses and, in turn, the economy as a whole.

We believe that providing our customers with products and services they value while achieving operational efficiencies will create a reinforcing cycle of growth and competitive advantage, generating long term sustainable returns for shareholders and financial stability for our customers.

Turning to our achievements over the last three years. We set out our strategy in June 2011, and have made significant progress on delivering against each of the four objectives we set at the time: reshape, strengthen, simplify and invest. It was this strong progress that allowed the UK Government to start selling down its stake in the Group, late last year, beginning the process of returning the company to full private ownership at a profit for the UK taxpayer.

We have significantly reshaped the Group; reducing non-core assets by more than £140 billion and achieving our original 2014 target for reducing the run-off portfolio 18 months ahead of target and in a capital accretive way. We have also concentrated our focus on the UK by reducing our international presence from over thirty countries to seven countries at the end of Q3 this year, significantly ahead of plan.

Regarding "Strengthen", we have transformed the Group's capital position, and achieved a fully loaded common equity tier 1 ratio of 12 per cent, comfortably exceeding our original target of 10 per cent. We have significantly improved our funding position by reducing our reliance on wholesale funding by more than £170 billion, and have reduced our loan to deposit ratio to less than 110 per cent from over 150 per cent at the end of 2010.

Simplifying the business has driven efficiency savings across the Group, and we are on track to deliver total annual run rate savings of £2 billion, £300 million ahead of the original target that we set.

This has enabled us to achieve significantly ahead of plan, our original target for 2014 to reduce our annual cost base to £10 billion, and we remain firmly on course for full year costs this year, excluding TSB, to come in at around £9 billion.

Later in the presentation George will explain how we plan to extend and enhance our cost leadership position over the next three years.

These efficiencies have created capacity to increase our investment in the business. We have invested one third of our cost savings, enabling us to double our discretionary investment spend in growth initiatives and to improve the customer service and experience.

Our complaint scores are now significantly lower than our peers and we have seen continued and significant improvement in our customer net promoter scores, which have increased by over 50 per cent during the planned period.

The actions we have taken have supported our model of being customer focused and UK centric. We have created a culture with values that focus on our customers, and we are committed to ensuring the Group remains an organisation with the highest level of integrity and standards.

Now let me tell you why our business model is the right one for the UK economy, the evolving regulatory environment and for UK customers. Starting with the economy.

As I have said many times, a strong economy requires a strong banking sector, in the same way as a strong banking sector requires a healthy economy. We are the largest retail and commercial bank in the country, and therefore our future and the prosperity of the UK economy are inextricably linked. This means we have a special responsibility to help Britain and its communities to prosper.

UK GDP is now growing robustly and unemployment is falling, increasing both consumer and business confidence.

House prices have also recovered strongly, increasing by twenty one per cent since the low point in 2009 and nearly recovering to their pre-crisis peak. With house prices expected to remain high, and rise further in comparison to incomes, first time buyers will continue to face challenges entering the market.

Against this backdrop, bank base rates are expected to rise only slowly, with the first increases predicted to come through in 2015, as the MPC seeks to support growth and allow opportunity for the economy's supply capacity to improve, and should stay low for longer than in previous economic cycles. We expect interest rates to reach 3 per cent in 2018 and to stay at this level for some time.

While the outlook for these key economic indicators is encouraging and will drive significant shifts in our customers' needs, the economy is still fragile and risks remain, especially geopolitical and relating to the evolution of the Eurozone.

Turning to the changes we are witnessing in the UK banking environment.

In the three years since we announced our strategy, there has been a marked shift in both the competitive and regulatory environment for banking.

Regarding competition, the UK banking sector, which I believe is very competitive at a retail level, has become even more so in recent years.

Earlier this year, we saw a number of our traditional competitors' strategies converge on the one we have been successfully executing over the past three years.

Competition within the banking sector has also increased, with new challenger banks coming to market. In addition, non-banks such as technology firms and supermarkets have been and have the potential to further disrupt the banking industry.

While we have significant competitive advantages through our unique multi-brand and multi-channel business model, low risk DNA and cost leadership position, we are not complacent and it is important that our strategy adapts to this expanding competitive environment.

The regulatory landscape is also evolving with greater focus on protecting consumers and small business customers through conduct and competition regulation, and on capital ratios, ring-fencing and resolution models through prudential regulation.

I have said before, there is a role for strong, but constructive regulation, which we welcome. This is in the interests of the industry in helping to rebuild trust.

Within the UK, the Treasury and the PRA are working towards creating a stable and safer banking sector, without exposing taxpayers to the unacceptable costs of banks failing in a disorderly manner. Having an independent, ring-fenced, traditional retail and commercial bank, separated from non ring-fenced investment banking and other activities, is considered a key step "ex ante" for resolvability through a crisis.

While the final height and implementation of ring-fencing is still to be determined, the perimeter of the ring-fence has been clearly set by the regulator. As a UK focused retail and commercial bank, most of our assets will be eligible within the ring fence, so implementation of ring fencing will be much easier for Lloyds than for other banks.

Regarding conduct, as a customer-focused business, we are committed to delivering the best outcome for our customers and continuing to provide fair value products that are appropriate to their needs, with clear, simple and relevant terms. We are also strongly embedding a culture across the organisation that is based on the highest standards of integrity.

Now let me turn to long-term customer trends. The proportion of the UK population who now have access to the internet has increased significantly over the past few years, as has the proportion of people accessing the internet via their mobile phone. Both these trends are expected to increase markedly. This in turn has changed customer behaviours in terms of how they shop for goods and undertake banking. We must reflect these changes in the products, services and channels we provide for our customers.

An ageing population is expected to affect the products and services that our customers require, with younger customers requiring help with planning and providing for retirement, while the older generation is becoming increasingly interested in accessing their equity to support their retirement.

With our multi-channel distribution model, coupled with our broad product reach and expertise across insurance and banking, the Group is uniquely positioned to meet these needs for both our individual customers and our corporate customers.

Let me now introduce to you the new priorities for this next phase of our strategy. The business model we set out in June 2011 remains unchanged, together with our aim to be the Best Bank for Customers and Shareholders. Our strategic focus for the next three years is based on three priorities.

Firstly, to create the best customer experience. Customers are and remain at the heart of our strategy, and we are committed to ensuring we deliver the best customer experience through our multi-brand and multi channel approach. We will continue to rebuild trust with our customers by providing a reliable, fairly priced and convenient service, which is executed through enhanced digital capabilities and a multi brand branch network.

The second priority is to become simpler and more efficient, making us more responsive to changing customer expectations, whilst further enhancing our cost leadership amongst UK high street banks, and enabling us to keep superior levels of investment in the business for future growth, as we did over the last three years.

Thirdly, we will target the delivery of sustainable growth, by maintaining growth in line with the market in our key retail business lines and seeking opportunities where our customer propositions provide competitive advantage in target segments and products where we are underrepresented. I will come back to growth opportunities in more detail later.

Turning to customer experience. We know our customers value the multi channel access we provide, and these customers are more valuable, purchasing 27 per cent more products and interacting five times more than branch only customers. Therefore our ambition is to create the best customer experience through combining our comprehensive digital capabilities with personal services delivered through our branch network and telephony.

To do this we will embrace the growing opportunities that digital technology provides. Miguel will describe this later. To support this, we will invest a further £1 billion in our digital propositions over the next three years to reflect our customers' changing channel preferences, and to build on our success in developing a resilient and secure digital infrastructure, that offers customers better service with greater efficiency.

As a result of this investment, our retail and commercial customers will increasingly be able to transact, be serviced and purchase through their channels of choice, with simple needs increasingly being met digitally.

In contrast to market trends, we recognise the value in maintaining a significant branch network as part of a multi brand and multi-channel approach to serving customers. But we will adapt by evolving the role of branches to reflect our customers' changing preferences, integrating the role of branches with digital and telephony as part of a seamless multi-channel approach.

As our customers continue to value the convenience of branches, we remain committed to maintaining a wide reaching, multi brand branch network, where over 90 per cent of Lloyds and Bank of Scotland customers will continue to have a usable branch within five miles, while the Halifax network is maintained.

We will, however, look to optimise our branch network by focusing on areas of urban overlap. We anticipate that these changes will involve a net reduction of around 150 branches but also an increase in our overall market share of branches in the UK, given present and anticipated branch closure trends in the market.

Alison will talk to you in more detail about our branch network later.

Through the initiatives we are outlining today, we aim to create the best customer experience that is reflected in the lowest reportable complaints and a top three position for customer satisfaction within our peer group by 2017.

We have demonstrated our ability to deliver significant efficiency savings, and we will continue the simplification of our business to both improve customer satisfaction and to extend our cost leadership position.

As part of this, we will continue to redesign and automate key processes and customer journeys, while embedding a more efficient change capability across the business and building more resilient systems and processes.

The changes we are announcing today will lead to a rebalancing of roles within the group to reflect the increasingly digital, multi channel nature of our business. While we plan significantly ahead, including attrition and looking to redeploy colleagues where possible, this will regrettably result in a reduction of around 9,000 roles over the plan period.

In the first phase of simplification, we reduced our supplier numbers by over 50 per cent. Looking ahead, we will build on this success, by reducing our dependency on contractors and third party suppliers.

George will explain later how these initiatives will simplify the business further and enhance our cost leadership by achieving an additional £1 billion of gross run rate savings by the end of 2017, from an investment of £1.6 billion, which will, in turn, lead to an improvement in the cost: income ratio every year and a ratio of 45 per cent as we exit 2017.

Now turning to growth. As I have previously said, the Group remains fully committed to support the UK economy and to Help Britain Prosper. Lloyds has an extensive customer franchise with strong relationships, well established market positions, iconic brands and a leading multi channel proposition. These will enable us to drive further competitive advantages as we implement the next phase of our strategy.

We aim to deliver sustainable growth by growing in line with the market in our key business lines of mortgages and current accounts, while targeting above market growth in SMEs and Mid Market clients, and also in retail areas where we are underrepresented.

We are well positioned to grow in our targeted areas of Consumer lending, Financial Planning and Retirement and Business Banking. We are also confident in increasing net lending to SME and Mid Market clients by over £1 billion each annually and that we can continue to achieve double digit percentage average annual growth in our asset finance business, leading to an increase in net lending of around £4 billion in this segment over the plan period. We also expect to achieve over 20 per cent growth in credit cards balances, amounting to circa £2 billion over the period. In total, when including retail mortgages, that will increase by more than £20 billion, this equates to more than £30 billion additional net lending over the plan period in our key target segments.

Let me highlight our market shares by key customer and product lines as this provides a useful overview of where we see our growth opportunities.

As you can see, we have around 25 per cent market share of retail customers and around 19 per cent of SME and Mid Markets customers, but have products and areas of under penetration such as London and the South East, which represent significant growth opportunities, that we will pursue within our prudent risk appetite, given our low risk business model.

We have already made good progress in building our digital capabilities. In the last three years we've invested more than £750 million in digital, achieving a 20 per cent digital market share, with over ten million active digital customers, five million of which are active mobile banking customers and £1.5 trillion of commercial client transactions have been conducted through our digital platforms.

Our digital propositions are also receiving industry recognition, with our Consumer and SME apps achieving a top iOS rating earlier this month.

Late last year we launched Digital as a separate stand alone division, whose Head reports directly to me and is a member of the Executive Committee of the Bank. This has provided the necessary focus that will enable us to extend our digital capabilities throughout the Group and to ensure we develop propositions that are at the forefront of our customers' evolving needs across all our divisions.

To achieve this, we will invest in new mobile applications, a new platform for commercial banking, online sales and servicing, video conferencing capabilities and an enhanced self-service technology, increasing overall spending over the next three years to £1 billion, so a third higher than the previous plan period.

Turning now to look at this by business area. In our Retail division, we have a strong portfolio and presence in the market, and have significantly improved the financial performance, together with the credit quality of the business over the past three years.

In the year to date we have met our Helping Britain Prosper Plan commitments by helping one in four people buy their first home and we are the largest participant in the Government's Help to Buy scheme.

In a highly competitive market with new entrants, low customer barriers to exit and improved price transparency, our multi brand, multi channel strategy and the value of our segmented customer proposition have remained differentiators, enabling us to acquire 60 thousand new customers in the first half of this year through the new current account switching mechanism, with our Halifax brand achieving the number one position for net switchers across the whole industry.

As we look ahead, we will strengthen our franchise by maintaining share in our core markets, using enhanced customer data analytics to offer new insights into customer needs, and by pursuing regional growth opportunities where we are under-represented, such as in London.

Earlier this year, we restructured the Retail division to serve our customers better, by leveraging the scale, customer insight and efficiencies of our retail infrastructure and processes through the inclusion of our domestic wealth business and the development of segmented mass affluent propositions. In addition, we decided to serve our smallest business customers better and in a more cost effective model, by fully integrating them in the Retail division.

Looking forward, we will look to combine all of this with the reshaping of distribution as part of a seamless, multi-channel approach, supported by innovation in digital and mobile and a redefined role for branches and telephony.

And finally, we will continue to simplify and automate processes on an end to end basis, in turn leading to a better customer experience and greater cost efficiency. Alison will cover this in more detail later in the presentation.

Turning to Commercial. The Commercial business has already made substantial progress in delivering its strategy. In the first half of this year, it achieved a return on risk weighted assets of 1.96 per cent: already close to the target of two per cent that was set for 2015. It has also successfully de-risked its business, reducing risk-weighted assets by around 40 per cent during the last three years.

Commercial Banking is playing a key role in Helping Britain Prosper and in supporting the UK economic recovery. We have committed more than £11.5 billion of gross funds through the Funding for Lending scheme and have grown our commercial transaction banking deposit base by 11 per cent in the first nine months of this year. We have also consistently increased lending to SME clients in a contracting market over the last three and a half years, thereby demonstrating the value of our relationship and community focused strategy.

As we look ahead, small and medium companies will continue to play an integral role in the UK economic recovery, and we aim to continue to be their chosen banking partner through our SME and Mid Markets businesses, where we will target additional growth of £6bn, over the plan period, by improving our key market sector specialism and improving our position in London where we are underrepresented.

Across the wider Commercial business we will create front line capacity through simplification and digital, with key areas of focus including client onboarding and servicing as well as client insight and analytics. We will continue to invest in critical infrastructure to build on our digital capability in Global Transaction Banking.

As we grow the business, we will focus on maintaining our capital discipline by optimising our Global Corporate relationships and targeting a new and even more ambitious return on risk-weighted assets of at least 2.4 per cent by 2017.

Turning to our insurance business now. Our insurance business is a core part of the Group and is focused on four key markets: corporate pensions; protection; retirement and home insurance.

We are a market leader in corporate pensions and the largest writer of home insurance in the UK. The business is run efficiently, benefiting from the scale advantages of the wider Group and achieving a market-leading combined operating ratio of 80 per cent in the general insurance business.

The benefits of having an insurance business within the Group extend beyond product breadth and customer reach. These include a number of operational and financial synergies including capital diversification benefits and a reliable dividend stream, with the insurance business having repatriated circa £4 billion of capital to the Group in the period since the strategic review of 2011.

We will look to continue to leverage our unique Group capabilities. As the UK population ages, financial planning for retirement is becoming a critical and growing customer need. The Group is well placed to serve this need for both individuals and corporates, given our integrated insurance business. By connecting products, services and customer insight already in existence in Scottish Widows, we will enable our Retail customers to make long-term preparations for retirement, growing assets by over £10 billion by 2017.

Through our longevity and investment expertise, we are well placed to support our Corporate customers across the Group as they look to de-risk their defined benefit pension schemes, and will continue to support them with appropriate products and services as they look to improve the pensions for their employees through defined contribution schemes and through the transition to auto enrolment.

Finally, our digital investment will significantly enhance the customer reach of our insurance business through a seamless integration with our digital banking platform. In home insurance we can lead the new business market through a customer led, low cost, multi channel approach with significant investment in direct channels, while the end to end digitisation of pensions will lead to greater efficiencies and an improvement in the customer experience.

Turning to our Consumer Finance business. Our Consumer Finance division was created at the end of last year and comprises our consumer and corporate credit cards businesses, along with the Black Horse motor financing and Lex Autolease car leasing businesses in Asset Finance.

Consumer Finance has already demonstrated its capacity for growth, particularly in the motor finance business, where Black Horse saw new business growth of seventy per cent at the half year, driven both by the acquisition of the Jaguar Land Rover representation, and by substantial organic growth.

Our market shares of 12 per cent in new and used car lending and 16 per cent in fleet cars, and the significant anticipated market growth provide us with a firm foundation to deliver double digit average annual lending growth across asset finance, amounting to around £4 billion over the period; for example, through the provision of better propositions across the franchise customer base and by helping dealers and manufacturers increase customer loyalty.

In credit cards, we currently have a 15 per cent market share and have achieved the number one position for sales since 2013, having repositioned the business for growth. Looking ahead, we aim to outgrow the market in this under represented area, achieving over 20 per cent growth in cards balances over the next three years, circa £2 billion, by providing customers with fair value products through our digital capability and leveraging opportunities across both the franchise and non-franchise customer base.

Before I hand over to Miguel to talk to you about creating the best customer experience through digital, I would like to briefly turn to our capabilities to deliver the strategic priorities we are outlining today.

As we look to the next three years, and at our capabilities to deliver the next phase of our strategic journey, we do so from a position of strategic, operational and financial strength.

We have a clear and simple strategy as a low cost and low risk UK retail and commercial bank that has been successfully executed over the past three years. Our multi brand and multi channel approach are differentiators within the UK banking sector and enable us to address the different and evolving needs of our customers in a segmented way.

The successful execution of our strategy by a strong management team that has built up a track record of delivery, coupled with the change management capabilities developed through integration and simplification, and our high quality, committed workforce provide us with a solid foundation to grow and raise the bar in pursuing our vision of becoming the best bank for customers and shareholders.

I would now like to hand over to Miguel.

Miguel-Ángel Rodríguez-Sola, Group Director, Digital

Thanks, António. Good morning everyone. Today, we want to share with you our Digital strategy, and how it helps to create the best experience for customers, across all our channels.

Digital has changed the world of banking. We all know that digital has changed the way customers interact with banks and retailers. As António mentioned, Digital will be a significant driver underpinning our strategy over the next three years.

Over the last three years, Lloyds Banking Group has built the largest Digital banking franchise in the UK. And we are not stopping there. We will continue to invest in Digital, to create the best bank for customers and make us a more efficient bank.

Whilst Digital has changed banking, our customers' needs have not changed. They still want to save for the future, buy a home, or protect their families, what is changing is how they want to interact and fulfil those needs with us.

We expect that by 2016 E-commerce will account for 25 percent of overall business turnover in the UK. And UK banking mirrors these trends. Digital retail banking sales across the sector, excluding savings, have increased by 16 per cent over the last year.

Over 14 million banking apps have been downloaded to date, and £1.7 billion are transferred weekly by mobile in the UK.

This is a massive change.

Lloyds Bank sees digital as part of a much broader multichannel approach. One that allows us to meet customers' needs wherever and whenever they choose.

For the customer it is about choice and convenience.

For the bank it is about creating opportunities to meet additional needs, improve service and save costs.

Put simply, multichannel customers hold on average 27 per cent more products with us, and they interact five times more with the Bank.

Over the last three years we have built the largest digital banking franchise in the UK. We have invested over £750 million in our digital capabilities, building and extending our digital platforms, rolling out new propositions, and in-creasing system resilience and security.

As a result, the Group has circa 20 per cent of the Retail Digital market share of new flows, above the average market share of 18% that António mentioned earlier.

Thanks to our customers we have over 10 million active digital customers: We have over 5 million active mobile customers, only mobile we are almost the largest digital bank franchise in the UK.

Our customers logged on to our secure site more than 1 billion times over the last 12 months. And we transact online over £1.5 trillion pounds for our commercial clients per year, around the same size as the UK's GDP.

But it is not just a question of numbers. It is also a question of customer satisfaction. As of last night, for example, Apple confirms we are the top-rated banking app for both retail and business banking customers, in the UK.

We are prepared for the future.

Today over 40 per cent of our customers' simple needs are met online.

In terms of deepening relationships, 40 per cent of direct mortgage product transfers now take place online and 90 per cent of all commercial client payments.

The shift in servicing has been even more dramatic.

Excluding cash, around 85 per cent of customer account servicing is now conducted digitally, such as making a payment or checking a balance.

Also our digital platform has been made available to customers and colleagues in branch and over the phone for servicing. It's simple, it's familiar, and it saves time and gives us a consistent base to build the future. And it's great to hear our colleagues in branch have seen a 50 per cent reduction in the time taken to serve simple customer needs.

Our customers have also decided to go paperless. 14 million accounts are now enrolled in paperless statements. Imagine the convenience for our customers and the efficiency savings for us.

As we have said, multichannel drives customer benefits, growth opportunities and business efficiency.

Our customer's behaviour has changed and this will only accelerate. By 2017 we could see 60 per cent of simple needs and 10 per cent of complex needs met digitally.

Our customers' first ISA might be opened in branch, but it will be managed online; today more than 50 per cent of our customers are already doing so. By 2017 we expect 90 per cent of simple service transactions to take place online.

Our ambition is also to grow digital market share. Digital represents a significant growth opportunity for us in areas like cards, personal loans and insurance, where we are below our natural market share.

As you heard from António, Digital remains core to our strategy and over the next three years we will invest £1 billion pounds to give our customers what they want.

We will achieve this by: First, delivering to our customers the right solution, at the right time in their personal financial journey. You can expect new digital customer propositions that will support our growth strategy.

Second, by enhancing our digital capabilities, upgrading our technology, creating consistent service across all channels and transforming our customer in-sights.

Finally, by transforming the customer experience end to end. We have listened to our customers and we will redesign the "moments that matter to them", such as getting a mortgage or opening a business account. We will create a better customer experience, and in doing so we will reduce cost.

So, what does delivering customer-centric propositions really mean?

For Retail customers it's about completing all of our servicing journeys online, and enabling 100 per cent of simple purchases online, providing anytime, anywhere choice and convenience.

At the same time, we will give customers access to more complex products like mortgages and protection. And you can expect significant focus on mobile propositions.

For Commercial clients, the end-goal is similar, creating a single consistent digital front door that allows them to transact and service. From cash management and payments to trading and FX.

Next year, we will launch our new strategic online channel for our Commercial clients that will support our growth strategy in Commercial.

Digital is a gateway between customers and the bank, a gateway that transforms our ability to manage the customer relationship. For the customer it provides a convenient front door into our propositions and services. For the bank it creates the opportunity to present highly personalised offerings to customers and clients based on an integrated view of their needs.

To deliver on the promise of Digital we will extend our capabilities across product innovation, multichannel, and digital resilient and secure platforms.

Digital brings also a new world of customer in-sight that we will leverage to better serve our customers and support our future strategy growth.

Being the best bank for customers is about getting the moments that matter right. Moments like when we buy a home, open a current account, or establish a business. We will transform the ten most important customer journeys over the next three years. The ten customer journey's we are planning to digitise include taking on a new mortgage, on boarding a new business relationship, opening a personal current account or preparing for retirement.

The benefits for the customers are clear. In the case of buying a home, the time required to reach a mortgage offer could go from 25 days to one week. Customers accounts will have fewer touch points, which will simplify the experience for customers.

In Commercial Banking, business account opening could reduce from six weeks to only one.

Finally, Insurance could move from almost no online servicing capability to circa 70 per cent of service needs being met online.

Digital will bring a massive transformation to current customer journey's providing significant benefits to them.

It's all about doing the right thing for customers: Anytime, anywhere self-service, with less errors. Seamless experience across channels, and contextual, relevant propositions for customers.

At the same time, doing the right thing for customers carries growth opportunities and significant efficiency improvements for the bank.

For the processes we want to digitise, we estimate a future reduction in end-to-end costs of around 15-35 per cent.

So, we have the largest digital banking franchise in the UK. And as I said, we are not stopping there. Over the next three years we will invest £1 billion in our digital future, to transform the customer experience, support our growth and become a more efficient Bank.

However, we do not see Digital in isolation. We know that our customers want is multi-channel.

I am now going to hand over to Alison who is going to tell you how all this will fit together from a Retail distribution point of view.

Thank you. Over to you Alison.

Alison Brittain, Group Director, Retail

Good morning and thank you Miguel. This section will focus on how our digital transformation will work in harmony with changes in our branch and telephony networks to produce a coherent and customer focused distribution strategy. And let me explain how we have arrived at our conclusions starting with a reminder of our current strategy.

Our multi-brand, multi-channel and multi-segment strategy gives us fabulous reach across all customer demographics, customer need types and attitudinal preferences.

Lloyds and Bank of Scotland are relationship brands; they are expert and knowledgeable and relationship oriented colleagues, whilst Halifax is a high street challenger, offering friendly, easy and straightforward banking.

Our scale allows us the flexibility to develop tailored propositions, and to deliver them at a lower cost, because we use shared platforms and shared back office functions.

A great example of our competitive delivery of the same product area through different brands would be comparing the highly successful launch of Lloyds Club account launch which delivers long term value in the current account space to Lloyds customers; alongside the continued success in Halifax Current account switcher offer, delivering immediate Reward and simplicity.

Our multi-brand approach helps us to maximise distribution reach. Just looking at our primary active current account holders the customer overlap is very small, just 2 per cent of our 14 million customers.

Customers are increasingly adopting a multi-channel approach and multi channel customers create more value for the Group.

The needs of our customers are changing as we have talked about in the last two presentations. Increasingly they are expecting more convenience, personalised products and services and seamless service across channels.

The continued evolution of digital and mobile is key. As Miguel mentioned our new mobile banking app allows customers to stay in touch with us and has delighted customers so far. All three of our branded apps have an average rating of 4.5 out of 5 stars.

Simple branch transactions have fallen and are expected to continue to fall, as customers opt for the convenience of self service, and that is both with the branch using self service devices and through mobile and digital. Within four years we are estimating that branch transactions should be half their current yearly totals.

We know that our multi-channel customers are more engaged and more valuable. They hold more products as António said, and our research has shown that customers who begin their journey with us as multi-channel customers are seven times less likely than single channel customers to become inactive or unengaged with us.

So let's turn to our channels, and turning first to telephony. Telephony's core purpose will migrate from transaction enquiries to complex queries and remote advice, enabling increased branch productivity. So how does that work?

Well telephony is a channel undergoing radical change. We have seen call volumes fall at over 10 per cent year-on-year since 2012 as we have enabled and supported customers' preference for self-serve. We see further scope in Telephony for additional Simplification initiatives which will drive further savings and that, along with an ever reduced demand, will drive a 28% reduction in our 'simple telephony' activities.

However, the mix of telephone roles will change, and the proportion of specialised and highly skilled colleagues will increase. One of our key investments will be the creation of a scalable 'centre of excellence'. These centres of excellence will be remote advisors, leveraging telephony capability, through sophisticated video conferencing technology. We will Initially focus on Mortgages which is a complex and highly regulated sales activity.

There will be a number of benefits for both our customers and our business. Firstly, there will be a step change in convenience for customers. Whilst currently our large branches can fill the diary everyday for a Mortgage Advisor (and will continue to do so) many smaller branches cannot. And they have to share an advisor or have none at all, meaning that customers can't get an appointment straight away and have to wait or they have to travel to one. The remote advisor model will mean that all outlets will be able to serve customers immediately through the technology. And whilst I focus this example on the delivery into the branch network, it is not a great leap to see how we could extend that capability into digital and deliver advice directly into a customer's personal device, serving them at a time and place of their own choosing.

But there are additional benefits on top of that. The use of a centralised unit in telephony to deliver this remote advice proposition, will ensure high levels of advisor productivity as you manage call volume, and much reduced conduct risk outlook. The sales force will be centrally trained, it would be onsite and with greater management oversight and of course, full recording of the advice given to the customers. I think this is an example of how we will use strategic capability and technology to achieve full distribution coverage, higher productivity, lower risk and a great customer experience.

But our convenient branches will continue to have an important role for acquiring new and serving existing customers. Branches have been consistently important for customer acquisition. For the last six years the proportion of current accounts opened in branches has been greater than 80 per cent and that trajectory is flat not declining.

The single most important reason for a customer to choose a current account provider is convenience and that has been a consistent metric since 2008.

Branches continue to be used by all customer segments, and are highly valued by customers for complex advice, for guidance and for service.

The majority of even the youngest age group use branches at least annually with more than half use them monthly. So the emergence of a generation that is "digital only" looks a little overplayed and we see more value in a multi channel approach. It is clear that most of our most profitable customers use our branches on a regular basis, for example three quarters of our mass affluent customers use a branch once a month.

Also, while we do expect some further migration to digital, we see a continued role for the branch in customer acquisition, complex products, and guidance and service.

So turning to what our branch presence will look like during this plan period, it is important to remember that through the creation of the TSB brand and its subsequent divestment, we have created a new challenger brand on the high street but we also reduced our own network by 22 per cent.

Our branch network needs to be considered in the context of our three distinct brands, each with three distinct competitor sets and the need for each brand to have a convenient foot-print.

As you can see from the chart, Lloyds Bank now sits middle of the pack of its competitor set; Halifax is on a par with its challenger bank peers, and Bank of Scotland is the largest player in Scotland.

Pure premises costs are a very modest part of the total Retail cost base. So we see far bigger cost opportunities elsewhere. Over the next three years we will maintain a significant network, and whilst we will close on a net basis around 150 branches, we expect to hold or slightly grow market share as our competitors potentially decline faster.

So in terms of the strategy, we know that customers value our branch network, and that our strategy will allow us to meet customer expectations for convenience and support brand awareness and customer confidence.

As I said earlier, property costs are a relatively small proportion of the Retail Cost base. Indeed people costs in branch are more than three times property costs of the branch. Consequently our efficiency programme will focus on removing manual processes and simple servicing across the whole of our estate rather than just closing some small Branches.

Branches will become champions for our multi-channel strategy. Colleagues will be multi-skilled to support sales and service activity, and will be asked to play a lead role in helping customers get the most from their multi-channel bank. As we leverage our multi-channel platform and we increase the number of straight through processes, we expect to improve both colleague productivity and customer satisfaction. That has been a significant success in 2014 and we have plans for further substantial deployment further into 2015.

As António mentioned, in the short-term, net branch closures will focus predominantly on consolidating over-lapping branches and transferring activity into a neighbouring branch. By focussing on overlap locations, and by closing at a slower rate than the competitors, we aim to minimise revenue loss whilst delivering an attractive payback. We will do further investment.

We will improve our presence by relocating some branches into key retail centres, and increasing our presence in London and the South East, through targeted openings. We have relaunched Halifax into Scotland and we will continue to explore opportunities for that Brand in the Scottish market.

We will invest in our key location branches in major retail centres. And that investment will support our multi-channel approach creating a ‘digital high street bank’. For example, screens will be removed to enable our staff to have more valuable conversations in the banking hall and to interact freely between cash transactions and advice.

Additional self-serve technology will be installed, allowing customers to further migrate to the most convenient channel at a lower cost. Our staff will be increasingly multi-skilled, to maximise the potential of our ,market leading multi-channel platform, improve their productivity and improve the customer experience in every day banking.

So to sum up, the needs of our customers have defined our distribution strategy. We believe that effective multi channel approach is the right way forward and that our multi-brand position continues to be valued by our customers. Great execution of this proposition will be our focus.

Branches will continue to play an important role for many years to come, and we will focus on cost reduction by changing what happens in all our branches, rather than focussing just on branch reductions.

This will see us migrate service to the most efficient channels, enhance the customer experience and reduce our back office costs.

We believe that the combination of a great local branch network operating in harmony with re-purposed Telephony and using our leading digital capability is a winning combination. It will leave us well placed to retain our existing customers and to acquire new ones.

I will now hand back to George who will cover how we will continue to focus on being a simpler and efficient business.

George Culmer, Chief Financial Officer

Thank you Alison and good morning again. I am going to briefly cover the third of our strategic priorities: becoming simpler and more efficient and then make a few comments on financial strength and targets.

Starting then with becoming simpler and more efficient.

We are entering the next phase of simplification from a position of strength, with a strong track record of delivery and outperformance against previous targets. As you'll recall, our original simplification programme was launched in 2011 and set out to deliver financial benefits through the reduction in the cost base and the re-investment of a third of those savings back into the business.

In terms of targets, by the time the programme completes later this year, we will have achieved run-rate savings of £2 billion per annum, some £300 million ahead of our initial guidance, at a cost of about £2.4 billion which we have charged below the line.

These savings have been achieved through automation, simplification of end to end processes, better workflow management and improved demand management including reducing our supplier numbers by over half.

For our customers, this improvement in operational efficiency has also helped improve the service and value we provide and their experience. As a result, we have seen our Net Promoter Score increase by over 50 per cent and complaints are down also by over 50 per cent.

For our colleagues, we have eliminated highly manual tasks, promoted training and development and given them more time to focus on the needs of the customer. We have, at the same time, improved efficiency by reducing the layers of the organisation to seven, and these changes have all had a positive impact on our workforce, with employee engagement up 27 per cent.

With the success of the original programme, what we're announcing today is the next phase of Simplification and we are targeting further cost savings, more investment in the business and further improvements to our customer and colleague experiences.

In terms of cost savings we are targeting improved run rate savings over the next three years of an additional £1 billion. Around £0.4 billion of this will come from the digitisation and redesign of key customer journeys, building on the progress we made in the first phase. £0.3 billion will come from further savings from sourcing, and around £0.3 billion from optimising the shape of the organisation, primarily through efficiencies in distribution channels, head office and support functions and by adopting more agile ways of working. These initiatives will, we believe, result in approximately 9,000 fewer roles across the Group.

To achieve these savings we are investing around £1.6 billion across the business over the same period. This money will be spent on initiatives to simplify end to end customer journeys and increase the use of automation. Around £400 million of this spend also relates to expected redundancy costs, which we will show outside of underlying profit.

The balance of £1.2 billion will be charged above the line and we will match investment and run rate savings and are targeting a year on year reduction in our cost income ratio.

In terms of what this ultimately delivers. As you have seen in our Q3 results announcement, our cost to income position is already market leading, at just below 50 per cent. Maintaining this market leading ratio is an integral part of our strategy, delivering value to our customers and sustainable, superior returns to shareholders.

And we are targeting, as you have heard, achieving a cost income ratio of around 45 per cent as we exit 2017.

Turning now to the financial shape. As you know, and have heard, we have made huge progress over the past three years in strengthening our balance sheet and funding position while at the same time reshaping and simplifying the business.

With a core tier 1 ratio of 12 per cent, total capital of 21 per cent, leverage of 4.7 per cent, and hugely reduced wholesale funding and run-off assets, we have a strong and de-risked balance sheet and are very well placed to meet the evolving regulatory requirements.

Going forward, our commitment is to maintain this strong balance sheet and capital position. We will maintain a wholesale funding requirement, weighted to longer durations, with a loan to deposit ratio of between 105 per cent and 110 per cent.

In terms of capital, as you know requirements continue to evolve, and while we currently believe our steady state CET1 ratio should be around 11.0 per cent, there are obviously risks that this could well increase.

We are also well positioned to meet other evolving capital and leverage requirements, and for total capital we will have ratio of at least 20 per cent and a leverage ratio above 4.5 per cent, the latter significantly higher than our UK peers.

Finally, some words on targets. Successful execution of the initiatives we have outlined today will help us achieve our vision to become best bank for customers and shareholders.

As you've heard, the Simplification programme will deliver £1.0 billion of further cost run-rate savings by the end of 2017, where the changes to our organisational design and branch operating model will result in approximately 9,000 role reductions.

As a consequence, and again as mentioned, our market-leading cost to income ratio will come down every year, with an exit rate of around 45 per cent at the end of 2017.

At the same time, with low risk at the heart of our business model and strategy, we will look to deliver further improvements in the credit quality of our loan portfolio, with a target of maintaining an AQR of approximately 40 basis points through the economic cycle, and we expect it to be lower than this over the next three years.

Through the initiatives we are outlining today, we are targeting a return on required equity in the range of 13.5–15 per cent starting in the strategic planning period and then through the economic cycle.

And our dividend policy remains to deliver a medium term payout ratio of at least 50 per cent.

These targets evidence the confidence we have in the business and our clear goal of delivering superior, sustainable returns for shareholders.

I will now hand back to António.

António Horta-Osório, Group Chief Executive

Thank you George. The strategy we set back in 2011 remains unchanged. We will continue to be a low risk, low cost, customer focused UK Retail and Commercial bank.

But from "Reshaping" and "Strengthening", together with "Simplify" and "Invest", we will move into "Digital" and "Growth", together with "Simplify" and "Invest".

I believe we are well positioned to deliver this next phase of the strategy given our proven track record, execution to date and clear business model.

We can now raise the bar, as we will accelerate the investments in our digital capabilities to position us for the future, which will be done as part of our multi brand and multi-channel approach to serving our customers.

Given we have substantially reshaped and strengthened the Group's financial position and performance, we have developed a solid foundation as we enter the next phase of our strategic journey.

Having successfully delivered on the priorities we set out in 2011, we are now in a position to focus on sustainable growth and to take advantage of the UK's economic recovery, together with making further investments that will allow us to continue to serve our customers' evolving needs and expectations of their bank.

Our priorities for the coming three years will be to deliver the best customer experience. This will be achieved via our multi-brand, multi-channel model, which our customers value. We will also, through digitalising the Bank further, develop our digital offering further, allowing our customers to undertake not only daily banking transactions digitally, but also more complex needs in a way they expect in the evolving digital world.

And we will continue to focus relentlessly on our cost base and become simpler and more efficient. We have set a new cost income ratio target of around 45 per cent by the end of 2017 with improvements every year, through which we will maintain our competitive advantage and our ability to offer superior value propositions to our customers, as well as superior returns to our shareholders.

Finally, we will target sustainable growth in line with our prudent risk appetite by continuing to grow in line with the market in our market leading key retail business lines, above the market in SMEs and Mid Markets clients and above market as well in areas where we are underrepresented such as car financing and credit cards. The Group remains totally committed to supporting the UK economy and Helping Britain Prosper, by providing more than £30 billion of net lending to our key customer segments over the next three years.

We have an exciting future ahead of us as we enter this next phase of the strategic journey. We have unique assets: our iconic brands and our multi-channel distribution model spanning over 25 million active customers across retail and commercial banking and our integrated insurance business, which differentiate us from our peers.

And this business model is based on a consistent, simple and clear strategy as a UK focused retail and commercial bank, which has been successfully executed over the past three years, and is well positioned in light of future economic and regulatory trends.

Therefore, these achievements position us well for the next three years to achieve our key strategic objective of becoming best bank for customers, through delivering the best customer experience, and also becoming the best bank for shareholders, by delivering superior and sustainable returns, while Helping Britain Prosper.

Thank you. And this concludes our presentation. We are now available to take any questions you may have.

End of presentation

Question and Answer Session

Question 1: Martin Leitgeb, Goldman Sachs
It's Martin Leitgeb from Goldman. Just a clarification please. One on the move to Digital and your branch presence. Could you provide a bit more light on, obviously the focus is here on personnel in the number of branches. Out of the 9,000 job cuts, how many of those will be in the branches - how can I image the branch to be in terms of average employee per branch now and going forward? And I am just trying to understand really in terms of this massive move from here to digital, is this 2015-17 plan as far as it gets or is there basically one or two year for potential for full improvement if this transition really happens to that extent?

And the second question is with regards to competition on the mortgage side. You mentioned there was an increasing competition on the retail side. And I was just wondering if you could share a bit of light on your expectation of net interest margin there. And previously I think you mentioned that the leverage ratio is a potential mitigant here. So where would the leverage ratio this Friday probably need to be to probably impact a certain element of competition on the mortgage side? Thank you.

Answer: António Horta-Osório
It is a very comprehensive set of questions. Relating to your first question, Alison can give you some colour on that and in relation to the financial questions, George can also give you some colour on that. But what I think is important to understand is, we are here to serve our customers like any other company. And customers are strongly evolving in the way they bank. And they are now in an exponential if you want behaviour. They are contacting us through multichannel so they do more interactions with us as a whole. And within those interactions, the mix is changing very significantly as Alison showed you, whereby they contact us much less through branches like 9% less counter transactions a year and much less through telephony, a significant decrease last year. And much more through digital and specially through mobile banking. So as the customer interactions with us evolve, we have to adapt ourselves and we have to serve them when and how they want. And therefore in terms of the way we see the trends going over the next three years, we are going to need less people in the branches because there is less interactions and less sales through the branches and we should adapt because we have to use the resources in the best optimal way in order to deliver what customers want. So I will not give you specific details between operations and other areas, but as Alison said, significant proportion of this will be done in the branches. But we have as well as Miguel shared with you, internal process redesign which will avoid manual interventions and will have significant back office improvements, apart from the fact we are continuously looking at our organisation. And as we have less people we review the layers and we review the spends of control. Because what we ultimately want to be as we also said three years ago, is a highly agile and responsive

organisation that goes in the right direction with the best internal organisation of resources and at a quicker speed than our peers.

Alison would you like to comment on the branches?

Further answer: Alison Brittain
Yes I will just add a little in terms of the consolidation strategy which is a sort of 200 closure with some openings netting down to around 150 over the three year period. The fact that we are using a consolidation strategy means that we will close slightly larger branches because the two branches you know within reasonable distance of each other are necessarily urban branches rather than rural. And we will still deploy other alternative strategies with some of our smaller branches staying open, but with very reduced hours and staff sharing between branches and even, as we do in many communities in Scotland, delivery of service from the other mobile source which is a mobile van, that goes round and delivers to the communities during the week. So there are other alternatives that we have to sort of dial up and down our position. But we are expecting that 200 to be the plan if all goes as we have predicted.

Further answer: George Culmer
And on the leverage, I presume we will all find out on Friday and I assume we have all heard various stories along the way. I think the most extreme I heard was a 5 per cent of pure core tier 1 equity which would have interesting consequences one presumes. I don't expect it to be that. I do expect that it will start with a 4. Whether it then goes up in 25 basis point blocks, who knows. But I would have thought when you get north of 4, when you look at where some of our peers currently are, that will have an immediate impact one would have thought on pricing from where one positions oneself. So I would have thought in terms of where it bites, it is pretty close to biting already and I feel pretty sure that what is said on Friday will bite whether it is monolines or other people that we compete against.

Answer: António Horta-Osório
If I can elaborate on what George said, and I had said this at the half year with the results. If you consider that depending on where the leverage ratio will be. But most likely, if you believe the leverage ratio will be between 4 and 5 as George was saying, you have at least three of the largest five banks in the UK below 4. And if the marginal cost of capital for our mortgages which today will be if you want, if you assume 15 per cent risk weighted assets on mortgages with 11 per cent capital ratio, it will go from 70 times to either 20 or 25. And therefore given that it is the marginal cost of capital of the restrictive ratio that will work out for the future, and given that the banks in the UK have the restriction on the leverage ratio, you can see what can happen if the marginal cost of equity goes from 70 times to 20 or 25. So I really believe that going forward, banks will have to include the new capital, the new cost of capital of the restriction in terms of capital on their pricing. And it is likely that mortgages will be the ones where restriction is greater given the difference between fully loaded ratios and leverage ratios, so on strategic thoughts assuming between 4 and 5 depending on intensity, you can assume what will have to happen over time. This is like negative discrimination!

<u>Question 2: Chirantan Barua, Bernstein</u>
Hi Chira from Bernstein. I have a simple question on Slide 20 of your deck which is kind of scary when you look at the ageing population and the number of people going beyond 60. So I totally understand that risk on your P&L and credit risk is very low. I agree with you lower risk bank. But the point is, from the Regulator's perspective, does it mean that there is a huge chunk of the population with massive amount of mortgage who at some point in the future will just hand over the keys and say, enough is enough, not working until 75. Which means do you have to run with excess capital for the next five to ten years?

Answer: António Horta-Osório
I really don't see that as a big risk. And I think that graphic it is not that dreadful. Because they are much older, but people live much longer. And I think that is as well by the way, a strong consideration when you have to consider your branch network. Because where most of the savings are is in the older generation. And it is older this generation significantly values the interaction with the branch and you can see them and you know how many people are now above 90 and are both 100 in the UK and what are the trends for the next 30 to 40 years? So no doubt the population is getting older, but they live much longer and that is where the savings are which is a lateral comment.

Relating to your specific comment and I think you are referring to the fact that in the UK like 48 per cent of mortgages are interest only. We don't see that as a big risk because that is now over a 30 year period and houses over time, significantly increase in value. So I see it very unlikely in a country like the UK, where people are by culture, home owners. They cannot hand over the keys like in the US because they are liable for the debt in any case. And thirdly, if they have huge equity value locked in their houses, why would they hand over the keys. We really don't see that as a risk.

Further question
I totally agree with you on the P&L perspective but for the regulatory perspective, because of tail risk as we have seen in the stresses, does it mean that they ask you to park an excess amount of capital against the balance sheet for the tail end. I am not saying there is a P&L risk. So basically stepping back, where you planned your strategy on 11 per cent core tier 1 ratio, why is it getting worse? What has fundamentally changed in the last three years? Why has capital gone up? When you planned your strategy, you said you planned it around 11 per cent core tier 1 ratio, but we see it increasing with every year, where it is actually you have simplified your business model, so where is the disconnect between where you started off with your strategy and the regulatory pressures coming in right now. What are they scared of?

Answer: George Culmer
It is a question best asked to Moorgate, Canary Wharf and Europe I would have thought. As I said in the Q3 stuff, we work off about 11 per cent, we work off steady state because when we do our bottom up, that was to us an appropriate capital position given the risks inherent in our business which we model etc. Now since we did that, the longer the authorities be they here, be they Europe or wherever, talk about things, it only matches up. And I think, as I said this morning, there are risks out there, and there are risks when one looks at the symmetry of risks, it is more likely to be higher than the number we talked about than less. And I don't think that is an LBG issue, I think that is just us and part of sector and just in part of the world in which we currently live. So when I make the comments about where I think the risks might be going to our capital position, that isn't Lloyds that is us being part of the sector and how I read the prevailing mood music coming back from the authorities. So it is a sectoral rather than individual company comment.

Question 3: Ed Firth, Macquarie
Ed Firth here from Macquarie. Three quick questions. The first one was a strategic question. And I guess when you look at other industries that have been through the digitisation that you are talking about, we have seen a significant reduction in costs, but also a significant impact on revenue margins in particular. So I just wondered, I just invite you to give us some idea as to what you are expecting over the plan horizon and perhaps further forward in terms of what you think in terms of overall revenue margins?

Answer: António Horta-Osório
Well absolutely right and something we have debated among ourselves and that is absolutely part of digitisation, but I would see it in a slightly different context. I would see it in the context that given that people now access banking like any other sector in a much more effective distribution model, the costs of getting the services and goods they want are much less. And therefore as a consequence of the same model, also the revenues that you can generate can be lower given the lower cost structure.

Number two, this is not a three year programme, this will be a generational programme as well for the reasons I have told you relating to the different segments of the population and how they age. And in my opinion, and I know we have a different view on this. But we strongly believe that the branch network will have a very important role for the next foreseeable future and I have to tell you that I have now managed banks for 21 years and I already heard of the branch disappearance 21 years ago and they are still here. So the way we see this going forward is, the revenues through digital and so you have to see the mix versus the other channels. The revenues are normally lower margins. But on the other hand, volumes are increasing exponentially so it is not only margins. It is margin times volume and you have to see that the marginal cost is almost zero. And what we have to do and why we try to put ourselves at the forefront of this long-term process like creating a Digital division, making that Digital division across the Group, present at Executive Committee, to have a central attention, central allocation of resources, is exactly to start adjusting our cost over base with the front foot, so starting doing that ahead of our competitors, exactly because the lower trends are in the direction that you mention. But I think this is good for society and it will be good for the banks that adapt in a proactive way by lowering their costs structure successfully as you increase significantly the volume sold. But of course it will have lower margins per product.

Further question
And can I just ask one supplementary. In terms of mortgages and your expectations in terms of a leverage ratio somewhere I don't know 4–5 per cent, something like that, obviously you have also got the discussion about minimum risk weightings on mortgage and obviously if you do apply a 4 per cent leverage you have got a huge disparity between capital allocation under leverage and capital allocation under risk based capital. So are you also expecting some sort of increase in risk or imposition of a minimum risk weighting to try and reduce that disparity?

Answer: António Horta-Osório
From our discussions with the Regulators which we have already shared with your several times, and they have not changed, our view is that, no that they will do what you are saying through the leverage ratio. They are not worried about the path of the housing market. We have just started to recover one and a half years ago, based on the Help to Buy schemes and Funding for

Lending schemes. And should they become worried, we believe what they would do risk-weights on new business only and through LTV bands, but we do not believe this is on their priority at the moment from the conversations we have with them.

Question 4: Manus Costello, Autonomous

Thank you. I have two questions actually, one for António and one for George. António you said in your Presentation that you think the UK market is highly competitive, but the CMA would appear to disagree with you and the Labour Party certainly disagrees with you. I wondered if you could discuss how your strategy as presented today, might have to evolve if that competition review comes out differently. What would be your approach?

And my second question for George is, George you talked about 20 per cent total capital ratio, whereas you are currently at about 18 per cent on a fully loaded basis. So should we now assume that you actually have a deficit of sub-debt rather than a surplus of sub-debt? Because in the past we had always thought there might be a margin benefit from knocking out some sub-debt, but it now looks like you might actually have some headwind from having to fill that TLAC gap?

Answer: António Horta-Osório

Let me answer the first one while George has time to think about your second one. I think it is great to have this type of debate in the UK and to be very precise what I said is that I believe that the retail sector in the UK is highly competitive. I do not believe that is exactly the case in small business customers as I have said already previously several times. And the reason why is because while we look at the retail sector, you have a wide variety of choices for customers with quite transparent conditions and you now have the seven day switching mechanism which enables people to switch without risks. When you go to the small business sector, people are normally single bank as you know. In the retail sector people are multi bank, they have different introductory offerings and they have multiple bank accounts so they can compare easily and they can switch easily now. In the small business sector they have normally only one bank. Conditions are not that transparent and not that comparable because they only have one bank and the switching mechanism is not yet extendable to the small business customers. So while I think that in retail, given the customer behaviour mainly, of being single bank, you have more competition issues. On the retail markets, given what I have just told you, coupled with the fact that internet is going everywhere and internet is by definition the most competing channel that you can have. And thirdly, you have the significant presence of intermediaries in the UK market, 11,000 and they have half the market in insurance, investments and mortgages, I strongly believe it is a very competitive market. Having said that, we will see what the CMA decides in terms of launching the studies which we are expecting them to launch. We will see what type of remedies and what type of actions they will propose. We are absolutely willing to co-operate with them and we will see what the outcome is. And we think that it is good that this is done by the way, like the Vickers's Commission proposed, that analysis proposed that to be in 2015. Whether it is good that it is done on its merits by the professional body, which is the CMA and of course whatever Government will come from the elections, we will have to respect the decision that the professional body will take.

Answer: George Culmer

On TLAC, yes as you know we have on a fully loaded basis, our total capital is about 18 per cent and on a transitional it is about 20 per cent. And I think irrespective of whether one thinks that is enough, I think that stands very good comparison with our UK peers who have less ratios than certainly with our European peers, a number of who have significantly less ratios, they have smaller capital stacks than that I should say.

In terms of where to from here? Again you will have read and you will have seen, whether it is leaked papers or briefings or whatever, in terms of expectations to where that TLAC is going to land. So I would agree with you, my expectation over the years will be a net issuer rather than a net redeemer. And whether I am shooting for 22 or whatever the final figure lands upon, is still to be determined, but I would say we start that journey in a much better position than everybody else. What I would also say is that whilst the quantum of that capital stack might increase, in terms of the sort of unit cost there is a lot of again, more expensive issuance that we put on in terms of the crisis years rolls off, you will basically see the sort of unit cost come down. But I would certainly expect to be a net issuer but I would certainly expect a large number of our peers to be issuing significantly more amounts of sub-debt than ourselves.

Question 5: Fahed Kunwar, Redburn

It's Fahed from Redburn. I had a couple of questions. The first was on a cost:income ratio so your 45 per cent cost:income ratio target, is that in line with your 2.5 per cent base rate assumption in 2017 as well and if base rates weren't to go up and stay flat, does your 45 per cent cost:income ratio come under threat a little bit?

And the second question was on your 13.5 to 15 per cent RORE guidance. So based on an 11.5 per cent cost of equity, sorry core tier 1, but if you are talking about a 4 to 5 per cent leverage ratio which is your expectations, then they have talked a lot about paralleling those in the core tier 1 leverage. So that is probably more to like a 12 to 13 per cent and considering you are already at 12 and capital generation is not your issue, why not set your RORE target on a higher capital base rather than setting it at 11.5 per cent? Thanks.

Answer: George Culmer

Yeah I mean the fundamental presumption, maybe and plan if we get to about 2.5 per cent in terms of base rate in 2017 and that fades through into the cost:income ratio. And you are right, basically an 11.5 per cent capital climate. Now in terms of those targets, yes there is whole things that can change, whether it is the competition, whether it is macro economics, whether it is the regulatory in terms of the capital. I think what we are saying to you, particularly that RORE target is it is built on a number of those assumptions. Were a number of those assumptions to deviate we would still be striving to hit that RORE, be it the base rates, be it the slight movements in capital requirements etc. The range that we have set we would still be striving to hit within the prescribed framework. So obviously if it moves extremely, then that will have consequences. I would have to go back and look at that. But if I am talking about differences between 11.5 and 12.5 or whatever, if I am talking about 2.5 or 1.5, we will do what we can to hit those targets, be it the cost:income or be it the ROE target. What we have said is built on assumptions. We all know that assumptions can change, but obviously if they change within reasonable parameters we will run the business to endeavour to hit those targets we have set today.

Question 6: Raul Sinha, JP Morgan

Hi it's Raul Sinha from JP Morgan. Can I have two questions please? One following from a previous discussion about the impact of the Digital strategy. Clearly I think one of the concerns the market might have is the impact on income off the digital strategy where cross-sale becomes a lot more difficult, especially in the new regulatory environment and customers clearly are able to distinguish and choose banks quite easily online, which obviously changes customer behaviour materially compared to maybe the last decade you have seen. So to what extent do your targets already anticipate maybe a shift from OOI to NII in pricing? And can you talk about structural pressures that you see on other income going forward, whether you think the outlook for growth there is as strong as it is for NII? That is my first question.

And then second one, sorry.

Answer: António Horta-Osório

Wait, I'm just going to make a very small comment, and then Miguel will elaborate on the big idea of the cost span and what we anticipate and George can tell you about OOI. And what you said is correct, we have been saying for some quarters now that given the evolving regulatory environment, especially relating to conduct, you should consider our income more as a whole because the recent transfer between commissions and therefore OOI into NII. We have been saying that for a few quarters now. Secondly, what you said about the trends are correct. We have incorporated that in our plans and Miguel can give you some colour and examples about that.

Further answer: Miguel-Angel Rodriguez-Sola

So the transfer from OOI and NII, the terms as you know are multi-channel we don't see immediately, it is through there are some pressures in both in margin, but we manage this in an integrated way of multi-channel and multi-brand. So in terms of OOI, let me put in an example. 85 per cent of all international payments the Lloyds Banking Group does is online. It is easy, it is convenient, it is OOI. So from the next wave until now we have put all the simple products in our Digital platform. The next stage ahead of going to complex products is to execution only products. Next year you can expect that we will launch protectional line. So this will be an opportunity to generate more business in an OOI or NII. The more complex products is a question in the near future, but we will need to work and we are working closely how we deliver and the whole will evolve in terms of financial needs. But I would like to stress the point of what we have done in the Presentation. So when you get a customer which is multi-channel and operates Digital, really the customer and the client in Commercial is more engaged with the bank, 30 per cent more product, more interactions. This is not new to banking. In Digital and fortunately the principles of all the good and traditional banking applies. When you have the engagement, when you are in the flow of payment you have a payroll, the most important bills. As I said, when you are in the flow of incomes and payments of a household or a client, then you are the primary bank and these customers on average transact five times more with you, on average have three times more balances and have more profitable for the bank.

Further question
The second one was on interest rate sensitivity. Obviously in the past you have talked about the fact that you have hedged particularly for the current balance sheet on interest rate rises and you don't scan amongst the other UK banks as particularly sensitive to interest rates. Some of them don't have as much hedging as you have in place. But is it fair to assume that if we look at potentially a three year time horizon and we look at the back end of that, is your interest rates sensitivity a lot higher than is implied by the current hedge position?

Answer: George Culmer
That would be broadly correct, as previously communicated in terms of the hedging position etc, we will not be on a a short term basis sensitive to interest rates because it is the Bank's policy to set out and be as predictable and sustainable as possible in terms of our NII stream. But obviously as you move out of that in terms of the hedge, rolling over and being reinvested etc, as the ability of margin management increases, yes as we move out in terms of towards our longer base rate type assumptions, you will get earnings pick up. And it sort of plays back into the last sort of question in terms of base rates, deviate from the central assumption. You know, what is our ability to manage it. And all I can do is I can exhort to you that we will do our utmost to hit the targets if the base rate deviates from that assumption or the capital deviates from that assumption etc. But the later out you go the more beneficial to income.

Question 7: Jason Napier, Deutsche Bank
Jason Napier from Deutsche. A question on the Commercial Banking division if I could. Near enough half of the risk-weighted assets in the Group, pretty close to your long-run cost:income target, and the return in the first half probably did better than you would expect it to, given that bad debts were almost nil. Could you just talk a little bit perhaps P&L wise where the uplifts are supposed to come from in the 2.4 per cent return on risk weights? Is it better margins? Is there really a cost story in this division? Do you expect the risk weighted assets to grow in the next three years and those sorts of things? Thank you.

Answer: António Horta-Osório
Well some comments about that. You are right it has a huge proportion of our capital, fortunately quite less now because RWAs have been reduced 40 per cent over the planned period which was very disciplined with appropriate capital management from Andrew and his team. And as you said, we have better than expected results in terms of return on risk weighted assets in spite of quite adverse market conditions. So at 1.96 per cent return on RWAs we are quite close to the 2.0 per cent target for next year. That is why Andrew and we as a GEC we decided we could lift the bar again and target 2.4 per cent return on risk weighted assets by 2017.

What is on the basis of that strategy? Well on the basis of that strategy is on one hand increased volume growth as we continue in terms of Mid Markets and SMEs, we continue to grow SMEs significantly above the market, but Mid Market lending growth is now turning positive as we had anticipated. And we expect it to grow as well above the market and positively going forward on one hand. And secondly, relating to the client approach which is client orientated and not product orientated, the objective of the division is to deepen client relationships, either at large corporate levels or at any level of the segmentation. So most of the increase in income should come from the deepening of those relationships and from better share of wallet of those customers. Where for example, during this year, all the good work done on the division in terms of doing more for exchange transactions for customers, more money market transactions, additional capital markets or transaction banking, have been a bit offset as you were saying by the fact that these markets have contracted and the margins have shrunk a lot. There were significant market share gains of the division on those markets reflected on higher share of wallet which as markets will recover and as we continue to deepen client relationships, those should be reflected on our P&L going forward. So it is especially a story about continuing to deepening client relationships, translating to higher share of wallet and OOI in this specific division and continuing better capital management as I said in my speech, given that we are much treating the way we manage capital according to the cost of capital and the weight of the division in the total Group.

Question 8: Sandy Chen, Cenkos Securities
Hi, it's Sandy Chen from Cenkos again. I just want to ask about the Digital side. I think particularly on the Retail, the other part of Digital which seems really a part that you haven't talked much about is price comparison websites and the effect they might have on pricing. Could you give some additional colour in terms of the percentage of say new mortgages, new savings, term deposits that flow through price comparison websites? What is the price sensitivity of that? How that has changed and maybe if there is expectations that the high price sensitivity, rate sensitivity of those price comparison websites will lessen? It seems like what you are assuming is that there might be some ability to get better spreads in your mortgage business and I am wondering how that plays versus that channel?

Answer : António Horta-Osório
Okay some comments. I really can't tell you exactly how many come from price comparison, I really don't know. We can give you more colour later on. But strategically speaking, and as I was telling to Manus, that is another factor, when I mentioned the internet, that is another factor why I believe that the retail market in the UK is very competitive. People go to the internet either to access the channel in savings for example, or to compare pricings in a transparent way. And they switch because they have different bank accounts. That is why I strongly believe that is an additional factor why it is very competitive.

Second point, we are not predicating our planner, this is very important, on an increase of mortgage margins. I just said upon a question from you as I have said previously, that looking strategically, I think the leverage ratio depending on where it comes out on Friday, will have a less or a bigger impact on mortgage pricing because it will become a restriction. But I think it will be an important strategic consideration. But that is not what we are predicating on our planner. Because as I have said many times, we manage pricing differently in Lloyds. We manage assets and deposits together. What matters for us is the difference of the two now that we have achieved a core loan to deposit ratio of 100 per cent. So every loan that we give is totally funded by deposits. So the masses are the same in both sides of the balance sheet. What matters is the difference. And we do the management together. We do it on a weekly basis while our peers normally do it on a monthly basis. We think it is critical to do it almost on real time. And we do it at the highest level of the organisation. And as I said sometimes before, coupled with the fact that we have a multi-brand and multi-channel offering and we do the integrated pricing in that context, I strongly believe this provides us with a competitive advantage over time which is not irrelevant I think to the fact that we have been able several times in the past three years to enhance our margin guidance as we go forth, because it is part of creating a more agile and more responsive and a better organisation. But our plan is not at all predicated on special behaviour of mortgage margins, it is predicated on dis-pricing which is the two masses together, the difference of the two, which as we have been saying throughout the year. We gave you guidance along the way and we think it is reasonably stable at the moment and we will as George said, give you more information at the end of the year.

Question 9: Chintan Joshi, Nomura
Chintan Joshi from Nomura. Another mass market bank in Sweden gave a very similar strategy around digitalisation cost savings last week, but there the focus was on absolute cost savings as digitalisation saves costs. Thinking about your cost saving target, £1 billion. Looking at your track record, you have got £2 billion of cost savings which meant that absolute cost base went from £11 to £9 billion looking at slide number 53. What should we think about absolute costs? Because essentially this is going into the direction of lower revenues and lower costs and that seems to be gist of your message as well. And then a couple of quick follow-ups.

Answer: António Horta-Osório
I thought you were going to say Chintan that they were imitating our strategy route!

Chintan Joshi
Both mass markets, both are doing the same thing, so there is clearly logic there.

Answer: António Horta-Osório
Yes but there is a big difference in my opinion in what is happening in Scandinavia and the UK, not to speak of other parts of continental Europe. In Scandinavia the trends for customers to be only digital in my opinion and according to what I speak to my colleagues here and in Scandinavia, are much more advanced. So I don't know if the UK that means ten years, twenty years, thirty years, but they are much more advanced according to what they tell me. They want to reduce their branch network to almost zero as you probably know and that is why probably they have a nominal cost trend downwards. We have a different view in terms of how UK customers value and want to use banking. We have a different view on the timing of this trend which is clear, but we think the timing is different so we want to go behind the curve because we think there is a huge correlation between current account market share and branch market share as Alison explained. So if we go behind the curve we think we minimise the loss of revenue opportunities while we maintain the bulk of our multi-channel model. And in our specific case, according to the assumptions that George told you economically, we think that the costs will go slightly up with revenues going up more than costs. That is why the cost to income decreases every year. But of course assumptions may change. Things may change like three years ago. And we are very careful as you said in terms of how we deploy our costs. Should the revenue opportunities look different, we have the lever of the costs and the risk appetite to model and that is what management is all about. But on our central case we think we are now on a growth phase, that the UK economy has started to grow sustainably only after twelve months and it is in the beginning of the cycle. We have finished strengthening and reshaping and we are completely ready to move from strengthening and reshaping into digital and growth keeping, simplifying and therefore we have significant growth opportunities in our opinion that require significant investments as we described to you. But given that we do not want to increment costs we are going to fund those investments with additional simplification programme that funds those

investments. And therefore we expect costs to go slightly up with revenues going a bit more and that is why the cost to income goes down every year and trends over time to the 45 per cent.

Further question
Thanks that was helpful. Just a couple of quick follow-ups. With the branch closures focused on urban areas, is there a potential for gains from asset sales given where property prices are?

Answer: Alison Brittain
No. I will just add to the rest of the sentence which is a large proportion of our real estate is lease.

Further question
And the second question just for George, the £1.6 billion how is it divided? Do you expect it to be more up front or will it be evenly spread out?

Answer: George Culmer
There will be a slight phasing to the start as opposed to the end. So I know that sounds incredibly vague, but that is probably all I am going to say. So there will be more in year one than in year three.

Question 10: Andrew Coombs, Citi
Andrew Coombs from Citi, I will keep it short, just two questions, rather than three. I just want to ask one question in terms of the branding. I fully understand the rationale for retaining Lloyds, Halifax, Bank of Scotland. But given the extent to which you see deposit outflows from Birmingham Midshires and Scottish Widows Bank, and that has been active on your behalf, does the flexibility on pricing that those brands offer, more than offset the additional complexity and costs on those? And essentially what is the rationale for retaining those two brands?

And then my second question on dividends. I think it is fair to assume that you won't be able to communicate anything until the 16th December in terms of this year, but going forward, given that we are going to be getting an annual PRA stress test exercise and the methodology will be adapted each year, how confident can you be on a 50 per cent payout ratio?

António Horta-Osório
Alison will start with the brands.

Answer: Alison Brittain
I will start with the brands first. You name two, but we do have other tactical brands as well and we continuously keep them under review and in fact recently decided that we would withdraw from one of our tactical brands for the reasons that you have just outlined. Birmingham Midshires is a particularly important brand for us because it is also mortgage brand and so it covers both sides of the balance sheet and we do a number of specialist area of mortgages through that brand. And Scottish Widows Bank you know is wholly owned and has its own banking licence and at the moment we are quite comfortable that it fits neatly within the portfolio and gives us flexibility if we want to scale up quickly on savings for some reason or keep the back book just ticking over.

Answer: António Horta-Osório
And just to comment on what Alison said in terms of does it make sense you say in terms of complexity versus simplicity? Let me explain to you in terms of the brands, why they make a lot of sense. But going a bit further, I strongly believe that customers going forward and also through Digital, they will want as segmented offering as possible. So ideally each customer wants as you all know, an offering for himself, he wants a targeted offering, but individual. The reason why you can't do that as you said is because of the complexities and cost of doing that. So in my opinion, if we are able as I think we are, through a multi-brand strategy to segment with differentiated offerings according to different customer needs and at the same time having all that the client does not see integrated and therefore lowering the unit cost, is the best way to maximise the cost to income in terms of revenue versus costs. And that is a very strategic point.

Then of course according to our tactical positioning at any moment, as Alison explained to you, we have a different approach to relationship brands versus tactical brands in the context of our total loan to deposit ratio, And in terms of profitability considerations.

Further answer: George Culmer.
And second one, I am very confident on the deliverability of our dividend strategy. I mean you see that in what we have said to you in terms of capital generation, you have seen it in the numbers that we have set out today. You have seen the RNS that we

set out on Sunday in terms of response to the EBA. We have already talked about the capital generation that you have seen in the first half and again you have seen in the nine months. We have talked about next year, you have things like the ATIs which will be included in that. And also the EBA stress test results themselves, where everyone focuses obviously on the 6.2s or the 6. There was a number in there in terms of capital generation by 2016, which had us at I think 13.6. And I think well ahead of our UK peers. So in terms of capital generation over the period, you see that in the numbers in the nine months, what the Bank can deliver.

Lord Blackwell
I think as Antonio said, we will need to draw the session to a close at that point. I am conscious it has been a very long morning, but hopefully it has given you a good sense of what is driving our strategy and what that means in terms of objectives and targets of our business model. There will obviously be opportunities to ask more questions in the weeks, months ahead, but for the moment, thank you all very much for coming, we very much appreciate it.

End of Q&A