BARCLAYS GLOBAL FINANCIAL SERVICES CONFERENCE WITH WILLIAM CHALMERS – PRESENTATION TRANSCRIPT
(amended in places to improve readability only)

Monday 9 September 2024 – 2.00pm (9.00am New York)

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Aman Rakkar, Director, Banks Equity Research, Barclays (Moderator)

Aman Rakkar
Thank you very much everyone and welcome to the Barclays Global Financial Services Conference here in New York. Delighted to be joined by William Chalmers, Chief Financial Officer of Lloyds Banking Group. William, thank you very much for your time.

William Chalmers
Our pleasure, thank you.

Aman Rakkar
To give a brief introduction, I'm Aman Rakkar and I head up coverage of UK banks at Barclays. I've been at the firm since 2011 and have been covering Lloyds for most of that time.

I'll also just briefly introduce William to those who are not familiar, I'm sure everyone is. William joined Lloyds' board in August 2019, you were appointed Chief Financial Officer. You were interim Chief Executive Officer during 2021. And previous to Lloyds, you've been working in financial services for over 25 years, held a number of senior roles, most notably at Morgan Stanley you were co-head of Global FIG, head of EMEA FIG; and before that, had a stint at JP Morgan, amongst other institutions. So, this is an example of William's tenure. Thank you very much. Really appreciate you making yourself available today.

So, let me just kick things off. The sentiment towards the UK has been improving in recent months, albeit from a low base. Inflation is falling, interest rates are falling, and the political backdrop does feel more stable following this summer's general election. But despite this, there remains market concerns around the potential for bank taxes. So, given your unique vantage point, I'd be interested in your assessment of the operating environment.

William Chalmers
Thank you, Aman, and perhaps before we get going, one, say thank you very much indeed for hosting today's conference, it's great to be here. And two, thank you to everybody in the audience for taking the time to join us.

Aman, as you say, sentiment on the UK has improved but as you also say, it's from, let's face it, a pretty low base. So, we've got a way to go, I think.

I think with that sentiment improvement, with that overall macroeconomic stability, if you like, we have seen the first fruits of that, including before the election, I would guess. So, the backdrop is, generally speaking, pretty constructive. It's good for asset growth. It's good for deposit stability. It's good for other operating income growth. It's good for, likewise, asset quality. So, we're seeing that all come through in the numbers. And we saw a fair touch of that in the context of Q2. Saw asset growth overall, about £3.9 billion in Q2. We saw deposit growth about £5.5 billion, of which I think about £3.6 billion was within retail. We've seen other operating income growth up about 9 per cent over the quarter, year on year.

So, with all that we're in pretty good shape. And again, it's supported by a generally benign macro environment. Again, as testified to by asset quality experience, which we'll talk more about, I'm sure.

I think, overall, that is good. I think the political backdrop, as said, is one of stability. It's one of a growth imperative. It's also, I think, encouragingly, one where the politicians seem to understand the value of a healthy banking sector. I think, to your point – and not surprisingly – the market's a little bit in wait-and-see mode on that. They'll be looking, I'm sure – you'll be looking, I'm sure – for the kind of pre-election words to turn themselves into action. And frankly, we all are. So, in that respect at least, the October budget will be an important event.

But I think underneath it, stripping all of that away, in that constructive environment we do think that the commitment to growth is genuine. It certainly seems that way from our perspective, and we'll look to see more of that, going forward.

Aman Rakkar

Perfect. Let's switch to the business then. So, net interest income, it's been under pressure for a while now, falling for six consecutive quarters, from a peak in the fourth quarter of 2022, but you've been pointing to a recovery in coming quarters. Can you talk to the main drivers that sit behind that view, including any potential sources of upside and downside risk?

I'm particularly interested also in your view on the mortgage and deposit headwinds that you face, how these are playing out and whether you see any green shoots.

William Chalmers

Sure, maybe just to come to the second part of your question first actually and to follow on from that economics commentary that we were just discussing, I think overall, as you have seen, we've marginally upgraded our economic expectations at the half versus what they were at the first quarter. We're seeing expectations of GDP growth about 0.4 per cent this year, 1.5 per cent next year. We're seeing rates falling, as you mentioned earlier on. We're seeing HPI increases expected to be about 1.5 per cent this year.

Actually, I think the outcomes overall will probably exceed (i.e. be better than) our forecasts, is my expectation right now, based on what we've seen. And that, to your point, Aman, is conducive to asset growth. It's kind of supportive of margin swings, which I'll come to in just a second. So, that backdrop, just following on from the first question, is overall pretty constructive, and you're seeing it evidenced, as I said earlier on, in terms of the numbers so far.

Specifically, on the margin, Aman, what are we seeing? We saw 293 in the margin, that's Q2, as you know. That was down gently, if you like, from the 295 that we saw at Q1.

What's the context for that? First of all, that is consistent with our expectations. That gentle decline, that pattern of gentle decline, very much consistent with our expectations. Second is, as I said before, we do expect that margin to tick up in H2, and certainly by year-end. Third, it is consistent with our greater-than-290 basis points guidance for the year as a whole, I'll come back to that in just a second. And then, fourth, as we said before, we do expect net interest income to tick up ahead of the margin. So, all of that, I think, all of what we're seeing within the margin development is very much consistent with what we had expected. Maybe a touch better at the margin, if you'll forgive the pun, as it were, but nonetheless, that's pretty much what we're seeing.

Within that, what are we seeing? Three main driving forces, as you'll know from our previous comments Aman. That is to say, mortgages headwinds, number one, continues to play out. We're putting mortgages on the book at about 70 basis points. We're seeing the maturity margin of about 110.

Deposit churn continues. That is to say, we saw PCAs down about £1.4 billion in the second quarter, that, by the way, is not a bad result. But we're also seeing movement, if you like, from instant access into fixed-term, limited withdrawal. That, we do expect to slow in the second half, and all of the evidence that we're seeing in June, July, and August really confirms that expectation. So, that's a good sign.

And then, the structural hedge. We didn't see much evidence of that in Q2, that's mainly because of maturity volumes and maturity yields. But nonetheless, that's a major supportive factor for the margin.

And so, looking forward, what do we expect to see? Again, first of all, consistency with our guidance of greater than 290 basis points for the year as a whole. A turn, again, at year-end that we expect to see. And that, in turn, is supported by reduced churn, by increased contribution from structural hedge, which will more than offset the drag, if you like, from bank base rate reductions and the associated pass-on lag that comes with that.

The upsides and the downsides. I mean, I think it will come down to how does churn develop, as said, the signs that we've seen in June, July, and August, on the whole, have been pretty constructive. How does mortgage pricing develop? There's much talk about a price war in mortgages right now in the UK, but frankly, from our perspective at least, that just seems to be taking us back to more or less where we were in Q2. So, I would continue to stick with our Q2 expectation for completion margins c.70 basis points. And then, are there going to be more bank base rate reductions than we expect? We expect two bank base rate reductions, of which we've had one. If there are more than that, then of course that's a drag, but I suspect it might be compensated for by other factors, including things like slower deposit churn, for example, including things like less SVR attrition, for example. So, those are the kind of sources of upside and downside overall, Aman.

The one point perhaps that I'll finish off with is we do feel comfortable – in fact, I'd say increasingly comfortable – with our overall margin guidance. So, from here, it looks pretty good.

Aman Rakkar
Great, so, you alluded to rate cuts, pass throughs. So, the Bank of England delivered its first rate cut the 1st August. Markets are pricing in at least one more cut by year-end. These cuts are expected to impact deposit pricing, with the pass through – or betas, as we refer to – always a key area of interest. You outperformed many of your peers on the way up, passing on a relatively lower proportion of rate hikes. How do you think about your ability to lower rates as we progress through prospective base rate cuts?

William Chalmers
Thanks, Aman. I can't resist to come back to one part of your question there, which is that I don't think we did really pass on much lower than normal, much less than any of our peer group. We were pretty much in the pack, is what I'd say.

Our pass-on strategy fundamentally is driven by a combination of customer value, first and foremost; funding needs of the business, secondarily; and how are our competitors moving, thirdly. I mean, those are the drivers of our pass-on. And as said, I think on the way up we were pretty much in the pack. And as testimony to that, you'll have seen our deposit performance over the course of '23 and again in the course of '24, all of which is very healthy from a volume point of view; in fact, I would say at the leading edge, if you like, of our peer group. So, that I think is testimony to the pricing strategy.

The bank base rate reductions are included, as said, in our guidance of greater than 290 basis points for the year as a whole. As we see bank base rates come down, we will pass on. We will pass on based upon the same factors as we did on the way up (i.e. the same three dynamics that I just highlighted), but it won't be lockstep. So, just as it wasn't on the way up, it won't be lockstep on the way down.

It's worth just stepping back actually and just commenting on the way in which we manage the margin, which is in a very holistic fashion. So our pricing decisions on deposits, Aman, as you can imagine, are going to be – in part, at least – influenced by what we see on the asset side. That margin is managed in its totality, and that's what we'll be looking for.

The overall setup then for the margin I think is looking in a pretty good space. There's a lot of talk – perhaps you're alluding to this in your comments a little, Aman – there's a lot of talk around regulatory and political pressure on deposit pricing, in particular. What would I say to that? First of all, I'd say we're obviously keenly aware of what Consumer Duty brings to the table. But having said that – and I hope this is consistent with what we've said before – the concepts behind Consumer Duty are nothing new.

What I mean by that is to say that we have managed the business for customer outcomes for some time. Frankly, in the UK, as in many other jurisdictions, it's just too punishing not to. And so, great customer outcomes have been part of the philosophy of the bank for many years now, including preceding my time. And that is quite independent of whatever the regulatory and political tenor might be at any given point in time. And therefore, the thoughts, if you like, behind Consumer Duty have been with us for some time. In that context, I'm not sure the political and the regulatory pressure make a whole lot of difference to the way we should go about the business.

Aman Rakkar
Perfect, we're going to maybe turn to the ARS questions. So, you've got these devices on your desk. I know this will probably be the first time you're using it today, please do participate. We've got six questions, we'll go through a couple now and then maybe pepper in the others as we go along.

Question 1: "What would cause you to become more positive on Lloyds' shares: (1) better NII; (2) stronger fees; (3) better cost control; (4) better asset quality; (5) greater capital return; (6) clarity on the FCA's motor finance review?"

William Chalmers
That's a good outcome. I was going to make a comment, actually, as you introduced 1 through 6 there, Aman, but then I thought I'd better not lead the audience, but rather leave it up to them. Maybe you want to comment first on that, Aman. I'm happy to.

Aman Rakkar
I think it's pretty consistent with the kind of conversations that we're having. It's hard to get beyond net interest income, a dominant part of the earnings stream. I mean, I guess we'll kind of come back to the discussion on Motor Finance later on, but again, I think that's pretty consistent with the conversations we're having.

William Chalmers
I think it is, yes. I mean, the one comment that I would make is, as we discussed at the half year, I'm pretty confident that net interest income is going to be better in the second half than it is in the first half. And that'll be led by the types of dynamics that we've just been discussing this morning.

Aman Rakkar

Perfect, let's move to Question 2: "What are you most concerned about at Lloyds: (1) weaker earnings; (2) weaker capital; (3) distributions; (4) reg risk; (5) political risk; (6) M&A?"

William Chalmers

Well, I think, as a bank investor, you've always got to be focused on the earnings streams, haven't you? You can tell, I think, from our commitments both as to 2024 and, indeed, as to 2026, that, (a), we feel confident in near-term delivery, but also, (b), we feel confident in the more medium-term delivery.

The regulatory legal risk, the political risk, it goes back to one of your questions, I think, Aman, which is to say we've got a new government in. It's very committed to restoring the UK's position, and indeed growth is part of that. I think we are all looking forward to that.

Aman Rakkar

So, the 30 October budget, I guess, is a key date in people's mind.

Okay, let's turn back to the business. Structural hedge, turning to your structural hedge. A significant multi-year tailwind. You've guided for a greater-than-£700 million income uplift in '24, driven by higher reinvestment yields. That's been tempered by falling notional. That's going to be substantially offset this year by things like mortgages and rate cuts, I guess, you've alluded to, but how confident are you that this can drive the bottom line beyond this year?

William Chalmers

Thanks, Aman, structural hedge, clearly, an incredibly important part of our overall earnings story. I think, stepping back, it continues to be a really healthy outlook for the structural hedge. That is to say, consistent with our objectives of stability in earnings and indeed value for our shareholders.

Specifically, what do I mean by that? As you know, we've committed to the structural hedge delivering an in-excess-of-£700 million increase in contribution in '24, on top of the £3.4 billion that it earned in '23. And that is a function, if you like, of a yield of around 1.7 per cent this year, refinancing to a kind of 3.5 per cent plus rate as we stand today, so that's a significant step-up.

That, as you say, has been offset this year at least by a little bit of notional attrition. Overall, we saw attrition in the notional of around £8 billion last year. We expect to see something roughly similar this year, of which we've seen about £5 billion so far.

And then of course, to your point, Aman, we've seen one or two headwinds in that mix; that is to say, the mortgage headwind that I talked about earlier on, a bit of deposit churn, non-banking net interest income, likewise. Those have all kind of ebbed away a little bit of the structural hedge benefit and contributed to the earnings story that we have seen, which is a strong one, but nonetheless it's a function of that balance.

2025, what do we expect to see? We expect to see a jump in structural hedge contribution in excess of that greater than £700 million that we see in 2024, number one.

Number two, in 2026, we expect that jump in structural hedge contribution to be again a material step-up; and in fact, in '26, a more material step-up than what we expect to see in 2025. So, a jump in excess of £700 million in '24; step-up again in excess of £700 million gain, if you like, in '25; and then a more material step-up from that in respect to 2026. That's pretty much how we expect the hedge to play out.

And as you can imagine, we're trying to lock that position in, if you like. We'll always be a little bit exposed to upwards and downwards trends in interest rates. You've seen our sensitivities in that respect. But nonetheless, we are trying to lock in that earnings path that we have given you for '24 and in respect of the '26 follow-through.

So, what does that mean in terms of structural hedge? We're pretty much done for 2024 now, number one. We're probably around four-fifths done, thereabouts, for '25. And we're probably around two-thirds done for 2026, and we're building in that respect.

The difference by the time we get to 2026 is that many of the headwinds that we've all been talking about for a while now are either eliminated or dissipating. Specifically, what do I mean by that? The mortgage headwind that we've talked about is pretty much gone as of the first half of 2026, number one.

The deposit churn headwind in the context of a more stable rates environment we expect to have gone, in fact, well before that, but nonetheless will be basically not happening during the course of 2026.

The bank base rate reductions that are, if you like, a headwind over the course of the second half of this year, going into 2025, that'll be largely done because we're moving to a more stable bank base rate environment, if you look at our forecasts. And the headwind that we've seen in the context of non-banking net interest income, likewise, that's pretty much gone by the time we get to 2026. In fact, aspects of it may be in slight reverse by that time.

So, as a result, what you're seeing in 2026, I think, is the structural hedge continuing to contribute in a kind of ever-larger way with that step-change in particular in 2026, but not being met by the types of headwinds that we're seeing in '24 and a little bit in '25. So, the contribution, if you like, takes a net significant step-up during that time.

Now, if you add that to the strategic initiatives contribution, which, as you know, is expected to be £1.5 billion incremental revenues in '26, allied to the fruits of some of our investments coming through in the cost line, which contributes to greater stability within costs, then what you've got is an operational leverage story. And that operational leverage story fundamentally is what drives our greater-than-15 per cent RoTE target and, indeed, our in-excess-of-200 basis points capital expectation. There's nothing, frankly, magic about it, it's more or less a function of arithmetic, a lot of which is already built in as we stand today. And that, in turn, is a position that, as you know, we continue to restate with every major earnings announcement that we make – whether it's the year-end, whether it's the half-year – because it's one that we feel confident in.

Aman Rakkar
Turning to growth. So, there's a view that UK banks are under-risked or, indeed risk-averse. I think that's evidenced across a number of metrics; but not least, a sustained period of sub-normalised impairments. I mean, that's a remarkable out-turn given what is a challenging backdrop (sorry for the noise in the background). As demand recovers, is there an opportunity for you to take more risk as you drive growth?

William Chalmers
It's a good question and I think there has been a perception around the UK banks in particular. I think it's, frankly, still a bit of a hangover from the financial crisis and the regulatory response to that. So, it's a function of the environment, in part.

I do think, to your point, Aman, this has been evidenced, frankly, by the performance of the bank; not just ours, but I think, to be fair, most of the banks in the sector. And we've seen more of that in the quarter. Q2, as you know, AQR – asset quality ratio – of 5 basis points. Now, admittedly, that was informed by MES judgments in our favour, but if you strip that out, it's 16 basis points i.e. still pretty low.

And then if you strip out one or two model judgments, including the removal of inflationary adjustments within our modelling, even after stripping that out, it's still 23 basis points in Q2, which is, again, a pretty favourable AQR result and consistent with our Q1. So, you've seen a very solid and consistent pattern of asset quality performance during the course of 2024.

I think actually – and of course, I would say this, but I think it is observable – that it is part of a track record. That is to say, the true losses in the context of the COVID environment were really very modest. Likewise, you've seen our stress test performance, which has continued to improve over time. And I think what's going on behind that is a strategic focus on the prime customer base, on the lower-risk parts of lending. So, our mortgage LTV, for example, is 43 per cent. Our CRE LTV is 46 per cent. We've been progressively either reducing or alternatively, selling some of our legacy exposures. And all of that, together with one or two other factors, has led to a progressive and significant de-risking of the bank.

And I think to your point, Aman, that has led to asset quality performance of the type that we've seen and an overall perception that perhaps the bank sector – and us amongst it – could take potentially at least more risk. I think let's see how the economics develop over time, going forward.

I do think one point that is worth making is that despite that low-risk attribute, our lending has actually been pretty positive. So, £3.9 billion over the course of Q2, that's not bad, that's a 1 per cent increase in loans and advances in one quarter. We expect that growth to continue in Q3, and we expect it to continue in the remainder of the year. Maybe not quite at that clip. I mean, 1 per cent per quarter is a lot from what is fundamentally a kind of GDP-plus-based entity, but nonetheless, we do expect growth to continue, going forward.

That in turn, will be supported by any kind of macroeconomic benefits that we see off the back of a more stable government, for sure, that is helpful. But I think the point that I'd like to push back on a little bit is that there is a correlation between risk and growth. I think if you look at the performance of the bank over the recent quarters, we've managed to achieve growth – witness the lending comments that I just made – at the same time as pretty minimal risk. And I think by virtue of our strategy, which has a focus on customer segments that we are currently in and indeed exploit – "exploit" is the wrong word – further explore, let's say, customer relationships. Overall, I would expect us to be able to deliver growth and low risk at the same time.

That has certainly been a hallmark of our strategy for many periods, including preceding me, and I think many periods looking forward. That's what we expect to see.

So, no necessary opposition, I think, between the growth of the business and the risk that we may need to take. Albeit, I do hope that within the UK we see a political environment that is more conducive to risk-taking as a whole.

Aman Rakkar
Great. To round out the discussion on revenues then, so other operating income. I think it's been mostly positive in recent quarters, it was up 9 per cent year on year in Q2. That followed similarish growth in Q1. Part of that, bolstered by improving activity but also strategic investment behind that revenue item. Can we expect a continuation of this level of growth?

William Chalmers
Thank you, Aman, for the question, in short the answer is, yes, I think you should expect to see a continuation of OOI growth.

What is behind that comment? As you say, the record recently has been not bad: 9 per cent second quarter growth year on year; 8 per cent H1 growth year on year. And I think, pleasingly, that has been informed by performance across each of the business lines. So, specifically within that, Retail, for example, PCA revenues growing, likewise, transportation. Within Commercial, markets business growing. Within IP&I, GI growing. So, it's good to see it kind of have a pretty broad base.

I think that's been a function both of BAU performance (i.e. off the back of reasonably stable economic background) and then off the back of the fruit, if you like, of some of the strategic investments that we've been making and talking a lot about in the public domain. So, both of those two factors, I think, have been coming through.

That's led to OOI, as you've seen, around £1.4 billion over the course of the quarter. Looking forward, I think that is going to continue to grow off the back of the two points that I just made; that is to say, inspired by BAU, inspired by strategic investments. Fundamentally, coming from similar places.

As you know, we've committed to £0.7 billion of incremental revenues as a result of the strategic investments in '24, £1.5 billion in '26, of which half, 50 per cent, is coming from OOI. So quite a substantial contribution from OOI, going forward.

Why is that? What do we see within other operating income? We see an opportunity to serve more of our customer needs. We see an opportunity to grow capital-light revenue streams. We see an opportunity to build growth, generally speaking, within the business and achieve that operational leverage that I talked about earlier on. We see an opportunity to increase diversification and reduce our traditional dependency on net interest income and the volatility that goes with that when rates go up and down.

So, overall, there's lots of reasons as to why we're chasing this other operating income growth. And as said, from both a BAU perspective and, indeed, from the strategic investments that we're making, we are starting to see some results. And we believe that those will continue, which is what's behind my comment that this audience, our investors, should expect to see continued other operating income growth as part of our plan. And that's our expectation.

Aman Rakkar
I guess, just relatedly then, I mean, operating lease depreciation has kind of been the counter balance, it has been going up. I mean, I think you pointed to continued growth from here.

William Chalmers
I mean, operating lease depreciation is worthy of a comment, it's a very fair point, Aman. What have we seen there? I think two things that we've seen there. One is we've seen normalisation. Actually, three things, I should say, that we've seen in operating lease depreciation. One is normalisation of the operating lease depreciation line. We had an extraordinarily benign period of very high used car prices, I think in part inspired by the COVID issues, which in turn gave us some significant gains in operating lease depreciation. So, we went from a charge that was c.£1 billion – just shy of £1 billion – before the pandemic to a charge that looked more like £300 million, £400 million, £500 million during the pandemic. And part of the trend within operating lease depreciation has been to revert back to normality, if you like.

The second thing that has been going on is that we've been growing the business. Now, that is a very profitable attractive business that serves an important societal and customer need. We make, as said, a very attractive return from it. Our customers require the service. It's something that we should be in, and strategically we have a very attractive platform in that space. And so, we grow the business and, with that operating lease depreciation grows a little bit.

The third point, frankly, which is less welcome, is the volatility that we've recently seen in used car prices, particularly in electric vehicle prices. And that's what's been behind basically an incremental c.£100 million in our operating lease depreciation charge, as of Q2. You'll have seen our charge of just shy of £400 million, the underlying charge there is more like £300 million. And so, when we look at Q3 and beyond, I would expect it to revert to that type of level. It will obviously be augmented by a bit of growth within the business, which is frankly what we want to see because it's profitable and attractive and it serves our customers' objectives. But nonetheless, you should see a reversion in Q3 to something more like a kind of run rate plus growth c.£300 million, maybe a touch above, something like that.

And then allied to that, the final point that I'll make is when we look at that stream, if you like, the operating lease depreciation stream, we are very focused on the volatility point that I just mentioned. That £100 million hit that we took in Q2 is not particularly welcome and so, we're looking closely at what we can do to de-risk that element. Whether it is sharing any element of residual value with the manufacturers, for example, whether it is engaging with the capital markets and the risk pricing of that, for example, whether it is pulling the various levers that we have available to us in the financing market versus the leasing market, for example, all of those are tools and others that we are looking at in the context of just trying to mitigate, reduce that volatility. Because it's unwelcome to us in the context of a bank that should be a very reliable set of earnings and a very reliable source of capital repatriation to our owners. So, that's what we'll be looking to do, but make no mistake, the motor business is an attractive, profitable, and strategically important business for us.

Aman Rakkar
Excellent, let's move to the ARS questions, please. Question 3: "What do you see as the biggest risk to Lloyds' earnings: (1) rate cuts; (2) competition; (3) cost inflation; (4) loan losses; (5) government or reg intervention, bank taxes?"

Pretty dispersed answers, isn't it?

William Chalmers
It is, yes. I mean, looking at that, a couple of thoughts really. One is I'm not terribly worried about the rate cuts, that is to say, this bank will do better even in a cutting-rate environment, as hopefully some of my comments around the structural hedge illustrate.

Two is that competition is a part of the business, it's there with us. The one fortunate point, I think, is our start point. That is to say, it's a fantastic franchise with scale and we really ought to be able to compete effectively in that market, and that's our expectation.

I think three, a third point, government regulatory intervention, fair enough, I mean, we've had the comments around the politics, and let's see what happens. As I say, the underpinning that gives me confidence is what appears to be a pretty unequivocal commitment to growth. And with that, I think it solves a lot of questions, it answers a lot of questions.

Aman Rakkar
Question 4: "What do you expect for Lloyds' revenues into '25: (1) growing, driven by NII; (2) growing, driven by fees; (3) flat, year on year; (4) falling, driven by NII; (5) falling, driven by fees?"

I'm trying to extract a '25 revenue guide out of you...

William Chalmers
I thought this was a trap actually, Aman, I must say.

Aman Rakkar
I'm interested in whatever comment you have on those answers.

William Chalmers
Of course, I'm sure you are. I think outside of the answers that I've given to your other questions, Aman, I probably shouldn't comment any further, but hopefully I've given this room a bit of confidence in terms of our outlook for the business as a whole.

Aman Rakkar
I get a sense, actually, from the UK banks that I speak to, there's kind of – it's actually easier to talk about medium term than it is even the kind of near term.

William Chalmers
I think it is. I mean, I think within the UK – maybe it's just true of banks markets, generally, particularly in the type of backdrop that we've seen – people get very focused on the very immediate term, the very near term. And I think we're constantly trying to say to people, step back a little and look at the bigger picture. And the bigger picture, as said, is really constructive.

Now, that's not to say that you should expect volatility in the intermediate period. You shouldn't, you should expect what you invest in. But nonetheless, I do think the bigger picture is really what gives us confidence in the story of the bank. We'll deliver on our commitments this year, for sure, but we are equally focused, if not more so, on delivering in '26.

Aman Rakkar
I'm going to switch back to the business. The motor finance review has been a key area of focus this year. So, the FCA launched a review into the historical commission arrangements in the motor finance market. You took a £450 million provision with FY results. And from my observation, it's been remarkable how comfortable you sounded on this issue, from the outset. The FCA has since announced a delay in proceedings to May next year. Interested in kind of, what do you make of the delay? And does this increase the risk of a further provision?

William Chalmers
It's a fair question, Aman. The one point that this room should be aware of, I suppose is we totally recognise the investor concern on this point and frankly, we are also very focused on it.

I think, within that – rather, beyond that, what would I say? The first point is everybody recognises – the regulator, politicians, society, banks, etc – everybody recognises the importance of motor finance to the UK economy. And indeed, I think that is what is behind the FCA trying to seize the thing, to ensure that we move towards a speedy and orderly resolution of the issue.

The FCA focus has been and continues to be, Aman, on finding evidence of misconduct and customer harm. And as you've heard me say before, from our perspective at least, nothing has changed. That is to say, we believe that we've been in compliance with all the regulatory requirements at the relevant time. So, nothing has changed from our perspective in that respect.

The provision that we've taken of £450 million, it was predicated on two things, as you perhaps have heard. One is the inevitability of administrative expenses, I'm afraid to say we're beyond that. We're going to incur administrative expenses, we already have done. That was point one.

The second point was a risk of redress – a risk of redress as opposed to the inevitability of it – which, in turn, we have provisioned within that £450 million based upon a variety of potential outcomes.

When we look at the FCA announcement, the delay into 2025, frankly comes against a backdrop of us wanting just to get beyond this. In that context, a delay, I'll be honest, it isn't particularly welcome. It just suspends a period of uncertainty for you as investors and for us. So, that part of it isn't particularly welcome. But then if I look at the substance behind it, nothing has actually changed in the FCA's position on this. Nothing's actually changed as to the facts of the matter, if you like. And so, from our perspective, Aman, we stay very much in the same place. That is to say, repeating the comments that I made earlier on, our understanding of the situation has not changed from where we were at the beginning of this year, and we remain comfortable with the position.

That said, anything that delays this inevitably, however, it isn't what we want to see. We want to see speedy resolution of this, just as you do.

Aman Rakkar
I guess a related question then is around capital. So, you're on course to end the year with a surplus capital position. You had a 14.1 per cent CET1 ratio at H1. You're likely to build into H2. You've committed to paying down to 13.5 per cent by year end. But interested, how do we get down to this level then from what is likely to be a surplus capital position at year-end? And how does the delay in the motor finance review kind of feed into that process?

William Chalmers
Both good questions. First of all, just to take a step back and comment briefly on the capital stock and the capital generation, it is as you say – and of course, I would say this, but I think it's true – we have seen strong capital generation so far this year: 87 basis points year to date, 47 in Q2. That is on top of or, rather, has resulted in a strong capital stock position 14.1 per cent, as you say.

Our build in H2 will continue, it's my expectation that we'll deliver on our guidance for circa 175 over the course of the year. So, you should expect to see that H2 capital build continue in line with that guidance.

And I just want to step back for a moment on this. And you'll have to forgive me for a kind of momentary straying into vindicating the story if you like, but I do think that is consistently strong capital generation, number one, because of financial performance that we describe as robust, but in the context of a business model that has reliably done that and should reliably do that, going forward, because of its focus, because of its retail and commercial orientation, and so forth.

So, strong capital generation from a focused business model, I mean, that to me is what Lloyds should be about and I very much hope that our strategy continues to set us in that place.

Capital targets and how we get there, Aman, to your question. The capital target that we're focused on now is 13 per cent by 2026. Along the way, we're going to get to 13.5 per cent by 2024. How are we going to get there? I think three things that I would stress. One is we're going to continue to capitalise and invest in the business, very much consistent with the guidance that we've given you. But that, clearly, is a deployment of capital within the business to ensure that we deliver on our transformation, that the business is as strong tomorrow as it is today.

The second point is a progressive and sustainable dividend. You'll have seen our dividend was up by 15 per cent as of the half. As I think everybody in this room knows, the first half tends to be more or less a foreteller of what the overall story is for the dividend growth. And therefore, one should expect something like that over the course of the year as a whole. And indeed, going beyond that, I would expect progressive and stable dividend growth to continue to be a hallmark of our story. There's plenty more room for dividend growth in my expectation, in my view, over the course of the coming years.

And then, the third point is further capital repatriation above and beyond that and so far at least, we've used buybacks. And we've used buybacks because we think it offers a great value proposition, and the owners prefer it that way, I suspect informed by the same thing. That is to say, our owners are telling us that buybacks are their favourite form of capital repatriation, we think, because they see the same value in the stock as we do.

We are committed to attaining the types of capital targets that I mentioned. Obviously, year-end capital decisions will always be a function of the board. So, I should say – rather, I should make that caveat.

And then, to come to the final part of your question there, Aman, what does the motor finance review do to that? How does that feed into that calculus, if you like? Hopefully, as you could tell from my previous answer, the motor finance review and the provision that we've taken associated with it has not changed. It has not changed as a function of the delay.

Our position, in our view, continues to be totally appropriate based on everything that we know today. Now, if things change in an unexpected way, bear in mind the capital stock of the bank is great. The capital generation of the bank is great. We'll deal with it if it comes to that eventuality. But as we stand today, we see no reason to change.

Aman Rakkar
Excellent. Let's do the final two ARS questions, please. Question 5: "What do you expect from Lloyds on capital and dividends versus market expectations:" – I'll expect everyone to be completely familiar with consensus estimates for dividends, and buybacks here – "(1) beat on better earnings and volume growth; (2) beat on lower capital requirements; (3) miss on weaker earnings and volumes; (4) miss on higher regulatory requirements; (5) miss on inorganics?"

William Chalmers
Well, I'm glad to see that. We just need that to be reflected in our multiples on the valuation front, and we'll be just fine.

The only one I'll comment on – I mean, that all seems fair enough to me. The only one I'll comment on, just because I think it's interesting, particularly given my background, is point 5, miss on inorganic acquisitions. I think that's very unlikely. Our approach to inorganic, or M&A, if you like, is we will look at M&A if it is consistent with our strategy. We will only execute upon it if it is value accretive from a shareholder point of view, if it is acceptable from a risk point of view, and if it gets us there quicker than our organic strategy ever would. And so, very few opportunities pass that test. And when they do, they typically tend to be quite modest in size. They'll either add to our capabilities or they may add to our scale, but pretty limited. We've done two or three in the time that I've been here. One has been a scale, an add-on, if you like, within mortgages. One has been a capability build within investments. And the other has been a capability build in salary sacrifice, motor finance. All of which have been great, but they've also been very small and pretty modest.

Aman Rakkar
Final Question 6 – okay, we've asked you about bank taxes a few times, but we'll give it another go: "How concerned are you by the risk of UK bank taxes: (1) not concerned, don't think it'll happen; (2) low concern, either low likelihood or a manageable impact; (3) moderately concerned; (4) very concerned?"

William Chalmers
How do you see that, Aman? I mean, to me, that reflects pretty much the sentiment not just in the room, but more broadly.

Aman Rakkar
A balanced response. I think we're out of time, so, I think we'll call the session to an end there. William, I wanted to thank you for your time for what was an excellent session. And thank you, everyone, for joining us.

William Chalmers
Thank you very much indeed.

END

FORWARD LOOKING STATEMENTS

This document contains certain forward-looking statements within the meaning of Section 21E of the US Securities Exchange Act of 1934, as amended, and section 27A of the US Securities Act of 1933, as amended, with respect to the business, strategy, plans and/or results of Lloyds Banking Group plc together with its subsidiaries (the Group) and its current goals and expectations. Statements that are not historical or current facts, including statements about the Group's or its directors' and/or management's beliefs and expectations, are forward-looking statements. Words such as, without limitation, 'believes', 'achieves', 'anticipates', 'estimates', 'expects', 'targets', 'should', 'intends', 'aims', 'projects', 'plans', 'potential', 'will', 'would', 'could', 'considered', 'likely', 'may', 'seek', 'estimate', 'probability', 'goal', 'objective', 'deliver', 'endeavour', 'prospects', 'optimistic' and similar expressions or variations on these expressions are intended to identify forward-looking statements. 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Factors that could cause actual business, strategy, targets, plans and/or results (including but not limited to the payment of dividends) to differ materially from forward-looking statements include, but are not limited to: general economic and business conditions in the UK and internationally; acts of hostility or terrorism and responses to those acts, or other such events; geopolitical unpredictability; the war between Russia and Ukraine; the conflicts in the Middle East; the tensions between China and Taiwan; political instability including as a result of any UK general election; market related risks, trends and developments; changes in client and consumer behaviour and demand; exposure to counterparty risk; the ability to access sufficient sources of capital, liquidity and funding when required; changes to the Group's credit ratings; fluctuations in interest rates, inflation, exchange rates, stock markets and currencies; volatility in credit markets; volatility in the price of the Group's securities; tightening of monetary policy in jurisdictions in which the Group operates; natural pandemic and other disasters; risks concerning borrower and counterparty credit quality; risks affecting insurance business and defined benefit pension schemes; changes in laws, regulations, practices and accounting standards or taxation; changes to regulatory capital or liquidity requirements and similar contingencies; the policies and actions of governmental or regulatory authorities or courts together with any resulting impact on the future structure of the Group; risks associated with the Group's compliance with a wide range of laws and regulations; assessment related to resolution planning requirements; risks related to regulatory actions which may be taken in the event of a bank or Group failure; exposure to legal, regulatory or competition proceedings, investigations or complaints; failure to comply with anti-money laundering, counter terrorist financing, anti-bribery and sanctions regulations; failure to prevent or detect any illegal or improper activities; operational risks including risks as a result of the failure of third party suppliers; conduct risk; technological changes and risks to the security of IT and operational infrastructure, systems, data and information resulting from increased threat of cyber and other attacks; technological failure; inadequate or failed internal or external processes or systems; risks relating to ESG matters, such as climate change (and achieving climate change ambitions) and decarbonisation, including the Group's ability along with the government and other stakeholders to measure, manage and mitigate the impacts of climate change effectively, and human rights issues; the impact of competitive conditions; failure to attract, retain and develop high calibre talent; the ability to achieve strategic objectives; the ability to derive cost savings and other benefits including, but without limitation, as a result of any acquisitions, disposals and other strategic transactions; inability to capture accurately the expected value from acquisitions; assumptions and estimates that form the basis of the Group's financial statements; and potential changes in dividend policy. A number of these influences and factors are beyond the Group's control. Please refer to the latest Annual Report on Form 20-F filed by Lloyds Banking Group plc with the US Securities and Exchange Commission (the SEC), which is available on the SEC's website at www.sec.gov, for a discussion of certain factors and risks. Lloyds Banking Group plc may also make or disclose written and/or oral forward-looking statements in other written materials and in oral statements made by the directors, officers or employees of Lloyds Banking Group plc to third parties, including financial analysts. Except as required by any applicable law or regulation, the forward-looking statements contained in this document are made as of today's date, and the Group expressly disclaims any obligation or undertaking to release publicly any updates or revisions to any forward-looking statements contained in this document whether as a result of new information, future events or otherwise. 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