LLOYDS TSB GROUP PLC
Form 20-F
June 23, 2003

As filed with the Securities and Exchange Commission on 23 June 2003

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 20-F

REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR 12(g)
OF THE SECURITIES EXCHANGE ACT OF 1934
OR
X ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended 31 December 2002
OR
TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

Commission file number 001-15246
LLOYDS TSB GROUP plc
(Exact name of Registrant as Specified in Its Charter)

Scotland

(Jurisdiction of Incorporation or Organization)

25 Gresham Street
London EC2V 7HN
United Kingdom
(Address of Principal Executive Offices)

Securities registered or to be registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Ordinary shares of nominal value 25 pence each, represented by American Depositary Shares.	The New York Stock Exchange.

Securities registered or to be registered pursuant to Section 12(g) of the Act:

None

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act:

None

The number of outstanding shares of each of Lloyds TSB Group plc's classes of capital or common stock as of 31 December 2002 was:

Ordinary shares, nominal value 25 pence each, as of 31 December 2002 5,583,099,804
Limited voting shares, nominal value 25 pence each, as of 31 December 2002... 78,947,368
Preference shares, nominal value 25 pence each, as of 31 December 2002... 0
Preference shares, nominal value 25 cents each, as of 31 December 2002..... 0
Preference shares, nominal value 25 euro cents each, as of 31 December 2002... 0
Preference shares, nominal value Japanese Y25 each, as of 31 December 2002... 0

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.

Yes X No

Indicate by check mark which financial statement item the registrant has elected to follow:

Item 17 Item 18 X

TABLE OF CONTENTS

PRESENTATION OF INFORMATION

In this annual report, references to "Lloyds TSB Group" are to Lloyds TSB Group plc and its subsidiary and associated undertakings; references to "Lloyds TSB Bank" are to Lloyds TSB Bank plc; and references to the "Consolidated Financial Statements" are to Lloyds TSB Group's Consolidated Financial Statements included in this annual report. References to the "Financial Services Authority" are to the United Kingdom (the "UK") Financial Services Authority.

Lloyds TSB Group publishes its Consolidated Financial Statements expressed in British pounds ("pounds sterling", "sterling" or "GBP"), the lawful currency of the UK. In this annual report, references to "pence" and "p" are to one-hundredth of one pound sterling; references to "US dollars", "US$" or "$" are to the lawful currency of the United States (the "US"); references to "cent" are to one-hundredth of one US dollar; and references to "euro" or "Euro" are to the lawful currency of the member states of the European Union that have adopted a single currency in accordance with the Treaty establishing the European Communities, as amended by the Treaty of European Union. Solely for the convenience of the reader, this annual report contains translations of certain pounds sterling amounts into US dollars at specified rates. These translations should not be construed as representations by Lloyds TSB Group that the pounds sterling amounts actually represent such US dollar amounts or could be converted into US dollars at the rate indicated or any other rate. Unless otherwise stated, the translations of pounds sterling into US dollars have been made at the noon buying rate in New York City for cable transfers in pounds sterling as certified for customs purposes by the Federal Reserve Bank of New York (the "Noon Buying Rate") in effect on 31 December 2002, which was $1.6095 = GBP1.00. The Noon Buying Rate on 31 December 2002 differs from certain of the actual rates used in the preparation of the Consolidated Financial Statements, which are expressed in pounds sterling, and therefore US dollar amounts appearing in this annual report may differ significantly from actual US dollar amounts which were translated into pounds sterling in the preparation of the Consolidated Financial Statements in accordance with accounting principles generally accepted in the UK.

BUSINESS OVERVIEW

Lloyds TSB Group is a leading UK-based financial services group, whose businesses provide a comprehensive range of banking and financial services in the UK and overseas. At 31 December 2002 total Lloyds TSB Group assets were GBP252,758 million and Lloyds TSB Group had over 79,000 employees. Lloyds TSB Group plc's market capitalisation at that date was some GBP24,800 million. The profit on ordinary activities before tax for the 12 months to 31 December 2002 was GBP2,607 million and the risk asset ratios as at that date were 9.6 per cent for total capital and 7.8 per cent for tier 1 capital.

The operations of Lloyds TSB Group in the UK were conducted through approximately 2,200 branches of Lloyds TSB Bank, Lloyds TSB Scotland plc and Cheltenham & Gloucester plc at the end of December 2002. International business is conducted mainly in the Americas, New Zealand and continental Europe. Lloyds TSB Group's services in these countries are offered through a combination of branches of Lloyds TSB Bank and subsidiary companies, principally The National Bank of New Zealand Limited, New Zealand's second largest bank measured by assets during 2002, and Losango, the Lloyds TSB Group's consumer finance business in Brazil. Lloyds TSB Group also offers offshore banking facilities in a number of countries. For additional information see "Regulation".

The following table shows the profit before tax of Lloyds TSB Group's UK Operations and its International Operations in each of the last three years.

	2002 GBPm	2001 GBPm	2000 GBPm
UK Operations	2,111	2,595	3,352
International Operations	496	566	433

Profit before tax	2,607	3,161	3,785

Lloyds TSB Group's activities are organised into three segments: UK Retail Banking and Mortgages, Insurance and Investments and Wholesale Markets and International Banking. Services provided by UK Retail Banking and Mortgages encompass the provision of banking and other financial services to personal and small business customers, private banking, stockbroking and mortgages. Insurance and Investments offers life assurance, pensions and investment products, general insurance and fund management services. Wholesale Markets and International Banking provides banking and related services for major UK and multinational companies, banks and financial institutions, and medium-sized UK businesses, including venture capital finance. It also provides asset finance and share registration services to personal and corporate customers, manages Lloyds TSB Group's activities in financial markets through its Treasury function and provides banking and financial services overseas.

The following table shows the results of Lloyds TSB Group's UK Retail Banking and Mortgages, Insurance and Investments and Wholesale Markets and International Banking segments and Central group items in each of the last three fiscal years. In order to provide a clearer representation of the underlying performance, the results of the Insurance and Investments segment include investment earnings calculated using longer-term rates of return and annual management charges based on unsmoothed fund values. Management separately analyse the difference between these normalised earnings and the actual return ('the investment variance') together with the impact of changes in the economic assumptions used in the embedded value calculation.

	2002 GBPm	2001 GBPm	2000 GBPm
UK Retail Banking and Mortgages	1,172	1,205	1,363
Insurance and Investments	1,231	1,421	1,158
Wholesale Markets and International Banking	1,005	1,209	1,035
Central group items	96	185	378
	3,504	4,020	3,934
Changes in economic assumptions	55	-	127
Investment variance	(952)	(859)	(276)
Profit before tax	2,607	3,161	3,785

Lloyds TSB Group plc was incorporated as a public limited company and registered in Scotland under the UK Companies Act 1985 on 21 October 1985 with the registered number 95000. Lloyds TSB Group plc's registered office is Henry Duncan House, 120 George Street, Edinburgh EH2 4LH, Scotland, and its principal executive offices in the UK are located at 25 Gresham Street, London, EC2V 7HN, United Kingdom, telephone number + 44 (0) 20 7626 1500.

SELECTED CONSOLIDATED FINANCIAL DATA

The selected consolidated financial information set out in the table below has been derived from the annual reports and accounts of Lloyds TSB Group plc for each of the past five years adjusted for subsequent changes in accounting policy and presentation. The Consolidated Financial Statements for each of the years 1998 to 2001 have been audited by PricewaterhouseCoopers, independent accountants; the Consolidated Financial Statements for 2002 were audited by their successor firm PricewaterhouseCoopers LLP, independent accountants.

The Consolidated Financial Statements have been prepared in accordance with UK GAAP, which differs in certain significant respects from US GAAP. A discussion of such differences and a reconciliation of certain UK GAAP amounts to US GAAP is included in Note 48 to the Consolidated Financial Statements.

	2002	2001	2000	1999	1998
Profit and loss account data for the year ended 31 December (GBPm) (1)					
Net interest income	5,171	4,922	4,587	4,783	4,398
Other finance income	165	307	424	268	252
Other income	3,542	3,660	3,765	3,267	2,792
Trading surplus	3,963	4,113	4,497	4,434	3,566
Provisions for bad and doubtful debts	(1,029)	(747)	(541)	(615)	(555)
Profit on ordinary activities before tax	2,607	3,161	3,785	3,529	2,948
Profit on ordinary activities after tax	1,843	2,286	2,703	2,445	2,086
Profit for the year attributable to shareholders	1,781	2,229	2,654	2,439	2,073
Dividends	1,908	1,872	1,683	1,451	1,204
Balance sheet data at 31 December (GBPm) (1)					
Called-up share capital	1,416	1,411	1,396	1,389	1,379
Shareholders' funds (equity)	7,972	10,356	11,901	11,760	9,333
Customer accounts	116,334	109,116	101,989	93,714	90,445
Undated subordinated loan capital	5,496	4,102	3,391	3,294	1,518
Dated	4,672	4,006	4,119	3,199	2,503

subordinated loan capital					
Loans and advances to customers	134,474	122,935	114,432	102,233	95,243
Assets(2)	207,418	189,404	169,587	153,172	146,475
Total assets	252,758	235,793	220,672	179,714	170,167
Share information (1)					
Basic earnings per ordinary share	32.0p	40.3p	48.4p	44.8p	38.4p
Diluted earnings per ordinary share	31.8p	39.9p	47.9p	44.0p	37.6p
Net asset value per ordinary share	141p	184p	213p	212p	170p
Dividends per ordinary share(3)	34.2p	33.7p	30.6p	26.6p	22.2p
Equivalent cents per share(3) (4)	54.1c	49.3c	44.2c	42.3c	36.7c
Market price (year-end)	446p	746p	708p	774p	855p
Number of shareholders (thousands)	973	981	1,026	1,024	1,028
Number of ordinary shares in issue (millions)	5,583	5,564	5,507	5,475	5,435
Financial ratios (1) , (5)	%	%	%	%	%
Dividend payout ratio	107.1	84.0	63.4	59.5	58.1
Post-tax return on average shareholders' equity	16.7	18.1	21.1	23.9	23.5
Post-tax return on average assets	0.93	1.28	1.68	1.63	1.48
Post-tax return on average risk-weighted assets	1.61	2.26	3.07	2.94	2.62
Average shareholders' equity to average assets	5.4	6.9	7.8	6.8	6.3
Efficiency ratio(6)	55.4	53.7	48.8	46.7	52.1
Capital ratios (1)					
Total capital	9.6	8.8	8.7	14.9	11.2
Tier 1 capital	7.8	7.8	8.0	9.9	8.6

(1) Figures for 2001 and earlier years have been restated to reflect the implementation of FRS 12, "Provisions, Contingent Liabilities and Contingent Assets", FRS 15, "Tangible Fixed Assets", FRS 18, "Accounting Policies", FRS 17, "Retirement Benefits", FRS 19 "Deferred Tax", UITF 33 "Obligations in Capital Instruments", detailed guidance from the Association of British Insurers for best practice in the preparation of results using the achieved profits method of accounting and other minor adjustments.
(2) Assets exclude long-term assurance assets attributable to policyholders.
(3) Annual dividends are comprised of both interim and final dividend payments. Final dividends (which are always paid in the following year) are included in the year to which they relate rather than in the year in which they are paid.
(4) Translated into US dollars at the Noon Buying Rate on the date each payment is made.
(5) Averages are calculated on a monthly basis from the consolidated financial data of Lloyds TSB Group.
(6) The efficiency ratio is calculated as total operating expenses as a percentage of total income.

4

SELECTED US GAAP FINANCIAL	2002	2001*	2000*	1999*
DATA				
Income statement data for the year ended 31 December (GBPm)				
Total revenues, net of interest expense	10,498	9,335	10,380	9,493
Policyholder benefits and claims expense	(1,565)	(2,228)	(1,735)	(936)
Provision for bad and doubtful debts	(1,029)	(747)	(541)	(615)
Income before tax	2,376	2,215	2,755	3,352
Net income	1,751	1,632	1,986	1,993
Dividends	1,903	1,738	1,522	1,285
Balance sheet data at 31 December (GBPm)				
Shareholders' equity	10,190	13,533	13,712	13,109
Deposits	141,777	133,419	117,473	110,545
Loans, net of provisions	134,202	122,485	110,788	99,120
Total assets	254,389	243,226	225,776	180,825
Share information (pence per ordinary share)				
Basic earnings	31.4	29.5	36.2	36.6
Diluted earnings	31.3	29.2	35.8	35.9
Net asset value	180	240	246	236
Dividends	34.2	31.5	27.8	23.6
Financial ratios(1)	%	%	%	%
Dividend payout ratio	108.7	106.5	76.6	64.5

Post-tax return on average shareholders' equity	14.8	12.0	14.8	15.6
Post-tax return on average assets	0.73	0.72	1.00	1.13
Average shareholders' equity to average assets	4.8	5.8	6.6	7.2

* restated (see page F-67)

(1) Lloyds TSB Group does not have sufficient information to calculate US GAAP average balances on a monthly basis. Where applicable, these financial ratios have been based upon simple averages of the opening and closing balances.

5

EXCHANGE RATES

In this annual report, unless otherwise indicated, all amounts are expressed in pounds sterling. For the months shown the US dollar high and low Noon Buying Rates per pound sterling were:

	2003					2002
	May	April	March	February	January	December
	(US dollars per pound sterling)					
High	1.65	1.60	1.61	1.65	1.65	1.61
Low	1.59	1.55	1.56	1.57	1.60	1.56

For the years shown the averages of the US dollar Noon Buying Rates per pound sterling on the last day of each month were:

	2002	2001	2000	1999	1998
	(US dollars per pound sterling)				
Average	1.51	1.44	1.52	1.61	1.66

On 18 June 2003, the latest practicable date, the US dollar Noon Buying Rate was $1.6798 = GBP1.00. Lloyds TSB Group makes no representation that amounts in pounds sterling have been, could have been or could be converted into US dollars at that rate or at any of the above rates.

6

BUSINESS

History and development of Lloyds TSB Group

The history of Lloyds TSB Bank can be traced back to the 18th century when the banking partnership of Taylor and Lloyds was established in the UK. The early years of the 20th century were marked by many acquisitions and mergers, significantly expanding the number of banking offices in the UK. For much of the last 30 years Lloyds TSB Bank has also had an international exposure principally in New Zealand and Latin America. Lloyds TSB Bank expanded further in the late 1980's by the creation of the insurance-led group of Lloyds Abbey Life following the merger of five Lloyds TSB Bank businesses and Abbey Life Group plc, and in 1995 the business of Cheltenham and Gloucester Building Society was acquired.

TSB Group plc became operational in 1986 when, following UK government legislation, the operations of four Trustee Savings Banks and other related companies were transferred to TSB Group plc and its new banking subsidiaries. By 1995, the TSB Group had, either through organic growth or acquisition, developed life and general insurance operations, investment management activities, a motor vehicle hire purchase and leasing operation, and an estate agency business to supplement its retail banking activities.

In 1995, TSB Group plc merged with Lloyds TSB Bank. Under the terms of the merger, the TSB and Lloyds TSB Bank groups were combined under TSB Group plc, which was re-named Lloyds TSB Group plc. In 1999, the businesses, assets and liabilities of TSB Bank, the principal banking subsidiary of the TSB Group prior to the merger, and its subsidiary Hill Samuel Bank were vested in Lloyds TSB Bank. In 2000, Lloyds TSB Group acquired Scottish Widows, for a total consideration of GBP5,947 million. This transaction positioned Lloyds TSB Group as one of the leading suppliers of long-term savings and protection products in the UK. The Lloyds TSB Group has remained in substantially this form since that time. For additional information on the Lloyds TSB Group see "Business Overview".

Management and resources

Lloyds TSB Group recognises that it will create value for its shareholders if it creates value for its customers. Its constant aim is to meet the rapidly changing needs and expectations of its customers. Lloyds TSB Group believes that success depends upon service, consistency and commitment. Nothing is more important to Lloyds TSB Group's business than maintaining the trust and confidence of its customers and Lloyds TSB Group aims, wherever possible, to maintain long-term relationships with its customers. Lloyds TSB Group has an established code of business conduct which is published and available, on request, to the public. The policy defines the standards and values which are used to operate the business and covers Lloyds TSB Group's relationship with customers, suppliers, employees, the community, shareholders and competitors. The code is incorporated within procedures for each area of the business and has been communicated to all employees.

Lloyds TSB Group operates in a marketplace which is continually changing. No organisation can successfully manage change without the support and commitment of its staff. The pace and scope of change will not diminish as competition in the financial services market continues to increase. Lloyds TSB Group recognises that it is the staff of the organisation who have delivered, and will continue to deliver, its success and considers that one of its greatest competitive advantages is the ability of its people to adapt to rapid and far reaching change. The knowledge and skills of Lloyds TSB Group's employees are a key element in its success and therefore it invests significantly in training, ensuring that it is accessible by everyone in the organisation.

Lloyds TSB Group recognises that long-term success depends on the quality of its management. It is therefore committed to developing the potential of all managers; in particular ensuring that it has the succession management capability to meet future needs for top management. On 20 December 2002 Lloyds TSB Group announced that Eric Daniels, group executive director, UK Retail Banking, would succeed Peter Ellwood who retired as group chief executive on 31 May 2003, and that Peter Ayliffe, managing director, Personal Banking, would succeed Eric Daniels as group executive director, UK Retail Banking and join the Board. On 6 February 2003 it was announced that Steve Targett, formerly chief executive officer, Europe, for National Australia Group would succeed David Pritchard as group executive director, Wholesale and International Banking upon Mr Pritchard's retirement as an executive director on 16 April 2003. David Pritchard became deputy chairman replacing Alan Moore who retired from the Lloyds TSB Group on the same day. Also on 16 April 2003, the following non-executive directors left the Board: Kent Atkinson, Clive Butler and Sheila Forbes; and on 1 May 2003, Wolfgang Berndt and Angela Knight joined the Board as non-executive directors.

Strategy of Lloyds TSB Group

The governing objective of Lloyds TSB Group is to maximise shareholder value over time. Lloyds TSB Group believes that this objective can only be achieved by having clear strategic aims, plans capable of translating strategy into shareholder value, and the determination and ability to implement and deliver those plans. Lloyds TSB Group plans to maximise shareholder value over time by a combination of organic growth and acquisitions, balancing short-term profit growth and investment in the future of the business to create sustainable long-term value for all its stakeholders.

7

Lloyds TSB Group's three strategic aims are to be a leader in its chosen markets, to be the first choice for its customers and to reduce day-to-day operating costs to allow greater scope for investment in better products, enhanced service and multi-channel distribution.

* To be a leader in its chosen market Lloyds TSB Group aims to be a leader in its chosen markets as market leaders earn higher returns and create greater value. Lloyds TSB Group has pursued this aim by seeking opportunities to consolidate its position in businesses where it is already strong by a combination of organic growth and acquisitions and by divesting businesses in markets where it is not a leader and cannot aspire reasonably to leadership. The acquisition of Scottish Widows in March 2000 has greatly enhanced Lloyds TSB Group's market position in the life assurance market. Based on figures provided by the Association of British Insurers, Lloyds TSB Group's share of the UK life and pensions market in 1999 was 1.5 per cent, excluding Abbey Life. By September 2002, following the acquisition of Scottish Widows, this rose to 5.3 per cent. Within Asset Finance, Lloyds TSB Group has acquired Chartered Trust, First National Vehicle Holdings, Abbey National Vehicle Finance and the Dutton-Forshaw Group to enhance the Group's leading position in UK motor finance. In 1998, the acquisition of Countrywide Banking Corporation further strengthened Lloyds TSB Group's position in New Zealand; although, following approaches in 2003, Lloyds TSB Group is undertaking a strategic review so that potential offers for The National Bank of New Zealand, as well as retention of the business, can be considered. Lloyds TSB Group has also divested businesses such as Mortgage Express, International Factors, Black Horse Agencies, Schroder Munchmeyer Hengst & Co and Lloyds TSB Asset Management S.A. which were either duplicated or were in markets in which Lloyds TSB Group did not wish to

become a leader.

* To be first choice for its customer Lloyds TSB Group aims to be first choice for its customers by understanding and meeting their needs more effectively than any of its competitors. Central to this objective is Lloyds TSB Group's Customer Relationship Management programme, which brings together all the customer information that Lloyds TSB Group holds so that it can build on its relationship with individual customers by providing them with products, services and access suited to their individual requirements. Lloyds TSB Group has continued to broaden its product range which, supported by the knowledge and expertise of its staff, ensures that the Lloyds TSB Group provides comprehensive financial solutions to meet the needs of all its customers. Lloyds TSB Group's multi-channel banking infrastructure, including internet and telephony services, means that it can provide its customers with significant options in terms of convenience and choice.

* To reduce day-to-day operating costs Reducing day-to-day operating costs allows Lloyds TSB Group greater scope for investment in products, enhanced service and multi-channel distribution. In February 2000 Lloyds TSB Group announced the commencement of a substantial medium-term efficiency programme to improve the Lloyds TSB Group's overall efficiency to support increasing levels of investment in the Lloyds TSB Group's businesses. The efficiency programme has been a major contributing factor to the net reduction in staff numbers during 2002 of 4,191, after adjusting for an additional 2,328 staff following a number of acquisitions, against a targeted reduction of 3,000. The major projects comprising the efficiency programme are now coming to an end, although the Lloyds TSB Group remains committed to strict cost control and, largely as a result of continuing efficiency initiatives, operating expenses in 2003, excluding the impact of acquisitions and operating lease depreciation, are expected to grow by no more than the rate of inflation.

Lloyds TSB Group continues to develop new strategies which will leverage the strength of its brands and its multi-channel distribution capability, its enhanced understanding of what its customers want and its cost advantage to deliver greater value to customers.

Lloyds TSB Group remains alert for opportunities to grow through acquisitions that complement its good organic strategies and help provide new opportunities for profitable growth, both in the UK and overseas. Whilst Lloyds TSB Group remains well placed to participate in cross-border consolidation with potential to create value by exploiting its retailing and cost management skills and its ability to manage change effectively, the prevailing stock market conditions appear to have slowed down the consolidation process, both in the UK and Europe. Lloyds TSB Group's proposed acquisition of Abbey National in 2001, which was blocked by the UK Competition Commission, signalled an end to large-scale consolidation within the UK by domestic participants.

Businesses and activities of Lloyds TSB Group

The main businesses and activities of Lloyds TSB Group's three segments are described below.

UK Retail Banking and Mortgages

UK Retail Banking and Mortgages provided banking and financial services to some 15 million customers during 2002. With approximately 2,200 branches of Lloyds TSB Bank, Lloyds TSB Scotland and Cheltenham & Gloucester at the end of 2002, Lloyds TSB Group provides comprehensive geographic branch coverage in England, Scotland and Wales. The profit before tax of UK Retail Banking and

Mortgages in 2002 was GBP1,172 million.

UK Retail Banking

Current accounts, savings and investment accounts, and consumer lending. The retail branches of Lloyds TSB Bank offer a broad range of branded products and Cheltenham & Gloucester provides retail investments through its branch network and a postal investment centre.

Business banking. Small businesses were served by over 1,750 dedicated business managers based in some 450 locations throughout the UK at the end of 2002. Customers have access to a wide range of tailored business services ranging from traditional banking products through factoring, insurance and investments to non-financial solutions to their business problems such as Debtor Management service, providing legal support to help customers recover debts, and Prospect Finder, providing customers with a tailored list of potential customers for their business. Lloyds TSB Group is one of the leading banks for new business start-ups with around one in five opening accounts with Lloyds TSB Group.

Card services. Lloyds TSB Group provides a range of card-based products and services, including credit and debit cards and card transaction processing services for retailers. Lloyds TSB Group is a member of both the VISA and MasterCard payment systems and is the third largest credit card issuer in the UK with a 10 per cent share of outstanding card balances at 31 December 2002.

Cash machines. Lloyds TSB Group has one of the largest cash machine networks of any leading banking group in the UK and, at 31 December 2002, personal customers of Lloyds TSB Bank were able to withdraw cash, check balances and obtain mini statements through some 4,200 cashpoint machines at branches and external locations around the country. In addition, they had access to a further some 37,000 cash machines via LINK in the UK and to cash machines worldwide through the VISA and MasterCard networks.

Telephone banking. Telephone Banking continues to grow and Lloyds TSB Group provides one of the largest telephony services in Europe, in terms of customer numbers. At the end of 2002, some 3.2 million customers had registered to use the services of PhoneBank and the automated voice response service PhoneBank Express. Lloyds TSB Group's telephone banking contact centres handled some 46 million calls during 2002.

Internet banking. Internet Banking provides online banking facilities for personal and business customers and enables them to conduct their financial affairs without the need to use the branch network. Some 2 million customers have registered to use Lloyds TSB Group's internet banking services.

UK Wealth Management. Private Banking provides a range of tailor-made wealth management services and products to individuals from 40 offices throughout the UK. In addition to asset management, these include tax and estate planning, executor and trustee services, deposit taking and lending, insurance and personal equity plan and individual savings account (ISA) products. At 31 December 2002, client funds under management totalled some GBP10,000 million. Lloyds TSB Stockbrokers undertakes retail stockbroking through its Sharedeal Direct telephone service.

Mortgages

Cheltenham & Gloucester is Lloyds TSB Group's specialist residential mortgage provider, providing a range of mortgage products to personal customers through its own branches and those of Lloyds TSB Bank in England and Wales, as well as through the telephone, internet and postal service, C&G TeleDirect. Lloyds TSB Group also provides mortgages through Lloyds TSB Scotland and Scottish Widows Bank. Lloyds TSB Group is the third largest residential mortgage lender in the UK on the basis of outstanding balances, with mortgages outstanding at 31 December 2002 of GBP62,467 million, representing an estimated market share of 9.3 per cent.

Insurance and Investments

The operating profit, calculated as explained under "Operating and Financial Review and Prospects - Line of business information - Summary", of Insurance and Investments in 2002 was GBP1,231 million.

Life assurance, pensions and investments. Scottish Widows is Lloyds TSB Group's specialist provider of life assurance, pensions and investment products, which are distributed through Lloyds TSB Bank's branch network, through independent financial advisors and directly via the telephone and the internet. Before its acquisition in 2000, Scottish Widows distributed life assurance, pensions and long-term savings products mainly through independent financial advisors. Following the acquisition, the Scottish Widows brand became the sole brand for Lloyds TSB Group's life, pensions, unit trust and other long-term savings products, and Lloyds TSB Group extended the brand's product range to Lloyds TSB Group's retail banking branch network.

In common with other life assurance companies in the UK, the life and pensions business of each of the life assurance companies in the Lloyds TSB Group is written in a long-term business fund. The long-term business fund is divided into a With-Profits and a Non-Participating sub-fund.

9

With-profits life and pensions products are written from the With-Profits Fund. The benefits accruing from these policies are designed to provide a smoothed return to policyholders who hold their policies to maturity through a mix of annual and final (or terminal) bonuses added to guaranteed basic benefits. The guarantees generally only apply on death or maturity. The actual bonuses declared will reflect the experience of the With-Profits Fund.

Other life and pensions products are generally written from the Non-Participating sub-fund. Examples include unit-linked policies, annuities, term assurances and health insurance (under which a pre-determined amount of benefit is payable in the event of an insured event such as death). The benefits provided by such linked policies are wholly or partly determined by reference to a specific portfolio of assets known as unit-linked funds.

General Insurance. Lloyds TSB General Insurance provides general insurance through the retail branches of Lloyds TSB Bank and Cheltenham & Gloucester, and through a direct telephone operation and the internet. Based on a survey conducted for Lloyds TSB Group, Lloyds TSB General Insurance had a new business market share of 12 per cent of the new household insurance market in 2002 (compared to 14 per cent in 2001). The new household insurance market is defined as those customers switching suppliers, taking out first ever policies and customers re-entering the household insurance market.

Scottish Widows Investment Partnership. Scottish Widows Investment Partnership manages funds for Lloyds TSB Group's retail life, pensions and investment products. Clients also include corporate pension schemes, local authorities and other institutions in the UK and overseas. At 31 December 2002 funds under management amounted to some GBP70,000 million, compared to some

GBP78,000 million a year earlier. The decline mainly reflects the lower stock market levels experienced in 2002.

Wholesale Markets and International Banking

Wholesale Markets

The profit before tax of Wholesale Markets in 2002 was GBP626 million. Lloyds TSB Group's relationships with major UK and multinational companies, banks and institutions, and medium-sized UK businesses, together with its activities in financial markets, are managed through dedicated offices in the UK and a number of locations overseas, including New York.

Treasury. Lloyds TSB Group is a leading participant in the Sterling money market. It is also active in currency money markets, foreign exchange markets and also in certain derivatives markets, primarily to meet the needs of customers. It also plays a central role in the funding, cash and liquidity management of Lloyds TSB Group.

Corporate. Lloyds TSB Group provides a relationship banking, financial and advisory service to the corporate market place for customers with turnovers in excess of GBP2 million, along with access to specialists in a number of banking support areas, including financial institutions and trade finance, strategic asset finance including large value lease finance, structured finance, share registration, acquisition finance and capital markets. The Agricultural Mortgage Corporation provides long-term finance for the agricultural sector, and through Lloyds TSB Development Capital, venture capital finance is provided to developing companies.

Asset Finance. Lloyds TSB Group's asset finance businesses provide individuals and companies with finance through leasing, hire purchase and contract hire packages. Hire purchase, or instalment credit, is a form of consumer financing where a customer takes possession of goods on payment of an initial deposit but the legal title to the goods does not pass to them until the agreed number of instalments have been paid and the option to purchase has been exercised. Through its invoice discounting and factoring subsidiary Lloyds TSB Commercial Finance, Lloyds TSB Group provides working capital finance for customers by releasing to the customer up to 90 per cent of the value of their unpaid invoices, with the balance payable, after deduction of a service fee, once the invoices have been settled. Invoice discounting differs to factoring in that the customer retains control of the debt collection and the credit risk. Specialist personal lending, store credit, small/medium ticket leasing and the recently acquired Dutton-Forshaw motor dealership complete this group of businesses.

International Banking

The profit before tax of International Banking in 2002 was GBP379 million.

New Zealand. The National Bank of New Zealand Limited ("NBNZ") was New Zealand's second largest bank measured by assets during 2002 and provides a wide range of banking services through some 160 retail branch outlets. NBNZ serves retail customers' needs for current and savings accounts, credit cards, consumer lending and home loans. NBNZ also has a substantial non-personal business providing working capital, term lending, trade finance and treasury services to the business and agricultural sector.

Europe. Lloyds TSB Group has private banking operations for wealthy individuals outside their country of residence. The business is conducted through branches of Lloyds TSB Bank located in Switzerland, Luxembourg, Monaco and Gibraltar. There are also private and corporate banking operations in Belgium, Netherlands, Spain and France.

Offshore banking. The Lloyds TSB Group's offshore banking operations comprise offices in the Channel Islands and Isle of Man, providing a full range of retail banking, private banking and financial services to overseas residents and islanders, together with deposit services offshore for UK residents.

The Americas. Lloyds TSB Group has operated in the Americas for over 130 years and has offices in Brazil, Argentina, Colombia, Ecuador, Guatemala, Honduras, Panama, Paraguay and Uruguay. In addition Lloyds TSB Group has private banking and investment operations in the US. In Brazil, where Lloyds TSB Bank has a corporate banking operation, Lloyds TSB Group also owns Losango, a consumer lending operation providing three retail products: borrowing at the point of sale in stores, unsecured personal lending and borrowing to fund new and second-hand car purchases. The Losango lending business is mainly conducted through Banco Lloyds TSB S.A., a locally incorporated subsidiary of Lloyds TSB Bank. Lloyds TSB Bank also provides specialist banking and treasury products to corporate clients in Brazil. In Argentina where Lloyds TSB Bank has 36 branches and Colombia, where Lloyds TSB Bank's subsidiary Lloyds TSB Bank S.A. has 17 branches, Lloyds TSB Group provides corporate banking services, including trade finance, working capital loans, import finance, term deposits and money transmission. It also provides retail banking services through a network of branches, including current and savings accounts, credit cards, personal loans and mortgages.

Middle East and Asia. There are banking operations in Hong Kong, Singapore, Tokyo, Malaysia and Dubai.

Recent developments

Lloyds TSB Group issued a trading update on 23 June 2003, which made the following comments:

Lloyds TSB Group expects to deliver a satisfactory trading performance for the half-year to 30 June 2003.

At 31 March 2003 total Lloyds TSB Group loans and advances to customers were GBP138,640 million, an increase of 3 per cent in the first quarter of 2003. This increase largely reflected good quality growth in the Lloyds TSB Group's UK mortgage and credit card portfolios. Total Lloyds TSB Group risk weighted assets at 31 March 2003 were GBP125,659 million. Customer deposits totalled GBP120,535 million, an increase of 3.6 per cent in the first quarter of 2003, as a result of strong growth in current account balances and international deposits. The Lloyds TSB Group net interest margin for the first three months of 2003 was 3.05 per cent compared with a Lloyds TSB Group net interest margin of 3.16 per cent in the fourth quarter of 2002. The implementation of the remedies proposed in March 2002 by the Competition Commission's report, following its investigation into the supply of banking services to small and medium sized enterprises (SMEs), reduced the Lloyds TSB Group net interest margin in the first quarter of 2003 by some 10 basis points.

Despite a general slowdown in the growth of consumer credit in the UK, the Lloyds TSB Group continues to deliver good growth in mortgage and credit card lending and is growing market share in many of its key product areas, supported by the recent launch of a number of highly segmented, competitive and innovative product offers. Net new mortgage lending in the first quarter of 2003 was some GBP2,200 million, an estimated market share of 10.9 per cent, compared with some GBP700 million in the first quarter of 2002.

Overall, weighted sales of life, pensions and unit trust products in the first five months of 2003 were at a similar level to the comparative period in 2002. By distribution channel, in the first five months of 2003, weighted sales of life, pensions and unit trusts via Independent Financial Advisors increased strongly by 37 per cent, against the same period in 2002, building on the strength of the Scottish Widows brand and its resources. By contrast, sales via the branch network remained subdued and fell by 26 per cent against the comparative period last year.

Overall sales of general insurance products continue to perform well despite creditor insurance sales, in the first five months of 2003, being lower than the comparative period in 2002, as a result of the general slowdown in growth in personal loan lending.

Strict control of the Lloyds TSB Group's costs has been maintained and the Lloyds TSB Group expects that its cost growth for 2003, excluding the impact of acquisitions and operating lease depreciation, will be less than the rate of inflation. In the first quarter of 2003 the impact of acquisitions added GBP51 million to the Lloyds TSB Group's cost base and operating lease depreciation was GBP52 million (first quarter 2002: GBP56 million).

Overall asset quality remains satisfactory, with no material increase in the level of arrears or non-performing lending. As a result, the annualised charge for bad and doubtful debts in the first quarter of 2003, as a percentage of average lending, was lower than the 0.77 per cent charge as a percentage of average lending for the full year 2002.

In May 2003 the Lloyds TSB Group agreed the sale of its French fund management and private banking businesses. A net loss of approximately GBP15 million will be included in the profit and loss account of Lloyds TSB Group for the half-year ending 30 June 2003. Following approaches, Lloyds TSB Group is considering its options relating to its subsidiary, The National Bank of New Zealand. The Lloyds TSB Group is undertaking a strategic review so that potential offers for The National Bank of New Zealand, as well as retention of the business, can be considered.

During the first quarter of 2003 improved secondary bond market conditions have allowed the Lloyds TSB Group to reduce its Emerging Markets Debt portfolio. As a result, profits on bond sales, and mark-to-market gains in the first quarter of the year totalled some GBP90 million. This income was however partly offset by lower than expected 'other finance income' as the Lloyds TSB Group pension schemes' returns have been reduced by the effect of lower asset values. In the first quarter of 2003, other finance income totalled GBP8 million (first quarter 2002: GBP42 million). The increase in the FTSE All Share Index in the first five months of 2003 led to a positive investment variance of GBP58 million during that period.

The Lloyds TSB Group continues to carry out, in conjunction with the regulator, its investigation into the appropriateness of certain sales of the Extra Income & Growth Plan, a stock market related investment product sold in 2000 and 2001. This investigation is expected to be completed within the next few months when the Lloyds TSB Group will be in a better position to quantify the financial effect. During the first quarter of 2003 there has also been an increase in the level of complaints relating to Lloyds TSB Group sales and performance of certain endowment based and long-term savings products. Whilst the Lloyds TSB Group maintains provisions for redress to policyholders in respect of past sales, further provisions and charges will arise in 2003 to cover these issues.

Properties

As at 31 December 2002, Lloyds TSB Group occupied 3,617 properties in the UK. Of these, 849 were held as freeholds, 92 as long-term leaseholds and 2,676 as short-term leaseholds. The majority of these properties are retail branches and are widely distributed throughout England, Scotland and Wales. The most significant of these properties are Lloyds TSB Group's new head office in London, together with administrative buildings in Bristol, Gloucester and Edinburgh.

In addition, Lloyds TSB Group owns, leases or uses under licence properties for business operations elsewhere in the world, principally in Argentina, Brazil, New Zealand, Spain and Switzerland.

On 13 March 2002, Lloyds TSB Group disposed of its freehold head office, although it continued to occupy these premises until May 2003 when the move to its new head office building was completed. The new head office, which is held on a long leasehold, is also located within the City of London.

Legal actions

Lloyds TSB Group is periodically subject to threatened or filed legal actions in the ordinary course of business. Lloyds TSB Group does not expect the final outcome of any legal proceedings currently known to it to have a material adverse effect on its consolidated results of operations or financial condition.

Guaranteed annuity options

A guaranteed annuity option policy is a pension policy that provides a cash benefit at retirement age, which can be converted into an annuity at a specified minimum rate. When market rates fall below the specified minimum and policyholder funds are not expected to be sufficient to meet the excess cost of the annuity at retirement a provision is established. In 1998, a provision was made within Abbey Life for liabilities under certain unit-linked products with guaranteed annuity options written between the mid 1960s to the mid 1980s. Unit-linked insurance policies are insurance policies where the policyholder's premiums are used to buy units in a fund run by the insurer. At 31 December 2002 this provision was GBP111 million; Lloyds TSB Group is satisfied that this remains adequate.

The implications of guaranteed annuity option contracts for the distribution of profits in the form of bonuses to with-profits policyholders were clarified by the House of Lords in its judgement in the guaranteed annuities case, Equitable Life vs. Hyman. The House of Lords ruled that a life company could not use its discretion to undermine or negate a contractual guaranteed annuity rate, and that the cost of funding such rates could not be met by guaranteed annuity option policyholders alone. After an extensive review of its existing practices carried out in the light of this judgement, Scottish Widows revised the way it calculates benefits for guaranteed annuity policies with effect from 1 February 2002. As a result of this change, the terminal bonuses for guaranteed annuity option policies were increased.

Under the terms of the transfer of Scottish Widows' business, a separate memorandum account was created within the With Profits Fund called the Additional Account. This Account had a value at 31 December 2002 of approximately GBP1,500 million (2001: GBP1,700 million) and is available to meet any additional costs of providing guaranteed benefits on transferred policies, including guaranteed annuity option policies. The assets allocated to the Additional Account include certain hedge assets, which are intended to protect the With-Profits Fund against the consequences of a future fall in interest rates.

The eventual cost of providing the enhanced benefits is dependent upon a number of factors, including in particular:

* The proportion of policyholders with a guaranteed annuity option policy who choose to exercise their options;

* The effect of future interest rate and mortality trends on the cost of annuities; and

* The future investment performance of the With-Profits Fund.

Having considered a range of possible outcomes, Lloyds TSB Group currently expects that the most likely outcome is that the balance in the Additional Account available for this purpose will be sufficient to meet the cost of the enhanced benefits payable to the guaranteed annuity option policyholders, as well as other contingencies. The cost of enhanced benefits, currently estimated to be approximately GBP1,100 million (2001: GBP1,400 million) on a net present value basis, will be paid out over many years as policies mature. In the event that the amount in the Additional Account proves, over time, to be insufficient, the shortfall will be met by Lloyds TSB Group. At this time, no provision is considered necessary for such risk.

Customer remediation payments

Redress to past purchasers of pension policies

As a measure to reduce the burden on the state benefit system resulting from the increasing size of the retired population the government introduced, as part of the UK Income and Corporation Taxes Act 1988, legislation aimed at encouraging the working population to make their own private pension arrangements. For several years following the introduction of this legislation, insurance companies and intermediaries advised a large number of customers to set up private pension plans, often by transferring out of, or choosing not to join, occupational pension schemes offered by their employers. As a further way of relieving the possible pensions burden on the state, individuals had been given the option, by the government, to forego their entitlement to the earnings related element of state pension benefits - the State Earnings Related Pension Scheme ("SERPS") - in return for having part of their National Insurance contributions diverted into personal pension plans.

During the early 1990s, the UK government and regulatory authorities became increasingly concerned that many of these customers had been given poor advice and that they would, in fact, have been in a better position if they had remained in, or joined, employer sponsored pension schemes. The regulator of the UK pension industry (then the Securities and Investments Board now the Financial Services Authority) carried out an industry-wide investigation into the conduct of business involving the transfer of pensions. The conclusion of this investigation was that a large number of customers had been poorly advised by insurance companies and intermediaries across the industry.

As a result of its investigation, the regulator established an action plan for the UK pensions industry to follow in reviewing all cases of possible misselling as described in the preceding paragraph and determining necessary compensation. For the purposes of this review, all relevant cases were segregated into two classes:

* Phase 1 cases ("priority cases") - these were mainly cases where the customer had retired since taking out the private pension plan, was approaching retirement or had since died.

* Phase 2 cases ("non-priority cases") - these cases primarily relate to

younger customers who were not yet approaching their expected retirement dates.

In February 2000, the regulator widened the scope of the review to encompass Free Standing Additional Voluntary Contributions ('FSAVC') business, which constitutes sales of personal pensions to members of company pension schemes. Individuals who purchased these pensions instead of investing their money and any matching contributions from their employer in the Additional Voluntary Contributions ('AVC') scheme connected to their company's pension scheme may have been financially disadvantaged, due to not being properly informed of the benefits foregone from not investing in their AVC scheme.

In common with a number of other banks and insurance companies, in January 1997 Lloyds TSB Bank was fined GBP325,000 by the Investment Management Regulatory Organisation Limited for regulatory breaches and failings in connection with the sale of personal pensions between April 1988 and July 1993. Lloyds TSB Group does not expect any further fines or regulatory investigations in connection with the regulator's action plan for reviewing cases of possible misselling.

The most significant costs are the compensation of past purchasers of pensions. As the review of pension cases in Lloyds TSB Group has progressed, provisions have been established for the cost of compensation to past purchasers of pensions.

Movements in the provisions established by the Lloyds TSB bancassurance business and Abbey Life over the last three years have been as follows:

	2002 GBPm	2001 GBPm	2000 GBPm
Provision at 1 January	203	352	397
Accrual of interest on the provision	17	20	26
Additional amounts provided	40	70	100
Compensation paid	(223)	(238)	(173)
Phase 1 guarantees(1)	-	(1)	3
Phase 2 guarantees(1)	-	-	(1)
Provision at 31 December (2)	37	203	352

(1) In some cases, rather than pay cash compensation directly into the customer's private pension plan, Lloyds TSB Group has guaranteed to 'top-up' the customer's pension income, on retirement, to the level that they would have received under the relevant occupational scheme. A separate provision for these amounts is carried in Lloyds TSB Group's balance sheet.

(2) This provision is included within the figure for the long-term assurance business attributable to the shareholder ("embedded value") in Lloyds TSB Group's balance sheet.

At the beginning of 2000 a provision totalling GBP397 million was held in respect of Phase 1 and Phase 2 cases. This provision was calculated by making assumptions about the number of cases that would be identified during the review as requiring compensation and the estimated cost of the resulting payment. As the review has progressed greater experience has enabled management to refine these assumptions. The size of the provision has also been affected by the widening in the scope of the review to encompass certain parts of the FSAVC business and periodic revisions to the actuarial guidelines issued by the Financial Services Authority for the calculation of redress payments. Lower stock market levels have also had a significant impact on total redress costs as the cost of restitution into company pension schemes increases as personal pension fund values reduce. These factors have resulted in additional charges being made to the Lloyds TSB Group's profit and loss account of GBP100 million in 2000, GBP70 million in 2001 and GBP40 million in 2002.

Following normal actuarial practice, each year the provision has also been increased to recognise the interest accruing upon the assets held to match the liability. This increase in the provision amounted to GBP17 million in 2002, GBP20 million in 2001 and GBP26 million in 2000, although there was no net effect on Lloyds TSB Group's profit and loss account.

By 31 December 2002, Lloyds TSB Group had met the requirement of the Financial Services Authority to have completed the review and where appropriate issued offers of compensation to customers, except for those cases with mitigating circumstances. Lloyds TSB Group was satisfied as to the adequacy of the provision as at 31 December 2002.

Before its acquisition in 2000, Scottish Widows mainly distributed its products through independent financial advisors and for this reason the liability of the business to pay redress to past purchasers of pension policies is less significant. At 31 December 2002 a provision of GBP5 million (2001: GBP11 million) was held within the With-Profits Fund. The review has been completed and no further costs are anticipated. However in the event that this is not the case the cost will be met from assets held in the With-Profits Fund and will therefore have no financial impact upon Lloyds TSB Group.

Mortgage endowment and other savings products

A current industry issue concerns the sale of life assurance products related to the repayment of residential mortgages ('mortgage endowments'). At sale, the premium is set at a level such that the projected benefits assured, including an estimate of growth over the life of the policy and allowing for an estimate of the expenses to be charged, will equal or exceed the mortgage debt. Falling investment returns have led to increased concern that the value of some of these policies will be less than the amount required to repay the mortgage. Certain customers have complained that this risk was not properly explained to them at the time of the sale.

During 2002, a review was carried out in conjunction with the Financial Services Authority into past sales of mortgage endowment and other long-term savings products made by the Abbey Life sales force prior to its disposal by the Lloyds TSB Group in February 2000. As a result of this review, in December 2002 the Financial Services Authority fined Abbey Life GBP1 million for mortgage endowment misselling and other deficiencies in its compliance procedures and controls. A provision of GBP165 million has been established for the cost of compensation due to customers based upon assumptions as to the number of cases requiring redress and the estimated average cost. Lloyds TSB Group was satisfied with the adequacy of the provision at 31 December 2002.

Other complaints, including those related to the sale of mortgage endowments by other parts of the Lloyds TSB Group, are dealt with on a case by case basis and where appropriate compensation is paid. Provision has been made, based upon the level of complaints, for the estimated cost of redress which at 31 December 2002 was not significant.

Concerns have also been expressed over the appropriateness of sales of certain stock market related savings products. In this regard, Lloyds TSB Group is carrying out, in conjunction with the Financial Services Authority, an investigation into sales made in 2000 and 2001 of the Extra Income & Growth Plan. The Extra Income & Growth Plan is a term investment providing a fixed return either by way of quarterly income, annual income or a single payment at maturity. The capital repayment at maturity is linked to the performance of a basket of shares, selected from the FTSE 100. This investigation is expected to be completed during 2003.

Recent Developments

Since the end of 2002, the Lloyds TSB Group has continued to carry out, in conjunction with the regulator, its investigation into the appropriateness of certain sales of the Extra Income & Growth Plan. This investigation is expected to be completed within the next few months when the Lloyds TSB Group will be in a better position to quantify the financial effect. During the first quarter of 2003 there has also been an increase in the level of complaints relating to sales and performance of mortgage endowments made by Lloyds TSB Group and other long-term savings products. In addition, in the light of further experience the Lloyds TSB Group has revised some of the assumptions used in the calculation of the cost of redress in the areas described above. As a result of these developments, and volatility in global stock markets, further provisions and charges will arise in 2003 to cover these issues.

Competitive environment

General

Lloyds TSB Group operates in a financial services world that is experiencing consolidation at both national and international levels. The last few years have seen the establishment of global players in the industry together with the beginnings of pan-European consolidation and considerable consolidation within the US. Product manufacture and support in markets such as credit cards, mortgages, savings and funds management will increasingly be driven on a global scale.

Globalisation and developments in technology are significantly expanding Lloyds TSB Group's range of competitors, by removing many barriers to entry. These new entrants are expected to put Lloyds TSB Group's margins under increasing pressure with products becoming increasingly simplified and standardised. Nonetheless, Lloyds TSB Group expects competition within the industry to continue to be partially based on service and relationships as well as price, particularly for core banking services. Furthermore, complex products such as pensions are expected to be more resistant to standardisation and selling across the internet. In addition, Lloyds TSB Group has significant strengths with which to counter the pressure on margins in its portfolio of powerful brands, its existing customer base, its distribution capability and its purchasing power.

The UK

Lloyds TSB Group's key markets are in the UK, predominantly in the retail sector, where the market for basic financial and banking services is relatively mature. The market for life and pensions and general insurance products has exhibited growth in a number of key sectors.

The removal of regulatory and financial barriers in recent years has blurred the traditional financial services industry lines and allowed new competitors into the market. Lloyds TSB Group's competitors include all the major retail financial services and fund management companies operating in the UK. De-mutualised building societies which have become banks and life assurers which have entered the banking market have become direct competitors in the provision of banking products, whilst several UK banks have announced the launch of stand-alone internet banks to complement their existing services. In the mortgage market competitors include the traditional banks and building societies and new entrants to the market, with the market becoming increasingly competitive as both new entrants and incumbents endeavour to gain market share. Lloyds TSB Group's competitors in the credit card market again include both the traditional banks and new entrants, including overseas companies. In the last few years a large share of new business has been acquired by US and new UK competitors. In the provision of life, pensions and investments products Lloyds TSB Group has seen increased competition from new market entrants, such as traditional retailers, primarily in specialist areas. The fragmented nature of the life, pensions and investments market in the UK has resulted in some consolidation within the sector; government regulations on product charges and competitive pressures are likely to drive further consolidation as providers seek to achieve the benefits of economies of scale. In the general insurance sector, the market has seen significant consolidation amongst underwriters but continued fragmentation in distribution and an increasing number of new market entrants including both overseas insurers and direct operators.

In addition to the challenging competitive environment, the UK financial services industry is characterised by recent government intervention and regulation. Lloyds TSB Group is currently facing over 120 potential legislative issues which may have an impact on its business, over half of which emanate from Europe as part of the Financial Services Action Plan or in the shape of EU social legislation. Many of the reviews instigated by the UK government into the financial services sector have been against a backdrop of increased consumerism, driven by support for open competition and a fair deal for the consumer.

In 1998, the UK government commissioned an investigation into competition in the banking industry whose findings were published in March 2000. The investigation specifically examined the levels of innovation, competition and efficiency in various sub-markets within the industry. The investigation found that the small and medium-sized business market was not sufficiently competitive, with barriers to entry existing for new players. The provision of banking services to this sector was referred to the UK Competition Commission under the Fair Trading Act 1973 for a full competition inquiry.

In pursuing its investigation, the UK Competition Commission provisionally decided to regard the small and medium-sized business market to be comprised of sole traders, firms and companies generating an annual turnover of up to GBP25 million. There are a number of operating units within Lloyds TSB Group engaged in the small and medium-sized business market, the largest of which is Business Banking. Business Banking provides services to those businesses with an annual turnover of less than GBP2 million and has a 19 per cent share of this market, based on research by NFO WorldGroup.

On 14 March 2002, the Competition Commission's report into the competitiveness of banking for small and medium-sized enterprises (SME's) was published by the government. The Competition Commission concluded that a number of specific practices had the effect of restricting or distorting price competition between the main banks. Particular examples that were identified included the similarity of pricing structures and the fact that in general no interest is paid on current account balances; a pattern of differentiation in the charges made by the main banks, with free banking generally confined to certain categories of SME such as new start-ups or customers switching banks; and the use of negotiation for those considering switching. The Competition Commission also concluded that there were significant barriers to entry, in part caused by the lack of price competition, but also because of the unwillingness of SME's to change banks because of the perceived complexity. In the view of the Competition Commission the restriction and distortion of price competition has led to excessive prices and profits. The government has accepted in full the recommendations made by the Competition Commission. To remedy this situation one of the most significant proposals is that banks should offer any SME customer operating a current account in England and Wales, either:

* a current account that pays interest of at least the Bank of England Base Rate, minus 2.5 per cent; or

* a current account free of money transmission charges; or

* a choice between the two.

The principal behavioural remedies intended to reduce barriers to entry and expansion are measures to ensure fast error-free switching of accounts between banks. In addition, measures have been proposed limiting the bundling of services and improving market information and transparency.

15

Lloyds TSB Group has introduced initiatives to address a number of these remedies, such as ease of switching and transparency of charging, either on its own initiative or via the Business Banking Code. The estimated annual cost to Lloyds TSB Group of implementing the Competition Commission's findings is likely to be in the region of GBP150 million.

Other recent reviews into the Financial Services sector include:

* The DeAnne Julius Banking Code Review aimed at improving services to bank customers, including the regulation of mortgage advice and the introduction of an independent reviewer to develop the Banking Code.

* The Sandler Review into the UK's long-term retail savings industry which was commissioned to identify structural flaws in the financial services industry which might prevent customers from saving. The report's core recommendation is the introduction of simple regulated products with capped charges, restrictions on investment profile and the ability to exit on reasonable terms.

* The Pickering Review of Pensions, published in July 2002, which focused on the simplification of the pensions framework. Core recommendations included a new Pensions Act to consolidate all existing pensions legislation; a new, more pro-active regulator; a more targeted approach to communicating with pension scheme members; and allowing employers to make membership of their occupational pension schemes a condition of employment.

Lloyds TSB Group has always supported the principle of competition and agrees with the importance of building consumer confidence in financial services. Lloyds TSB Group has concerns about the introduction of price controls, which would be a barrier to entry and believes that voluntary codes, rather than statutory regulation, are in the best interests of consumers and competition.

Other markets

Lloyds TSB Group also operates in other countries, principally in New Zealand and Latin America, where it is exposed to different competitive pressures.

Lloyds TSB Group operates in New Zealand through its wholly-owned subsidiary NBNZ. NBNZ's competitors principally comprise the major Australian banks each of which offers retail and wholesale products through branch networks and, more recently, over the telephone and internet. Consolidation in the Australian banking industry would, therefore, have a direct effect upon the competitive environment in New Zealand.

Lloyds TSB Group has operated in the Americas for over 130 years and has offices in Brazil, Argentina, Colombia and seven other countries. The competitive environment in each country varies significantly where the number of players, both local and international, is substantially different. In Brazil there are over 200 banks, a third of which are either partially or wholly owned by foreign interests; in addition, there are a number of specialist consumer finance businesses. In Argentina and Colombia the competition is limited to a small number of domestic and foreign banks.

16

OPERATING AND FINANCIAL REVIEW AND PROSPECTS

The results discussed below are not necessarily indicative of Lloyds TSB Group's results in future periods. The following information contains certain forward-looking statements. For a discussion of certain cautionary statements relating to forward-looking statements, see "Forward-Looking Statements".

The following discussion is based on and should be read in conjunction with the Consolidated Financial Statements and the related notes thereto included elsewhere in this annual report. For a discussion of the accounting policies used in the preparation of the Consolidated Financial Statements, see "Accounting policies" in Note 1 to the Consolidated Financial Statements. The Consolidated Financial Statements are prepared in accordance with UK GAAP, which varies in certain significant respects from US GAAP. A discussion of such differences and a reconciliation of certain UK GAAP amounts to US GAAP is included in Note 48 to the Consolidated Financial Statements.

TABLE OF CONTENTS

17

Overview and trend information

Lloyds TSB Group has operations in both the UK and overseas, however, its earnings are heavily dependent upon its domestic activities. In 2002, 81 per cent of Lloyds TSB Group's profit before tax was derived from its UK operations. The state of the UK economy, therefore, has significant implications for the way in which the Lloyds TSB Group runs its business and its performance.

Although the UK economy has avoided recession, performance across different sectors has been varied with growth in the services sector reflecting strong domestic demand tempered by recession in the manufacturing sector, largely caused by the strength of sterling and weak overseas demand. The level of indebtedness of the UK corporate sector has started to reduce. However, profit growth is expected to remain sluggish and if interest rates start to increase there may be an effect upon the level of corporate failures. Low interest rates, low unemployment and low inflation have helped drive strong growth in the UK residential housing market and an increase in consumer borrowing, which has allowed a rise in savings flows without having a significant effect upon spending patterns. However, there are now indications that the growth in the housing market is starting to slow which would have an effect upon future levels of growth in customer lending and deposits.

Within the UK banking businesses of the Lloyds TSB Group there has been continued growth in personal, mortgage and corporate lending and a steady increase in savings balances. The arrears position in the personal lending and mortgage portfolios has remained stable, although there has been an increased bad debt charge against corporate exposures to certain sectors of the UK economy which are experiencing a slowdown in economic growth. However, the low interest rate environment has also resulted in a lower net interest margin as the full effect of base rate reductions has not been reflected in the rates of interest paid on deposit accounts and the benefit of low and interest free current accounts has been reduced.

The continued fall in the level of the stock market in the UK has had a significant effect upon the Lloyds TSB Group's insurance and investment businesses. There has been a marked reduction in customer demand for equity based savings products and significant losses have been incurred following a fall in the value of the investments held to support the long-term assurance business. Although steps have been taken to reduce Lloyds TSB Group's exposure to further reductions in equity market levels, the future performance of this business is, to a certain extent, dependent upon a recovery in these markets.

Overseas, the benign economic conditions in New Zealand contributed to a 16 per cent increase in local currency profits as a result of strong lending growth; in sterling terms the increase in profit was 32 per cent. However, the economic situation in Latin America remains uncertain. Since the October presidential election in Brazil the economic situation has somewhat stabilised. The Lloyds TSB Group reduced its total exposure to Brazil, net of provisions, to some GBP1,900 million during 2002 from some GBP3,300 million at the end of 2001, largely from not replacing maturing government bonds. Economic activity in Brazil has remained reasonably robust, and this relative strength in the local economy, in conjunction with the significant International Monetary Fund support package which the newly elected president and incoming government have indicated they will support, should alleviate current concerns about the Brazilian economy. The economic situation in Argentina continues to be difficult and the outlook is likely to remain uncertain during 2003. Lloyds TSB Group's total exposure to Argentina at the end of 2002 had reduced to some GBP190 million net of provisions and charges, compared to GBP610 million at the end of 2001.

See also "Business - Competitive environment"

Critical accounting policies

Introduction

The results of Lloyds TSB Group are sensitive to the accounting policies, assumptions and estimates that underlie the preparation of its Consolidated Financial Statements. The accounting policies used in the preparation of the Consolidated Financial Statements are set out in Note 1 to the Consolidated Financial Statements. In preparing the accounts, the directors are required to select suitable accounting policies, apply them consistently and make judgements and estimates that are reasonable and prudent. Where UK GAAP allows a choice of policy, Financial Reporting Standard 18 'Accounting Policies' requires Lloyds TSB Group to adopt those policies judged to be most appropriate to its particular circumstances for the purpose of giving a true and fair view.

In its 2002 Consolidated Financial Statements Lloyds TSB Group adopted fully the accounting requirements of Financial Reporting Standard 17 "Retirement Benefits" although the UK Accounting Standards Board has deferred mandatory adoption until 2005. Implementation of this accounting standard has had a significant effect on the results of the Lloyds TSB Group, which is explained further in Notes 1 and 43 of the Consolidated Financial Statements.

The accounting policies that are deemed critical to the Lloyds TSB Group's results and financial position, based upon materiality and significant judgement and estimates, are discussed below.

Provisions for bad and doubtful debts

In circumstances where there is significant doubt over the recoverability of specific loans and advances, provisions are made to reduce the carrying value of those advances to their expected ultimate net realisable value. The methodology used to calculate the required provision varies according to the type of lending portfolio. For portfolios of smaller balance homogenous loans, such as residential mortgages, personal loans and credit card balances, specific provisions are calculated using formulae which take into account factors such as the length of time that the customer's account has been delinquent, historic loss rates and the value of any collateral held. The variables used in the formulae are kept under regular review to ensure that as far as possible they reflect the current economic circumstances, although actual experience may differ from that assumed.

For the Lloyds TSB Group's other lending portfolios, provisions are calculated on a case-by-case basis having regard to expected future cash flows including those arising from the realisation of collateral. The determination of these provisions often requires the exercise of considerable judgment by management involving matters such as future economic conditions and the resulting trading performance of the customer and the value of collateral, for which there may not be a readily accessible market. As a result these provisions can be subject to significant variation as time progresses and the circumstances of the customer become clearer.

The Lloyds TSB Group also maintains a general provision to cover latent bad and doubtful debts which are present in any portfolio of advances but which have not been specifically identified. The calculation of the general provision requires a significant amount of judgement to assess the level of losses inherent in the portfolio and is based upon factors such as the level of watchlist or potential problem debt, the propensity for such debt to become impaired and historical loss rates. The general provision is reviewed on a regular basis to ensure that it remains appropriate in prevailing economic conditions and in the light of the perceived level of credit risk within the lending portfolios.

Goodwill impairment

Lloyds TSB Group reviews the goodwill arising on the acquisition of subsidiary undertakings when events or changes in economic circumstances indicate that impairment may have taken place and at the end of the first full year after an acquisition. In addition, since the goodwill arising on the acquisition of Scottish Widows is considered to have an indefinite useful life, because of the strength of the brand and the position of the business as one of the leading providers of life, pensions, unit trust and fund management products, and is therefore not amortised, the Lloyds TSB Group is required under UK GAAP to perform an annual review to determine whether an impairment has occurred.

The impairment review is performed by projecting future cash flows, excluding finance and tax, based upon budgets and plans and making prudent assumptions about longer term rates of growth and discounting these using a rate approximating to the Group's weighted average cost of capital. If the present value of the projected cash flows is less than the carrying value of the underlying net assets and related goodwill an impairment has occurred and a charge would be made to the profit and loss account. This calculation requires the exercise of significant judgment by management; if the estimates made prove to be incorrect or changes in Scottish Widows' performance affect the amount and timing of future cash flows, the goodwill may become impaired in future periods.

Embedded value

Lloyds TSB Group accounts for the value of the shareholder's interest in the long-term assurance business using the embedded value basis of accounting, which is UK GAAP for banking groups owning life assurance operations. The embedded value is comprised of the net tangible assets of the life assurance subsidiaries and the present value of the in-force business, which is calculated by projecting future surpluses and other net cash flows attributable to the shareholder arising from business written by the balance sheet date and discounting the result at a rate which reflects the shareholder's overall risk premium.

Future surpluses will depend on experience in a number of areas such as investment returns, lapse rates, mortality and investment expenses. Surpluses are projected by making assumptions about future experience, having regard to both actual experience and forecast long-term economic trends. Changes to these assumptions may cause the present value of future surpluses to differ from those assumed at the balance sheet date and could significantly affect the value attributed to the in-force business. In Note 29 of the Consolidated Financial Statements the effect of theoretical changes in the principal economic assumptions upon the embedded value included in the balance sheet and new business income is set out.

The value of the in-force business could also be affected by changes in the amounts and timing of other net cash flows, principally annual management charges and other fees levied upon the policyholders, which are reflected in the profit and loss account using unsmoothed fund values. In addition, to the extent that actual experience is different from that assumed, the effect will be recognised in the profit and loss account for the period. The effect of changes in the underlying assumptions and variations between actual and assumed experience on the results of the current and prior periods are disclosed in Note 29 in the Consolidated Financial Statements.

Results of operations - 2002 compared with 2001 and 2001 compared with 2000
Summary

	2002 GBPm	2001* GBPm	2000* GBPm
Net interest income	5,171	4,922	4,587
Other finance income	165	307	424
Other income	3,542	3,660	3,765
Total income	8,878	8,889	8,776
Operating expenses	(4,915)	(4,776)	(4,279)
Trading surplus	3,963	4,113	4,497
General insurance claims	(229)	(174)	(142)
Provisions for bad and doubtful debts	(1,029)	(747)	(541)
Amounts written off fixed asset investments	(87)	(60)	(32)
Operating profit	2,618	3,132	3,782
Income from joint ventures	(11)	(10)	3
Profit on sale of businesses	-	39	-
Profit on ordinary activities before tax	2,607	3,161	3,785
Tax on profit on ordinary activities	(764)	(875)	(1,082)
Profit on ordinary activities after tax	1,843	2,286	2,703
Minority interests - equity	(19)	(17)	(13)
- non-equity	(43)	(40)	(36)
Profit attributable to shareholders	1,781	2,229	2,654
Economic profit(1)	821	1,119	1,524

* Figures for 2001 and 2000 have been restated to reflect changes in accounting policy and presentation adopted in 2002; for further details see Note 1 to the Consolidated Financial Statements.

(1) Lloyds TSB Group defines economic profit as the earnings on the equity invested in the business less a notional charge for the cost of the equity invested in that business. See "- Economic Profit".

2002 compared with 2001

In 2002, Lloyds TSB Group's profit before tax decreased by GBP554 million, or 18 per cent, to GBP2,607 million from GBP3,161 million in 2001. Profit attributable to shareholders was 20 per cent lower at GBP1,781 million and earnings per share decreased by 21 per cent to 32.0p. Shareholders' equity decreased by GBP2,384 million to GBP7,972 million following a reduction of GBP2,331 million in the value of the Group's pension schemes, largely caused by the significant fall in equity market values. The post-tax return on average shareholders' equity was 16.7 per cent, compared to 18.1 per cent in 2001. Economic profit decreased by 27 per cent to GBP821 million. The post-tax return on average assets was 0.93 per cent, and the post-tax return on average risk-weighted assets was 1.61 per cent.

Total income was GBP11 million lower at GBP8,878 million, compared to GBP8,889 million in 2001. Lloyds TSB Group's net interest income increased by GBP249 million, or 5 per cent, to GBP5,171 million. Average interest-earning assets increased by GBP16,873 million, or 12 per cent, to GBP161,818 million, adding GBP655 million to net interest income. In the UK, average personal lending and mortgage balances increased by GBP6,732 million driven by the strong residential housing market and the low interest rate environment; wholesale balances were GBP7,195 million higher with increased corporate term and money market lending and a number of new structured finance transactions. Average balances overseas increased by GBP3,215 million, with the majority of the growth being in New Zealand reflecting a strengthening exchange rate and increased mortgage and agricultural lending. The effect of this volume growth was partly offset by a 20 basis point fall in the net interest margin, reducing net interest income by GBP290 million, reflecting the reduced benefits accruing from the Lloyds TSB Group's low interest and interest-free liabilities and a change in mix toward finer margin products. Adverse exchange movements reduced net interest income by GBP116 million.

Other finance income, at GBP165 million, was down GBP142 million, or 46 per cent, from GBP307 million in 2001. The expected return on pension scheme assets was GBP27 million lower, reflecting the lower market value of scheme assets at the start of 2002, as a result of stock market conditions. The interest charge in respect of the unwinding of the discount on scheme liabilities was GBP115 million higher, due to the increased level of scheme liabilities at the start of 2002 mainly reflecting the greater longevity of the members of the schemes.

Other income was GBP118 million, or 3 per cent, lower at GBP3,542 million compared to GBP3,660 million in 2001. Income from long-term assurance business was GBP274 million lower, mainly as a result of the depressed stock market conditions reducing the returns from the investments supporting the life funds and the capitalised value of annual management charges, together with a GBP135 million increase in provisions for redress to past purchasers of endowment and pension products. There was also a charge of GBP57 million to reflect the implementation of revised mortality assumptions. Dealing profits were GBP45 million lower, largely as a result of less favourable market conditions. These factors more than offset an increase in net fees and commissions receivable which were GBP88 million higher. Growth in general insurance broking income and income from credit and debit cards was only partly offset by reduced levels of stock market related fees. General insurance premium income was GBP58 million higher and other operating income increased by GBP55 million as reductions in venture capital gains and profits from sale and leasebacks of premises were more that offset by increased operating lease rental income, mainly reflecting the impact of acquisitions during the year.

Operating expenses were GBP139 million, or 3 per cent, higher at GBP4,915 million compared to GBP4,776 million in 2001. Administrative expenses were GBP12 million lower than in 2001. Staff costs reduced by GBP36 million as the benefits of reductions in staff numbers and lower levels of pension scheme augmentation costs more than offset the impact of acquisitions, the annual pay review and increased severance costs. Premises and equipment costs were GBP26 million higher as a result of increased rental costs and repairs and maintenance expenditure. Depreciation was GBP131 million higher, largely reflecting a GBP95 million increase in respect of operating lease assets as a result of acquisitions and organic growth in the Lloyds TSB Group's existing businesses. Goodwill amortisation was GBP20 million higher. The efficiency ratio increased to 55.4 per cent from 53.7 per cent.

General insurance claims increased by GBP55 million, or 32 per cent, to GBP229 million, reflecting volume related increases in property claims and a higher level of weather and flood related insurance claims.

The charge for bad and doubtful debts was 38 per cent higher at GBP1,029 million compared with GBP747 million in 2001. In UK Retail Banking and Mortgages the provisions charge increased by GBP148 million, or 36 per cent, to GBP563 million, largely as a result of volume related asset growth in the personal loan and credit card portfolios, which grew by 15 per cent and 27 per cent respectively and the non-recurrence of one-off releases recognised in 2001. In Wholesale Markets and International Banking the provisions charge increased by GBP135 million to GBP473 million. Provisions against the corporate lending portfolio increased by GBP145 million as a result of a small number of large provisions against certain US customers following the discovery of accounting or other operational irregularities and higher provisions against exposures in specific sectors of the UK economy which are now starting to experience a slowdown in activity. Within International Banking provisions fell mainly as a result of lower specific provisions in Losango, Lloyds TSB Group's consumer finance business in Brazil, largely reflecting exchange rate movements. The general provision held against the Lloyds TSB Group's exposure to Argentina was increased by GBP50 million, compared to a charge of GBP55 million in 2001.

Amounts written off fixed asset investments increased by GBP27 million, or 45 per cent, to GBP87 million in 2002, compared to GBP60 million in 2001. There was a GBP21 million write down following operating irregularities on one specific securitisation issue and a GBP21 million increase in the charge in respect of the venture capital business in the UK, reflecting portfolio growth. These increases were partly offset by a GBP15 million reduction in the charge in respect of Argentine government debt.

In 2001, a profit of GBP39 million arose on the sale of the Lloyds TSB Group's Brazilian fund management and private banking businesses.

At the end of 2002, the total capital ratio increased to 9.6 per cent as new issues of tier 1 and tier 2 capital instruments during the year more than offset the effect of a GBP14,550 million, or 13 per cent, increase in risk weighted assets to GBP122,411 million, from GBP107,861 million at the end of 2001. Balance sheet assets increased by GBP16,965 million, or 7 per cent, to GBP252,758 million. Loans and advances to customers increased by GBP11,539 million, mainly reflecting growth in UK mortgage and personal period end lending balances, which increased by GBP8,036 million, and growth of GBP2,012 million in New Zealand. Debt securities were GBP5,089 million higher due to further growth in the Lloyds TSB Group's asset-backed portfolio.

2001 compared with 2000

Profit on ordinary activities before tax fell by GBP624 million or 16 per cent to GBP3,161 million from GBP3,785 million, driven by a reduction in income from Lloyds TSB Group's insurance businesses caused by the overall fall in stock market values. Shareholders' equity fell by 13 per cent and earnings per share fell by 17 per cent to 40.3p. The post-tax return on average shareholders' equity was 18.1 per cent.

Total income grew by GBP113 million, or 1 per cent, from GBP8,776 million in 2000 to GBP8,889 million in 2001. Net interest income increased by GBP335 million, or 7 per cent, from GBP4,587 million to GBP4,922 million, although after adjusting for the effect of the inclusion of a full year's funding cost relating to the acquisition of Scottish Widows in March 2000, there was an underlying growth of GBP437 million or 9 per cent. Average interest earning assets increased by GBP13,923 million or 11 per cent to GBP144,945 million. Most of this growth was in the UK where average interest earning assets grew by GBP10,670 million; personal lending and mortgage balances grew by GBP6,139 million and corporate balances increased by GBP4,628 million. Overseas average interest earning assets increased by GBP3,253 million with growth in New Zealand and Brazil. The effect of this growth was partly offset by a 6 basis point fall in the underlying net interest margin reflecting the increasingly competitive operating conditions and a lower contribution from interest-free liabilities, caused by the lower interest rate environment.

Other finance income decreased by GBP117 million or 28 per cent from GBP424 million in 2000 to GBP307 million in 2001. The decrease reflects a lower level of assets held in Lloyds TSB Group's defined benefit pension schemes at the start of 2001, coupled with lower expectations for market returns during the year.

Other income in 2001 fell by GBP105 million, or 3 per cent, from GBP3,765 million to GBP3,660 million. Income from long-term assurance business fell by GBP472 million as a 15 per cent fall in the FTSE All-Share index during the year caused a sharp reduction in the earnings from the investments held to support Lloyds TSB Group's life and general insurance activities. This was partly offset by a GBP272 million improvement in other operating income caused mainly by an increase of GBP178 million in operating lease rental income, reflecting both the inclusion of Chartered Trust for the full year and underlying volume growth, and profits of GBP57 million from the sale and leaseback of branch and head office premises. There was an increase in net fees and commissions receivable, after deducting fees and commissions payable, of GBP31 million, dealing profits increased by GBP35 million and premium income from the general insurance underwriting business grew by GBP29 million.

Operating expenses in 2001 increased by GBP497 million, or 12 per cent to GBP4,776 million from GBP4,279 million. The efficiency ratio increased from 48.8 per cent to 53.7 per cent. Of this increase, GBP145 million was due to the inclusion of Scottish Widows and Chartered Trust for a full year, the remainder of the growth was due to increased business development expenditure including increased staff and other costs supporting the improvement in retail banking sales volumes achieved during the year, together with costs of GBP82 million relating to benefit improvements in Lloyds TSB Group's pension schemes.

The total charge in respect of bad and doubtful debt provisions increased by GBP206 million or 38 per cent to GBP747 million from GBP541 million, although this was adversely affected by an increase in the general provision of GBP55 million in respect of Lloyds TSB Group's exposures in Argentina. The charge for bad and doubtful debts attributable to UK operations grew by GBP144 million to GBP570 million partly reflecting the inclusion of Chartered Trust for a full year, but also as a result of an GBP83 million increase in the charge against the retail banking and mortgages portfolio due to the growth in the level of outstanding balances and partly as a result of a one-off benefit of GBP42 million in 2000. Provisions against the corporate and commercial lending portfolios also increased as provisions were required against a small number of large exposures. Overseas provisions, excluding the general provision in respect of Argentina, increased by GBP7 million as higher charges in Uruguay, Dubai and the Netherlands more than offset improvements in Colombia and New Zealand.

Amounts written off fixed asset investments increased by GBP28 million, or 88 per cent, from GBP32 million to GBP60 million. In 2001 Lloyds TSB Group provided GBP45 million against the carrying value of its holding of Argentine government bonds as a result of the deterioration in the economic environment in that country. The 2000 results included a provision of GBP18 million against Lloyds TSB Group's holding of Ecuadorian bonds.

The profit on sale of business of GBP39 million arose as a result of the sale of Lloyds TSB Group's Brazilian fund management and private banking business including its subsidiary, Lloyds TSB Asset Management S.A., to Banco Itau S.A. The sale of this business did not affect Lloyds TSB Group's other Brazilian businesses.

At 31 December 2001, the total capital ratio was 8.8 per cent and the tier 1 capital ratio was reduced to 7.8 per cent, reflecting a 16 per cent growth in risk-weighted assets from GBP93,211 million to GBP107,861 million. Balance sheet assets grew by GBP15,121 million, or 7 per cent, from GBP220,672 million to GBP235,793 million. Loans and advances to customers increased by GBP8,503 million, or 7 per cent mainly as a result of growth in UK mortgage and personal lending, which increased by GBP5,565 million, and higher levels of corporate and commercial lending. Debt securities increased by GBP9,620 million due to higher year-end liquidity requirements and a number of new structured finance transactions which result in lower cost funding for the Group.

22

Net interest income

The yields, spreads and margins in the table below are those relating to the banking business only.

	2002	2001	2000
Lloyds TSB Group:			
Net interest income GBPm	5,171	4,922	4,587
Average interest-earning assets GBPm	161,818	144,945	131,022
Average rates			
Gross yield on interest-earning assets%(1)	6.52	7.84	8.44
Interest spread %(2)	2.94	3.00	2.98
Net interest margin %(3)	3.20	3.40	3.50
Domestic:(4)			
Net interest income GBPm	4,425	4,202	3,956
Average interest-earning assets GBPm	134,902	121,244	110,574
Average rates			
Gross yield on interest-earning assets %(1)	6.10	7.38	8.07
Interest spread %(2)	3.08	3.11	3.06
Net interest margin %(3)	3.28	3.47	3.58
International:(4)			
Net interest income GBPm	746	720	631
Average interest-earning assets GBPm	26,916	23,701	20,448
Average rates			
Gross yield on interest-earning assets %(1)	8.63	10.19	10.40
Interest spread %(2)	2.12	2.43	2.58
Net interest margin %(3)	2.77	3.04	3.09

(1) Gross yield is the rate of interest earned on average interest-earning assets.

(2) Lloyds TSB Group interest spread is the difference between the rate of interest earned on total average interest-earning assets and the rate of interest paid on total average interest-bearing liabilities. The domestic interest spread is the difference between the rate of interest earned on domestic average interest-earning assets and the rate of interest paid on domestic average interest-bearing liabilities. The international interest spread is the difference between the rate of interest earned on international average interest-earning assets and the rate of interest paid on international average interest-bearing liabilities.

(3) The net interest margin represents the interest spread together with the contribution of interest-free liabilities. It is calculated by expressing net interest income as a percentage of average interest-earning assets.

(4) The analysis of net interest income by domestic and international operations shown above is based on the location of the office recording the transaction, except for lending by the international business booked in London.

2002 compared with 2001

Lloyds TSB Group net interest income increased by GBP249 million, or 5 per cent, to GBP5,171 million, representing 58 per cent of total income compared to 55 per cent in 2001. Average interest-earning assets increased by GBP16,873 million, or 12 per cent, to GBP161,818 million, adding GBP655 million to net interest income. Within UK Retail Banking and Mortgages, continued strong growth lead to increases of GBP2,251 million in average personal lending and credit card balances and GBP4,481 million in average mortgage balances. Within Wholesale Markets and International Banking, average interest-earning assets increased by GBP10,352 million, reflecting growth in corporate and money market lending and increased volumes of structured finance products. Overseas, growth in balances in New Zealand was partly offset by reductions in Latin America as exchange rates have weakened and the Lloyds TSB Group's exposures to Brazil and Argentina have been reduced.

The net interest margin fell by 20 basis points to 3.20 per cent from 3.40 per cent in 2001, reducing net interest income by GBP290 million. Reductions in interest rates in the UK in the second half of 2001 have resulted in a reduced benefit from Lloyds TSB Group's low interest rate deposits and interest-free liabilities. There has also been a continuing shift in the mix of average interest-earning assets towards high quality, but finer margin, corporate and wholesale lending. Adverse exchange rate movements, principally in Latin America, reduced net interest income by GBP116 million.

Domestic net interest income increased by GBP223 million, or 5 per cent, to GBP4,425 million. This represents 86 per cent of consolidated net interest income. Average interest-earning assets increased by GBP13,658 million, or 11 per cent, to GBP134,902 million, adding GBP449 million to net interest income. Average personal lending and mortgage balances grew by GBP6,732 million and wholesale balances increased by GBP7,195 million.

23

The domestic net interest margin decreased by 19 basis points, reducing net interest income by GBP226 million, as a result of a reduction in the contribution of interest-free liabilities and the continuing shift in the mix of average interest-earning assets towards finer margin, corporate and wholesale lending. In UK Retail Banking and Mortgages there was a 4 basis point decrease in the net interest margin as an erosion in the mortgage margin was partly offset by a shift in the mix of retail business towards personal lending and credit cards. In Wholesale Markets there was an 18 basis point reduction caused by further growth in finer margin corporate lending.

Net interest income from international operations increased by GBP26 million, or 4 per cent, to GBP746 million, representing 14 per cent of consolidated net interest income. In sterling terms, average interest-earning assets increased by GBP3,215 million, or 14 per cent, to GBP26,916 million, adding GBP206 million to net interest income. Average balances in New Zealand increased by GBP2,420 million reflecting both organic growth and positive exchange rate movements; growth in US structured finance and government guaranteed export credit transactions increased average interest-earning assets by a further GBP1,277 million. Balances in Latin America fell by GBP841 million as modest growth in local currency terms, principally in the Brazilian consumer finance business, was more than offset by the effect of exchange rate movements.

The net interest margin from international operations reduced by 27 basis points, leading to a fall of GBP64 million in net interest income, as a result of lower margins in our Latin American and US structured finance businesses which more than offset an improved margin in New Zealand.

2001 compared with 2000

Lloyds TSB Group net interest income increased by GBP335 million, or 7 per cent, to GBP4,922 million, representing 55 per cent of total income compared to 52 per cent in 2000. After adjusting for the effect of funding the Scottish Widows purchase consideration for a full year in 2001 compared to only ten months in 2000, the underlying growth was GBP437 million, or 9 per cent. Average interest-earning assets increased by GBP13,923 million or 11 per cent to GBP144,945 million, adding GBP566 million to net interest income. Personal lending and mortgage balances in the UK grew by GBP6,139 million as Lloyds TSB Group sought to develop these portfolios prudently, but profitably. Within Wholesale Markets and International Banking, average interest earning assets increased by GBP7,902 million. The asset finance portfolio grew by GBP1,074 million, partly reflecting the inclusion of Chartered Trust for a full year and there was an increase of GBP4,628 million in corporate and commercial lending balances in the UK. There was also growth in structured finance balances in the UK and overseas.

The net interest margin fell by 10 basis points, although after adjusting for the funding cost of Scottish Widows, there was an underlying reduction of 6 basis points reducing net interest income by GBP70 million. A lower interest rate environment in the UK resulted in a reduced contribution from Lloyds TSB Group's low interest rate and interest-free liabilities and this was coupled with lower margins earned on corporate and commercial and some personal lending balances, due to competitive pressures. These factors more than offset the benefits obtained from positive interest rate management within Lloyds TSB Group's treasury and central functions. Adverse exchange rate movements, mainly in Brazil, reduced net interest income by GBP59 million.

Domestic net interest income in 2001 increased by GBP246 million, or 6 per cent, to GBP4,202 million, representing 85 per cent of consolidated net interest income. After adjusting for the effect of the inclusion of a full year's funding cost in respect of the Scottish Widows acquisition in March 2000, there was an underlying increase of GBP348 million. Average interest-earning assets increased by GBP10,670 million, or 10 per cent, to GBP121,244 million adding GBP401 million to net interest income. Personal lending and mortgage balances increased by GBP6,139 million and corporate and commercial balances increased by GBP4,628 million.

The domestic net interest margin fell by 11 basis points reflecting the higher funding cost of Scottish Widows, which caused a reduction of 6 basis points. There was an underlying reduction of 5 basis points costing GBP53 million mainly as a result of a reduced contribution from low interest and interest-free liabilities due to the lower interest rate environment. The net interest margin on retail lending products fell 5 basis points and margins on corporate and commercial lending also reduced, although the margin earned on mortgage products was little changed.

Net interest income from international operations increased by GBP89 million, or 14 per cent, to GBP720 million, representing 15 per cent of consolidated net interest income. Average interest-earning assets increased by 20 per cent on a local currency basis, but this was partly offset by the effect of exchange rate movements. In sterling terms, average interest-earning assets increased by GBP3,253 million, or 16 per cent, to GBP23,701 million adding GBP155 million to net interest income. Average interest-earning assets in Latin America increased by GBP592 million with growth in corporate and consumer lending in Brazil, and in New Zealand there was an increase of GBP574 million due to higher volumes of corporate and commercial lending. Overseas structured finance and government guaranteed export credit transactions resulted in a GBP1,932 million increase in average interest-earning assets. Adverse exchange rate movements, mainly in Brazil, reduced net interest income by GBP59 million.

The net interest margin from international operations decreased by 5 basis points lowering net interest income by GBP7 million. Lower margins in Lloyds TSB Group's Latin American businesses more than offset small improvements in New Zealand and the benefits of lower funding costs for the overseas wholesale businesses.

24

Other income

	2002 GBPm	2001 GBPm	2000 GBPm
Fees and commissions receivable:			
UK current account fees	579	573	629
Other UK fees and commissions	1,163	1,220	1,171
Insurance broking	647	528	398
Card services	414	332	304
International fees and commissions	250	269	266
	3,053	2,922	2,768
Fees and commissions payable	(645)	(602)	(479)
Dealing profits (before expenses):			
Foreign exchange trading income	173	158	141
Securities and other gains	15	75	57
	188	233	198
Income from long-term assurance business	(303)	(29)	443
General insurance premium income	486	428	399
Other operating income	763	708	436
Total other income	3,542	3,660	3,765

2002 compared with 2001

Other income decreased by GBP118 million, or 3 per cent, to GBP3,542 million although after adjusting for the effect of acquisitions made during 2002 there was a reduction of GBP231 million or 6 per cent.

Fees and commissions receivable increased by GBP131 million, or 4 per cent, to GBP3,053 million, mainly due to increases in income from insurance broking and card services. Insurance broking commission income increased by GBP119 million, with continued strong growth in creditor insurance products, reflecting the increased lending volumes in the branch network, and higher levels of retrospective commission income. Income from credit and debit card services increased by GBP82 million, mainly as a result of higher merchant service charges and fees. UK current account fee income rose by GBP6 million, reversing the downward trend experienced in recent years; a GBP37 million increase in fee income from added value current accounts more than offset a reduction in service charges following their partial withdrawal during 2001. This more than offset a reduction in other UK fees and commissions of GBP57 million, or 5 per cent, from GBP1,220 million to GBP1,163 million following a GBP59 million reduction in unit trust and asset management fees, as the continued fall in the level of stock markets during 2002 have reduced the level of funds under management and significantly reduced customer demand for equity based products. There was also a fall in the level of recharges to Goldfish Bank, Lloyds TSB Group's joint venture with Centrica plc, which were down GBP10 million, and a reduction of GBP6 million in income from the company registration business, as the exceptionally high levels of corporate transactions in 2001 were not repeated.

Fees and commissions payable increased by GBP43 million, or 7 per cent, compared to 2001 as a result of higher reciprocity fees and an increase in package costs relating to a number of products. Commissions paid to motor dealers by the asset finance business also increased, in line with business volumes.

Dealing profits decreased by GBP45 million, or 19 per cent, compared with 2001 as a result of a reduction of GBP60 million in gains from securities trading; there were reduced opportunities for the Lloyds TSB Group's London Treasury department, due to less favourable market conditions, and losses resulting from the economic turmoil in Brazil. Foreign exchange trading income improved by GBP15 million as a result of an improved performance from Lloyds TSB Group's UK operations.

Income from long-term assurance business decreased by GBP274 million however, excluding the effect of changes in the economic assumptions used in the embedded value calculation which in 2002 resulted in profits of GBP55 million and the impact of a GBP135 million increase in provisions for redress to past purchasers of endowment and pension products, income was GBP194 million lower. Falling stock markets have increased the losses from the investment portfolio supporting the long-term assurance funds by GBP46 million and reduced the capitalised value of annual management charges by a further GBP66 million. The expected return from existing business was GBP36 million lower, reflecting the lower value of in-force business at the start of the year as a result of the reduction in stock market levels during 2001. There was also a reduction of GBP55 million in benefits from experience variances and actuarial assumption changes, largely reflecting the implementation of revised actuarial mortality assumptions which resulted in a one-off cost of GBP57 million. Despite the difficult market conditions sales of life and pensions products grew, with an improved performance in the more profitable products. This resulted in a GBP9 million or 7 per cent increase in new business profitability, after taking distribution costs into account.

Premium income from general insurance underwriting increased by GBP58 million, or 14 per cent, to GBP486 million compared to GBP428 million in 2001. There was growth of GBP69 million in premiums from home insurance products, reflecting successful cross-selling to Lloyds TSB Group's mortgage customers and the strength of the UK housing market. This has been partly offset by a further small decline in creditor insurance as this portfolio is now in run-off, following the outsourcing of the card protection book in 2000. Re-insurance premiums payable increased by GBP7 million following the decision to mitigate risks on policies with large sums assured.

Other operating income increased by GBP55 million, or 8 per cent, to GBP763 million. Increases of GBP25 million in earnings on the sale and restructuring of emerging markets debt investments and GBP111 million in operating lease rentals, largely as a result of the acquisition of First National Vehicle Holdings and Abbey National Vehicle Finance, were offset by a GBP35 million reduction in the realisation of venture capital gains by Lloyds TSB Development Capital and a reduction of GBP25 million in profits on the sale and leaseback of premises.

2001 compared with 2000

Other income reduced by GBP105 million, or 3 per cent, to GBP3,660 million representing 41 per cent of total income. Excluding the impact of the Chartered Trust acquisition made in September 2000, other income fell by GBP231 million or 6 per cent.

Fees and commissions receivable increased by GBP154 million, or 6 per cent, largely reflecting strong growth in income from insurance broking. Other UK fees and commissions increased by GBP49 million, or 4 per cent, from GBP1,171 million to GBP1,220 million mainly due to the inclusion in 2001 of fees earned by Chartered Trust which resulted in fee income from the Asset Finance business increasing by GBP45 million. There was a GBP26 million increase in fees from large corporate and factoring activity; and fee income from Lloyds TSB Group's share registration operation increased by GBP12 million. However, unit trust and asset management fees fell by GBP20 million and stockbroking income fell by GBP10 million, as a result of the substantial reduction in stock market activity in the second half of the year. Fees from the retail banking operations also fell following the withdrawal of ATM fees, which reduced income by GBP29 million, although this was partly offset by the inclusion of GBP22 million of recharges to Goldfish Bank, Lloyds TSB Group's joint venture with Centrica plc.

Insurance broking commission income increased by GBP130 million, or 33 per cent, as a result of higher levels of creditor insurance sales which increased income by GBP98 million and growth in other major product lines. There was also a benefit of GBP30 million from a one-off change in broking commission arrangements. Income from credit and debit cards increased by GBP28 million, mainly as a result of higher merchant service charges and fees. However, UK current account fee income fell by GBP56 million; a GBP28 million increase in fee income from Added Value accounts was more than offset by a GBP51 million fall in unauthorised borrowing fees and a GBP40 million reduction in service charges, as part of the Group's programme to make its customer proposition more competitive.

Fees and commissions payable increased by GBP123 million, or 26 per cent, compared to 2000 as a result of the impact of the Chartered Trust acquisition, higher reciprocity fees and an increase in package costs relating to a number of products.

Dealing profits increased by GBP35 million, or 18 per cent, to GBP233 million, reflecting benefits from opportunities created from managing certain exposures arising within the Group's insurance businesses, an improved performance from the treasury operations in London and higher foreign exchange trading income from The National Bank of New Zealand.

Income from long-term assurance business fell by GBP472 million from GBP443 million in 2000 to a loss of GBP29 million in 2001. Income from long-term assurance business in 2000 benefited from a change in the economic assumptions used to calculate the embedded value, which increased income by GBP127 million, although this was partly offset by a one-off charge of GBP80 million in respect of stakeholder pensions. Excluding these items there was an underlying decrease of GBP425 million.

There was growth in new business, in part reflecting successful sales of Lloyds TSB Group's stakeholder pension product and a change in the mix of new business to more profitable regular premium business, which after distribution costs increased income by GBP47 million. There was a GBP27 million increase in the expected return from existing business reflecting the growth in the size of the in-force book and a GBP30 million reduction in provisions for redress to past purchasers of pension policies as the review nears its completion. However these factors were more than offset by a GBP529 million reduction in the earnings from the investments held to support the life assurance operations, which were GBP259 million lower, and the capitalised value of annual management charges, which was GBP270 million lower, both largely reflecting the decline in stock market values during the year.

Premium income from insurance underwriting increased by GBP29 million, or 7 per cent, from GBP399 million to GBP428 million. This was due to higher home insurance sales during 2001, which increased by GBP53 million to GBP281 million reflecting the success of the home insurance product and improved cross-selling to Lloyds TSB Group's mortgage customers. This has more than offset a GBP16 million fall in income from creditor insurance, following the outsourcing of the card protection book to Norwich Union in 2000, and small reductions in income from other products.

Other operating income increased to GBP708 million from GBP436 million in 2000 reflecting an increase in income from operating lease rentals, partly as a result of the acquisition of Chartered Trust, from GBP151 million in 2000 to GBP329 million in 2001. Other significant contributions to other operating income were the realisation of venture capital gains within Lloyds TSB Development Capital of GBP57 million, earnings on the sale and restructuring of emerging market investments of GBP109 million and GBP57 million profit on the sale and leaseback of premises.

Operating expenses

	2002 GBPm	2001 GBPm	2000 GBPm
Administrative expenses			
Staff:			
Salaries and profit sharing	1,758	1,776	1,644
National insurance	134	140	131
Pensions	318	347	225
Restructuring	105	69	85
Other staff costs	202	221	212
	2,517	2,553	2,297
Premises and equipment:			
Rent and rates	280	261	247
Hire of equipment	18	18	26
Repairs and maintenance	131	115	115
Other	114	123	112
	543	517	500
Other expenses:			
Communications and external data processing	446	483	438
Advertising and promotion	147	154	180
Professional fees	113	110	159
Other	448	409	319

	1,154	1,156	1,096
Administrative expenses	4,214	4,226	3,893
Depreciation	642	511	364
Amortisation of goodwill	59	39	22
Total operating expenses	4,915	4,776	4,279
Efficiency ratio (in %)	55.4	53.7	48.8
Efficiency ratio (adjusted) (in %)(1)	50.3	49.0	47.9

(1) Excluding changes in economic assumptions and investment variance. (See "- Line of business information - Insurance and Investments")

2002 compared with 2001

Total operating expenses increased by GBP139 million, or 3 per cent, to GBP4,915 million compared to GBP4,776 million in 2001; acquisitions added GBP105 million to costs in 2002.

Administrative expenses of GBP4,214 million in 2002 were GBP12 million lower than in 2001. Staff costs reduced by GBP36 million or 1 per cent. Salaries and profit sharing were GBP18 million lower as the impact of the annual pay review and the effect of acquisitions during the year were more than offset by the effect of an underlying reduction of 4,191 staff (full time equivalent) and lower levels of accruals for bonuses and profit related payments. Pension costs were GBP29 million lower as an increased current service cost, reflecting the impact of changes in the mortality assumptions made at the end of 2001, and higher costs relating to staff taking early retirement, were more than offset by the non-repetition of costs of GBP82 million incurred in 2001 in relation to benefit improvements. Severance costs were GBP36 million higher at GBP105 million, but other staff costs were GBP19 million lower, reflecting a GBP22 million reduction in agency staff costs.

Premises and equipment costs were GBP26 million, or 5 per cent, higher as a result of higher rental costs on branch and head office premises, in part reflecting the sale and leaseback of a number of properties in 2001, and increased repairs and maintenance expenditure reflecting costs incurred in advance of vacating a number of central properties. This was partly offset by a reduction in other premises and equipment costs.

Other expenses reduced by GBP2 million. Communications and external data processing costs were GBP37 million lower as a result of reduced levels of expenditure on the development of the Lloyds TSB Group's e-commerce and real-time banking systems. Other costs were GBP39 million higher, reflecting the impact of acquisitions and increased charges from iPSL, Lloyds TSB Group's clearings joint venture.

Depreciation was GBP131 million, or 26 per cent, higher reflecting a GBP95 million increase in operating lease depreciation. Of this amount GBP33 million relates to the Lloyds TSB Group's existing operations, reflecting both organic growth and the non-repetition of a one-off benefit of GBP23 million recognised in 2001 in respect of certain ship leases, and GBP62 million relates to the businesses acquired during 2002. The remaining increase in the charge reflects the ongoing impact of the significant investment in computers, software and other equipment made by the Lloyds TSB Group in recent years. Goodwill amortisation increased by GBP20 million, reflecting the acquisitions made in the year.

The efficiency ratio in 2002 was 55.4 per cent compared to 53.7 per cent in 2001.

2001 compared with 2000

Total operating expenses in 2001 increased by GBP497 million, or 12 per cent, to GBP4,776 million from GBP4,279 million in 2000. Of this growth in costs, GBP145 million was due to the acquisitions of Scottish Widows and Chartered Trust and GBP16 million to costs incurred in connection with the unsuccessful offer for Abbey National.

Administrative expenses in 2001 increased by GBP333 million, or 9 per cent, from GBP3,893 million to GBP4,226 million. Staff costs grew by GBP256 million, or 11 per cent. There was a GBP132 million growth in salaries and profit sharing reflecting both the growth in staff numbers, the effect of the annual pay review, and the increased cost of incentive payments to customer facing staff. There was also a GBP122 million increase in pension costs, reflecting additional costs of GBP82 million as a result of benefit improvements in the Lloyds TSB Group's pension schemes, together with costs of GBP35 million in connection with staff taking early retirement.

Premises and equipment costs increased by GBP17 million, or 3 per cent, principally due to higher rental costs on branch and head office properties and losses on the disposal of equipment which more than offset lower IT equipment hire costs. Other costs increased by GBP60 million. There was a GBP45 million growth in communications and external data processing costs to support the development of Lloyds TSB Group's e-commerce activities and real-time banking systems. Advertising and promotion expenses were GBP26 million lower, largely due to the non-repetition of the costs incurred in 2000 in relation to the merging of the Scottish Widows and Lloyds TSB brands. Professional fees were GBP49 million lower due to lower levels of consultancy and advisory fees related to efficiency programme projects, internet banking and the assimilation of Scottish Widows into the Lloyds TSB Group. There was a GBP23 million increase in charges made by iPSL, Lloyds TSB Group's new clearings joint venture, and a GBP19 million increase in operational losses, partly caused by a higher incidence of credit card fraud.

Depreciation increased by GBP147 million, or 40 per cent. There was an increase of GBP95 million in the charge in respect of operating lease assets, following a reduction of GBP23 million in the depreciation charge on certain ship leases, of which GBP82 million was due to the acquisition of Chartered Trust. In addition, there was a GBP49 million increase in the depreciation charge in respect of equipment reflecting the impact of capital expenditure, in particular on IT equipment, during 2000. Goodwill amortisation increased by GBP17 million due to the amortisation of the goodwill arising on the acquisition of Chartered Trust.

The efficiency ratio in 2001 was 53.7 per cent compared to 48.8 per cent in 2000.

Charge for bad and doubtful debts

	2002	2001	2000
	GBPm	GBPm	GBPm

UK Retail Banking and Mortgages	563	415	332
Wholesale Markets and International Banking	473	338	228
Central group items	(7)	(6)	(19)
Total charge	1,029	747	541
Specific provisions	965	736	547
General provisions	64	11	(6)
Total charge	1,029	747	541
Charge as % of average lending:	%	%	%
Domestic	0.70	0.54	0.45
International	1.28	1.10	0.80
Total charge	0.77	0.62	0.50

2002 compared with 2001

The total charge for bad and doubtful debts increased by GBP282 million, or 38 per cent, to GBP1,029 million from GBP747 million in 2001. In UK Retail Banking and Mortgages the provisions charge increased by GBP148 million, from GBP415 million in 2001, to GBP563 million, as a result of asset growth in the personal loan and credit card portfolios and a lower level of recoveries and releases, following the non-recurrence of the release of surplus provisions in 2001.

In Wholesale Markets and International Banking the provisions charge increased by GBP135 million, or 40 per cent, to GBP473 million from GBP338 million in 2001. The charge in respect of corporate banking operations was GBP145 million higher partly as a result of provisions against the Group's exposure to certain large US corporate customers which totalled some GBP100 million compared to GBP30 million in 2001. There was also an increase in the provisions charge against the UK corporate lending portfolio, reflecting the slowdown in activity in certain sectors of the UK economy. The charge in respect of the Lloyds TSB Group's asset finance businesses increased by GBP11 million, reflecting volume growth. There was a GBP27 million reduction in the specific provisions charge in Losango, the Lloyds TSB Group's consumer finance business in Brazil, largely reflecting exchange rate movements. The general provision against the Lloyds TSB Group's exposure to Argentina was increased by GBP50 million, compared to a charge of GBP55 million in 2001.

In Central group items there was a credit of GBP7 million, little changed from a credit of GBP6 million in 2001; these credits represent the release of provisions following the repayment of medium-term debt in the emerging markets portfolio.

2001 compared with 2000

The total charge for bad and doubtful debts increased by GBP206 million, or 38 per cent, to GBP747 million from GBP541 million. In UK Retail Banking and Mortgages, the charge increased by GBP83 million. During 2000, UK Retail Banking had a one-off benefit of GBP42 million following the full centralisation of its arrears processing, which was not repeated in 2001. Adjusting for this, provisions in UK Retail Banking increased by GBP52 million reflecting the growth in the size of the personal loan and credit card portfolios. This was partly offset by a GBP32 million release of the general provision relating to the Lloyds TSB Group's mortgage portfolio following a change in provisioning methodology.

The provisions charge in Wholesale Markets and International Banking increased by GBP110 million, or 48 per cent, although excluding the impact of the acquisition of Chartered Trust, which increased the charge by GBP27 million, provisions were GBP83 million higher. The charge against the corporate and commercial lending portfolios increased by GBP53 million largely as a result of provisions being required against a small number of corporate exposures, reflecting the slowdown in economic growth, but also as a result of a GBP30 million provision made against the Group's loans and advances to one specific corporate customer. There was an GBP18 million reduction in the provisions made against the consumer finance portfolio of Lloyds UDT reflecting improved credit procedures. Provisions overseas increased by GBP49 million, largely as a result of a GBP55 million increase in the general provision, taken as a measure of prudence, to cover ongoing credit difficulties in Argentina. Increased provisions against specific corporate exposures in Uruguay, Dubai and the Netherlands were, however, offset by improvements in Colombia and New Zealand.

In Central group items these was a credit of GBP6 million in 2001, compared to a credit of GBP19 million in 2000. The higher credit in 2000 arose following repayments of GBP15 million of Moroccan debt that had previously been provided for.

Taxation

The rate of tax is influenced by the geographic and business mix of profits. In the absence of special factors, Lloyds TSB Group does not expect the tax rate to vary significantly from the average UK corporation tax rate.

	2002 GBPm	2001 GBPm	2000 GBPm
UK corporation tax			
Current tax on profits for the year	784	769	889
Adjustments in respect of prior years	12	(14)	3
	796	755	892
Double taxation relief	(129)	(87)	(72)
	667	668	820
Foreign tax			
Current tax on profits for the year	216	179	137
Adjustments in respect of prior years	(15)	(17)	(5)
	201	162	132
Current tax charge	868	830	952
Deferred tax	(106)	44	129
Associated undertakings and joint ventures	2	1	1
Total charge	764	875	1,082

2002 compared with 2001

The effective rate of tax in 2002 was 29.3 per cent, slightly lower than the corporate tax rate of 30 per cent, compared to an effective rate of tax of 27.7 per cent in 2001. The higher effective rate of tax in 2002 is largely due to a lower level of tax relief on payments to the Lloyds TSB qualifying share ownership trust ('QUEST') to satisfy Save As You Earn options and a lower level of gains on the disposal of properties which are sheltered by capital losses. There was also a higher effective rate of tax in the Lloyds TSB Group's life and pensions businesses because of increased losses on the investment portfolio. See Note 8 to the Consolidated Financial Statements.

2001 compared with 2000

The effective rate of tax in 2001 was 27.7 per cent compared with 28.6 per cent in 2000; the corporation tax rate for both years was 30 per cent. The lower effective tax rate in 2001 is largely due to tax relief on payments to the QUEST which reduced the effective rate by 1.9 per cent and gains on the disposal of investments and properties sheltered by capital losses which reduced the effective rate by 1.2 per cent; offset by the impact of different overseas tax rates which increased the effective rate by 0.4 per cent.

Economic profit

In pursuit of our aim to maximise shareholder value over time, management has for the last eleven years used a system of value based management as a framework to identify and measure value creation. Management uses economic profit as a measure of performance because it captures both growth in investment and return. Lloyds TSB Group defines economic profit as the earnings on the equity invested in the business less a notional charge for the cost of the equity invested in that business.

Lloyds TSB Group believes that economic profit instils financial discipline in determining investment decisions throughout Lloyds TSB Group and that it enables Lloyds TSB Group to evaluate alternative strategies objectively, with a clear understanding of the value created by each strategy, and then to select the strategy which creates the greatest value. Awards to senior executives under Lloyds TSB Group's annual bonus arrangements are partly determined by the achievement of economic profit targets.

Management only changes its estimates of the cost of equity to reflect significant changes in long-term interest rates and other external market factors which are considered sustainable. The principal factor in estimating the cost of equity is sustainable long-term interest rates. If long-term interest rates increase, management will consider raising its estimate of the cost of equity; if long-term interest rates fall, management will consider reducing its estimate of the cost of equity. The principal other external market factors considered are equity risk premium and Lloyds TSB Group's share price volatility relative to the UK stock market as a whole. Any change to the estimated cost of equity will be disclosed. For the last three years, management has used a cost of equity of 9 per cent to reflect the shareholders' minimum required rate of return on equity invested.

The table below summarises Lloyds TSB Group's calculation of economic profit for the periods indicated.

	2002	2001	2000
	GBPm	GBPm	GBPm
Average shareholders' equity	10,672	12,338	12,551
Profit attributable to shareholders	1,781	2,229	2,654

Less: notional charge	(960)	(1,110)	(1,130)
Economic profit	821	1,119	1,524

The notional charge has been calculated by multiplying average shareholders' equity by the cost of equity.

2002 compared with 2001

Economic profit fell by GBP298 million or 27 per cent from GBP1,119 million in 2001 to GBP821 million in 2002. Profit attributable to shareholders fell by GBP448 million (20 per cent) to GBP1,781 million, however the notional charge on average equity was GBP150 million lower, as a result of a 14 per cent fall in average equity to GBP10,672 million from GBP12,338 million in 2001.

2001 compared with 2000

Economic profit fell by GBP405 million, or 27 per cent, from GBP1,524 million in 2000 to GBP1,119 million in 2001. Profit attributable to shareholders fell by GBP425 million (16 per cent) to GBP2,229 million but there was a slightly lower notional charge on equity resulting from a 2 per cent fall in average equity from GBP12,551 million to GBP12,338 million.

Line of business information

Summary

In order to provide a clearer representation of the underlying performance, the results of the Insurance and Investments segment include investment earnings calculated using longer-term rates of return and annual management charges based on unsmoothed fund values. Management separately analyse the difference between these normalised earnings and the actual return ("the investment variance") together with the impact of changes in the economic assumptions used in the embedded value calculation. The results of the business units are set out below:

	2002 GBPm	2001 GBPm	2000 GBPm
UK Retail Banking and Mortgages	1,172	1,205	1,363
Insurance and Investments	1,231	1,421	1,158
Wholesale Markets and International Banking	1,005	1,209	1,035
Central group items	96	185	378
	3,504	4,020	3,934
Changes in economic assumptions	55	-	127
Investment variance	(952)	(859)	(276)
Profit before tax	2,607	3,161	3,785

UK Retail Banking and Mortgages

The UK retail businesses of Lloyds TSB Group provide banking and financial services to personal and small business customers, private banking and stockbroking. Lloyds TSB Group's UK mortgage business is conducted through Cheltenham & Gloucester, Lloyds TSB Bank, Lloyds TSB Scotland, Scottish Widows Bank and C&G TeleDirect.

	2002 GBPm	2001 GBPm	2000 GBPm
Net interest income	3,340	3,102	2,951
Other income	1,076	1,135	1,143
Total income	4,416	4,237	4,094
Operating expenses	(2,670)	(2,607)	(2,401)
Trading surplus	1,746	1,630	1,693
Provisions for bad and doubtful debts	(563)	(415)	(332)
Income from joint ventures	(11)	(10)	2
Profit before tax	1,172	1,205	1,363
Efficiency ratio	60.5%	61.5%	58.6%
Total assets (year-end)	GBP85,868m	GBP77,982m	GBP71,292m
Total risk-weighted assets (year-end)	GBP54,157m	GBP48,220m	GBP44,009m

2002 compared with 2001

Profit before tax from UK Retail Banking and Mortgages decreased by GBP33 million, or 3 per cent, to GBP1,172 million, compared with GBP1,205 million in 2001.

Total income increased by GBP179 million, or 4 per cent, to GBP4,416 million. Net interest income increased by GBP238 million, or 8 per cent, to GBP3,340 million. Growth in lending and deposit balances added GBP266 million to net interest income, which was only partly offset by a reduction of GBP28 million caused by a reduction of 4 basis points in the overall margin. Since 31 December 2001, personal loans and credit card lending increased by 15 per cent and 27 per cent respectively and, within Retail Banking, balances on current accounts and savings and investment accounts grew by 10 per cent. Mortgage balances outstanding increased by 10 per cent to GBP62,467 million representing a market share of 9.3 per cent. Gross new mortgage lending increased by 36 per cent to GBP19,039 million, compared with GBP13,986 million a year ago. Net new lending increased to GBP5,889 million resulting in a market share of net new lending of 7.5 per cent; the Lloyds TSB Group's market share of net new lending in the second half of 2002, at 8.8 per cent, was considerably better than in the first half of the year. Mortgages offer the Lloyds TSB Group the opportunity to sell a range of additional products and, during 2002, the Lloyds TSB Group's key objective in the mortgage business has been to achieve an appropriate balance between market share and profitability.

The net interest margin fell by 4 basis points, reducing net interest income by GBP28 million. The margin on retail lending products was 17 basis points higher than in 2001, with improved business banking overdraft and personal loan margins. Margins on personal overdrafts and credit card lending fell, but volume growth in these products resulted in a positive impact on the overall lending margin, since these relatively high margin portfolios now represent a higher proportion of the retail lending portfolio. The retail deposit margin was 16 basis points lower as the full impact of interest rate reductions in the second half of 2001 has not been reflected in the rate of interest paid on some savings products and the benefit of interest-free and low interest current accounts has been reduced. The margin on mortgage lending fell by 20 basis points.

Other income decreased by GBP59 million, or 5 per cent, to GBP1,076 million. There was an improvement in income earned from credit and debit cards, and increased income from added value current accounts, but this was offset by a higher level of fees and commissions payable and a reduction of GBP57 million in profits from the sale and leaseback of premises, as the Group's strategy of converting much of its branch portfolio from freehold tenure to leasehold is almost complete.

Operating expenses were GBP63 million, or 2 per cent, higher at GBP2,670 million compared to GBP2,607 million in 2001. Costs associated with the Lloyds TSB Group's efficiency programme totalled GBP197 million compared to GBP151 million in 2001, an increase of GBP46 million, as the Lloyds TSB Group continues to invest in initiatives to enhance Retail Banking performance and rationalise software and systems. There were also increased costs relating to the implementation of the Lloyds TSB Group's business banking strategy and staff costs within the Mortgages business increased as additional staff were taken on in order to maintain customer service levels in the expanding portfolio. These increases and the effect of annual pay awards were partly offset by reduced headcount in the branch network and lower development costs in respect of internet banking and other initiatives. The efficiency ratio, however, improved to 60.5 per cent from 61.5 per cent in 2001.

Provisions for bad and doubtful debts were GBP148 million, or 36 per cent, higher at GBP563 million, compared to GBP415 million in 2001, as a result of volume related asset growth in the personal loan and credit card portfolios and a lower level of recoveries and releases following the non-recurrence of the release of surplus provisions of GBP72 million in 2001. Excluding these provision releases, the charge as a percentage of average lending for personal loans and overdrafts decreased to 3.73 per cent from 3.88 per cent in 2001, and the charge in the credit card portfolio decreased to 3.52 per cent from 3.60 per cent in 2001. Overall the arrears position remained stable.

Lloyds TSB Group's share of the results of its joint venture operations was a loss of GBP11 million, little changed from 2001.

2001 compared with 2000

The profit before tax from UK Retail Banking and Mortgages in 2001 fell by GBP158 million, or 12 per cent, to GBP1,205 million.

Total income increased by GBP143 million, or 3 per cent to GBP4,237 million. Net interest income increased by GBP151 million to GBP3,102 million as growth in lending and savings balances, adding GBP241 million to income, more than offset a 14 basis point fall in the margin, reducing net interest income by GBP90 million. Compared to 2000, period end personal loan and credit card balances increased by 18 per cent and balances on current accounts and savings and investment accounts grew by 9 per cent. Mortgage balances also increased; gross new mortgage lending increased by 21 per cent to GBP13,986 million compared with GBP11,518 million in 2000, however net new lending was GBP3,919 million compared to GBP4,627 million in 2000. This resulted in a fall in Lloyds TSB Group's estimated market share of net new lending from 11.3 per cent to 7.2

per cent. Mortgage balances outstanding at the end of 2001 amounted to GBP56,578 million compared to GBP52,659 million at the end of 2000, an estimated market share of 9.5 per cent. The net interest margin was little changed.

The net interest margin on retail lending products was 6 basis points lower, with improved margins on credit cards and overdrafts following base rate cuts, offset by lower margins on personal loans due to a combination of a higher proportion of lending being at concessionary rates offered to attract new business and higher average loan values which are provided at lower interest rates. The retail deposit margin fell by 25 basis points as the lower interest rate environment reduced the benefit from low interest rate and interest-free current accounts. The margin on mortgage lending reduced by 1 basis point.

Other income decreased by GBP8 million, or 1 per cent, to GBP1,135 million. There was a GBP21 million improvement in income earned from credit and debit cards and income from added value current accounts increased by GBP19 million due to increased volumes. In 2001, profits on the sale and leaseback of premises totalled GBP57 million reflecting Lloyds TSB Group's ongoing strategy, started some years ago, to sell and lease back a number of branches to create greater flexibility in the changing environment for retail sales. This was largely offset by a GBP76 million decrease in income following the withdrawal of ATM fees and planned reductions in unauthorised borrowing fees; stockbroking income fell by GBP10 million due to lower transaction volumes.

Operating expenses increased by GBP206 million, or 9 per cent, to GBP2,607 million compared to GBP2,401 million in 2000. Costs associated with the Group's efficiency programme totalled GBP151 million, compared to GBP78 million in 2000. The increase of GBP73 million reflects investment in customer management and handling systems and costs related to the reassessment of software used in the internet banking and wealth management businesses. There was an increase in staff costs reflecting the growth in staff numbers during the year as a result of the recruitment of additional service and sales staff into the branch network and the effect of the annual pay review. Communications costs were higher following revisions to network rental charges and the depreciation charge increased reflecting the high levels of capital expenditure, particularly in respect of IT equipment, in 2000. The efficiency ratio increased from 58.6 per cent in 2000 to 61.5 per cent in 2001.

Provisions for bad and doubtful debts increased by GBP83 million, or 25 per cent, to GBP415 million. During 2000 there was a benefit of GBP42 million as a result of a change in provisioning methodology following the centralisation of arrears processing. If this is adjusted for there was an underlying increase of GBP52 million in the provisions charge against personal and credit card lending, reflecting the growth in the size of the portfolios. There was a net release from the provisions held against the mortgage portfolio of GBP24 million as a result of a GBP32 million reduction in the general provision following a change in provisioning methodology; in 2000 there was a net release of provisions of GBP13 million.

Lloyds TSB Group's share of the results of its joint venture operations was a loss of GBP10 million, due to start-up costs incurred by Goldfish Bank.

Insurance and Investments

Lloyds TSB Group's insurance and investments activities comprise the life, pensions and unit trust businesses of Scottish Widows and Abbey Life, general insurance underwriting and broking, and Scottish Widows Investment Partnership.

	2002 GBPm	2001 GBPm	2000 GBPm
Net interest income	74	80	88
Other income	1,876	2,006	1,673
Total income	1,950	2,086	1,761
Operating expenses	(490)	(491)	(462)
Trading surplus	1,460	1,595	1,299
General insurance claims	(229)	(174)	(142)
Income from joint ventures	-	-	1
Operating profit	1,231	1,421	1,158
Changes in economic assumptions	55	-	127
Investment variance	(952)	(859)	(276)
Profit before tax	334	562	1,009

2002 compared to 2001

The operating profit from Insurance and Investments, calculated as explained under "- Line of business information - Summary", at GBP1,231 million, was GBP190 million, or 13 per cent, lower than 2001.

Net interest income was GBP6 million, or 8 per cent, lower at GBP74 million, compared to GBP80 million in 2001, largely reflecting the impact of lower interest rates on the cash balances held in the general insurance business.

Other income was GBP130 million, or 6 per cent, lower at GBP1,876 million, compared to GBP2,006 million in 2001. Income from the long-term assurance businesses, excluding changes in economic assumptions and investment variance, was GBP245 million lower. New business income was GBP40 million higher, as a result of sales growth, but this was partly offset by a GBP28 million increase in distribution costs. The expected return on existing business reduced by GBP34 million, partly reflecting the lower average volume of in-force business caused by the fall in the stock market in 2001, and investment earnings were GBP33 million lower, as a result of the reduction in the value of the investments supporting the long-term assurance funds. Following a review carried out in conjunction with the Financial Services Authority into past sales made by the Abbey Life sales force, a provision of GBP165 million was established in 2002 for the estimated cost of redress due to customers. See "- Business - Customer remediation payments - Mortgage endowment and other savings products". In addition a further provision of GBP40 million was made in respect of compensation payable to past purchasers of pension policies, compared to GBP70 million in 2001; this review is now substantially complete. See "- Business - Customer remediation payments - Redress to past purchasers of pension policies". There was a reduction of GBP55 million in benefits from experience variances and actuarial assumption changes, largely reflecting the implementation of revised mortality assumptions which resulted in a one-off charge of GBP57 million. Fee income from the unit trust and asset management businesses fell by GBP59 million, reflecting the continued fall in the level of stock markets during 2002. This more than offset an increase in premium income from general insurance underwriting which was GBP58 million higher, as a result of strong growth in home products; commissions from insurance broking were GBP119 million higher, with continued growth in creditor insurance products.

Operating expenses, at GBP490 million, were down slightly from GBP491 million in 2001. Cost reductions resulting from lower levels of sales and marketing activities in the unit trust and asset management operations have been largely offset by higher client service costs and increased costs in the general insurance business, to manage the significant increase in volumes.

General insurance claims were GBP55 million, or 32 per cent, higher at GBP229 million compared to GBP174 million in 2001. The increase in claims reflects the significant growth in the size of the underwritten portfolio together with higher claims due to flood and storm damage during the early part of 2002.

2001 compared to 2000

The operating profit from Insurance and Investments in 2001, calculated as explained under "- Line of business information - Summary" increased by GBP263 million, or 23 per cent, to GBP1,421 million from GBP1,158 million.

33

Net interest income, at GBP80 million, was GBP8 million, or 9 per cent, lower than in 2000. The reduction in income is primarily a reflection of lower market interest rates reducing the earnings on the cash deposits held by the general insurance business.

Other income was GBP333 million, or 20 per cent, higher at GBP2,006 million, compared to GBP1,673 million in 2000. Income from the long-term assurance businesses, excluding changes in economic assumptions and investment variance, was GBP204 million higher. New business income was GBP64 million, or 22 per cent, higher at GBP358 million following a 41 per cent increase in weighted sales, primarily as a result of the inclusion of Scottish Widows for a full year, compared to only ten months in 2000; however this was partly offset by a GBP25 million increase in distribution costs reflecting the growth in sales. The expected return from existing business was GBP20 million higher, as a result of portfolio growth during 2001. There was a GBP30 million reduction in provisions for redress to past purchasers of pension policies (see "- Business - Customer remediation payments - Redress to past purchasers of pension policies") and a further GBP80 million benefit from the non-repetition of a one-off charge in 2000 related to stakeholder pensions. Investment earnings were GBP35 million higher reflecting the inclusion of Scottish Widows for a full year.

General insurance underwriting premiums were GBP29 million, or 7 per cent, higher, as strong growth in home protection products more than offset reduced creditor insurance income and general insurance broking commissions were GBP130 million higher with particular growth in creditor insurance products, following the decision to outsource the underwriting of this portfolio in 2000. This was partly offset by a decrease in unit trust and asset management fees which fell by GBP20 million, as a result of the substantial fall in the level of stock market activity in the second half of 2001.

Operating expenses were GBP29 million, or 6 per cent, higher at GBP491 million compared to GBP462 million in 2000, reflecting the inclusion of costs in respect of Scottish Widows' non-life businesses for a full year compared to ten months in 2000 and higher costs in the general insurance business to support portfolio growth.

General insurance claims, at GBP174 million, were GBP32 million, or 23 per cent, higher than in 2000. The increase reflected higher property claims in line with rising volumes of new business, only partly offset by lower creditor insurance claims.

Area of business

	2002 GBPm	2001 GBPm	2000 GBPm
Life, pensions and unit trusts:			
Scottish Widows	573	585	433
Abbey Life	(98)	175	127
	475	760	560
General Insurance	754	651	574
Scottish Widows Investment Partnership	2	10	24
Operating profit	1,231	1,421	1,158
Changes in economic assumptions	55	-	127
Investment variance	(952)	(859)	(276)
Profit before tax	334	562	1,009

2002 compared with 2001

The operating profit from life, pensions and unit trusts decreased by GBP285 million, or 38 per cent, from GBP760 million in 2001 to GBP475 million in 2002. Operating profit at Scottish Widows was GBP12 million lower at GBP573 million, compared to GBP585 million in 2001. Life and pensions new business income increased by GBP40 million, or 11 per cent, to GBP398 million, following a 7 per cent increase in weighted sales and a change in mix towards more profitable products. See "- Line of business information - Life, pensions and unit trusts operating profit". Income from life and pensions existing business was GBP38 million higher, principally reflecting a GBP40 million reduction in provisions for redress to past purchasers of pension policies. See "- Business - Customer remediation payments - Redress to past purchasers of pension policies". Investment earnings were GBP27 million lower, reflecting reduced asset values at the start of 2002, and life and pensions distribution costs rose GBP28 million, in line with sales. Unit trust profits were GBP35 million lower reflecting lower sales and reduced management income, both as a result of adverse stock market conditions.

Abbey Life's operating profit reduced by GBP273 million to a loss of GBP98 million in 2002. This reduction in profitability principally reflected a GBP165 million provision for redress to past purchasers of endowment policies (see "- Business - Customer remediation payments - Mortgage endowment and other savings products"), together with reduced expected return from existing business and investment earnings as a result of lower asset levels at the start of 2002 and a reduction in benefits from experience variances and actuarial assumption changes, which were GBP73 million lower, as a number of one-off benefits in 2001 were not repeated.

The operating profit from the general insurance businesses increased by GBP103 million or 16 per cent, to GBP754 million from GBP651 million in 2001. Profit from the broking business was GBP126 million higher as a result of increases in commission income, particularly in respect of creditor products, and higher levels of retrospective commissions. However, there was a GBP23 million reduction in operating profits from the underwriting business as a result of an increase in weather related claims following floods and storms early in 2002 and increased distribution and administration expenses, as a result of higher transaction volumes. See "- Line of business information - General Insurance".

Operating profit from Scottish Widows Investment Partnership ("SWIP") was GBP2 million, compared to GBP10 million in 2001, the reduction in profitability being driven primarily by lower stock market levels and significant investment in new infrastructure to support future business growth. At the end of the year SWIP had some GBP70,000 million of funds under management compared to GBP78,000 million at the end of 2001; the decline reflects the continued fall in stock market levels.

2001 compared with 2000

The operating profit from Lloyds TSB Group's life, pensions and unit trusts businesses increased by GBP200 million, or 36 per cent, to GBP760 million. Operating profit from Scottish Widows was GBP152 million higher at GBP585 million, principally reflecting the inclusion of the acquired Scottish Widows business for a full year, compared with only ten months in 2000, together with the non-repetition of a one-off charge of GBP80 million made in 2000 in respect of stakeholder pensions. The market for medium and long-term investments was adversely affected in the second half of 2001, as a consequence of the events of September 11 and the general decline in global stock markets. However, weighted sales (regular premiums plus one-tenth single premiums) increased by 12 per cent helped by the inclusion of Scottish Widows for the full twelve months. See "- Line of business information - Life, pensions and unit trusts operating profit". Operating profit from Abbey Life, at GBP175 million, was GBP48 million higher than in 2000. This increase in profits reflects a GBP28 million lower charge for provisions for redress to past purchasers of pension policies and increased benefits from experience variances and actuarial assumption changes, only partly offset by a reduction in the expected return from existing business and investment earnings as the closed business begins to run down.

The operating profit from general insurance operations increased by GBP77 million, or 13 per cent, to GBP651 million. There was continued growth in sales of card and loan protection products which resulted in an GBP86 million improvement in profits from broking activities, although there was a GBP9 million reduction in profits from the underwriting business following a 23 per cent increase in claims expense due to higher property claims. See "- Line of business information - General Insurance".

During 2001 Scottish Widows Investment Management and Hill Samuel Asset Management were fully integrated into Scottish Widows Investment Partnership ('SWIP'). A complete overhaul of the management structure has also been undertaken, together with a fundamental review of investment philosophy, processes and systems. The operating profit from SWIP in 2001 was GBP10 million compared to GBP24 million in 2000, the reduction in profitability being partly driven by lower stock market levels. At the end of 2001 SWIP had some GBP78,000 million of funds under management compared to some GBP87,000 million at 31 December 2000. The decline has been primarily caused by the lower stock market levels experienced in 2001.

Changes in economic assumptions

Lloyds TSB Group accounts for the value of the shareholder's interest in the long-term assurance business using the embedded value basis of accounting. The embedded value comprises the net tangible assets of the life assurance subsidiaries and the present value of the in-force business. The present value of the in-force business is calculated by projecting future surpluses and other net cash flows attributable to the shareholder and discounting the result at a rate which reflects the shareholder's overall risk premium.

When projecting future surpluses and other net cash flows Lloyds TSB Group makes a series of assumptions about long-term economic conditions. In the past these assumptions were only updated infrequently for changes that were considered sustainable. In order to achieve greater comparability with other listed insurers in the UK, in 2002 the Lloyds TSB Group changed its practice and in future will revise these assumptions at each reporting date.

The economic assumptions have been revised at 31 December 2002 as follows:

	2002 %	2001 %
Risk-adjusted discount rate (net of tax)	7.35	8.50
Return on equities (gross of tax)	7.10	8.00
Return on fixed interest securities (gross of tax)	4.50	5.25
Expenses inflation	3.30	3.00

The revised assumptions have resulted in a net credit to the profit and loss account in 2002 of GBP55 million.

The economic assumptions were last reviewed following the acquisition of Scottish Widows in March 2000 to ensure that they remained appropriate for the enlarged life and pensions business. As a result of this review changes were made to the assumptions used by Abbey Life and the bancassurance business of Lloyds TSB in order to make the assumptions used by these businesses consistent with those used by Scottish Widows. The risk adjusted discount rate was reduced from 10.00 per cent to 8.50 per cent and the assumed gross return on equities was reduced from 8.50 per cent to 8.00 per cent leading to a credit of GBP127 million being recognised in the profit and loss account in 2000.

Investment variance

In accordance with generally accepted accounting practice in the UK, it is Lloyds TSB Group's accounting policy to carry the investments comprising the reserves held by its life companies at market value. The reserves held to support the with-profits business of Scottish Widows are substantial and changes in market values will result in significant volatility in the Group's embedded value earnings, which are beyond the control of management. Consequently, in order to provide a clearer representation of the underlying performance, the results of the life and pensions business are separately analysed to show an operating profit including investment earnings calculated using longer-term investment rates of return, and annual management charges based on unsmoothed fund values. The investment variance represents the difference between the actual investment return in the year on investments backing shareholder funds and the expected return based upon the economic assumptions made at the beginning of the year, and the effect of these fluctuations on the value of in-force business. The effects of other changes in economic circumstances beyond the control of management are also reflected in the investment variance. A similar approach has been adopted for Lloyds TSB Group's general insurance business.

In 2002, there was a negative investment variance of GBP952 million (2001: GBP859 million; 2000: GBP276 million) reflecting in particular the poor performance of the UK stock market, where the FTSE All-Share index fell by 24 per cent.

Life, pensions and unit trusts operating profit

The operating profit of the life, pensions and unit trust businesses is analysed in the following table. The basis of this analysis is as follows: The life and pensions results are split into four elements:

* New business: this represents the value recognised at the end of each financial year from the new business written during that year after taking into account the cost of establishing technical provisions and reserves. This is shown before the significant costs of acquiring that new business, which are shown separately as "Distribution costs".

* Existing business: this comprises the following elements:

  - the expected return arising from the unwinding of the discount applied to the expected cash flows at the beginning of a year;

  - experience variances caused by differences between the actual experience during the year and the expected experience;

  - the effects of changes in assumptions, other than economic assumptions, and other items; and

  - provisions for redress to past purchasers of pension and endowment policies and, in 2000, a stakeholder pension related charge.

* Investment earnings: this represents the expected investment return on both the net tangible assets and the value of the shareholder's interest in the long-term business account, based upon the economic assumptions made at the beginning of the year.

* Distribution costs: the costs of acquiring the new business generated in the year. These comprise the cost of selling products through Lloyds TSB Bank's branch network, the commissions paid to independent financial advisors and the costs of other direct sales channels.

Unit trust income is shown before the acquisition costs of new business which are separately disclosed.

36

	2002 GBPm	2001 GBPm	2000 GBPm
New business	398	358	294
Existing business:			
- expected return	273	307	287
- experience variances	(1)	37	36
- assumption changes and other items	78	95	96
- provisions for redress to past purchasers of pension policies	(40)	(70)	(100)
- provision for redress to past purchasers of endowment policies	(165)	-	-

- stakeholder pension related charge	-	-	(80)
	145	369	239
Investment earnings	214	247	212
Life and pensions distribution costs	(283)	(255)	(230)
	474	719	515
Unit trusts	90	141	156
Unit trust distribution costs	(89)	(100)	(111)
	1	41	45
Operating profit of life, pensions and unit trusts	475	760	560
Changes in economic assumptions	55	-	127
Investment variance	(892)	(813)	(249)
(Loss) profit before tax	(362)	(53)	438

The table below shows the level of new business premium income and unit trust sales. Management monitor these figures because they provide an indication of both the rate of growth and the profitability of the business.

	2002 GBPm	2001 GBPm	2000 GBPm
New business premium income and unit trust sales:			
Regular premiums	286.3	282.0	156.9
Single premiums	3,089.0	2,741.0	2,376.1
Unit trusts - regular premiums	71.5	65.0	91.0
- single premiums	1,009.5	1,335.5	1,902.3
Total unit trusts	1,081.0	1,400.5	1,993.3

Weighted sales is a UK insurance industry standard which measures the new business volumes; the weighting is made towards regular premium policies to reflect the long-term nature of these contracts. There are three main distribution channels for the sale of Lloyds TSB Group's life, pension and unit trust products and the table below shows the relative importance of each.

	2002 GBPm	2001 GBPm	2000 GBPm
Weighted sales (regular + 1/10 single) by distribution channel:			
Branch network	350.6	376.2	353.3
Independent financial advisors	348.5	279.8	254.9
Direct	68.5	98.7	67.6
	767.6	754.7	675.8

2002 compared with 2001

The operating profit, calculated as explained under "- Line of business information - Summary" of the life, pensions and unit trust businesses in 2002 was GBP475 million, compared to GBP760 million in 2001, a decrease of GBP285 million, or 38 per cent.

New business income from the life and pensions businesses was GBP40 million, or 11 per cent, higher at GBP398 million. This 11 per cent increase in profits reflects a 7 per cent increase in weighted sales from life and pensions products, and an improved performance in the more profitable life products. The life and pensions new business margin, defined as new business income less distribution costs divided by weighted sales, improved to 19.3 per cent from 18.5 per cent in 2001. The improvement largely arose from an improved product mix, as a result of the growth in sales of higher margin term assurance and regular premium life products. Distribution costs increased by GBP28 million, or 11 per cent, to GBP283 million from GBP255 million partly due to the growth in weighted sales but also because of the increasing proportion of sales made through independent financial advisors.

Regular premium sales, at GBP286.3 million, were GBP4.3 million, or 2 per cent, higher than 2001. Regular premium mortgage-related product sales, providing life cover on repayment mortgages, were GBP10.3 million higher as a result of the buoyant housing market in the UK and successful cross-selling to mortgage customers in the branch network. Sales of non-mortgage related life products were also higher reflecting strong sales of term assurance products following a number of sales initiatives in the branch network. These increases, however, were partly offset by a GBP20.1 million reduction in sales of regular premium pension products. Sales of the stakeholder pension product have been strong since the launch in April 2001, as the lower charges on this product continue to make it attractive; however this growth has been more than offset by reduced sales of the older pension products, reflecting the less attractive charging structures and adverse stock market conditions.

Single premium sales were GBP348.0 million, or 13 per cent, higher at GBP3,089.0 million, compared to GBP2,741.0 million in 2001. Sales of single premium life products were GBP152.4 million lower, reflecting reduced sales of investment bond products which have been affected by low stock market levels and adverse press comment. Annuity sales, however, were GBP158.4 million higher; Scottish Widows have improved their position in the annuity market by maintaining rates, in the face of competitor reductions, and through the launch of a number of new products. Single premium pension sales increased by GBP342.0 million, benefiting from an increase in Department of Social Security rebates.

Overall sales of unit trust products were GBP319.5 million lower. There was a large fall in sales of equity-based Individual Savings Accounts, as a result of the continuing volatility in global stock markets throughout 2002.

Weighted sales of life and pensions and unit trust products were GBP767.6 million compared to GBP754.7 million in 2001. By distribution channel, weighted sales through the branch network have fallen by 7 per cent, with decreases in sales of life and pension products, particularly investment bond products which have been affected by low stock market levels and adverse press comment, and lower unit trust sales as a result of the depressed market conditions. Weighted sales by independent financial advisors increased by 25 per cent as a result of the strong sales of single premium stakeholder pensions and annuities products. Direct sales are down 31 per cent, partly a result of market conditions; in particular volumes of pension and annuity product sales have fallen with customers preferring to purchase these products from independent financial advisors.

Existing business earnings fell by 61 per cent to GBP145 million, from GBP369 million in 2001. The expected return from existing business was GBP34 million lower at GBP273 million. This item reflects the unwinding of the long-term discount rate applied to the expected cash flows from in-force business and the reduction reflects the lower value of in-force business at the beginning of 2002, caused by the effect of lower stock markets on annual management charges.

It is standard practice for life companies to regularly review the underlying assumptions that support the embedded value calculations, taking into account latest experience in respect of lapse rates, expense inflation, investment mix, mortality rates and other items. In 2002, there was a reduction of GBP55 million in benefits from experience variances and actuarial assumption changes, largely reflecting the implementation of revised actuarial mortality assumptions. There was a GBP30 million reduction in provisions for redress to past purchasers of pension policies, although this was more than offset by a GBP165 million provision for possible redress to past purchasers of endowment policies. These items are discussed further under "Business - Customer remediation payments - Redress to past purchasers of pension policies" and "Business - Customer remediation payments - Mortgage endowment and other savings products".

Life and pensions investment earnings, at GBP214 million, were GBP33 million, or 13 per cent, lower than in 2001. This fall reflected the lower asset level at the start of 2002, following poor stock market performance in the latter part of 2001.

Unit trust profits in 2002, at GBP1 million, were down significantly from GBP41 million in 2001. Income in the unit trusts business is derived from both initial charges at the point of sale and annual management fees, the latter being calculated as a percentage of funds managed. During 2002, unit trust income, before distribution costs, reduced by 36 per cent compared to 2001. This reduction reflects a fall in income from initial charges, following a 13 per cent fall in weighted sales, and a GBP32 million decrease in annual management fee income, as global stock market conditions have reduced the value of the funds managed. Unit trust distribution costs have fallen in line with the reduced sales.

2001 compared with 2000

The operating profit in 2001 calculated as explained under "- Line of business information - Summary", of the life, pensions and unit trust businesses increased by GBP200 million, or 36 per cent, to GBP760 million from GBP560 million.

New business income from the life and pensions businesses increased in 2001 by GBP64 million or 22 per cent, from GBP294 million to GBP358 million following a 41 per cent increase in weighted sales, primarily as a result of the inclusion of Scottish Widows for a full year, compared with only ten months in 2000. During the year, the life and pensions new business margin, defined as new business income less distribution costs divided by weighted sales, increased to 18.5 per cent from 16.2 per cent in 2000. This improvement was largely a result of cost efficiencies driven by process enhancements, which limited the increase in distribution costs to 11 per cent, together with an improved product mix.

The growth in the weighted sales of life and pensions products was mainly due to an 80 per cent increase in the sales of regular premium products from GBP156.9 million to GBP282.0 million. The inclusion of Scottish Widows for the full year compared to only ten months in 2000 added GBP17.1 million with the remainder of the growth largely due to the launch of stakeholder pension products in April 2001. During 2001, Scottish Widows became the nominated stakeholder pensions provider for a number of associations and employers which gave access to more than 46,000 employers at 31 December 2001. By the end of 2001, over 20,000 employers had already nominated Scottish Widows as their stakeholder pensions provider resulting in 837,000 employees being offered stakeholder pensions. In 2001, weighted sales of stakeholder pension products totalled GBP76 million, a market share of 15 per cent based upon management estimates.

Sales of single premium life and pensions products increased by GBP364.9 million, or 15 per cent, to GBP2,741.0 million. The inclusion of Scottish Widows for a full year accounted for GBP174.3 million of this increase, the remainder of the growth being due to higher sales of the Scottish Widows with-profits bond through the branch network distribution channel. With-profits bonds comprise a lump-sum investment into a with-profits fund of a life insurance company. With-profit bonds are designed to be low risk investments which produce growth and allow the investor to take out money when needed. The overall return on the investment varies based on the annual bonuses declared by the life insurance company each year, which in turn will depend upon the performance of its investments. During a period of considerable volatility on the world's stock markets, customers regarded this as a safer investment than unit trusts and Individual Savings Accounts (ISAs).

Existing business earnings increased by 54 per cent from GBP239 million to GBP369 million. The expected return from existing business increased by GBP20 million, or 7 per cent, to GBP307 million. This reflects the unwinding of the long-term discount rate applied to the expected cash flows from the portfolio of in-force business; the increase reflects the growth in the size of the portfolio. In 2001, changes in actuarial assumptions, together with the planned harmonisation of actuarial models between Scottish Widows and other Lloyds TSB Group companies, resulted in a benefit of GBP95 million, compared to a benefit of GBP96 million in 2000.

As explained under "Business - Customer remediation payments - Redress to past purchasers of pension policies" there was a pension provision of GBP70 million in 2001, compared to GBP100 million in 2000.

There was also a stakeholder pension related charge of GBP80 million in 2000. During 1999, the UK government had announced changes intended to encourage more of the population to provide retirement income for themselves through increased rates of private savings. One of these initiatives was the introduction of stakeholder pensions with effect from April 2001. Stakeholder pensions are intended to provide a source of low cost retirement savings for individuals earning enough to be able to afford to make contributions towards a pension but not currently doing so. A key feature of these products is that charges are transparent and limited to 1 per cent per annum, which was significantly lower than historic charging rates on other personal pension products. In common with other pension providers in the UK, Scottish Widows introduced a stakeholder pension product in April 2001. In anticipation of this, in order not to disadvantage existing pensions customers, Lloyds TSB Group decided during 2000 to reduce charges made on certain existing policies. This had the effect of reducing the projected cash flows in Lloyds TSB Group's embedded value calculation, resulting in the charge to the profit and loss account.

Investment earnings in 2001, before taking into account investment variance, increased by GBP35 million, or 17 per cent, due to the inclusion of Scottish Widows for the full year and the growth in the size of the investment portfolio supporting the business.

Profits from the unit trust business fell by GBP4 million, to GBP41 million. Continued customer focus upon the Scottish Widows with-profits bond and uncertainty created by global stock market volatility resulted in a 29 per cent fall in weighted sales. However, this was only partly reflected in the decline in profitability of the business because of the income earned from fees charged for managing customers' funds invested in earlier years.

General Insurance

The following table shows premium income from underwriting and commission income from insurance broking.

	2002 GBPm	2001 GBPm	2000 GBPm
Premium income from underwriting			
Creditor	107	110	126
Home	350	281	228
Health	44	45	50
Reinsurance premiums	(15)	(8)	(5)
	486	428	399
Commissions from insurance broking			
Creditor	426	323	225
Home	44	41	34
Health	17	22	19
Other	160	142	120
	647	528	398
Operating profit	754	651	574
Investment variance	(60)	(46)	(27)
Profit before tax	694	605	547

39

2002 compared with 2001

The operating profit, calculated as explained under "- Line of business information - Summary", from general insurance was GBP754 million in 2002, up GBP103 million or 16 per cent from GBP651 million in 2001. This comprised a profit of GBP185 million from general insurance underwriting and GBP569 million from broking activities.

The operating profit of the underwriting business, at GBP185 million, was down GBP23 million, or 11 per cent, from GBP208 million in 2001. Premium income increased by GBP58 million, or 14 per cent, to GBP486 million, principally driven by a GBP69 million increase in income from home protection products reflecting the strength of the housing market in the UK and success in cross-selling home insurance products to mortgage customers. Creditor insurance premiums were GBP3 million lower, due to the continuing impact of the outsourcing of the card protection book in 2000. Reinsurance premiums payable have increased by GBP7 million to GBP15 million, following a decision to mitigate the risks on policies with large sums assured.

Operating expenses increased in line with sales, as more staff were taken on to deal with the increased business volumes, and commissions expense increased by GBP19 million as a result of increased sales volumes and, in particular, higher levels of affinity sales.

Claims were GBP55 million, or 32 per cent, higher at GBP229 million compared to GBP174 million in 2001. The overall claims ratio at 45.7 per cent was higher than in 2001 (39.9 per cent) largely as a result of increased property claims, due to a 26 per cent growth in the home underwritten portfolio, and higher weather and flood related insurance claims.

The operating profit of the general insurance broking business, at GBP569 million, was GBP126 million, or 28 per cent, higher than GBP443 million in 2001, principally reflecting a GBP119 million increase in broking commission income to GBP647 million in 2002. Creditor insurance commissions were GBP103 million higher at GBP426 million reflecting improved penetration into the Lloyds TSB Group's personal credit portfolios, coupled with the benefit of higher volumes of personal loans and credit card outstandings. There has also been a benefit from the Lloyds TSB Group's continuing shift towards broking more general insurance business. Other commission income was GBP18 million higher as increased commissions on motor and other smaller products, together with increased levels of retrospective commissions on a number of products, more than offset the impact of the non-repetition of a one-off benefit of GBP30 million in 2001 which resulted from a change in broking arrangements.

2001 compared with 2000

The operating profit, calculated as explained under "- Line of business information - Summary", from general insurance operations, comprising both underwriting and broking activities, rose by GBP77 million, or 13 per cent, to GBP651 million in 2001.

The operating profit of the underwriting business fell in 2001 by GBP9 million, or 4 per cent, to GBP208 million. Premium income increased by GBP29 million, or 7 per cent, due to a GBP53 million increase in premium income from home insurance partly due to the successful cross-selling of this product by Cheltenham & Gloucester to its mortgage customers. This more than offset a decline of GBP16 million in income from creditor insurance caused by the transfer of the card protection book to Norwich Union in the second half of 2000. Premiums from health insurance fell by GBP5 million and reinsurance premiums increased by GBP3 million.

General insurance claims increased by GBP32 million or 23 per cent to GBP174 million. The claims ratio was 39.9 per cent compared to 35.1 per cent in 2000, reflecting higher property claims.

The operating profit of the broking business increased by GBP86 million or 24 per cent to GBP443 million due to an increase in commission income of GBP130 million. Creditor insurance sales increased by GBP98 million as a result of the growth in Lloyds TSB Group's personal lending and credit card portfolios and the success of the branch network in selling related income protection products. In addition, there was a GBP22 million increase in other commissions as a benefit of GBP30 million resulting from a one-off change in broking arrangements more than offset a fall in the level of retrospective commissions. There was a fall in investment earnings reflecting the lower interest rate environment and costs increased by GBP30 million to support the higher business volumes.

Wholesale Markets and International Banking

Lloyds TSB Group's Wholesale Markets and International Banking business comprises banking, treasury, large value lease finance, long-term agricultural finance, share registration, venture capital, factoring and invoice discounting, and other related services for major UK and multinational companies, banks and financial institutions, and medium-sized UK businesses, and other forms of asset finance. It also includes banking and financial services overseas in four main areas (the Americas, New Zealand, Europe, and Offshore Banking).

	2002 GBPm	2001 GBPm	2000 GBPm
Net interest income	1,903	1,845	1,642
Other income	1,349	1,208	998
Total income	3,252	3,053	2,640
Operating expenses	(1,717)	(1,523)	(1,363)
Trading surplus	1,535	1,530	1,277
Provisions for bad and doubtful debts	(473)	(338)	(228)
Amounts written off fixed asset investments	(57)	(22)	(14)
	1,005	1,170	1,035
Profit on sale of Lloyds TSB Asset Management S.A.	-	39	-
Profit before tax	1,005	1,209	1,035
Efficiency ratio	52.8%	49.9%	51.6%
Total assets (period-end)	GBP110,845m	GBP100,777m	GBP85,243m
Total risk-weighted assets (period-end)	GBP67,156m	GBP58,634m	GBP48,161m

2002 compared with 2001

The profit before tax of Wholesale Markets and International Banking decreased by GBP204 million, or 17 per cent, to GBP1,005 million in 2002 from GBP1,209 million in 2001. The acquisition during the year of First National Vehicle Holdings, Abbey National Vehicle Finance and the Dutton-Forshaw Group had a significant impact on the trends in income and expenses within Wholesale Markets and International Banking. In 2002 these acquisitions contributed GBP101 million of income, and GBP102 million of operating expenses, including goodwill amortisation of GBP3 million, resulting in a loss before tax of GBP1 million.

Total income increased by GBP199 million, or 7 per cent, to GBP3,252 million. Excluding the impact of acquisitions, total income was GBP98 million, or 3 per cent, higher. Net interest income was GBP58 million higher at GBP1,903 million. Growth in interest-earning assets more than offset a 25 basis point reduction in the net interest margin and the effect of adverse exchange rate movements, which reduced net interest income by GBP116 million.

Total assets were GBP10,068 million, or 10 per cent, higher at GBP110,845 million. Of this increase, some GBP4,700 million resulted from a growth in debt securities within Wholesale Markets, reflecting an increase in the Lloyds TSB Group's portfolio of asset backed securities, most of which are triple A rated. The portfolio allows the Lloyds TSB Group to provide a securitised asset funding service for its corporate clients (see "- Operating and Financial Review and Prospects - Liquidity and Capital Resources"), and to participate in structured deals with a limited number of global financial institutions. The high level of growth in the portfolio largely reflects the development of the Lloyds TSB Group's capability in this market and, having now achieved a meaningful presence, it is not intended that recent rates of portfolio growth will continue into 2003 and beyond. Customer lending balances increased by some GBP2,600 million with growth in lending to large corporates and asset finance balances as these businesses have sought to grow their balance sheets. There was an increase in interbank lending of some GBP2,400 million mainly as a result of deposits made by the Lloyds TSB Group's Treasury department in London as part of its liquidity management activities. Within International Banking, total assets increased by GBP372 million as strong growth in New Zealand, where total assets increased by GBP2,370 million in sterling terms, was largely offset by reductions in the Lloyds TSB Group's exposure to Brazil and Argentina.

Other income increased by GBP141 million, or 12 per cent, to GBP1,349 million. Operating lease rentals were GBP111 million higher; of this growth GBP83 million was due to the acquisitions made during the year, with the balance due to organic growth in the Lloyds UDT and Lloyds TSB Leasing portfolios. A higher level of insurance commission income within the asset finance business and a GBP20 million increase in corporate banking and factoring fees were offset by a GBP35 million reduction in the realisations of venture capital gains. Fee income in the company registration business was GBP6 million lower, as the exceptionally high levels of company transactions in 2001 were not repeated. Overseas, other income increased by GBP29 million mainly as a result of profits on the sale and leaseback of premises totalling GBP32 million.

Operating expenses increased by GBP194 million, or 13 per cent, to GBP1,717 million. Excluding the effect of acquisitions made during the year, the underlying increase was GBP92 million. Of this increase GBP33 million was due to increased operating lease depreciation as a result of organic growth in the Lloyds UDT and Lloyds TSB Leasing portfolios and the non-repetition of a one-off benefit of GBP23 million recognised in 2001 in respect of certain ship leases. There was increased investment spend in corporate and commercial banking activities to support business growth and increased staff and other costs in the UK asset finance businesses. Overseas, costs were little changed as increases in New Zealand, to support recent business growth, and the effect of annual pay awards and increased pension costs, were offset by favourable exchange movements.

41

Provisions for bad and doubtful debts were GBP135 million, or 40 per cent, higher at GBP473 million compared to GBP338 million in 2001. The charge in respect of corporate banking operations was GBP145 million higher following a charge of some GBP100 million in respect of certain large US corporates, caused by accounting and operational irregularities, and an increased charge from the UK corporate lending portfolio reflecting the slowdown in activity in certain sectors of the UK economy. The charge in respect of the asset finance businesses increased by GBP11 million as a result of volume growth. Within International Banking, the charge was GBP21 million lower as a result of lower specific provisions in Losango, the Lloyds TSB Group's consumer finance business in Brazil, largely reflecting exchange rate movements. There was a general provision charge of GBP50 million in relation to the Lloyds TSB Group's exposure to Argentina, compared to GBP55 million in 2001.

Amounts written off fixed asset investments were GBP35 million higher at GBP57 million. There was a GBP21 million charge following operating irregularities on one securitisation issue and a GBP21 million increase in the charge in respect of the Lloyds TSB Group's development capital business, following the significant growth in the portfolio over recent years. These increases were partly offset by the non-repetition of a charge of GBP7 million incurred in 2001, in respect of Argentine government debt instruments held within International Banking.

2001 compared with 2000

The profit before tax from Wholesale Markets and International Banking in 2001 increased by GBP174 million, or 17 per cent, to GBP1,209 million from GBP1,035 million in 2000. In 2001, the impact of Chartered Trust was a profit of GBP19 million compared to a loss of GBP20 million, after restructuring costs, during the four months of ownership in 2000.

Total income increased by GBP413 million, or 16 per cent, from GBP2,640 million to GBP3,053 million. Net interest income increased by GBP203 million to GBP1,845 million; the inclusion of Chartered Trust for a full year accounted for GBP85 million of this increase, after funding costs, giving an underlying growth of GBP118 million, or 7 per cent. This increase resulted primarily from positive interest rate management and asset growth.

Period end assets increased by GBP15,534 million, or 18 per cent, to GBP100,777 million. Of this increase, over GBP9,000 million resulted from a growth in debt securities reflecting an increase in Lloyds TSB Group's asset backed and other investment grade securities, many of which were triple A rated. A high percentage of these assets, which are very liquid and marketable, have low capital weightings and represented a profitable deployment of Lloyds TSB Group's capital at a time when margins in this area were improving. Period end lending to corporate and commercial customers increased by some GBP3,900 million as a result of a significant growth in term and money market lending and short-term lending to specialist investment funds and UK and US insurance companies. Within International Banking, period end assets grew by GBP2,559 million primarily as a result of corporate and consumer lending growth in New Zealand and Brazil.

The net interest margin was little changed. The benefits of positive interest rate management in the treasury operations in the UK and improved margins in New Zealand more than offset lower margins earned on corporate and commercial lending balances due to competitive pressures and reductions in the margin in Brazil. Adverse exchange rate movements, mainly in Brazil, reduced net interest income by GBP59 million.

Other income increased by GBP210 million, or 21 per cent; the inclusion of Chartered Trust for a full year accounted for GBP126 million of this increase giving an underlying growth of GBP84 million, or 9 per cent. There was a GBP54 million increase in operating lease rentals from Lloyds UDT and Lloyds TSB Leasing as a result of growth in the portfolio and a GBP26 million increase in fees from large corporate activity, factoring and following the completion of a number of high quality structured finance transactions. Income from share registration activities increased by GBP12 million and dealing profits from the treasury operations improved, benefiting from opportunities created from certain exposures arising within Lloyds TSB Group's insurance businesses.

Overseas, other income decreased by GBP32 million as an increase in fee income in New Zealand of GBP10 million was more than offset by adverse exchange rate movements of GBP24 million and a reduction of GBP19 million in fee income from Lloyds TSB Group's overseas wealth management businesses, reflecting lower stock market values.

Operating expenses increased by GBP160 million, or 12 per cent; the inclusion of Chartered Trust for a full year added GBP145 million of costs giving an underlying increase of GBP15 million. Operating lease depreciation within Lloyds UDT and Lloyds TSB Leasing increased by GBP13 million, despite a GBP23 million reduction in the depreciation charge on certain ship leases. Overseas, increased operating costs in New Zealand of GBP13 million and Brazil of GBP12 million, to support higher business volumes, were more than offset by a GBP46 million benefit from exchange rate movements.

Provisions for bad and doubtful debts increased by GBP110 million, or 48 per cent; the inclusion of Chartered Trust for a full year resulted in an increase of GBP27 million giving an underlying growth of GBP83 million. The growth in the charge was mainly attributable to a GBP55 million increase in the general provision following economic difficulties in Argentina.

The charge for provisions for bad and doubtful debts relating to the corporate and commercial lending portfolios increased by GBP53 million largely as a result of new provisions required against a small number of corporate exposures. There was an GBP18 million reduction in the charge against the consumer finance portfolio of Lloyds UDT due to improved credit control procedures.

Amounts written off fixed asset investments increased by GBP8 million, or 57 per cent, following a provision of GBP7 million against the carrying value of certain Argentine government debt.

In October 2001, Lloyds TSB Group sold its Brazilian fund management and private banking business, including its subsidiary, Lloyds TSB Asset Management S.A. to Banco Itau S.A. The net asset value of the business sold was less than GBP2 million and assets under management were approximately US$2,000 million. The sale of this business did not affect Lloyds TSB Group's other Brazilian businesses.

Central group items

Included within Central group items are the costs of Lloyds TSB Group support functions, the accrual for the annual payment to the Lloyds TSB Foundations, other finance income arising on the Lloyds TSB Group's post-retirement defined benefit schemes together with the cost of any benefit augmentations in those schemes, the net earnings on that part of Lloyds TSB Group's capital base which is not required to support the operations of the business units together with earnings on the emerging markets debt investment portfolio, and other items of income and expenditure managed centrally.

	2002 GBPm	2001 GBPm	2000 GBPm
Accrual for payment to Lloyds TSB Foundations	(33)	(36)	(34)
Other finance income	165	307	424
Pension scheme benefit augmentations	-	(82)	-
Earnings on surplus capital and the emerging markets debt investment portfolio	2	63	22
Abbey National offer costs	-	(16)	-
Central costs and other unallocated items	(38)	(51)	(34)
Profit before tax	96	185	378

2002 compared with 2001

The four independent Lloyds TSB Foundations support registered charities throughout the UK that enable people, particularly disabled and disadvantaged people, to play a fuller role in society. The Foundations receive one per cent of Lloyds TSB Group's pre-tax profit averaged over three years instead of the dividend on their shareholdings. See Note 40 to the Consolidated Financial Statements. The reduction in the charge in 2002 reflected the fall in Lloyds TSB Group profits.

Other finance income at GBP165 million was GBP142 million, or 46 per cent, lower than in 2001, as a result of a reduced expected return on the pension scheme assets following the fall in their value during 2001, together with an increased charge in respect of the unwinding of the discount on the scheme liabilities. Costs of GBP82 million in 2001 in respect of benefit augmentations in the Lloyds TSB Group's main pension schemes were not repeated in 2002.

Earnings on surplus capital and the emerging markets debt investment portfolio were GBP61 million lower due to increased interest expense following issues of subordinated debt during 2002 and a reduction in the level of surplus capital because of dividend payments and increased investment in the business units. Benefits realised in 2001 of GBP30 million from changes in interest rate hedging arrangements were not repeated.

2001 compared with 2000

The increased accrual for the payment to the Lloyds TSB Foundations in 2001 reflected continued growth in the average profitability of the Lloyds TSB Group. The reduction in other finance income reflected a lower level of assets held in the Group's defined benefit pension schemes at the start of 2001, coupled with lower expectations for market returns during that year. In 2001, costs of GBP82 million were incurred in augmenting certain benefits available from the Group's defined benefit pension schemes. Earnings on surplus capital and the emerging markets debt investment portfolio were GBP41 million better than in 2000. A full year's funding cost of the consideration for the acquisition of Scottish Widows, compared to ten months in 2000, was more than offset by the gradual build-up of surplus capital and some GBP30 million of benefits to Lloyds TSB Group capital from changes in interest rate hedging arrangements.

During 2001, Lloyds TSB Group incurred costs of GBP16 million in connection with the proposed acquisition of Abbey National prior to the announcement by the Secretary of State for Trade and Industry that Lloyds TSB Group would not be permitted to proceed with an offer.

Future accounting developments

Information concerning future accounting developments is provided in Note 48 to the Consolidated Financial Statements.

UK GAAP compared with US GAAP

Under US GAAP, Lloyds TSB Group's net income for the year ended 31 December 2002 was GBP1,751 million (2001: GBP1,632 million) compared to GBP1,781 million (2001: GBP2,229 million) under UK GAAP. Reconciliations between the UK GAAP and US GAAP figures, together with detailed explanations of the accounting differences, are included in Note 48 to the Consolidated Financial Statements. Following a review of the Lloyds TSB Group's accounting treatment for derivatives held for risk management purposes, the US GAAP figures for 2001 and 2000 have been restated to reflect a revised interpretation of the accounting requirements. The effects of the restatement are set out on page F-67.

The most significant areas of difference between UK GAAP and US GAAP which affect net income are as follows:

Insurance accounting. Under UK GAAP applicable to banking groups, life assurance activities are accounted for using the embedded value basis of accounting which requires the recognition of the discounted value of the projected future net cash flows attributable to the shareholder at the point of sale. UK GAAP therefore results in a substantial proportion of the net profit accruing on a portfolio of life assurance polices being recognised at their inception. Under US GAAP income is recognised in the profit and loss account in the period in which it is earned and expenses in the period in which they are incurred. This results in a more even recognition of profit over the life of the related policies.

Goodwill and intangible assets. Under US GAAP, following the full implementation of SFAS No. 142 in 2002, goodwill is no longer amortised through the profit and loss account. Goodwill continues to be amortised under UK GAAP, however the charge in the Lloyds TSB Group's profit and loss account is relatively small since the directors have decided that it is not appropriate to amortise the goodwill that arose on the acquisition of Scottish Widows in 2000. In 2001 and earlier years, prior to the full implementation of SFAS No. 142, the US GAAP amortisation charge was significantly higher than under UK GAAP, since US GAAP then required the amortisation of the Scottish Widows goodwill balance and of the goodwill arising, under US GAAP, from the business combination of Lloyds Bank Plc and TSB Group plc in 1995. Under UK GAAP the combination of Lloyds Bank Plc and TSB Group plc was accounted for as a merger.

However, US GAAP net income is lower due to an amortisation charge in respect of customer related intangibles, the intangible assets representing the value of customer relationships associated with acquisitions, which are separately established under US GAAP.

Derivative instruments held for risk management purposes. Under UK GAAP, derivatives held for risk management purposes are accounted for on an accruals basis, in line with the underlying instruments being hedged. Under US GAAP, because Lloyds TSB Group has elected not to satisfy the more onerous hedging criteria of SFAS No. 133 'Accounting for Derivative Instruments and for Hedging Activities' in respect of derivative contracts, these instruments are treated as trading, with the unrealised mark-to-market gains and losses taken to income as they arise and the resulting assets or liabilities recorded on the balance sheet. As Lloyds TSB Group will continue to hold a significant number of derivatives which are hedge accounted under UK GAAP this means that net income and shareholders' equity under US GAAP will be subject to increased volatility.

44

Average balance sheet and net interest income

The following average balance sheet excludes the long-term assurance business assets and liabilities attributable to policyholders. The interest yields and costs for foreign office assets and liabilities are affected by Lloyds TSB Group's operations in Latin America. The countries in which Lloyds TSB Group operates are periodically subject to comparatively high rates of interest, which in certain instances in the tables below has had the effect of producing unusually high yields and costs.

	2002	2001	2000

	Average balance GBPm	Interest income GBPm	Yield %	Average balance GBPm	Interest income GBPm	Yield %	Average balance GBPm	Interest income GBPm	Yiel
Assets									
Treasury bills and other eligible bills									
Domestic offices	2,608	85	3.26	1,858	91	4.90	836	48	
Foreign offices	906	211	23.29	1,641	423	25.78	1,224	265	
Loans and advances to banks									
Domestic offices	11,839	470	3.97	12,086	692	5.73	13,384	828	
Foreign offices	2,275	129	5.67	2,308	153	6.63	2,332	180	
Loans and advances to customers									
Domestic offices	98,725	6,246	6.33	89,802	6,876	7.66	80,231	6,815	
Foreign offices	17,695	1,761	9.95	15,316	1,532	10.00	14,009	1,393	
Debt securities									
Domestic offices	8,661	347	4.01	4,394	230	5.23	3,882	252	
Foreign offices	6,022	220	3.65	4,397	300	6.82	2,827	271	
Lease and hire purchase receivables									
Domestic offices	13,069	1,078	8.25	13,104	1,061	8.10	12,241	984	
Foreign offices	18	2	11.11	39	6	15.38	56	18	
Total interest-earning assets of banking book	161,818	10,549	6.52	144,945	11,364	7.84	131,022	11,054	
Total interest-earning assets of trading book	15,518	602	3.88	12,252	544	4.44	10,189	511	
Total interest-earning assets	177,336	11,151	6.29	157,197	11,908	7.58	141,211	11,565	
Provisions for bad and doubtful debts	(1,623)			(1,489)			(1,531)		

Non-interest earning assets								
Domestic offices	19,941			20,653			19,389	
Foreign offices	2,822			2,255			2,121	
Total average assets and interest income	198,476	11,151	5.62	178,616	11,908	6.67	161,190	11,565
Percentage of assets applicable to foreign activities (in %)	14.8			14.3			13.8	

	2002			2001			2000		
	Average interest earning assets GBPm	Net interest income GBPm	Net interest margin %	Average interest earning assets GBPm	Net interest income GBPm	Net interest margin %	Average interest earning assets GBPm	Net interest income GBPm	in
Average interest-earning assets and net interest income:									
Banking business	161,818	5,171	3.20	144,945	4,922	3.40	131,022	4,587	
Trading business	15,518	-	-	12,252	-	-	10,189	-	
Net yield on interest-earning assets	177,336	5,171	2.92	157,197	4,922	3.13	141,211	4,587	

45

	2002			2001			2000		
	Average balance	Interest expense	Cost	Average balance	Interest expense	Cost	Average balance	Interest expense	Cos

	GBPm	GBPm	%	GBPm	GBPm	%	GBPm	GBPm	
Liabilities and shareholders' equity									
Deposits by banks									
Domestic offices	12,587	322	2.56	13,452	658	4.89	9,057	490	5.4
Foreign offices	4,234	137	3.24	3,949	288	7.29	3,506	247	7.0
Liabilities to banks under sale and repurchase agreements									
Domestic offices	2,799	80	2.86	1,547	74	4.78	2,022	113	5.5
Foreign offices	457	77	16.85	671	110	16.39	300	68	22.6
Customer accounts									
Domestic offices	82,009	2,240	2.73	72,633	2,724	3.75	72,071	3,232	4.4
Foreign offices	11,265	993	8.81	10,877	924	8.49	10,326	801	7.7
Liabilities to customers under sale and repurchase agreements									
Domestic offices	2,898	135	4.66	1,552	73	4.70	551	35	6.3
Foreign offices	140	4	2.86	128	4	3.13	127	4	3.1
Debt securities in issue									
Domestic offices	14,750	498	3.38	12,716	713	5.61	8,136	620	7.6
Foreign offices	7,953	355	4.46	6,052	359	5.93	4,707	366	7.7
Subordinated liabilities									
Domestic offices	10,921	526	4.82	9,333	506	5.42	7,383	481	6.5
Foreign offices	190	11	5.79	158	9	5.70	162	10	6.1
Total interest-bearing liabilities of banking book	150,203	5,378	3.58	133,068	6,442	4.84	118,348	6,467	5.4
Total interest-bearing									

liabilities of trading book	15,518	602	3.88	12,252	544	4.44	10,189	511	5.0
Total interest-bearing liabilities	165,721	5,980	3.61	145,320	6,986	4.81	128,537	6,978	5.4
Interest-free liabilities									
Minority interests and shareholders' funds									
Domestic offices	8,522			10,609			11,115		
Foreign offices	2,801			2,225			1,930		
Non-interest bearing customer accounts									
Domestic offices	5,985			6,182			6,058		
Foreign offices	789			595			635		
Other interest-free liabilities									
Domestic offices	13,118			12,721			12,430		
Foreign offices	1,540			964			485		
Total liabilities	198,476	5,980	3.01	178,616	6,986	3.91	161,190	6,978	4.3
Percentage of liabilities applicable to foreign activities (in %)	14.2			14.1			13.7		

Net interest margin for the banking book

	2002 %	2001 %	2000 %
Domestic offices	3.28	3.47	3.58
Foreign offices	2.77	3.04	3.09
Group margin	3.20	3.40	3.50

Loans and advances to banks and customers include non-performing loans.

Interest receivable on such loans has been included to the extent to which either cash payments have been received, in accordance with Lloyds TSB Group's policy on income recognition.

Approximately 85 per cent of the value of the balances are calculated on a daily basis with balances held by Lloyds TSB Group's leasing and asset finance businesses averaged on a monthly basis. Management believes that the interest rate trends are substantially the same as they would be if all balances were averaged on the same basis.

46

Changes in net interest income - volume and rate analysis

The following table allocates changes in net interest income between volume and rate for 2002 compared with 2001 and for 2001 compared with 2000. Where variances have arisen from both changes in volume and rate these are allocated to volume.

	2002 compared with 2001 Increase/(decrease)			2001 compared with 2000 Increase/(decrease)		
	Total change GBPm	Volume GBPm	Rate GBPm	Total change GBPm	Volume GBPm	Rate GBPm
Interest receivable and similar income						
Treasury bills and other eligible bills						
Domestic offices	(6)	24	(30)	43	50	(7)
Foreign offices	(212)	(171)	(41)	158	107	51
Loans and advances to banks						
Domestic offices	(222)	(10)	(212)	(136)	(74)	(62)
Foreign offices	(24)	(2)	(22)	(27)	(2)	(25)
Loans and advances to customers						
Domestic offices	(630)	565	(1,195)	61	733	(672)
Foreign offices	229	237	(8)	139	131	8
Debt						

securities						
Domestic offices	117	171	(54)	(22)	27	(49)
Foreign offices	(80)	59	(139)	29	107	(78)
Lease and hire purchase receivables						
Domestic offices	17	(3)	20	77	70	7
Foreign offices	(4)	(2)	(2)	(12)	(3)	(9)
Total banking book interest receivable and similar income	(815)	868	(1,683)	310	1,146	(836)
Total trading book interest receivable and similar income	58	127	(69)	33	92	(59)
Total interest receivable and similar income	(757)	995	(1,752)	343	1,238	(895)
Interest payable						
Deposits by banks						
Domestic offices	(336)	(22)	(314)	168	215	(47)
Foreign offices	(151)	9	(160)	41	32	9
Liabilities to banks under sale and repurchase agreements						
Domestic offices	6	36	(30)	(39)	(23)	(16)
Foreign offices	(33)	(36)	3	42	61	(19)
Customer accounts						
Domestic offices	(484)	256	(740)	(508)	21	(529)
Foreign offices	69	34	35	123	47	76
Liabilities						

to customers under sale and repurchase agreements						
Domestic offices	62	63	(1)	38	47	(9)
Foreign offices	-	-	-	-	-	-
Debt securities in issue						
Domestic offices	(215)	69	(284)	93	257	(164)
Foreign offices	(4)	85	(89)	(7)	80	(87)
Subordinated liabilities						
Domestic offices	20	76	(56)	25	106	(81)
Foreign offices	2	2	-	(1)	-	(1)
Total banking book interest payable	(1,064)	572	(1,636)	(25)	843	(868)
Total trading book interest payable	58	127	(69)	33	92	(59)
Total interest payable	(1,006)	699	(1,705)	8	935	(927)

Enterprise-wide risk management

Lloyds TSB Group has adopted an enterprise-wide framework for the identification, assessment and management of risk, designed to meet its customers' needs and maximise shareholder value by aligning risk management with the corporate strategy; assessing the impact of emerging risks from new technologies or markets; and developing risk tolerances and mitigating strategies.

Enterprise-wide risk management ("EWRM") is founded on four principal concepts: strong risk governance; empowerment; competitive advantage; and common risk language.

Strong Risk Governance

Common Risk Language

Current and Emerging Risks

Empowerment

Competitive Advantage

Strong risk governance

The risk governance structure is designed to create a risk-aware culture in which the nature and size of risks are well understood, and business decisions strike a balance between risk and reward which is consistent with the Lloyds TSB Group's risk appetite, whilst maximising shareholder value. The governance structure is based on the following elements:

The Board is responsible for determining the long-term strategy of the business, the markets in which the Lloyds TSB Group will operate and the level of risk acceptable to the Lloyds TSB Group in each area of its business.

The Group Executive Committee is responsible to the Group Chief Executive for the development and implementation of strategy, operational plans, policies and budgets. It monitors operating and financial performance, assesses and controls risk, and prioritises and allocates resources.

The Group Risk Committee is responsible to the Group Executive Committee for protecting shareholder value through assessment and control of the high level risks assumed by the Lloyds TSB Group; approving the Lloyds TSB Group's high level policies; ensuring that the necessary culture, practices and systems are in place to enable the Lloyds TSB Group to meet its internal and external obligations; and reviewing the allocation and deployment of capital at risk, taking into account the Lloyds TSB Group's risk appetite.

The Director of Group Risk Management is responsible for the implementation of risk policy and the provision of independent assurance to the Audit Committee and Board, who receive regular reports on risk issues prepared by Group Risk Management. The Director of Group Risk Management reports to the Group Chief Executive and has access to the Chairman and members of senior management; he is also a member of the Group Risk Committee.

The diagram below sets out the existing risk governance structure, but during 2003 the Lloyds TSB Group is carrying out a wide-ranging review aimed at further improving the risk governance framework which is likely to lead to changes before the end of the year.

Board

Audit Committee

Group Chief Executive

Chairman's Committee

External Auditors

Group Risk Management

Group Risk Committee

Group Executive Committee

ALCO

Regulators

Business

Units

Empowerment

The directors of the Lloyds TSB Group's business units have primary responsibility for measuring, monitoring and controlling risks within their areas of accountability. They are empowered to establish control frameworks for their businesses that are consistent with the Lloyds TSB Group's high level policies and within parameters set by Group Risk Management.

Competitive Advantage

The EWRM model strengthens the Lloyds TSB Group's ability to identify and assess risks; aggregate risks and define the corporate risk appetite; develop solutions for reducing or transferring risk, where appropriate; and exploit risks to gain competitive advantage, thereby increasing shareholder value.

Common Risk Language

The Lloyds TSB Group has adopted a risk language in which all risks are classified by one or more of the following 11 Risk Drivers:

Governance, People and Organisation

Strategy	Product and Service
Credit	Financial
Market	Customer Treatment
Insurance	Legal and Regulatory
Operational	Change Management

The Lloyds TSB Group's high level policy and reporting to the Group Risk Committee, Audit Committee and Board have been aligned to the Risk Drivers. Roll-out of the risk language to the business has commenced and will be completed during 2003, ensuring a consistent approach to classifying and describing risks.

Governance, People and Organisation

Definition

The risk of loss from poor corporate governance at Group and business unit level, sub-optimal organisational structuring, or failure to recruit, manage and retain appropriate skilled staff to achieve business objectives.

Lloyds TSB Group Policy Manual

The Lloyds TSB Group's policy for managing Governance, People and Organisation risk is set out in the Lloyds TSB Group Policy Manual, which is approved by the Group Risk Committee. The salient elements of the policy are summarised below.

Governance and Organisation

The Lloyds TSB Group's governance and organisation policy is to:

- Organise itself into three principal business units (UK Retail Banking and

Mortgages, Wholesale and International Banking, and Insurance and Investments) with centralised IT and operational support. These units are run in a manner consistent with strategic direction from the Board, tight financial and operating controls and the prudent management of risk.

- Develop and maintain a strong risk management and control culture across all businesses.

- Follow industry best practice on corporate governance, and conduct business with integrity, due skill, care and diligence.

Management of Risks

The Lloyds TSB Group sets high standards for the conduct of its business and values its reputation. Responsibility for establishing an effective organisational structure is vested in Group and business unit management. Sound internal risk management practices are promoted through business unit directors who are responsible for identifying, measuring, monitoring and controlling the risks within their specific areas of accountability.

49

The Lloyds TSB Group seeks to identify and classify risks in a timely manner. The likelihood of risks crystallising and the significance of the consequent impact on the business, the Lloyds TSB Group and its customers are evaluated. The Lloyds TSB Group's business control environment ensures effective and efficient operational management; reliability, integrity and consistency of financial and other reporting; and compliance with governing laws and regulations. Business unit directors ensure that material risks are reported to the relevant Group Executive Director and to Group Risk Management.

Information and Communication

It is the Lloyds TSB Group's policy for the Board and senior management at both Group and business unit level to receive relevant, reliable and timely management information in line with business objectives to ensure that activities are appropriately controlled, key risks are identified and monitored, decisions are implemented and regulatory obligations are met.

Audit Responsibilities and Rights

Group Audit independently reviews adherence to the policies and processes that make up the control environment, disseminating best practices throughout the Lloyds TSB Group in the course of its monitoring and corrective action activities. The Group Audit Director meets regularly with the Group Chief Executive and periodically with the Audit Committee.

People

The Lloyds TSB Group's approach to people management is to employ skilled, committed staff, working as a team for the benefit of customers and shareholders, who are given the opportunity to fulfil their potential; employ the highest ethical standards of behaviour and best practice management principles; and recruit on the basis of ability and competence.

Standards of Behaviour

The Lloyds TSB Group seeks to ensure that its employees act with integrity and seek to deliver high levels of customer service. It promotes a working environment free from discrimination, harassment, bullying or victimisation of any kind. Employees are encouraged and expected to alert management to suspected misconduct, fraud or other serious malpractice.

Performance and Reward Management

The Lloyds TSB Group seeks to:

- Ensure that all employees understand their role, the purpose of the role and where it fits into the wider team and organisational context.

- Manage and measure employees' performance and contribution to collective goals.

- Recognise the contribution of individuals in the context of the pay market and the performance of the business in which they work, and reward appropriately.

Training and Development

The Lloyds TSB Group believes that:

- Long term success depends on the quality and skills of its staff.

- It has a joint responsibility with employees for their personal and career development to improve current performance and to enhance future prospects.

Strategy Risk

Definition

The risk arising from the adoption of the Lloyds TSB Group's agreed strategy and its implementation at corporate or business unit level.

Processes

The Lloyds TSB Group's governing objective is to maximise value for its shareholders by:

- Being first choice for its customers.

- Being a leader in its chosen markets.

- Driving down day-to-day costs to facilitate investment.

The risks arising from the adoption of the Lloyds TSB Group's strategy at corporate and business unit level are managed by a number of processes.

A common approach is applied across the Lloyds TSB Group to assess the creation of shareholder value. This is measured by economic profit (the profit attributable to shareholders, less a notional charge for the equity invested in the business). The focus on economic profit allows the Lloyds TSB Group to compare the returns being made on capital employed in each business. The use of risk-based economic capital and regulatory capital is closely monitored at business unit and Group level. The Lloyds TSB Group's economic capital model covers credit, market, insurance, business and operational risks.

A rigorous annual strategic planning process is conducted at Group and business unit level and includes a quantitative and qualitative assessment of the risks in the Lloyds TSB Group plan.

The Lloyds TSB Group's strategy and those of its constituent business units are reviewed and approved by the Board. Regular reports are provided to the Group Executive Committee and the Board on the progress of the Group's key strategies and plans.

Revenue and capital investment decisions require additional formal assessment and approval. Formal risk assessment is conducted as part of the financial approval process.

Company mergers and acquisitions require specific approval by the Board. In addition to the standard due diligence conducted during a merger or acquisition, Group Risk Management conducts an independent risk assessment of the target company and its proposed integration into the Lloyds TSB Group.

Credit Risk

Definition

The risk of loss arising from counterparty default subsequent to the provision of credit facilities (both on and off-balance sheet).

Measurement

The Lloyds TSB Group has dedicated standards, policies and procedures to control and monitor credit and related risks. Examples of the way in which such risks are measured include:

Group Rating System - all business units are required to operate an authorised rating system that complies with the Lloyds TSB Group's standard methodology. The Lloyds TSB Group uses a 'Master Scale' rating structure with ratings corresponding to a range of probability of future default.

Portfolio Analysis - in conjunction with Group Risk Management, business units identify and define portfolios of credit and related risk exposures and the key benchmarks, behaviours and characteristics by which those portfolios are managed in terms of credit risk exposure. This entails the production and analysis of regular portfolio monitoring reports for review by Group Risk Management.

To further enhance the ability to measure and predict future risk, the Lloyds TSB Group continues to develop new policies and risk management systems.

Limits

A number of tools, including Group-level credit policy where appropriate, are used to control the Lloyds TSB Group's exposure to undue levels of credit risk:

Counterparty Limits - exposure to individual counterparties, groups of counterparties or customer risk segments is controlled through a tiered hierarchy of delegated sanctioning authorities. Approval requirements for each decision are based on the transaction amount, the customer's aggregate facilities, credit risk ratings and the nature and term of the risk. Regular reports on significant credit exposures are provided to the Group Executive Committee and Board.

Bank Exposures - an in-house proprietary rating system is used to approve bank facilities, which are sanctioned on a Group-wide basis.

Cross-border Exposures - Country limits are authorised and managed by a dedicated unit, using an in-house rating system, which takes into account economic and political factors.

Concentration Risk - formulation of concentration limits on certain industries and sectors. Group Risk Management sets Sector Caps that reflect risk appetite, and monitors exposures to prevent excessive concentration of risk.

Credit Risk Arising from the Use of Derivatives - Note 45a on page F-53 shows the total notional principal amount of interest rate, exchange rate and equity contracts outstanding at 31 December 2002. The notional principal amount does not, however, represent the Lloyds TSB Group's real exposure to credit risk, which is limited to the current cost of replacing contracts with a positive value to the Lloyds TSB Group, should the counterparty default. This replacement cost is also shown in Note 45a. To reduce credit risk the Lloyds TSB Group uses a variety of credit enhancement techniques such as netting and collateralisation, where security is provided against the exposure.

Credit Derivatives - these are a method of transferring credit risk from one counterparty to another and of managing exposure to selected counterparties. Credit derivatives include credit swaps, credit spread options and credit linked notes. Lloyds TSB Group has limited exposure to such instruments.

Processes

The processes by which Group Risk Management discharges its responsibilities in respect of credit risk include the following:

- Formulation of high-level credit policies designed to ensure a balanced and managed approach to the identification and mitigation of credit risk.

- Provision of lending guidelines. These define the responsibilities for lending officers and provide a disciplined and focused benchmark for credit decisions.

- Group Risk Management has direct involvement in the sanctioning of counterparty limits over defined thresholds and also notes decisions made within business unit and divisional credit functions to ensure appropriate oversight. Such activities assist not only in the management of the overall portfolio but also provide essential input to the development and maintenance of robust credit policies.

- Sector Caps, encompassing both industry sectors and specific product types are established by Group Risk Management to communicate Lloyds TSB Group's risk appetite for specific types of business, primarily in the non-retail markets.

- Establishment and maintenance of the Lloyds TSB Group's large exposure and provisioning policies, in accordance with regulatory reporting requirements.

- Monitoring of scorecards. The Lloyds TSB Group utilises statistically-based decisioning techniques (primarily credit scoring and performance scoring) for its principal consumer lending portfolios. Group Risk Management reviews and monitors new and material changes to scorecards.

- Maintenance of a facilities database. Group Risk Management operates a centralised database of large corporate, sovereign and bank facilities designed to ensure a consistent aggregation policy is maintained throughout the Lloyds TSB Group.

- Monitoring and controlling residual value risk exposure. The Lloyds TSB Group's appetite for such exposure is communicated to the business by a series of time referenced Sector Caps, ensuring an acceptable distribution of future risk.

- Communication and provision of general guidance on all credit-related risk issues, including regulatory changes and environmental risk policy, to promote consistent and best practice throughout the Lloyds TSB Group.

Day-to-day credit management and asset quality within each business unit is primarily the responsibility of the relevant business unit director. Such responsibility is fulfilled by:

- Each business unit having in place established credit processes which are consistent with the corresponding Lloyds TSB Group policies.

- Authority to delegate lending authorities within business units resting with officers holding divisional delegated lending authority. All material authorities are advised to Group Risk Management.

- Specialist units established within Lloyds TSB Group businesses to provide, for example: intensive management and control; security perfection, maintenance and retention; expertise in documentation for lending and associated products; sector-specific expertise; and legal services applicable to the particular market place and product range offered by the business unit.

Loan portfolio
Analysis of loans and advances to customers and banks
The following table analyses loans to banks and customers by geographical area and type of loan at 31 December for each of the five years listed.

	2002 GBPm	2001 GBPm	2000 GBPm	1999 GBPm	1998 GBPm
Domestic:					
Loans and advances to banks	15,291	12,737	13,165	14,341	15,905
Loans and advances to customers:					
Mortgages	62,467	56,578	52,659	47,451	44,660
Other personal lending	14,931	12,784	11,138	10,092	9,570
Agriculture, forestry and fishing	2,076	2,074	2,026	2,183	2,052
Manufacturing	3,373	3,321	3,357	3,262	2,987
Construction	1,482	1,309	1,016	754	671
Transport, distribution and hotels	4,696	4,440	3,836	3,540	3,308
Financial, business and other services	8,352	8,736	9,295	6,614	5,029

Property companies	4,008	2,907	2,470	2,303	2,304
Lease financing	7,285	7,552	8,070	8,369	8,165
Hire purchase	5,990	5,345	5,172	3,674	3,701
Other	3,397	2,992	2,526	2,127	1,921
Total domestic loans	133,348	120,775	114,730	104,710	100,273
Foreign:					
Loans and advances to banks	2,239	2,489	2,131	2,628	2,606
Loans and advances to customers:					
Mortgages	4,763	3,467	3,490	3,558	3,187
Other personal lending	1,098	1,672	1,602	1,784	1,832
Agriculture, forestry and fishing	2,220	1,708	1,528	1,606	1,703
Manufacturing	1,608	2,004	1,730	945	976
Construction	328	304	190	158	155
Transport, distribution and hotels	2,459	2,570	2,166	1,638	1,082
Financial, business and other services	3,196	2,631	2,174	2,553	2,542
Property companies	1,117	896	637	470	428
Lease financing	15	33	53	79	136
Hire purchase	-	-	-	-	19
Other	1,436	1,148	807	581	374
Total foreign loans	20,479	18,922	16,508	16,000	15,040
Total loans	153,827	139,697	131,238	120,710	115,313
Less provision for loan losses	(1,767)	(1,468)	(1,426)	(1,414)	(1,462)
Less interest held in suspense	(57)	(70)	(90)	(100)	(145)
Total loans and advances net of provisions and interest held in suspense	152,003	138,159	129,722	119,196	113,706

	2002 GBPm	2001 GBPm	2000 GBPm	1999 GBPm	1998 GBPm
Analysis of foreign loans by region:					
Loans and advances to customers:					
New Zealand	10,447	8,435	7,368	7,659	7,310
Latin America	1,591	2,347	2,222	1,761	2,120
Rest of the world	6,202	5,651	4,787	3,952	3,004
	18,240	16,433	14,377	13,372	12,434
Loans and advances to banks:					
New Zealand	622	534	357	467	375
Latin America	52	209	105	190	148
Rest of the world	1,565	1,746	1,669	1,971	2,083
	2,239	2,489	2,131	2,628	2,606
Total foreign loans	20,479	18,922	16,508	16,000	15,040

The classification of lending as domestic or foreign is based on the location of the office recording the transaction, except for certain lending of the international business booked in London.

Summary of loan loss experience

The following table analyses the movements in the allowance for loan losses for each of the five years listed.

	2002 GBPm	2001 GBPm	2000 GBPm	1999 GBPm	1998 GBPm
Balance at beginning of period					
Domestic	1,162	1,129	1,134	1,126	1,252
Foreign	306	297	280	336	519
Total balance at beginning of period	1,468	1,426	1,414	1,462	1,771
Exchange and other adjustments	(55)	(14)	51	(49)	(30)
Advances written off:					
Domestic:					
Loans and advances to customers:					
Mortgages	(21)	(23)	(35)	(30)	(38)
Other personal lending	(530)	(438)	(399)	(364)	(279)
Agriculture, forestry and fishing	(2)	(9)	(12)	(14)	(9)
Manufacturing	(25)	(18)	(13)	(33)	(33)
Construction	(17)	(8)	(9)	(10)	(6)
Transport, distribution and hotels	(27)	(34)	(27)	(46)	(108)
Financial, business and other services	(53)	(44)	(28)	(40)	(34)
Property companies	(19)	(21)	(17)	(24)	(45)
Lease financing	(17)	(11)	(12)	(14)	(30)
Hire purchase	(74)	(86)	(69)	(29)	(5)
Other	(2)	(9)	-	(6)	-
Total domestic	(787)	(701)	(621)	(610)	(587)
Foreign	(91)	(184)	(124)	(134)	(372)
Total advances written off	(878)	(885)	(745)	(744)	(959)
Recoveries of advances written off:					
Domestic:					
Loans and advances to customers:					
Mortgages	5	17	12	11	9
Other personal lending	81	80	63	60	27
Agriculture, forestry and fishing	3	4	2	2	4
Manufacturing	17	5	6	11	14
Construction	3	2	2	1	2
Transport, distribution and hotels	12	10	11	7	15
Financial, business and other services	13	11	10	6	10
Property companies	10	6	5	7	20
Lease financing	3	4	5	5	3

Hire purchase	17	23	24	10	7
Other	1	3	–	1	–
Total domestic	165	165	140	121	111
Foreign	38	29	25	9	14
Total recoveries of advances written off	203	194	165	130	125

	2002 GBPm	2001 GBPm	2000 GBPm	1999 GBPm	1998 GBPm
Net advances written off:					
Domestic	(622)	(536)	(481)	(489)	(476)
Foreign	(53)	(155)	(99)	(125)	(358)
Total net advances written off	(675)	(691)	(580)	(614)	(834)
Provision for loan losses charged against income for the year					
Domestic:					
Loans and advances to customers:					
Mortgages	(5)	2	(4)	9	34
Other personal lending	489	403	323	379	201
Agriculture, forestry and fishing	–	3	(6)	(4)	31
Manufacturing	31	40	21	28	20
Construction	14	(2)	1	5	8
Transport, distribution and hotels	28	28	3	23	7
Financial, business and other services	107	39	12	16	40
Property companies	(1)	4	8	4	(19)
Lease financing	3	5	8	14	8
Hire purchase	82	67	52	31	26
Other specific provisions	38	23	15	(5)	14
General provisions	14	(42)	(7)	–	(7)
Total domestic	800	570	426	500	363
Foreign	229	177	115	115	192
Total provision for loan losses charged against income for the year	1,029	747	541	615	555
Balance at end of					

period					
Domestic	1,344	1,162	1,129	1,134	1,126
Foreign	423	306	297	280	336
Total balance at end of period	1,767	1,468	1,426	1,414	1,462
Ratio of net write-offs during the period to average loans outstanding during the period	0.5%	0.6%	0.5%	0.6%	0.9%

The following table analyses the coverage of the allowance for loan losses by category of loans.

	2002		2001		2000		1999
	Allowance GBPm	Percentage of loans in each category to total loans %	Allowance GBPm	Percentage of loans in each category to total loans %	Allowance GBPm	Percentage of loans in each category to total loans %	Allowane GBPm
Balance at period end applicable to:							
Domestic:							
Loans and advances to banks	-	9.9	-	9.1	-	10.0	-
Loans and advances to customers:							
Mortgages	25	40.7	44	40.5	48	40.1	75
Other personal lending	447	9.7	407	9.2	362	8.5	358
Agriculture, forestry and fishing	10	1.3	9	1.5	11	1.5	27
Manufacturing	121	2.2	98	2.4	71	2.6	57
Construction	7	1.0	7	0.9	15	0.8	21
Transport, distribution and hotels	67	3.1	54	3.2	50	2.9	63

Financial, business and other services	136	5.4	65	6.3	59	7.1	65
Property companies	8	2.6	18	2.1	29	1.9	33
Lease financing	7	4.7	18	5.4	20	6.2	16
Hire purchase	123	3.9	98	3.8	94	3.9	49
Other	65	2.2	30	2.1	15	1.9	9
Total domestic	1,016	86.7	848	86.5	774	87.4	773
Foreign	318	13.3	251	13.5	295	12.6	280
General provision	433	-	369	-	357	-	361
Total balance at period end	1,767	100.0	1,468	100.0	1,426	100.0	1,414

Risk elements in the loan portfolio

Non-accrual, past due and restructured loans

The following discussion consists of an analysis of credit risk elements by categories which reflect US lending and accounting practices. These differ from those employed in the UK. In particular:

Suspended interest and non-performing lending

In accordance with the UK British Bankers' Association Statement of Recommended Practice on Advances, Lloyds TSB Group continues to accrue interest, where appropriate, on doubtful debts when there is a realistic prospect of recovery. This accrued interest is charged to the customer's account but it is not applied to income; it is placed on a suspense account and only taken to income if there ceases to be significant doubt about its being paid. Loans are transferred to non-accrual status where the operation of the customer's account has ceased. The lending is managed by specialist recovery departments and is written down to its estimated realisable value. Interest is not added to the lending or placed on a suspense account as its recovery is considered unlikely; it is only taken to income if it is received.

In the US, it is the normal practice to stop accruing interest when payments are 90 days or more past due or when recovery of both principal and interest is doubtful. When the loans are transferred to non-accrual status, accrued interest is reversed from income and no further interest is recognised until it becomes probable that the principal and interest will be repaid in full. Loans on which interest has been accrued but suspended would be included in risk elements as loans accounted for on a non-accrual basis.

In addition, in the US non-performing loans and advances are typically written off more quickly than in the UK. Consequently a UK bank may appear to have a higher level of non-performing loans and advances than a comparable US bank although the reported income is likely to be similar in both the US and the UK.

Troubled debt restructurings

In the US, loans whose terms have been modified due to problems with the borrower are required to be separately disclosed. If the new terms were in line with market conditions at the time of the restructuring and the restructured loan remains current as to repayment of principal and interest then the disclosure can be discontinued at the end of the first year.

There are no similar disclosure requirements in the UK.

Potential problem loans

Potential problem loans are loans where known information about possible credit problems causes management to have concern as to the borrowers' ability to comply with the present loan repayment terms. Interest continues to be accrued to the profit and loss account until, in the opinion of management, its ultimate recoverability becomes doubtful.

Assets acquired in exchange for advances

In most circumstances in the US, title to property securing residential real estate transfers to the lender upon foreclosure. The loan is written off and the property acquired in this way is reported in a separate balance sheet category with any recoveries recorded as an offset to the provision for loan losses recorded in the period. Upon sale of the acquired property, gains or losses are recorded in the income statement as a gain or loss on acquired property.

In the UK, although a bank is entitled to enforce a first charge on a property held as security, it typically does so only to the extent of enforcing its power of sale. In accordance with UK GAAP and industry practice, Lloyds TSB Group takes control of a property held as collateral on a loan at repossession but title does not transfer to it. Loans subject to repossession continue to be reported as loans in the balance sheet although the accrual of interest is suspended. Any gains or losses on sale of the acquired property are recorded within the provision for loan losses during the reporting period.

The difference in practices has no effect on net income reported in the UK compared to that reported in the US but it does result in a difference in classification of losses and recoveries in the income statement. It also has the effect of causing UK banks to report an increased level of non-performing loans compared with US banks.

The following table analyses risk elements in the loan portfolio as at 31 December for the last five years:

	2002	2001	2000	1999	1998
	GBPm	GBPm	GBPm	GBPm	GBPm
Loans accounted for on a non-accrual basis:					

Domestic offices	421	278	223	209	287
Foreign offices	241	101	181	139	130
Total non-accrual loans	662	379	404	348	417
Accruing loans on which:					
- interest is being placed in suspense:					
Domestic offices	553	637	617	502	479
Foreign offices	199	206	238	217	292
Total suspended interest loans	752	843	855	719	771
- interest is still being accrued and taken to profit, and against which specific provisions have been made:					
Domestic offices	1,217	1,265	1,713	1,924	2,056
Foreign offices	66	75	101	74	75
Total accruing loans against which specific provisions have been made	1,283	1,340	1,814	1,998	2,131
- interest is still being accrued and taken to profit, the lending is contractually past due 90 days or more as to principal or interest, but against which no provisions have been made:					
Domestic offices	776	693	520	506	313
Foreign offices	34	37	33	15	-
Total accruing loans against which no provisions have been made	810	730	553	521	313
Troubled debt restructurings:					
Domestic offices	1	1	2	10	1
Foreign offices	2	9	12	10	1
Total troubled debt restructurings	3	10	14	20	2
Total non-performing lending:					
Domestic offices	2,968	2,874	3,075	3,151	3,136
Foreign offices	542	428	565	455	498
Total non-performing lending	3,510	3,302	3,640	3,606	3,634

58

Interest forgone on non-performing lending

The table below summarises the interest forgone on loans accounted for on a non-accrual basis and troubled debt restructurings:

	2002 GBPm
Domestic lending:	
Interest income that would have been recognised under original contract terms	30
Interest income included in profit	25
Interest forgone	5

Foreign lending:	
Interest income that would have been recognised under original contract terms	17
Interest income included in profit	6
Interest forgone	11

Potential problem loans

In addition to the non-performing lending disclosed above, lendings which were current as to payment of interest and principal but where concerns existed about the ability of the borrowers to comply with loan repayment terms in the near future were as follows:

	2002 GBPm	2001 GBPm	2000 GBPm	1999 GBPm	1998 GBPm
Potential problem lending	1,734	1,423	1,142	936	958

The figures shown for potential problem lending are not indicative of the losses that might arise should the credit quality of this lending deteriorate since they do not take into account security held.

Cross border outstandings

The business of Lloyds TSB Group involves significant exposures in non-local currencies. These cross border outstandings comprise loans (including accrued interest), acceptances, interest-bearing deposits with other banks, other interest-bearing investments and any other monetary assets which are denominated in non-local currency. The following tables analyse, by type of borrower, foreign outstandings which individually represent in excess of 1 per cent of Lloyds TSB Group's total assets.

	% of assets	Total GBPm	Governments and official institutions GBPm	Banks and other financial institutions GBPm	Commercial, industrial and other GBPm
As at 31 December 2002					
Germany	3.1	6,511	57	5,624	830
United States of America	1.8	3,655	207	1,274	2,174
Italy	1.5	3,013	1,912	909	192
France	1.0	2,075	99	1,187	789
As at 31 December 2001					
Germany	2.0	3,756	59	2,920	777
United States of					

America	1.8	3,403	151	1,290	1,962
Italy	1.7	3,170	1,834	1,052	284
As at 31 December 2000					
Germany	1.6	2,659	171	2,222	266
United States of America	1.4	2,290	90	907	1,293

As at 31 December 2002, Germany had commitments of GBP1,511 million, United States of America had commitments of GBP1,783 million, Italy had commitments of GBP129 million and France had commitments of GBP424 million.

As at 31 December 2002, the countries with cross border outstandings of between 0.75 per cent and 1 per cent of assets, amounting to GBP5,080 million in total were Japan, the Netherlands and Belgium.

59

As at 31 December 2001, the countries with cross border outstandings of between 0.75 per cent and 1 per cent of assets, amounting to GBP3,504 million in total were Japan and the Netherlands. As at 31 December 2000 the countries with cross border outstandings of between 0.75 per cent and 1 per cent of assets, amounting to GBP4,529 million in total were France, Italy and Japan.

Market Risk

Definition

Market risk is the risk of loss arising from unexpected changes in financial prices, including interest rates, exchange rates, bond and equity prices.

Market risk arises in all areas of Lloyds TSB Group's activities and is managed by a variety of different techniques. The Lloyds TSB Group's banking activities expose it to the risk of adverse movements in interest rates or exchange rates, with little or no exposure to equity or commodity risk; this is covered in detail in this section. The Lloyds TSB Group's insurance activities also expose it to market risk (see "Insurance Risk" below).

Measurement

Measurement techniques - a variety of techniques are used to quantify the market risk arising from the Group's banking and trading activities. These reflect the nature of the business activity, and include simple interest rate gapping, open exchange positions, sensitivity analysis and Value at Risk. Stress testing and scenario analysis are also used in certain portfolios, and at Group level, to simulate extreme conditions to supplement these core measures.

Trading Value at Risk ("VaR") - VaR can be calculated using a number of different methodologies and at different confidence intervals. Lloyds TSB Group utilises more than one methodology for comparative purposes, thus avoiding undue reliance on a single measure.

The predominant measure within Lloyds TSB Group is the variance/covariance ("VcV") methodology. Based on the commonly used 95 per cent confidence level, assuming positions are held overnight and using observation periods of the preceding three years, the value at risk based on Lloyds TSB Group's global trading was as detailed in the table below.

The following table shows closing, average, maximum and minimum VaR for the years ended 31 December 2002 and 2001.

	31 December 2002				31 December 2001			
	Closing GBPm	Average GBPm	Maximum GBPm	Minimum GBPm	Closing GBPm	Average GBPm	Maximum GBPm	Minimum GBPm
Interest Rate Risk	0.5	0.7	1.5	0.4	0.6	0.6	0.9	0.4
Foreign Exchange Risk	0.5	0.5	0.9	0.3	1.0	0.6	1.0	0.3
Equity Risk	0.0	0.0	0.1	0.0	0.0	0.0	0.0	0.0
Total VaR	1.0	1.2	2.1	0.9	1.6	1.2	1.6	0.8

The risk of loss measured by the VaR model is the potential loss in earnings. The total and average trading VaR does not assume any diversification benefit across the three risk types. The maximum and minimum VaR reported for each risk category did not necessarily occur on the same day as the maximum and minimum VaR reported as a whole.

There are some limitations to the VcV methodology which are covered below:

- The model assumes that changes in the underlying asset returns can be modelled by a normal distribution. This assumption is an approximation of reality that may not reflect all circumstances.

- The use of a confidence limit does not convey any information about potential losses on occasions when the confidence limit is exceeded. In times of extreme market movements actual losses may be several times greater than the VaR number. Stress testing is used to supplement VaR to estimate the impact of extreme events.

- Any model that forecasts the future based on historic data is implicitly assuming that the conditions that generated the data will remain true in the future. Stress testing and using more than one VaR methodology for some local markets form part of the wider market risk framework.

- Periods of severe market illiquidity, both in terms of the extent of the illiquidity and the time that it lasts, would mean that it may not be possible to hedge, or close, all positions in the timescales assumed in the VaR model.

- VaR is calculated at the close of business each day, which excludes the profit and loss impact of intra-day trading.

- The variance/covariance approach to VaR is not well suited to options positions. As a result these positions are controlled by additional sensitivity limits.

In summary, although VaR is an important component of Lloyds TSB Group's approach to managing trading market risk, it is supplemented by position and sensitivity limits and stress testing.

Interest rate exposures - comprise those originating in treasury trading activities and structural interest rate exposures, which arise from the commercial and retail banking activities of Lloyds TSB Group.

Trading interest rate risk - the VaR relating to interest rate trading positions is set out in "- Market Risk - Measurement - Trading Value at Risk ("VaR")".

Structural interest rate risk - in Lloyds TSB Group's retail portfolios, including mortgages, and in Lloyds TSB Group's capital funds, arises from the different repricing characteristics of Lloyds TSB Group's banking assets and liabilities and is managed by the Group Balance Sheet Management department under the direction of the Asset and Liability Committee ("ALCO").

Liabilities arising in the course of business from Lloyds TSB Group's retail banking business fall into two broad categories:

- those which are insensitive to interest rate movements, non-interest bearing liabilities such as shareholders' funds and interest-free or very low interest current account deposits; and

- those which are sensitive to interest rate movements, primarily savings deposits bearing interest rates which are varied at Lloyds TSB Group's discretion ("managed rate liabilities") but which for competitive reasons generally reflect changes in the Bank of England's base rate.

There is a relatively small volume of naturally arising banking liabilities whose interest rate is contractually fixed typically for periods of up to two years.

Most banking assets, with the exception of such non-interest earning items as premises, are sensitive to interest rate movements. There is a large volume of managed rate assets such as variable rate mortgage loans, and these may be considered as a natural offset to managed rate liabilities. However many assets, such as personal loans and fixed rate mortgages, bear interest which is contractually fixed for periods of up to five years or longer.

Interest rate risk arises from the mismatch between interest rate insensitive liabilities and interest rate sensitive assets, and between the differing contractual periods for which interest rates are fixed on interest rate sensitive assets and liabilities. Group Balance Sheet Management department manages this risk centrally by:

- offsetting against each other any matching interest rate sensitive assets and liabilities;

- acquiring new financial assets and liabilities as matching hedges against net balances of mismatched interest rate sensitive banking liabilities and assets, respectively; and

- acquiring new financial assets with interest rates contractually fixed for a range of periods up to five years as hedges for net balances of interest rate insensitive liabilities.

The financial assets and liabilities referred to above are acquired by way of internal transactions between Group Balance Sheet Management and the Lloyds

TSB Group's Treasury department in London, typically in the form of interest rate swaps and loans or deposits.

Structural interest rate risk can also arise from the wholesale banking books in the UK, where it is managed by the Lloyds TSB Group's Treasury department in London, and internationally, where it is managed by an authorised local treasury operation in each overseas centre. The levels of exposure within these books are controlled and monitored within approved limits locally and centrally by Group Risk Management. Group Risk Management issues the limits to the international business units on interest rate gaps or, where more appropriate, VaR.

Lloyds TSB Group's non-trading exposure is summarised in the form of an interest rate repricing table, as set out in Note 45b to the Consolidated Financial Statements. Items are allocated to time bands by reference to the earlier of the next contractual interest rate repricing date and the maturity date. However, the table does not take into account the effect of interest rate options used by Lloyds TSB Group to hedge its exposure.

The simulation models used by Lloyds TSB Group include assumptions about the relationships between customer behaviour and the level of interest rates; the anticipated level of future business is also taken into account. The accuracy of these assumptions will impact the efficiency of hedging transactions. The assumptions are regularly updated and the projected exposure is actively managed in accordance with Lloyds TSB Group's Asset and Liability Committee policy.

It is estimated that a hypothetical immediate and sustained 100 basis point increase in interest rates on 1 January 2003 would decrease net interest income by GBP37.9 million for the 12 months to 31 December 2003, while a hypothetical immediate and sustained 100 basis point decrease in interest rates would increase net interest income by GBP30.3 million.

	UK GBPm	North America GBPm	Asia & Australasia GBPm	Latin America GBPm	Europe & Middle East GBPm	Total 2003 GBPm	Total 2002 GBPm
Change in net interest income from a +100 basis point shift in yield curves	1.2	(20.8)	(0.9)	(1.1)	(16.3)	(37.9)	(102.9)
Change in net interest income from a -100 basis point shift in yield curves	(8.8)	20.8	0.9	1.1	16.3	30.3	85.7

The analysis above is subject to certain simplifying assumptions including, but not limited to, the following:

- all rates of all maturities worldwide move simultaneously by the same amount;
- all positions in the wholesale books run to maturity; and
- there is no management action in response to movements in interest rates.

In practice, positions in both the retail and wholesale books are actively managed and actual impact on net interest income may be different than the model.

Foreign exchange risk - exposures comprise those originating in treasury trading activities and structural foreign exchange exposures, which arise from investment in Lloyds TSB Group's overseas operations.

Trading foreign exchange - the corporate and retail businesses incur foreign exchange risk in the course of providing services to their customers. These risks reside in the authorised trading centres who are allocated exposure limits by Group Risk Management. The limits are monitored daily by the local centres and reported to Group Risk Management. Group Risk Management calculates the associated VaR as shown in the table in "- Market Risk - Measurement - Trading Value at Risk ("VaR")".

Structural foreign exchange - risk arises from Lloyds TSB Group's investments in its overseas operations. Lloyds TSB Group's structural foreign currency exposure is represented by the net asset value of the holding company's foreign currency exchange equity and subordinated debt investments in its subsidiaries and branches. Gains or losses on structural foreign currency exposures are taken to retained earnings.

The structural position is managed by Lloyds TSB Group Capital Funds having regard to the currency composition of Lloyds TSB Group's risk-weighted assets and reported to the Asset and Liability Committee on a monthly basis. The objective is to limit the effect of the exchange rate movements on the published risk asset ratio.

Lloyds TSB Group's structural position at 31 December 2002 is set out in Note 45d to the Consolidated Financial Statements. The position implies that at 31 December 2002 a hypothetical increase of 10 per cent in the value of sterling against all other currencies would have led to a GBP201 million reduction in reserves, and vice versa. On this basis, there would have been no material impact on Lloyds TSB Group's risk asset ratios.

Equity exposure - a small number of Lloyds TSB Group's authorised centres can incur equity risk in dealings with their retail and commercial customers. Limits on these equity exposures are controlled and monitored by Group Risk Management. Group Risk Management calculates VaR on these equities positions as set out in the trading VaR table in "- Market Risk - Measurement - Trading Value at Risk ("VaR")".

Limits

Market Risk Limits - limits to control market risk in respect of trading positions, UK wholesale banking and overseas centres are set by Group Risk Management up to a total authorised by the Lloyds TSB Group Board. A combination of position and sensitivity limits is used, depending on the nature of the business activity.

Retail Portfolios - limits to control interest rate risk within the Lloyds TSB Group's UK retail portfolios are set out in the policy for Group Balance

Sheet Management ("GBSM"), which is established by the ALCO and ratified by the Lloyds TSB Group Board. The policy is to optimise the stability of future net interest income, and this is achieved by entering into hedging transactions using interest rate swaps and other financial instruments. Both short and long-term interest rate parameters are applied to management of the balance sheet. Overseas operations are managed within limits authorised by Group Risk Management, in addition to which some centres have adopted benchmark profiles for investment of interest rate insensitive liabilities as approved by Group Risk Management.

Processes

Trading Activities - trading is restricted to a number of specialist centres, authorised by Group Risk Management, the most important centre being the Lloyds TSB Group's principal Treasury department in London. The level of exposure is strictly controlled and monitored within approved limits locally and centrally by Group Risk Management. Most of the Lloyds TSB Group's trading activity is undertaken to meet the requirements of customers for foreign exchange and interest rate products. However, some interest rate and exchange rate positions are taken out using derivatives (forward foreign exchange contracts, interest rate swaps and forward rate agreements) and on-balance sheet instruments (mainly debt securities), with the objective of earning a profit from favourable movements in market rates. Accordingly, these transactions are reflected in the accounts at their fair value and gains and losses shown in the profit and loss account as dealing profits.

Wholesale Banking - market risk in the wholesale banking books is managed in the UK by the Lloyds TSB Group's Treasury unit in London, and internationally by an authorised local treasury operation in each overseas centre. The levels of exposure within these books are controlled and monitored within approved limits, both locally and also centrally by Group Risk Management. Active management of the book is necessary to meet customer requirements and changing market circumstances.

Retail Portfolios and Capital Funds - market risk in the Lloyds TSB Group's retail portfolios and in the Lloyds TSB Group's capital funds arises from the different repricing characteristics of the Group's banking assets and liabilities and is managed by Group Balance Sheet Management. The simulation models used by Group Balance Sheet Management include assumptions about the relationships between customer behaviour and the level of interest rates; the anticipated level of future business is also taken into account. The accuracy of these assumptions will impact the efficiency of hedging transactions. The assumptions are regularly updated and the projected exposure is actively managed in accordance with the policy.

Derivatives - these are used to meet customers' financial needs; as part of the Lloyds TSB Group's trading activities; and to reduce the Lloyds TSB Group's own exposure to fluctuations in interest and exchange rates. The principal derivatives used by the Lloyds TSB Group are interest rate contracts (including interest rate swaps, forward rate agreements and options) and exchange rate contracts (including forward foreign exchange contracts, currency swaps and options). Particular attention is paid to the liquidity of the markets and products in which the Lloyds TSB Group trades to ensure that there are no undue concentrations of activity and risk.

Insurance Risk

Definition

The risk of loss arising from the sensitivity of profits to movements in claims experience and expectation; movements in the market value of invested assets which are not matched by similar movements in the value of insurance liabilities; the presence of options and guarantees in insurance products; and changes in the legal, regulatory and fiscal environment as applicable to the insurance businesses.

Measurement

Financial risks are measured through deterministic studies of the impact of different insurance and investment market scenarios on the future free assets of the business as well as some stochastic modelling.

The composition, and value, of both the non-participating fund and the General Insurance portfolio are reported to Group Risk Management on a monthly basis and a VaR is calculated. Stress testing is also used to supplement the VaR models.

The risk of loss measured by the VaR model is the potential loss in earnings over a given time horizon. The VaR methodology used is a variance/covariance ("VcV") approach which is the same in all respects to that used for the traded risk in the banking book, except that in the case of equity risk, the model maps the portfolio composition onto a series of appropriate indices by region and sector. The figures quoted below are the sum of the two portfolios with no allowance for diversification between portfolios or asset classes and represents the potential loss in earnings.

The following table shows closing, average, maximum and minimum VaR for the years ended 31 December 2002 and 2001.

	31 December 2002				31 December 2001			
	Closing GBPm	Average GBPm	Maximum GBPm	Minimum GBPm	Closing GBPm	Average GBPm	Maximum GBPm	Minimum GBPm
Interest Rate Risk	3.1	3.2	3.7	2.8	3.3	3.7	4.1	3.3
Foreign Exchange Risk	1.0	1.4	1.8	1.0	2.1	2.2	2.4	2.0
Equity Risk	17.4	19.9	22.6	17.4	22.2	24.2	28.4	21.3
Total VaR	21.5	24.5	28.1	21.5	27.6	30.1	34.1	27.5

Processes

Insurance risks are both retained and reinsured with external underwriters. The retained risk level is carefully controlled and monitored, with close attention being paid to the analysis of underwriting experience, product design, policy wordings, adequacy of reserves, solvency management and regulatory requirements.

General insurance exposure to accumulations of risk and possible catastrophes is mitigated by reinsurance arrangements which are broadly spread over different reinsurers. Detailed modeling, including that of the probable maximum loss under various catastrophe scenarios, supports the choice of reinsurance arrangements. Appropriate reinsurance arrangements also apply within the life and pensions businesses. 63

Investment strategy is determined by the term and nature of the underwriting liabilities, and asset/liability matching positions are actively monitored. The aim is to invest in assets such that the cash flows on the investments will match those on the projected future liabilities. Actuarial tools are used to project and match the cash flows. It is not possible to eliminate risk completely as the timing of mortality is uncertain, and bonds are not available at all of the required maturities. As a result the cash flows cannot be precisely matched and so sensitivity tests are used to test the extent of the mismatch.

Investment strategy for surplus assets held in excess of liabilities takes account of the regulatory and internal business requirements for capital to be held to support the business now and in the future. Surplus assets are held primarily in two portfolios: the surplus in the Scottish Widows non-participating fund and an investment portfolio within the General Insurance business.

The surplus in the long-term non-participating fund of Scottish Widows plc exists to provide the long-term funds with liquidity and working capital. The surplus also forms a capital reserve to support the investments managed on behalf of the with-profits policies which were transferred from Scottish Widows Fund and Life Assurance Society. With-profits business involves guaranteed benefits; in extreme market conditions the surplus could be called upon to support with-profits benefits. As a consequence it is appropriate to invest this fund in a mixture of equities, investment properties, and fixed interest investments that is related to the With-Profits Fund. This investment policy maintains the value of the reserve as a proportion of the underlying With-Profits Fund. The existence and investment mix of the surplus in the non-participating fund can therefore be considered as structural rather than as a traded portfolio. Under UK GAAP the portfolio is shown at market value and gains and losses are recognised in the profit and loss account.

The General Insurance portfolio is invested in a mixture of assets: cash, bonds and equities. The size of the equity component allowed and the investment policy are approved by Group Risk Management.

Equity derivatives are used by the Lloyds TSB Group to match equivalent liabilities arising from some of its retail products. Derivatives may also be used for efficient portfolio management purposes in client funds where such activity is in accordance with approved policy and the customer mandate.

With-profits life and pensions business involves guaranteed benefits that create a contingent market risk to the Lloyds TSB Group. Accordingly, in extreme investment market conditions the surplus assets in the life and pensions business could be called upon to support with-profits benefits. Options and guarantees are only incorporated in new insurance products after careful consideration of the risk management issues that they present. This occurs as part of the new product approval process (see "Product and Service Risk" below).

Operational Risk

Definition

The risk of loss resulting from inadequate or failed internal processes, people and systems, or from external events. For internal purposes, reputational impact is also included.

Processes

Business units have primary responsibility for identifying and managing their operational risks. They employ internal control techniques to reduce their likelihood or impact to tolerable levels within the Lloyds TSB Group's risk appetite. Where appropriate, risk is mitigated by way of insurance.

Group Risk Management's responsibilities in relation to operational risk include:

- Defining high-level operational risk policies to ensure a comprehensive and consistent approach to the identification and management of operational risk.

- Implementation of a standard methodology to ensure consistency in the identification, assessment and management of operational risk.

- Communication and provision of general guidance on operational risk related issues, including regulatory changes and developments in the measurement and management of operational risk, to promote best practice throughout the Lloyds TSB Group.

- Continuous review and improvement of all aspects of operational risk management to reflect developments in industry best practice and regulatory requirements.

- Approval from a risk perspective of all new products launched throughout the Lloyds TSB Group, to ensure their risks are understood by the business and managed appropriately (see "Product and Service Risk" below).

- Identification of risk through formal risk reviews, covering specific risks, activities, business sectors or products, and ensuring that prompt and pre-emptive action is taken to address any actual or perceived risks that may emerge, whether specific to the Lloyds TSB Group or to the industry generally.

64

Product and Service Risk

Definition

The risk of loss arising from the inherent characteristics, management or distribution of products or services, or from failure to meet or exceed customer expectations and competitor offerings.

Processes

For the Lloyds TSB Group to achieve its strategic aims of leadership in chosen markets and being first choice for customers, product life cycles must be effectively managed and new products developed to meet customer needs.

Business units are responsible for maintaining a range of products which meets the needs of customers and the business strategy; managing and controlling product risks; and compliance with applicable regulations.

Product Planning and Development - business units have formal processes for reviewing the range of their product portfolios and subjecting all product development to rigorous assessment. They are also responsible for ensuring compliance with all relevant regulatory and legislative requirements.

Product Pricing - business units have pricing objectives consistent with Lloyds TSB Group strategy.

Product Promotion, Distribution and Sales - business units have a defined channel distribution strategy for products, consistent with the Lloyds TSB Group's distribution strategy. Business units launching new products are responsible for ensuring that proposed sales activity within delivery channels is compliant with regulatory requirements.

All advertising and marketing material is required to comply with the Lloyds TSB Group's governing policy on Business Conduct. Any statement of fact should be substantiated through documentary evidence; any comparison should be presented in a fair and balanced way; and any reference to past performance should clearly state the basis of measurement.

Business units are required, prior to publication of any sales material, to seek confirmation that it complies with the regulatory and legal requirements of the jurisdiction in which the product is offered and marketed. Terms and conditions (to include mandates, agreements and other documentation) are approved by legal advisors and reviewed periodically.

New Product Approval - the Lloyds TSB Group defines a New Product as a new or amended product that introduces a significantly different risk profile at Group or business unit level. In line with defined policy, business units provide Group Risk Management with details of New Products at an early stage of product or service development to ensure compliance with the Lloyds TSB Group's risk appetite and strategy.

Where appropriate, technical advice/approval is sought from specialist functions. Only products carrying the approval of Group Risk Management and the business units involved in their manufacture/delivery are offered to customers.

Product Performance - business units establish and monitor performance standards for all marketed products across a range of indicators, e.g. sales volumes, customer service, risk profile. Significant deviations from these standards are investigated and appropriate action taken.

Financial Risk

Definition

The risk of financial failure arising from lack of capital or liquidity, poor management or poor quality/volatile earnings.

Measurement

The international standard for measuring capital adequacy is the risk asset ratio, which relates to on- and off-balance sheet exposures weighted according to broad categories of risk. The Group's capital ratios, calculated in line with the requirements of the Financial Services Authority ("FSA"), are set out in detail on page 70.

Liquidity Policy - a policy is in place which requires a common methodology to measuring liquidity across the Lloyds TSB Group. The methodology derives a liquidity ratio calculated by taking the sum of liquid assets, five-day wholesale inflows and back-up lines, and then dividing this by the sum of five-day wholesale outflows and a percentage of retail maturities and contingent claims drawable over the next five days.

Accounting Policies - the Lloyds TSB Group seeks to use appropriate accounting policies, consistently applied and supported by reasonable and prudent judgements and estimates.

Limits

The Lloyds TSB Group and its regulated subsidiary banks have been allocated an Individual Capital Ratio by the Financial Services Authority, and the Board has agreed a formal buffer to be maintained in addition to the Individual Capital Ratio. Actual or prospective breaches of the formal buffer must be notified to the Financial Services Authority, together with proposed remedial action; no such notifications have been made during 2002. Informally, a further buffer is maintained. In addition, the Board has agreed a maximum limit of the proportion of debt instruments in the capital base. Risk-weighted assets are monitored by business unit, while capital is controlled centrally.

The liquidity policy requires all authorised local treasury operations to maintain a liquidity ratio of over 100 per cent, in addition to ensuring compliance with local regulatory requirements.

Processes

Capital ratios are a key factor in the Lloyds TSB Group's budgeting and planning processes, and updates of expected ratios are prepared regularly during the year. Capital raised takes account of expected growth and currency of risk assets, and also allows for the sensitivity of the Lloyds TSB Group's capital to movements in equity markets.

Each reporting entity within the Lloyds TSB Group has a finance function which is responsible for the production of financial, management and regulatory information. It is the responsibility of Group Finance to produce consolidated information for use internally and to meet external regulatory and statutory reporting requirements.

In conjunction with directives laid down by Group Finance, business units or reporting entities:

- Have formal month-end and quarter-end procedures in place for preparation of management and financial accounts respectively.

- Review and formally approve management accounts at a determined level of detail, ensuring consistency with financial accounts.

- Prepare forecasts and detailed annual budgets that are subject to formal review and approval.

- Implement measures to monitor performance at local level to identify significant fluctuations or unusual activity.

It is the responsibility of local line management to ensure that the liquidity policy is met, and the sources and maturities of assets and liabilities are continually managed and appropriately diversified to avoid any undue concentration as market conditions evolve. Compliance is monitored by regular liquidity returns to Group Risk Management.

Customer Treatment Risk

Definition

The risk of financial loss or reputational damage arising from inappropriate or poor customer treatment.

Measurement

Service improvements are monitored by customer satisfaction surveys. The results of the research are fed into the Lloyds TSB Group's CARE Index, which measures ongoing performance against five principal objectives: customer understanding; accessibility; responsibility; expertise; and overall service quality improvement.

Processes

Trends across all the CARE Index categories are monitored and fed into a programme of continuous customer service improvement. Lloyds TSB Group also provides its staff with clear Financial Services Authority compliant guidelines and processes for dealing with customer complaints.

Legal and Regulatory Risk

Definition

The risk of financial loss or reputational damage arising from failing to comply with the laws, regulations or codes applicable to the financial services industry.

Processes

The Lloyds TSB Group's business is regulated overall by the Financial Services Authority, and additionally by local regulators in offshore and overseas jurisdictions.

Each business has a nominated individual with 'Compliance Oversight' responsibility under Financial Services Authority rules. The role of such individuals is to ensure that management have in place within the business a control structure which creates awareness of the rules and regulations to which the Lloyds TSB Group is subject, and to monitor and report on adherence to these rules and regulations.

Group Compliance - all compliance personnel also have a reporting line to Group Compliance, which sets compliance standards across the Lloyds TSB Group and provides independent reporting and assessment to the Board and business unit directors.

Financial Crime - Group Compliance includes a dedicated unit, led by the Group Financial Crime Director, which is responsible for ensuring that the Lloyds TSB Group has effective processes in place to identify and report on suspicious transactions and customers in support of the world-wide fight against financial crime.

The Group Compliance Director has access to the Chairman, Group Chief Executive and members of senior management.

Change Management Risk

Definition

The risk of financial loss or reputational damage arising from programmes or projects failing to deliver to requirements, budget or timescale; or failing to implement change effectively.

Processes

To deliver the Lloyds TSB Group's strategic aims, change must be managed in an effective, risk-aware and appropriately controlled manner throughout the organisation. The Lloyds TSB Group's Change Management Standards provide consistency of approach across the Lloyds TSB Group's project portfolio. In particular, the following control processes are in place:

- The Lloyds TSB Group's approach to change management is regularly benchmarked against other organisations around the world.

- A specialist Group Project Services function provides a pool of experienced, professional project managers to be deployed on major projects across the Lloyds TSB Group.

- An Investment Committee oversees the Lloyds TSB Group's investment in projects, and is constituted as a sub-committee of the Group Executive Committee.

- Changes that significantly impact customers or staff are managed as part of an overall change plan managed by the Change Implementation Review Committee ("CIRC"). The CIRC ensures that the aggregate impact of the implementation of change on customers, staff and systems is understood, managed and controlled.

- A six-monthly update on the Lloyds TSB Group's aggregate change plan is provided to the Board.

Liquidity and Capital Resources

Liquidity risk is defined as the risk of a loss arising from Lloyds TSB Group's inability to meet its financial obligations as they fall due. These obligations include the repayment of deposits on demand or at their contractual maturity; the repayment of loan capital and other borrowings as they mature; the payment of insurance policy benefits, claims and surrenders; the payment of lease obligations as they become due; the payment of operating expenses and taxation; the payment of dividends to shareholders; the ability to fund new and existing loan commitments; and the ability to take advantage of new business opportunities, Lloyds TSB Group complies with the Financial Services Authority's liquidity requirements, with similar liquidity policies in place across all trading centres worldwide. Compliance is monitored by regular liquidity returns to Group Risk Management.

The principal sources of liquidity for Lloyds TSB Group plc are dividends received from its only directly owned subsidiary company, Lloyds TSB Bank and loans from this and other Lloyds TSB Group companies. The ability of Lloyds TSB Bank to pay dividends, or for Lloyds TSB Bank or other Lloyds TSB Group companies to make loans to Lloyds TSB Group plc, depends on a number of factors, including their own regulatory capital requirements, distributable reserves and financial performance. For additional information see "Dividends".

Lloyds TSB Group plc is also able to raise funds by issuing loan capital or equity, although in practice Lloyds TSB Group plc has never issued equity for this purpose and the majority of Lloyds TSB Group's loan capital has been issued by Lloyds TSB Bank. As at 31 December 2002, Lloyds TSB Group plc had GBP1,370 million of subordinated debt in issuance following the issue of GBP958 million of loan capital during the year, compared with GBP10,168 million for the consolidated Lloyds TSB Group. The cost and availability of subordinated debt finance are influenced by credit ratings. A reduction in these ratings could increase the cost and could reduce market access. At 31 December 2002, the credit ratings of Lloyds TSB Bank were as follows:

	Senior debt
Moody's	Aaa
Standard & Poor's	AA
Fitch	AA+

The credit ratings of Lloyds TSB Group plc were one notch lower. The ratings outlook from Moody's and Fitch for Lloyds TSB Bank is stable. The Standard & Poor's rating outlook is negative. These credit ratings are not a recommendation to buy, hold or sell any security; and each rating should be evaluated independently of every other rating.

A significant part of the liquidity of Lloyds TSB Group's banking businesses arises from their ability to generate customer deposits. A substantial proportion of the customer deposit base is made up of current and savings accounts which, although repayable on demand, have traditionally provided a stable source of funding. During 2002, amounts deposited by customers increased by GBP7,218 million from GBP109,116 million at 31 December 2001 to GBP116,334 million at 31 December 2002. These customer deposits are supplemented by the issue of subordinated loan capital and wholesale funding sources in the capital markets, as well as from direct customer contracts. Wholesale funding sources include deposits taken on the inter-bank market, certificates of deposit, sale and repurchase agreements, a Euro Medium Term Note programme, of which GBP2,364 million had been utilised for senior funding at 31 December 2002, and a US$5,000 million commercial paper programme, of which US$2,846 million had been utilised at 31 December 2002.

The ability to sell assets quickly is also an important source of liquidity for Lloyds TSB Group's banking businesses. Lloyds TSB Group holds sizeable balances of marketable Treasury and other eligible bills and debt securities which could be disposed of to provide additional funding should the need arise.

Lloyds TSB Group makes limited use of asset securitisation arrangements to provide alternative funding sources. Prior to its acquisition by Lloyds TSB Group, Black Horse Limited (formerly Chartered Trust plc) disposed of its interest in a portfolio of motor vehicles and caravan instalment credit agreements to a special purpose vehicle ("SPV"). Black Horse Limited has no interest in the share capital of this SPV, although it acts as credit manager for the administration of the portfolio and receives a fee for this service. Black Horse Limited has no obligation to the holders of the floating rate notes issued by this SPV to fund the original purchase of the portfolio, or to any other creditors of this SPV. At 31 December 2002, this SPV held GBP24 million of receivables which are included in Lloyds TSB Group's consolidated balance sheet using a linked presentation; further information is given in Note 13 to the Consolidated Financial Statements.

The following table sets out the amounts and maturities of Lloyds TSB Group's contractual cash obligations at 31 December 2002:

	Within one year GBPm	One to three years GBPm	Three to five years GBPm	Over five years GBPm	Total GBPm

Long-term debt - dated	67	505	548	3,552	4,672
Finance leases	1	-	-	-	1
Operating leases	230	388	362	290	1,270
Total	298	893	910	3,842	5,943

At 31 December 2002, Lloyds TSB Group also had GBP5,496 million of undated long-term debt outstanding.

The following table sets out the amounts and maturities of Lloyds TSB Group's other commercial commitments at 31 December 2002. These commitments are not included in Lloyds TSB Group's consolidated balance sheet.

	Within one year GBPm	One to three years GBPm	Three to five years GBPm	Over five years GBPm	Total GBPm
Acceptances	1,879	-	-	-	1,879
Guarantees	5,240	178	45	464	5,927
Other contingent liabilities	2,277	149	9	105	2,540
Total contingent liabilities	9,396	327	54	569	10,346
Lending commitments	48,106	8,847	4,983	1,853	63,789
Other commitments	548	32	5	130	715
Total commitments	48,654	8,879	4,988	1,983	64,504
Total contingents and commitments	58,050	9,206	5,042	2,552	74,850

Loan commitments are agreements to lend to customers in accordance with contractual provisions; these are either for a specified period or, as in the case of credit cards, represent a revolving credit facility which can be drawn down at any time, provided that the agreement has not been terminated. The total amounts of unused commitments do not necessarily represent future cash requirements, in that commitments often expire without being drawn upon.

Lloyds TSB Group's banking businesses are also exposed to liquidity risk through the provision of securitisation facilities to certain corporate customers. At 31 December 2002 Lloyds TSB Group acted as sponsor to two off-balance sheet entities, Monument and Obelisk, which are wholly owned by independent trusts and administered by third parties. These off-balance sheet entities purchase receivables from customers funded by secured lending from third parties, which in turn issue asset-backed commercial paper to investors. Lloyds TSB Group does not sell its own receivables to these entities, and the assets and obligations of Monument and Obelisk are not included in Lloyds TSB Group's consolidated balance sheet. However, Lloyds TSB Group provides short-term asset-backed commercial paper liquidity support facilities on commercial terms to the issuers of the commercial paper, for use in the event of a market disturbance should they be unable to roll-over maturing commercial paper or obtain alternative sources of funding.

During 2002, fee income earned by Lloyds TSB Group in relation to the Monument and Obelisk transactions totalled approximately GBP3 million. At 31 December 2002, Monument and Obelisk held assets of approximately GBP840 million, primarily loans and investments. The assets are generally of investment grade quality and are typically secured. Based upon the commitments of Monument and Obelisk to their customers as at 31 December 2002, Lloyds TSB Group provided asset-backed commercial paper liquidity support facilities of GBP910 million.

On 15 January 2003, Lloyds TSB Group entered into a new asset-backed commercial paper conduit structure. The conduit structure is divided into three subgroups of companies:

(a) the issuer companies, Cancara Asset Securitisation Limited and Cancara Asset Securitisation LLC, which issue the commercial paper and are bankruptcy remote special purpose limited liability companies, each wholly owned by an independent charitable trust;

(b) the purchasing companies, Dragon Securities Nos. 1, 2 and 3 Limited, which purchase the customers' receivables and are bankruptcy remote special purpose vehicles, each wholly owned by one or more independent charitable trusts; and

(c) an investment purchasing company, Dragon Securities No. 4 Limited, which purchases asset-backed securities from Lloyds TSB Group. As Lloyds TSB Group acts as investment advisor to the investment purchasing company and receives a performance related fee, the company will be consolidated by Lloyds TSB Group under the provisions of Financial Reporting Standard 5.

Lloyds TSB Group does not sell its own assets to the other purchasing companies or issuer companies nor does it, or any of its subsidiaries or affiliates, have an affiliation through ownership control or otherwise to these companies. However, Lloyds TSB Group does provide liquidity facilities to the issuer, purchasing and investment purchasing companies to fund short-term cash deficits that may arise through timing differences between cash receipts from the receivables and cash payments to the holders of the commercial paper. In the future it is intended that all of the business currently recorded in Monument and much of the business recorded in Obelisk will be transferred to the conduit structure. The Monument facility will then close.

Within Lloyds TSB Group's insurance and investments businesses, the principal sources of liquidity are premiums received from policyholders, charges levied upon policyholders, investment income and the proceeds from the sale and maturity of investments. The investment policies followed by Lloyds TSB Group's life assurance companies take account of anticipated cash flow requirements by matching the cash inflows with projected liabilities. Any liquidity requirements in excess of those anticipated are met from additional funds held to provide solvency margin cover; these include significant short-term cash deposits. As at 31 December 2002, these funds amounted to GBP2,211 million, representing an excess of GBP1,228 million over the required minimum solvency margin.

Based upon the levels of resources within the banking and insurance and investments businesses and the ability of Lloyds TSB Group to access the wholesale money markets or issue debt securities should the need arise, Lloyds TSB Group believes that its overall liquidity is sufficient to meet current obligations to customers, policyholders and debt holders, support expectations for future changes in asset and liability levels and carry on normal operations.

Because the principal business of Lloyds TSB Group is banking, it is able to raise substantial amounts of cash in the wholesale money markets to provide funds for acquisitions, should the need arise. In deciding whether Lloyds TSB Group has sufficient resources to be able to make an acquisition the key factor is not the availability of cash, but the ability of Lloyds TSB Group, and the authorised institutions within Lloyds TSB Group, to continue to meet the capital adequacy requirements of the regulatory authorities, see "Capital ratios" below.

Capital resources

The total capital resources of Lloyds TSB Group are set out below:

	31 December 2002 GBPm	31 December 2001 GBPm	31 December 2000 GBPm
Minority interests (equity and non-equity)	731	546	552
Called-up share capital	1,416	1,411	1,396
Share premium account	1,093	959	595
Merger reserve	343	343	343
Profit and loss account	5,120	7,643	9,567
Shareholders' funds (equity)	7,972	10,356	11,901
	8,703	10,902	12,453
Undated loan capital	5,496	4,102	3,391
Dated loan capital	4,672	4,006	4,119
Total capital resources	18,871	19,010	19,963

Lloyds TSB Group's total capital resources decreased by GBP139 million during 2002.

Shareholders' funds decreased by GBP2,384 million, due to the actuarial losses of GBP2,331 million relating to the Group's post-retirement benefit schemes, largely caused by the significant reduction in equity market values, which have been recognised in the Lloyds TSB Group's reserves. Loan capital increased by GBP2,060 million, due to the issue of additional subordinated loan capital to support the expansion of Lloyds TSB Group's balance sheet.

Capital ratios

The international standard for measuring capital adequacy is the risk asset ratio, which relates regulatory capital to balance sheet assets and off-balance sheet exposures weighted according to broad categories of risk.

Lloyds TSB Group's regulatory capital is divided into tiers defined by the European Community Own Funds Directive as implemented in the UK by the FSA's Interim Prudential Sourcebook for Banks. Tier 1 comprises mainly shareholders' funds, tier 1 capital instruments and minority interests, after deducting goodwill and intangible assets. Tier 2 comprises general loan loss provisions, and qualifying subordinated loan capital, with restrictions on the amount of general provisions and loan capital which may be included. The amount of qualifying tier 2 capital cannot exceed that of tier 1 capital. Total capital is reduced by deducting investments in subsidiaries and associates which are not consolidated for regulatory purposes and investments in the capital of other credit/financial institutions. In the case of Lloyds TSB Group, this means that the net assets of its life assurance and general insurance businesses are deducted from Lloyds TSB Group's regulatory capital.

Banking operations are categorised as either banking book or trading book (broadly, activities which are accounted for on a mark-to-market basis). Risk-weighted assets are determined according to a broad categorisation of the nature of each asset or exposure and counterparty and, for the trading book, by taking into account market-related risks.

	31 December 2002 GBPm	31 December 2001 GBPm	31 December 2000 GBPm
Capital: tier 1	9,490	8,408	7,446
tier 2	8,846	7,831	7,446
	18,336	16,239	14,892
Supervisory deductions	(6,588)	(6,752)	(6,809)
Total regulatory capital	11,748	9,487	8,083
Total risk-weighted assets	122,411	107,861	93,211
Post-tax return on average risk-weighted assets	1.61%	2.26%	3.07%
Risk asset ratios: total capital	9.6%	8.8%	8.7%
tier 1	7.8%	7.8%	8.0%

At 31 December 2002, the risk asset ratios were 9.6 per cent for total capital and 7.8 per cent for tier 1 capital. The 7.8 per cent tier 1 capital ratio appears higher than would perhaps be expected for Lloyds TSB Group. This reflects the higher level of supervisory deductions resulting from Lloyds TSB Group's significantly increased investment in its life assurance operations as a result of the acquisition of Scottish Widows.

70

There are strict limits imposed by the regulatory authorities as to the proportion of Lloyds TSB Group's regulatory capital base that can be made up of subordinated debt and preferred securities. Lloyds TSB Group's capacity to raise new debt capital for regulatory purposes increases as profits are retained; at 31 December 2002, Lloyds TSB Group had capacity to raise approximately GBP650 million of tier 2 debt capital, compared to approximately GBP600 million at 31 December 2001. This small increase reflects the combined effects of retained profits, which were adversely affected by losses on the investments supporting the long-term assurance business, the issuance of tier 1 and tier 2 securities, and exchange rate movements. The unpredictable nature of movements in the value of the investments supporting the long-term assurance funds could cause the amount of qualifying tier 2 capital to be restricted because of falling tier 1 resources. The Lloyds TSB Group seeks to ensure that even in the event of such restrictions, that total capital ratio will remain adequate.

During 2002, total capital for regulatory purposes increased by GBP2,261 million to GBP11,748 million. Tier 1 capital increased by GBP1,082 million, mainly from the issue of new tier 1 capital instruments. Tier 2 capital increased by GBP1,015 million and supervisory deductions decreased by GBP164 million, as a result of a decrease in the Lloyds TSB Group's embedded value to GBP6,228 million, from GBP6,366 million in December 2001.

Risk-weighted assets increased to GBP122,411 million at 31 December 2002 and the post-tax return on average risk-weighted assets was 1.61 per cent.

The free asset ratio is a common measure of financial strength in the UK for long-term businesses. It is the ratio of assets less liabilities (including actuarial reserves but before the required regulatory minimum solvency margin) expressed as a percentage of the liabilities. It is derived from annual insurance returns which were completed in March 2003. At 31 December 2002 the free asset ratio for Scottish Widows plc was 12.2 per cent, compared with 11.5 per cent at 31 December 2001. This free asset ratio included some GBP400 million allowance for future profits (December 2001: nil). After adjusting for the inclusion of the required regulatory minimum solvency margin within liabilities, the Scottish Widows plc ratio was 8.0 per cent at 31 December 2002. In common with its peers, Scottish Widows plc is required to maintain adequate solvency, as determined by the FSA's Interim Prudential Sourcebook for Insurers. One of the factors influencing solvency is the level of equity markets: the FTSE 100 index could fall below 3,000 (compared with 4,048 at 31 May 2003) before the Lloyds TSB Group would need to inject capital into its life operations. At this level the Lloyds TSB Group may need to inject up to GBP300 million to support business growth.

Corporate Social Responsibility

Lloyds TSB Group adopts a responsible attitude to Social, Environmental and Ethical ("SEE") issues, and publishes a separate document on its role in the community, its code of business conduct and its environmental performance.

The Group has a dedicated Environmental Risk unit which is responsible for the development of environmental policies and procedures, and provides practical advice and guidance on environmental issues to business units. During the year, the Lloyds TSB Group has reviewed its SEE performance and is of the opinion that it already complies with the majority of the guidelines published by the Association of British Insurers in 2001. The Lloyds TSB Group continues to develop its policies and procedures and will monitor its performance more rigorously in 2003.

Investment portfolio

Investment securities and other securities

The following table sets out the book value and valuation of Lloyds TSB Group's investment securities and other securities at 31 December for each of the three years indicated.

	2002		2001		2000	
	Book value GBPm	Valuation GBPm	Book value GBPm	Valuation GBPm	Book value GBPm	Valuation GBPm
Investment securities(1)						
Bank and building society certificates of deposit	3,147	3,148	4,670	4,677	3,034	3,034
Corporate debt securities	1,495	1,496	613	616	465	466
Mortgage backed securities	893	892	521	527	18	18
Other asset backed securities	2,817	2,820	1,193	1,198	162	163
Other debt securities	1,369	1,367	1,211	1,209	619	618
Securities of the US Treasury and US government agencies	1,740	1,736	1,148	1,147	379	378
Other government securities	400	405	1,633	1,829	1,717	2,136
Other public sector	1	1	-	-	1	1

securities						
Equity shares	38	67	38	66	41	102
	11,900	11,932	11,027	11,269	6,436	6,916
Other securities						
UK government securities	-	-	31	31	893	893
Securities of the US Treasury and US government agencies	40	40	-	-	16	16
Other government securities	5,995	5,995	4,072	4,072	2,151	2,151
Other public sector securities	112	112	151	151	131	131
Bank and building society certificates of deposit	340	340	234	234	105	105
Corporate debt securities	7,842	7,842	7,102	7,102	4,671	4,671
Mortgage backed securities	1,838	1,838	1,054	1,054	242	242
Other asset backed securities	1,191	1,191	592	592	-	-
Other debt securities	94	94	-	-	1	1
Equity shares	168	168	187	187	206	206
	17,620	17,620	13,423	13,423	8,416	8,416

---

(1) Investment securities are those intended for use on a continuing basis in the activities of Lloyds TSB Group and not for dealing purposes. Investment securities held by Lloyds TSB Group's insurance businesses are not included.

72

Maturities and weighted average yields of debt securities

The weighted average yield for each range of maturities is calculated by dividing the annualised interest income prevailing at 31 December 2002 by the book value of securities held at that date.

Maturing within one year		Maturing after one but within five years		Maturing after five but within ten years		Maturing after ten years	
Amount GBPm	Yield %	Amount GBPm	Yield %	Amount GBPm	Yield %	Amount GBPm	Yield %

Investment securities								
Bank and building society certificates of deposit	3,112	3.7	35	3.8	–	–	–	–
Corporate debt securities	59	4.2	973	5.2	409	2.1	54	3.3
Mortgage backed securities	–	–	588	4.4	305	4.9	–	–
Other asset backed securities	48	2.4	1,974	3.6	767	3.6	28	2.2
Other debt securities	215	1.8	696	3.1	458	4.2	–	–
Securities of the US Treasury and US government agencies	6	3.9	370	2.1	1,313	2.2	51	2.2
Other government securities	349	4.1	20	2.4	31	3.2	–	–
Other public sector securities	–	–	1	11.4	–	–	–	–
Total book value	3,789	3.6	4,657	3.9	3,283	3.1	133	2.7

	Maturing within one year		Maturing after one but within five years		Maturing after five but within ten years		Maturing after ten years	
	Amount GBPm	Yield %	Amount GBPm	Yield %	Amount GBPm	Yield %	Amount GBPm	Yield %
Other securities								
Securities of the US Treasury and US government agencies	–	–	–	–	40	3.9	–	–
Other government securities	715	4.0	2,376	3.6	2,238	4.2	666	7.9
Other public sector securities	–	–	77	3.1	35	4.1	–	–
Bank and building	326	6.6	14	22.5	–	–	–	–

society certificates of deposit								
Corporate debt securities	1,513	2.6	5,501	3.1	828	3.9	-	-
Mortgage backed securities	50	3.9	568	3.3	1,177	3.7	43	4.7
Other asset backed securities	-	-	684	3.4	428	3.8	79	4.5
Other debt securities	18	15.8	76	17.6	-	-	-	-
Total book value	2,622	3.6	9,296	3.4	4,746	4.0	788	7.5

Maturity analysis and interest rate sensitivity of loans and advances to customers and banks as at 31 December 2002

The following table analyses the maturity profile and interest rate sensitivity of loans by type on a contractual repayment basis as at 31 December 2002. All amounts are before deduction of provisions and interest in suspense. Demand loans are included in the "maturing in one year or less" category.

	Maturing in one year or less GBPm	Maturing after one year but not more than five years GBPm	Maturing after five years GBPm	Total GBPm
Domestic:				
Loans and advances to banks	13,715	1,245	331	15,291
Loans and advances to customers:				
Mortgages	1,620	8,150	52,697	62,467
Other personal lending	9,151	5,660	120	14,931
Financial, business and other services	4,070	2,242	2,040	8,352
Lease financing	521	1,667	5,097	7,285
Hire purchase	2,804	3,105	81	5,990
Others	9,314	4,811	4,907	19,032
Total domestic loans	41,195	26,880	65,273	133,348
Total foreign loans	8,600	5,457	6,422	20,479
Total loans	49,795	32,337	71,695	153,827
Of which:				
Fixed interest rate	31,821	15,385	26,592	73,798
Variable interest rate	17,974	16,952	45,103	80,029

Deposits

The following table shows the details of Lloyds TSB Group's average customer deposits in each of the past three years.

	2002		2001		2000	
	Average balance GBPm	Average rate %	Average balance GBPm	Average rate %	Average balance GBPm	Average rate %
Deposits in domestic offices						
Non interest bearing demand deposits	5,985	-	6,182	-	6,058	-
Interest bearing demand deposits	19,150	0.49	18,034	0.73	17,836	1.36
Savings deposits	43,585	3.14	38,743	4.49	34,468	5.26
Time deposits	19,274	4.04	15,856	5.39	19,767	5.95
Total domestic office deposits	87,994	2.55	78,815	3.46	78,129	4.14
Deposits in foreign offices						
Non interest bearing demand deposits	789	-	595	-	635	-
Interest bearing demand deposits	1,410	1.56	991	2.93	793	4.04
Savings deposits	2,049	5.08	1,842	5.16	1,901	4.58
Time deposits	7,806	11.11	8,044	9.95	7,632	8.94
Total foreign office deposits	12,054	8.24	11,472	8.05	10,961	7.31
Total average deposits	100,048	3.23	90,287	4.04	89,090	4.53

Certificates of deposit and other time deposits

The following table gives details of Lloyds TSB Group's certificates of deposit issued and other time deposits as at 31 December 2002 individually in excess of US $100,000 (or equivalent in another currency) by time remaining to maturity.

	3 months or less GBPm	Over 3 months but within 6 months GBPm	Over 6 months but within 12 months GBPm	Over 12 months GBPm	Total GBPm
Domestic					
Certificates of deposit	10,749	3,090	1,555	15	15,409
Time deposits	24,898	1,404	593	2,373	29,268
	35,647	4,494	2,148	2,388	44,677
Foreign					
Certificates of deposit and other time deposits	10,672	1,574	429	778	13,453
Total	46,319	6,068	2,577	3,166	58,130

Short-term borrowings

Short-term borrowings are included within the balance sheet captions "Deposits by banks", "Customer accounts" and "Debt securities in issue" and are not identified separately on the balance sheet. The short-term borrowings of Lloyds TSB Group consist of overdrafts from banks, securities sold under agreements to repurchase, certificates of deposit issued, commercial paper and promissory notes issued and other marketable paper. Securities sold under agreements to repurchase and certificates of deposit issued are the only significant short-term borrowings of Lloyds TSB Group.

74

The following table gives details of the significant short-term borrowings of Lloyds TSB Group for each of the past three years.

	2002 GBPm	2001 GBPm	2000 GBPm
Liabilities in respect of securities sold under repurchase agreements			
Balance at the period end	6,157	5,516	4,030
Average balance for the period	6,294	3,898	3,000
Maximum balance during the period	9,697	5,516	6,158
Average interest rate during the period	4.7%	6.7%	7.3%
Interest rate at the period end	4.6%	6.1%	6.4%
Certificates of deposit issued			
Balance at the period end	21,246	17,060	12,052
Average balance for the period	22,040	14,643	11,910
Maximum balance during the period	26,199	18,160	13,645
Average interest rate during the period	3.2%	5.0%	6.3%
Interest rate at the period end	3.2%	3.7%	6.3%

MANAGEMENT AND EMPLOYEES

Directors and senior management

Lloyds TSB Group plc is led and controlled by a board comprising executive and non-executive directors with wide experience. The appointment of directors is considered by the board and, following the provisions in the articles of association, they must retire by rotation, and may stand for re-election by the shareholders, at least every three years. Executive directors normally retire at age 60 as required by their service agreements. Independent non-executive directors are appointed for a specified term, not exceeding five years, which may be renewed.

The board meets nine times a year and a programme is prepared and agreed each year, which ensures that the directors are able regularly to review corporate strategy and the operations and results of the business units in the Lloyds TSB Group and to discharge their other duties. The roles of the chairmen, the group chief executive and the board and its governance arrangements are reviewed annually.

The board has a chairman's committee, comprising the chairman, the deputy chairman, the group chief executive and his deputy. The chairman's committee meets to discuss current issues and strategy, examine and test proposals and prepare for board meetings. It also has specific powers delegated to it by the board. The board also has audit, nomination and remuneration committees which comply with the code annexed to the UK Listing Authority's listing rules.

The chairman, the group chief executive and the group finance director have meetings with representatives of institutional shareholders and all shareholders are encouraged to participate in Lloyds TSB Group's annual general meeting.

Board of directors

Biographical details of the board of directors are given below.

Maarten A van den Bergh <   Chairman

Joined Lloyds TSB Group in 2000 as deputy chairman and was appointed chairman in 2001. Joined the Royal Dutch/Shell Group of companies in 1968 and after a number of senior and general management appointments in that group, became group managing director in 1992. Appointed president of Royal Dutch Petroleum Company and vice chairman of the committee of managing directors of the Royal Dutch/Shell Group in 1998 and continued in these roles until 2000. A non-executive director of Royal Dutch Petroleum Company, BT Group and British Airways. Elected by the shareholders to the board in April 2001. Aged 61.

David P Pritchard
Deputy Chairman

Joined TSB Group in 1995 as group treasurer. Seconded to the Securities and Investments Board as head of supervision & standards, markets & exchanges, from 1996 to 1998. Appointed to the board in 1998, as group executive director, Wholesale and International Banking. Retired from executive duties in 2003, when he was appointed deputy chairman. Held senior and general management appointments with Citicorp from 1978 to 1986 and Royal Bank of Canada from 1986 to 1995. A non-executive director of the London Clearing House. Most recently re-elected by the shareholders to the board in April 2001. Aged 58.

Executive directors

J Eric Daniels
Group Chief Executive

Joined the board in 2001 as group executive director, UK Retail Banking before his appointment as group chief executive in 2003. Served with Citibank from 1975 and held a number of senior and general management appointments in the USA, South America and Europe before becoming chief operating officer of Citibank Consumer Bank in 1998. Following the Citibank/Travelers merger in 1998, he was chairman and chief executive officer of Travelers Life and Annuity until 2000. Chairman and chief executive officer of Zona Financiera from 2000 to 2001. Elected by the shareholders to the board in April 2002. Aged 51.

Michael E Fairey
Deputy Group Chief Executive

Joined TSB Group in 1991 and held a number of senior and general management appointments before being appointed to the board in 1997 and deputy group chief executive in 1998. Joined Barclays Bank in 1967 and held a number of senior and general management appointments, including managing director of Barclays Direct Lending Services from 1990 to 1991. Most recently re-elected by the shareholders to the board in April 2002. Aged 55.

Michael D Ross CBE
Deputy Group Chief Executive

Joined the board in 2000. Joined Scottish Widows in 1964 and following a number of senior and general management appointments became group chief executive of that company in 1991. Chairman of the Association of British Insurers. Most recently re-elected by the shareholders to the board in April 2003. Aged 56.

Peter G E Ayliffe
Group Executive Director, UK Retail Banking

Joined the board in 2003, having held a number of senior and general management appointments in the Lloyds TSB Group since 1985. Appointed Managing Director, Personal Banking in 2000. Served with National Westminster Bank from 1974 to 1985. Aged 50.

Philip R Hampton
Group Finance Director

Joined the board in 2002. Previously, finance director of BT Group from 2000 to 2002, BG Group from 1996 to 2000 and British Steel from 1990 to 1996. Before that, he worked for Coopers & Lybrand from 1975 to 1980 and Lazard Brothers from 1981 to 1990. A non-executive director of RMC Group. Elected by the shareholders to the board in April 2003. Aged 49.

Archie G Kane
Group Executive Director, IT and Operations

Joined TSB Commercial Holdings in 1986 and held a number of senior and general management appointments in Lloyds TSB Group before being appointed to the board in 2000. After some 10 years in the accountancy profession, joined General Telephone & Electronics Corporation in 1980, serving as finance director in the UK from 1983 to 1985. Chairman of the council of the Association for Payment Clearing Services. Most recently re-elected by the shareholders to the board in

April 2003. Aged 51.

Steve C Targett
Group Executive Director, Wholesale and International Banking

Joined the board in 2003. Served with National Australia Bank from 1997, where he held a number of senior and general management appointments in Australia and the UK before becoming chief executive officer, Europe, in 2002. Previously held a number of senior and general management appointments in Cargill, a commodity trading group, from 1980 to 1988, State Bank of South Australia from 1988 to 1991 and ANZ Bank from 1991 to 1997. His early career, between 1972 and 1980, was spent with National Australia Bank. Elected by the shareholders to the board in April 2003. Aged 48.

Non-executive directors

Wolfgang C G Berndt >+

Joined the board in 2003. Joined Procter and Gamble in 1967 and held a number of senior and general management appointments in Europe and North America, before retiring in 2001. A non-executive director of Cadbury Schweppes and GfK AG. Chairman of the Institute for the Future. Aged 60.

Ewan Brown CBE FRSE >**
Chairman of Lloyds TSB Scotland

A director since 1999. A non-executive director of Lloyds TSB Scotland since 1997. Executive director of Noble Grossart since 1971. Chairman of Transport Initiatives Edinburgh. A non-executive director of John Wood Group and Stagecoach Holdings. Most recently re-elected by the shareholders to the board in April 2001. Aged 61.

Gavin J N Gemmell CBE >*
Chairman of Scottish Widows

Joined the board in 2002. A non-executive director of Scottish Widows, having been appointed to the board of that company before it became a member of the Lloyds TSB Group. Retired as senior partner of Baillie Gifford in 2001, after 37 years with that firm. A non-executive director of Archangel Informal Investment. Chairman of the court of Heriot-Watt University. Elected by the shareholders to the board in April 2002. Aged 61.

Christopher S Gibson-Smith >+

A director since 1999. Chairman of National Air Traffic Services and to be Chairman of the London Stock Exchange from July 2003. Joined BP in 1970, serving as managing director from 1997 to 2001, having held senior and general management appointments in the UK, USA, Canada and Europe. A non-executive director of The British Land Company. Most recently re-elected by the shareholders to the board in April 2002. Aged 57.

DeAnne S Julius CBE >+ss

Joined the board in 2001. Held a number of senior appointments in the UK and USA with the World Bank, Royal Dutch/Shell Group and British Airways, before membership of the Bank of England Monetary Policy Committee from 1997 to 2001. Chaired HM Treasury's banking services consumer codes review group in 2000/1. To be chairman of the Royal Institute of International Affairs from July 2003. A non-executive director of the Bank of England, BP, Serco Group and Roche

Holdings SA. Elected by the shareholders to the board in April 2002. Aged 54.

Angela A Knight >*

Joined the board in 2003. Deputy chairman of Scottish Widows, having been appointed to the board of that company before it became a member of the Lloyds TSB Group. A member of parliament from 1992 to 1997 and Economic Secretary to the Treasury from 1995 to 1997. Chief Executive of the Association of Private Client Investment Managers and Stockbrokers. A non-executive director of LogicaCMG, South East Water and the Port of London Authority. Aged 52.

Sir Tom McKillop ^#

A director since 1999. Joined ICI in 1969 and held a number of senior and general management appointments before the demerger in 1993, when Zeneca was created. Chief executive of Zeneca Pharmaceuticals from 1994 to 1999 and chief executive of AstraZeneca from 1999. Pro-chancellor of Leicester University. Most recently re-elected by the shareholders to the board in April 2002. Aged 60.

The Earl of Selborne KBE FRS >*ss

A director since 1995, having been a director of Lloyds Bank since 1994. Managing director of The Blackmoor Estate, his family business. Chancellor of Southampton University since 1996. President of the Royal Geographical Society from 1997 to 2000. Most recently re-elected by the shareholders to the board in April 2002. Aged 63.

*	Member of the audit committee
**	Chairman of the audit committee
+	Member of the remuneration committee
#	Chairman of the remuneration committee
ss	Member of the nomination committee
<	Chairman of the nomination committee
>	Independent director
^	Senior independent director

Compensation

Directors' remuneration

The remuneration committee makes recommendations to the board on the framework of executive directors' remuneration and its cost, and determines, on the board's behalf, specific remuneration packages for each of the chairman, the deputy chairman and the executive directors. Additionally, all the non-executive directors receive the minutes of remuneration committee meetings and have the opportunity to comment and have their views taken into account before the committee's decisions are implemented. See also "- Board practices - Remuneration committee".

Executive directors' remuneration policy

Lloyds TSB Group aims to ensure that the executive directors' remuneration arrangements, in line with the Lloyds TSB Group's overall practice on pay and benefits, are competitive and designed to attract, retain and motivate executive directors of the highest calibre, who are expected to perform to the highest standards. Account is taken of information, from internal and independent sources, on the remuneration for comparable positions in a wide range of FTSE 100 companies. The strategy for executive directors' pay is for basic salaries to reflect the relevant market median; for benefits such as a company car, medical insurance and pension to reflect market practice; and for total direct compensation (basic salary, annual incentives and the value of long-term incentives) to be at the upper quartile of the market place, provided that performance justifies the amount. This strategy is consistent with the Lloyds TSB Group's belief that performance should determine a significant proportion of the total remuneration package for executive directors. There are no plans to change the strategy.

The fees of the non-executive directors are agreed by the board within a total amount determined by the shareholders. They are designed to recognise the significant responsibilities of directors and to attract individuals with the necessary experience and ability to make an important contribution to the Lloyds TSB Group's affairs. The fees, which are neither performance related nor pensionable, are comparable with those paid by other companies.

78

Reward package. Each year, with the help of external management consultants, the total remuneration package of the directors is reviewed, and in 2002 The Hay Group Management Limited were commissioned by the remuneration committee to conduct the review. The current package for executive directors comprises the following elements:

Basic salary. The aim is to ensure that salaries are competitively set in relation to similar jobs in a wide range of FTSE 100 companies.

Current salaries for the chairman, deputy chairman and executive directors, following the most recent salary review are:

Mr Ayliffe	GBP375,000
Mr Daniels	GBP700,000
Mr Fairey	GBP498,000
Mr Hampton	GBP483,000
Mr Kane	GBP397,500
Mr Pritchard	GBP233,520
Mr Ross	GBP443,000
Mr Targett	GBP450,000
Mr van den Bergh	GBP422,500

Annual incentive. The annual incentive scheme is designed to reflect specific goals linked to the performance of the business. In 2002, the group chief executive had a maximum incentive opportunity equal to 100 per cent of his salary as did Mr Daniels, whose bonus opportunity and payment for 2002 were agreed as part of his recruitment package. Each of the other executive directors could earn an incentive equal to 75 per cent of their salary. The awards were based on Lloyds TSB Group performance and the attainment of predetermined targets relating to total income, profit before tax and economic profit. Each received an award equal to 4.7 per cent of salary based on achievement against the income target, which was met in part. No bonus has been earned for the other targets.

In 2003, all the executive directors will have a maximum incentive opportunity equal to 100 per cent of their salaries. Awards will be based on Lloyds TSB Group performance, with predetermined targets relating to profit before tax and economic profit. 75 per cent of the award will be payable on achievement of profit before tax and economic profit relating to the Lloyds TSB Group's stretching budget for 2003 and the remuneration committee has set a higher target for the maximum award. The threshold performance levels, below which no bonus will be payable, have also been set by the remuneration committee at higher figures than those achieved in 2002.

The remuneration committee reviewed the attainment of targets in 2002 and agreed the incentive payments, and the auditors confirmed the calculations.

These payments are not pensionable.

Medium-term incentive plan. In April 2000, shareholders approved the introduction of a medium-term incentive plan which gave the executive directors serving at that time the opportunity of an award, deferred until after the end of 2002, which was the subject of two performance targets, based on the efficiency ratio and return on equity. For the group chief executive, the maximum potential award was equal to 50 per cent of aggregate basic salary for the years 2000 to 2002 and for other executive directors, the maximum potential award was equal to 25 per cent of aggregate basic salary for those three years.

The two minimum performance targets were a reduction in Lloyds TSB Group's efficiency ratio to 37 per cent by the end of 2002 and a return on equity of 28 per cent by the end of 2002. No payment was to be made under the plan unless both these minimum targets were met. The performance targets were not met by the end of 2002 and, accordingly, the plan ended without any payments being made.

Executive share option schemes. All executive share options granted since March 1996 have been subject to performance conditions. Performance conditions are set when the grant of options is made and the options cannot normally be exercised unless the conditions have been met. To meet the performance conditions applied to options granted since August 2001, Lloyds TSB Group plc's ranking, based on total shareholder return (calculated by reference to both dividends and growth in share price) over the relevant (three year) period, within the comparator group, must be at least ninth. Hoare Govett independently provides the information on total shareholder return and Lloyds TSB Group plc's ranking and the auditors are also involved before the remuneration committee confirms whether the conditions have been met.

In 2002, options were granted to executive directors and senior executives within the scheme limits. These limits relate to the number of shares under option and the price payable on exercise. The maximum limit for the grant of options to an executive director in any one year is equal to one and a half times annual basic salary multiplied by a performance multiplier of 3.5 (although in exceptional circumstances, for example on the recruitment of a new executive, that could be increased to four times annual basic salary multiplied by 3.5).

The full grant of options for executive directors will only become exercisable if Lloyds TSB Group plc is ranked first within the comparator group.

The following table illustrates the percentage of the grant which would be exercisable depending on the ranking within the comparator group.

At the end of 2002 Lloyds TSB Group plc was ranked:

6th after two years of the performance period for options granted in 2001; and

11th after one year of the performance period for options granted in 2002.

Option awards have been made to the executive directors in February 2003 and were subject to the same scheme limits and performance conditions as outlined above.

Ranking position within comparator group	% of option which may be exercised

1	100
2	86
3	71
4	57
5	43
6	29
7	23
8	17
9	14
10 or below	Nil - options not exercisable

The current constituents of the comparator group are:

Abbey National	ABN Amro	Alliance and Leicester
Aviva	Barclays	Citigroup
Fortis	HBOS	HSBC Holdings
ING	Legal and General	National Australia Bank
Prudential	Royal Bank of Scotland	Royal & Sun Alliance
Standard Chartered		

In addition, share options have been granted in previous years in accordance with the relevant scheme rules and market practice at that time. The table on page 86 includes options granted under these previous schemes.

Options granted	Performance conditions
Prior to March 1996	None
March 1996 - August 1999	That Lloyds TSB Group plc's ranking based on shareholder return (calculated by reference to both dividends and growth in share price) over the relevant period should be in the top fifty companies of the FTSE 100 and that there must have been growth in earnings per share which is equal to the aggregate percentage change in the Retail Price Index plus two percentage points for each complete year of the relevant period.
March 2000 - March 2001	As for March 1996 - August 1999 except that there must have been growth in the earnings per share equal to the change in the Retail Price Index plus three percentage points for each complete year of the relevant period.

The remuneration committee chose the relevant performance condition, where applicable, because it was felt to be challenging, aligned to shareholder interests and appropriate at the time.

At the annual general meeting in April 2003, the shareholders approved an amendment to the rules of the executive share option schemes. Under the previous rules, a share option could not be granted to any person who, at the date of grant, was within 2 years of retirement. The rules of the schemes were amended to allow share options to be granted to executives up to six months before retirement.

Since the introduction of the new performance condition in 2001, the exercise of options after retirement would still require the condition to be satisfied over the original performance period. Also, if the optionholder retired within 3 years of the date of the grant, the number of shares which could be acquired on exercise would be reduced according to the length of time the optionholder was employed between the date of grant and the date of retirement.

Share retention plan and Lloyds TSB Group plc Share Plan 2003. Two further share plans have been established as part of the recent recruitment of executive directors to the Lloyds TSB Group. During 2001, the share retention plan was adopted, specifically to facilitate the recruitment of Mr Daniels, who was based in the USA, as part of the remuneration package considered necessary to attract him to the UK. Mr Daniels is the only participant in the plan and he became eligible to participate in it when he joined Lloyds TSB Group plc on 1 November 2001. On 2 November 2001, an option was granted to Mr Daniels under the plan to acquire 216,763 ordinary shares in Lloyds TSB Group plc (with a value of GBP1.5 million at the date of grant) for a total price of GBP1. No further options may be granted to him under the plan.

The Lloyds TSB Group plc Share Plan 2003 was adopted in March 2003, specifically to facilitate the recruitment of Mr Targett, to compensate him for the value of the options he had with his previous employer, which lapsed when he left them to join the Lloyds TSB Group. Mr Targett is the only participant in the plan and he became eligible to participate in it when he joined Lloyds TSB Group plc on 10 March 2003. On 11 March 2003, an option was granted to him under the plan to acquire 331,125 ordinary shares in Lloyds TSB Group plc (with a value of GBP1 million at the date of grant) for a total price of GBP1. No further options may be granted to him under the plan.

No new shares will be issued to satisfy the options under either of these plans.

The options are designed to encourage the participants to remain with Lloyds TSB Group plc. Accordingly, the options, which are not subject to any performance conditions, will normally become exercisable only if the participants remain as employees, and have not given notice of resignation, on 31 December 2004, in the case of Mr Daniels, and 31 December 2005, in the case of Mr Targett. The options will also be exercisable if the participants cease to be employees before those dates in certain circumstances described in their service agreements, in which case the options will be exercisable for six months and then lapse. For both plans, these circumstances include the participant being entitled to terminate his service agreement without notice by reason of his employer's conduct or the participant being removed as a director or employee otherwise than in accordance with that agreement. The options may also become exercisable early on a takeover or reconstruction of Lloyds TSB Group plc.

In the case of Mr Daniels' option, such circumstances also include there being any material diminution of his duties or, within 18 months of his employment, there being a change of circumstances of Lloyds TSB Group plc such that there was, in his reasonable judgement, a material and adverse effect on his prospects or a material diminution of his status.

In the case of Mr Targett's option, the circumstances also include his service agreement being terminated by Lloyds TSB Group plc due to sickness or injury, or if he dies (in which case his personal representatives would generally have twelve months from the date of death to exercise the option).

Both of these options will lapse if the participant ceases to be an employee, or gives notice of resignation, before the normal exercise dates, except in the circumstances described above. Mr Daniels' option will lapse if he dies before the normal exercise date.
The number and/or nominal amount of shares may be adjusted by the board on

certain variations in the share capital of Lloyds TSB Group plc.

The benefits conferred by these options are not pensionable and the options are not transferable.

Other share plans. The executive directors, the chairman and the deputy chairman may participate in the Group's 'Sharesave' scheme and 'Shareplan' on the same basis as other employees.

Pensions. Executive directors are entitled to pensions based on salary and length of service with Lloyds TSB Group, with a maximum pension of two-thirds of final salary.

81

Directors' emoluments for 2002

	Salaries/fees GBP000	Other benefits GBP000	Performance -related payments GBP000	Shareplan GBP000	2002 Total GBP000	2001 GBP000
Current directors who served during 2002:						
Ewan Brown	60				60	59
J E Daniels	450	349	450	14	1,263	192
M E Fairey	470	137	22	14	643	791
G J N Gemmell	68				68	-
C S Gibson-Smith	38				38	38
P R Hampton	268	9	13	8	298	-
D S Julius	38				38	9
A G Kane	375	14	18	11	418	548
Sir Tom McKillop	45				45	45
D P Pritchard	390	17	18	12	437	588
M D Ross	430	15	20	13	478	650
Lord Selborne	33				33	43
M A van den Bergh	400	15			415	406
Former directors who served during 2002:						
M K Atkinson	174	370	18	5	567	588
A C Butler	40				40	40
P B Ellwood	660	22	31	20	733	1,001
S M Forbes	38				38	38
A E Moore	210	11		6	227	229
L M Urquhart	25				25	93
Former directors who served during 2001						391
	4,212	959	590	103	5,864	5,749

"Other benefits" include the use of a car, private medical insurance, life insurance cover and payments to a former executive director on termination of his service contract (see below). Allowances for relocation, housing and legal advice arising from Mr Daniels' service agreement and an additional payment in respect of the contribution to the separate fund relating to Mr Fairey's pension, are also included. The separate fund was established to cover pension obligations of those who joined Lloyds TSB Group after 1 June 1989 and who are subject to the Inland Revenue earnings cap relating to pensions, introduced by the Finance Act 1989.

GBP348,637 included in "other benefits"' for Mr Atkinson represents the amount to which he was contractually entitled when his employment was terminated on 31 May 2002. This included 12 months' salary from which he elected to pay GBP318,637 to purchase additional pension from Lloyds TSB Group Pension Scheme No. 1. As part of his termination package, he is also entitled to a bonus reflecting what he would have received during his notice period. He became entitled to a pension of GBP273,514 immediately when his employment terminated, which took into account the additional 12 months' service for the notice period. He also continues to receive beneficial rights to medical insurance and use of a car for 12 months after departure. His outstanding share options are exercisable either up to 12 months after departure or, for those options granted after August 2001, at the later appropriate time providing the performance condition has been met.

Performance-related payments

These payments relate solely to cash bonuses earned in 2002 under the annual incentive scheme. They do not include any amounts relating to the former medium-term incentive plan, approved by shareholders in 2000, which ended in 2002 without any payments being made, as the relevant performance targets were not met.

Shareplan

Amounts shown are those received by directors in respect of the Group's Shareplan. Under the scheme, employees received, in April 2003, an award equal to 3 per cent of salary received in 2002. A maximum of GBP3,000 was received in shares for those eligible, with any balance paid in cash.

Directors' pensions in 2002

The executive directors are all members of one of the defined benefit schemes provided by the Lloyds TSB Group. Those directors who joined the Group after 1 June 1989 have pensions provided on salary in excess of the earnings cap either through membership of a Funded Unapproved Retirement Benefits Scheme ('FURBS') or by an unfunded pension promise.

Retirement pensions accrue at rates of between 1/60 and 1/30 of basic salary.

With the exception of Mr Pritchard, directors have a normal retirement age of 60. Mr Pritchard retired on 16 April 2003. For executive directors, in the event of death in service, a lump sum of 4 times salary is payable plus a spouse's pension of 2/3 of the member's prospective pension. On death in retirement, a spouse's pension of 2/3 of the member's pension is payable. The schemes are non-contributory.

Mr Pritchard has a deferred cash entitlement of GBP71,310 from his membership of the defined contribution section of the Group's FURBS.

	Accrued pension at 31 December 2002	Accrued pension at 31 December 2001	Transfer value at 31 December 2002	Transfer value at 31 December 2001	Change in transfer value	Add earne D
	(a)	(b)	(c)	(d)	(c) - (d)	
Current directors who served during 2002:						
J E Daniels	31,250	23,750	346,555	312,504	34,051	
M E Fairey	155,805	127,183	2,075,301	1,862,642	212,659	
P R Hampton	5,963	-	58,631	-	58,631	
A G Kane	144,353	118,599	1,514,190	1,503,489	10,701	
D P Pritchard	38,974	30,582	656,073	518,412	137,661	
M D Ross	274,125	245,229	4,395,896	3,564,387	831,509	
In addition, the following unfunded benefits have accrued for Mr van den Bergh instead of a sal						
M A van den Bergh	3,378	-	36,160	-	36,160	
Former directors who served during 2002:						
M K Atkinson	273,514	227,274	4,632,189	3,455,667	1,176,522	
P B Ellwood	393,875	336,441	7,093,775	5,943,051	1,150,724	

Columns (a) and (b) represent the deferred pension to which the directors would have been entitled had they left the Group on 31 December 2002 and 2001, respectively (ignoring the two-year requirement to qualify for a deferred pension).

Column (c) is the transfer value of the deferred pension in column (a) calculated as at 31 December 2002 based on factors supplied by the actuary of the relevant Lloyds TSB Group pension scheme in accordance with actuarial guidance note GN11.

Column (d) is the equivalent transfer value, but calculated as at 31 December 2001 on the assumption that the director left service at that date. Mr Hampton joined the Lloyds TSB Group on 1 June 2002 and previous years' figures are not shown.

Column (e) is the increase in pension built up during the year, recognising (i) the accrual rate for the additional service based on the pensionable salary in force at the year end, and (ii) where appropriate the effect of pay changes in 'real' (inflation adjusted) terms on the pension already earned at the start of the year.

Column (f) is the capital value of the pension in column (e).

Members of the Group's pension schemes have the option to pay additional voluntary contributions: neither the contributions nor the resulting benefits are included in the above table.

Board practices

Audit committee

The audit committee comprises Mr Brown (chairman), Mr Gemmell, Mrs Knight and

Lord Selborne. The deputy chairman is invited to attend all meetings of the committee. The audit committee's duties include considering the appointment, resignation or dismissal of the external auditors and their independence and objectivity. The audit committee also reviews all financial statements published in the name of the board and the quality and acceptability of the related accounting policies, practices and financial reporting disclosures; the scope of work of the group risk management division, where duties include internal audit and advising on and monitoring compliance with financial services legislation and regulations, and the adequacy of its resources; the results of the external audit and its cost effectiveness; communications from the external auditors on audit planning and findings on material weaknesses in accounting and internal control systems; the major findings of any relevant internal investigations; and its own efficiency and effectiveness. All audit and non-audit services provided by the auditors are approved by the audit committee.

Nomination committee

The nomination committee, comprising Mr van den Bergh (chairman), Dr Julius and The Earl of Selborne, considers potential candidates for appointment as directors and makes recommendations to the board. The deputy chairman and group chief executive are invited to attend all meetings of the committee. The committee also makes recommendations to the board concerning the following:

* the re-appointment of any non-executive director by the board at the conclusion of his or her specified term;

* the re-election of any director by the shareholders under the retirement by rotation provisions of the articles of association;

* any matters relating to the continuation in office as a director of any director at any time; and

* the appointment of any director to executive or other office, other than to the positions of chairman and group chief executive where special arrangements apply.

Remuneration committee

The remuneration committee, comprising Sir Tom McKillop (chairman), Dr Berndt, Dr Gibson-Smith and Dr Julius, reviews and makes recommendations to the board on the framework of executive directors' remuneration and its cost. It also determines, on the board's behalf, specific remuneration packages for each of the chairman, the deputy chairman, the executive directors, and any employee of Lloyds TSB Group plc or any subsidiary whose salary exceeds GBP300,000 per annum. In addition, it determines proposals for the granting of executive share options.

All the non-executive directors receive the minutes of remuneration committee meetings and have the opportunity to comment and have their views taken into account before the committee's decisions are implemented.

Directors' service agreements

The general Lloyds TSB Group policy is for executive directors to have service agreements with notice periods of no greater than one year, to reflect current corporate governance best practice. Executive directors are required to give the Lloyds TSB Group six months' notice if they wish to leave. The Association of British Insurers and the National Association of Pension Funds published a joint statement of best practice on executive contracts and severance in December 2002 and, during 2003, the remuneration committee will consider what changes would be desirable in respect of service agreements.

Mr Ayliffe, Mr Fairey, Mr Hampton, Mr Kane and Mr Targett each has a service agreement which the company may terminate by giving one year's notice. Mr Ross's service agreement, entered into in connection with the arrangements for the transfer of the business of Scottish Widows to the Lloyds TSB Group in March 2000, provided for two years' notice for the first two years, but since March 2002 the notice period has decreased by one month for each month of service, to one year's notice. Since March 2003, therefore, Mr Ross's agreement may be terminated on one year's notice.

Mr Daniels' service agreement provided for two years' notice for the first eighteen months (from November 2001): after that, the notice period reduced to one year. Since May 2003, therefore, Mr Daniels' agreement may be terminated on one year's notice. His contract also provided that if, within eighteen months of the commencement of his employment, there were to be a change of circumstances of the company (as defined in the agreement) so that there was, in his reasonable judgement, a materially adverse effect on his prospects or a material diminution in his status, he would be entitled to serve notice terminating his employment and appropriate compensation would be payable to him.

None of the other directors has a service agreement with a notice period of more than one year.

The remuneration committee has considered the provisions of the UK Listing Authority's corporate governance code and the recent ABI/NAPF joint statement mentioned above, relating to compensation in the event of early termination of directors' service agreements and a departing director's duty to mitigate his or her loss. The Lloyds TSB Group will have regard to that duty on a case by case basis when assessing the appropriate level of compensation which may be payable. It is the Lloyds TSB Group's policy that where compensation on early termination is due, in appropriate circumstances it should be paid on a phased basis.

Non-executive directors do not have service agreements and, in accordance with the articles of association, their appointment may be terminated at any time without compensation.

Employees

As at 31 December 2002, Lloyds TSB Group employed 79,537 people (full-time equivalent), compared with 81,400 at 31 December 2001. At 31 December 2002 68,697 employees were located in the UK, 4,859 in the Americas, 4,532 in New Zealand, and 1,449 in the rest of the world. At the same date, 47,895 people were employed in UK Retail Banking and Mortgages, 6,170 in Insurance and Investments, 23,173 in Wholesale Markets and International Banking, and 2,299 in other functions.

Lloyds TSB Group is committed to employment policies which follow best practice, based on equal opportunities for all employees irrespective of sex, race, national origin, religion, colour, disability, sexual orientation, age or marital status.

In the UK, Lloyds TSB Group supports Opportunity Now and Race for Opportunity; campaigns to improve opportunities for women and ethnic minorities in the work place. Lloyds TSB Group is a member of the Employers' Forum on Disability in support of employment of people with disabilities. This recognises the need for ensuring fair employment practices in recruitment and selection, and the retention, training and career development of disabled staff.

Employees are kept closely involved in major changes affecting them through a variety of means. In the UK, Lloyds TSB Group has long standing arrangements with finance sector unions covering both collective and individual representation of staff. Lloyds TSB Group has gone through substantial changes in recent years; adjusting for the effect of acquisitions and disposals underlying staff numbers have reduced by 15,000 since 1995. However, during this time no material strikes or work stoppages have occurred. Additionally staff are kept closely involved in major changes affecting them through such measures as regular briefings, internal communications and opinion surveys as a way of ensuring the views of employees are taken into account in reaching decisions.

Schemes offering share options or the acquisition of shares are available for most staff, to encourage their financial involvement in Lloyds TSB Group. Further details are given in "- Compensation".

Share ownership

Directors' interests

The interests of those who were directors at 31 December 2002, all beneficial, in shares in Lloyds TSB Group plc were:

Shares:	At 31 December 2002	At 1 January 2002 (or date of appointment if later)		31 December 2
M K Atkinson	93,394	124,815	P R Hampton	6,
Ewan Brown	3,548	3,402	D S Julius	2,
A C Butler	2,000	2,000	A G Kane	81,
J E Daniels	1,029	1,000	Sir Tom McKillop	1,
P B Ellwood	183,999	178,751	A E Moore	1,108,
M E Fairey	75,425	74,158	D P Pritchard	4,
S M Forbes	2,000	2,000	M D Ross	2,
G J N Gemmell	50,000	30,000	Lord Selborne	3,
C S Gibson-Smith	3,151	3,151	M A van den Bergh	5,

85

Options to acquire shares of Lloyds TSB Group plc:

	At 1 January 2002 (or date of	Granted	Exercised/ lapsed	At	Weighted average exercise price at	E p o

		appointment (if later)	during year	during the year	31 December 2002	31 December 2002	ex or
M K Atkinson	Exercisable	147,600			97,600	259p	
	Not exercisable	253,155			-	-	
	Exercisable*	-			92,000	670p	
	Not exercisable*	92,000			232,122	676p	
			275,349				
				916+			
				1,245+			
				91,817+			
				252,404+			
J E Daniels	Exercisable	-			-	-	
	Not exercisable	907,780			-	-	
	Exercisable*	-			-	-	
	Not exercisable*	-			1,238,597	700p	
			330,419				
			398				
P B Ellwood**	Exercisable	321,340			211,340	280p	
	Not exercisable	276,725			-	-	
	Exercisable*	-			190,000	657p	
	Not exercisable*	165,000			357,579	663p	
				4,146			
M E Fairey	Exercisable	54,000			-	-	
	Not exercisable	288,329			-	-	
	Exercisable*	-			102,809	675p	
	Not exercisable*	105,809			691,230	701p	
			345,104				
			797				
P R Hampton	Exercisable	-			-	-	
	Not exercisable	-			-	-	
	Exercisable*	-			-	-	
	Not exercisable*	-			326,351	740p	
			326,351				
A G Kane**	Exercisable	171,547			131,547	252p	
	Not exercisable	233,721			4,157	442p	
	Exercisable*	-			90,000	716p	
	Not exercisable*	77,000			531,913	701p	
			275,349				
D P Pritchard	Exercisable	-			-	-	
	Not exercisable	250,096			4,687	416p	
	Exercisable*	-			50,000	860p	
	Not exercisable*	90,000			571,772	700p	
			286,363				
M D Ross	Exercisable	-			-	-	
	Not exercisable	440,549			-	-	
	Exercisable*	-			-	-	
	Not exercisable*	-			756,283	657p	
			315,734				

Gain made by Dennis Holt, who left the board on 31 August 2001
Gain made by A E Moore, who no longer holds share options

Share retention plan

J E Daniels	Not exercisable	216,763	-	-	216,763	(see page 81)

Options may be exercised between 2003 and 2012.

Options were not exercisable because they had not been held for the period required by the relevant scheme or the performance conditions had not been met.

* Market price of shares is below the share option exercise price.

** These directors will receive additional Lloyds TSB Group shares on exercising share options held on 28 December 1995. These shares will compensate them for the special dividend of 68.3p per share which was paid to former TSB Group shareholders in 1996 following the merger with Lloyds Bank, but which was not paid to optionholders.

*** This is the difference between the market price of the shares on the day on which the share option was exercised and the price paid for the shares, and includes the value of shares issued to compensate directors for the special dividend mentioned above.

+ These share options lapsed following termination of Mr Atkinson's service contract.

The market price for a share in the Company at 1 January 2002 and 31 December 2002 was 746p and 446p respectively. The range of prices between 1 January 2002 and 31 December 2002 was 427.5p to 817p.

None of the other directors at 31 December 2002 had options to acquire shares in Lloyds TSB Group or its subsidiaries.

Scottish Widows loan capital

At the end of the year, Mr Ross had an interest in GBP28,394 of Scottish Widows Group Limited floating rate unsecured loan notes 2008 (2001: GBP43,194).

Directors' non-beneficial interests

Directors had non-beneficial interests as follows:

1. Mr Daniels, Mr Ellwood, Mr Fairey, Mr Hampton, Mr Kane, Mr Moore, Mr Pritchard, Mr Ross and Mr van den Bergh, together with some 80,000 other employees, were potential beneficiaries in the 1,721,503 and 1,684,041 shares held at the end of the year by the Lloyds TSB qualifying employee share ownership trust and the Lloyds TSB Group employee share ownership trust, respectively. 2,417,245 and 1,952,179 shares, respectively, were held by these trusts at the beginning of the year.

2. At the beginning and end of the year, Mr Ellwood also had a non-beneficial interest in 7,000 shares held in another trust.

None of those who were directors at the end of the year had any other interest in the capital of Lloyds TSB Group plc or its subsidiaries.

Corporate governance

The Board considers that good governance is central to achieving the Lloyds TSB Group's governing objective of maximising shareholder value. Lloyds TSB Group has complied throughout the year with the provisions of the UK Listing Authority's corporate governance code where the requirements are of a continuing nature.

Internal control

The board of directors is responsible for the Lloyds TSB Group's system of internal control, which is designed to ensure effective and efficient operations, internal control, including financial reporting, and compliance with laws and regulations. It should be noted, however, that such a system is designed to manage, rather than eliminate, the risk of failure to achieve business objectives. In establishing and reviewing the system of internal control the directors have regard to the materiality of relevant risks, the likelihood of a loss being incurred and the costs of control. It follows, therefore, that the system of internal control can only provide reasonable but not absolute assurance against the risk of material loss.

The directors and senior management are committed to maintaining a control-conscious culture across all areas of operation. This is communicated to all employees by way of procedures manuals and regular management briefings. Key business risks are identified, and these are controlled by means of procedures such as physical controls, credit, trading and other authorisation limits and segregation of duties. There are well established budgeting and forecasting procedures in place and reports are presented regularly to the Board detailing the results of each principal business unit, variances against budget and prior year, and other performance data. Internal controls contain procedures which assist the Board in identifying new and emerging risks.

The effectiveness of the internal control system is reviewed regularly by the Board and the Audit Committee, which also receives reports of reviews undertaken around the Lloyds TSB Group by Group Risk Management. The Audit Committee receives reports from the external auditors, PricewaterhouseCoopers LLP, (which include details of significant internal control matters that they have identified) and has a discussion with the auditors at least once a year without executives present, to ensure that there are no unresolved issues of concern.

The US Sarbanes-Oxley Act of 2002

The US Sarbanes-Oxley Act came into force at the end of July 2002. Many of the rules implementing the Act are currently being written and proposed by the Securities and Exchange Commission. As a result, the detailed provisions of the Act are likely to become effective during 2003. Lloyds TSB Group will comply with those provisions of the Act applicable to foreign issuers as and when they become effective. The Board takes the view that Lloyds TSB Group already has a sound corporate governance framework, good processes for the accurate and timely reporting of its financial position and results of operations and an effective and robust system of internal controls. Consequently, Lloyds TSB Group's approach to compliance with the Act principally involves the development and adjustment of the existing corporate governance framework and associated processes concerning reporting, internal controls and other relevant matters. In particular, some additional work has been undertaken to ensure that the Group Chief Executive and the Group Finance Director are in a position to provide the certifications required by the Act in respect of this report for the year ended 31 December 2002.

Disclosure controls and procedures

Within 90 days prior to the date of this report, the Lloyds TSB Group, under the supervision and with the participation of the Lloyds TSB Group's management, including the Group Chief Executive and Group Finance Director, performed an evaluation of the effectiveness of the Lloyds TSB Group's disclosure controls and procedures. Based on this evaluation, the Group Chief Executive and Group Finance Director concluded that the Lloyds TSB Group's disclosure controls and procedures are effective for gathering, analysing and disclosing the information that the Lloyds TSB Group is required to disclose in the reports that it files under the Securities Exchange Act of 1934, within the time periods specified in the SEC's rules and forms. The Lloyds TSB Group's management necessarily applied its judgment in assessing the costs and benefits of such controls and procedures, which by their nature can provide only reasonable assurance regarding management's control objectives.

There have been no significant changes in the Lloyds TSB Group's internal controls or other factors that could significantly affect internal controls subsequent to the date of their evaluation.

MAJOR SHAREHOLDERS AND RELATED PARTY TRANSACTIONS

Major shareholders

Lloyds TSB Group plc does not know of any shareholder owning beneficially, directly or indirectly, five per cent or more of the shares of Lloyds TSB Group plc, or of any shareholder having more than five per cent of the voting rights.

At 31 December 2002, those who were directors of Lloyds TSB Group plc on that day beneficially owned the following ordinary shares, not including options:

Title of Class	Identity of Person or Group	Amount Owned	Per cent of Class
Ordinary shares, nominal value 25 pence each	Directors (18 persons)	1,628,687	0.03

In addition, those directors held, as at 31 December 2002, options to acquire 5,896,750 shares, all of which were granted pursuant to the executive share option schemes, sharesave share option schemes and share retention plan.

Lloyds TSB Group plc is not owned or controlled directly or indirectly by another corporation or by any government and Lloyds TSB Group plc is unaware of any arrangements which might result in a change in control.

Related party transactions

Lloyds TSB Group, as at 31 December 2002, had related party transactions with 4 directors and 31 officers. See Note 42 to the Consolidated Financial Statements. The transactions in question were made in the ordinary course of business, were made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with other persons, and did not involve more than the normal risk of collectibility or present other unfavourable features.

89

REGULATION

European Union Directives

European Union ("EU") Directives, which are required to be implemented in member states through national legislation, have a strong influence over the framework for supervision and regulation of banking and financial services in the UK. The banking Directives aim to harmonise banking regulation and supervision throughout member states by setting out minimum standards in key areas such as capital adequacy and deposit and investor compensation schemes. The UK has now largely implemented these minimum requirements. The Directives also require member states to give "mutual recognition" to each other's standards of regulation. Under the Second Banking Co-ordination Directive the concept of mutual recognition has also been extended to create the "passport" concept: this gives a bank which has been authorised in its "home" state the freedom to establish branches in, and to provide cross-border services into, other member states without the need for additional local authorisation.

Whilst credit institutions such as those in Lloyds TSB Group are primarily regulated in their home state by a local regulator, the EU Directives prescribe minimum criteria for the authorisation of credit institutions and the prudential supervision applicable to them. Investment firms are subject to a similar regulatory environment and can obtain a "passport" under the Investment Services Directive. Despite the application of the "passports" a member state can impose certain requirements on the conduct of banking and investment activities in its boundaries (including conduct of business rules).

Credit institutions and investment firms are required to make adequate capital provisions for risks entered into: the Directives set out the deemed quality and acceptable relative proportions of various types of capital. The Directives also regulate permissible counterparty exposures, provide for the supervision of consolidated financial groups' capital adequacy requirements and define permissible exposures to individual or linked counterparties.

During 2001 the Basel Committee on Banking Supervision has issued further consultation documents with the purpose of replacing the Capital Accord of 1988 with a new capital adequacy framework. The outcome of these consultations is likely to result in comprehensive changes to the capital adequacy regulations applicable to Lloyds TSB Group. The proposals for the new framework cover three main areas:

* Minimum capital requirements and methodologies for allocation of regulatory capital for credit and other risks.

* A supervisory review process, including the setting of capital ratios by bank supervisors.

* Improvement in the stability of the financial system by reliable and timely disclosure of risk information.

It is not expected that the eventual framework will be implemented before 31 December 2006.

The UK financial services industry will be affected by a number initiatives currently being developed by the EU; work continues on the Financial Services Action Plan, which is intended to create a single market for financial services by 2005, and there are proposals for a new Consumer Credit Directive. The Lloyds TSB Group will continue to monitor the progress of these initiatives and assess the likely impact on its business.

UK regulations

In the UK, the fundamental concepts of constitutional issues, company registration and the format and production of company annual reports and accounts are controlled by the UK Companies Act 1985. In addition, as a company listed on the London Stock Exchange Limited, Lloyds TSB Group plc is obliged to comply with a code of practice known as the Combined Code regarding corporate governance. As part of the continuing obligations of Lloyds TSB Group under the rules of that Exchange it must disclose, through the Exchange, major developments in its sphere of activity which may lead to substantial movement in the price of its securities listed on that Exchange.

The undertaking of certain financial activities in the UK subjects the relevant entity to further regulatory regimes. The UK government has implemented major changes to the supervisory regimes affecting financial services businesses. In accordance with the provisions of the Financial Services and Markets Act 2000 ("FSMA") on 1 June 2002, the Financial Services Authority ("FSA") completed the process of assuming responsibility for the regulation and oversight of all financial services activity in the UK, including investment in securities and long-term insurance contracts.

Any individual who carries out what is known as a 'controlled function' in a financial services firm needs to be approved by the FSA. Controlled functions include those of directors, the finance officer, risk management, compliance, anti-money laundering and internal audit. The FSA have established a Code of Practice for Approved Persons; shortfalls in their conduct can lead to sanctions against the individual by the FSA.

The most significant regulatory regimes relevant to Lloyds TSB Group are discussed below.

Banking

Primary responsibility for the prudential supervision of UK banks was transferred from the Bank of England to the FSA under the Bank of England Act 1998. The Bank of England retained its monetary policy role and responsibility for the overall stability of the financial system. The FSA carries out its supervision of the UK banking sector through the collection of information from a series of periodic statistical and prudential returns covering both sterling and non-sterling operations, meetings with the senior management of the banks and reports obtained from skilled persons. The regular reports include operating statements and returns covering (amongst other things) capital adequacy, liquidity, large single exposures and large exposures to related borrowers, lendings by industry sector and geographical area, maturity analyses and foreign exchange activities. A risk-based approach for the supervision of all banks was introduced in 1998; under this approach, the starting point for the FSA's supervision of a bank is based on a systematic analysis of that bank's risk profile. Having determined the level of inherent risk in the bank a minimum capital adequacy requirement is established, which the bank is required to meet at all times.

UK banks are required to maintain, in interest-free accounts at the Bank of England, a non-operational cash balance calculated as a percentage of eligible liabilities, which are, broadly, a measure of the sterling resources available to the banks for lending purposes.

Depositors in the UK are provided with protection for their deposits with authorised institutions. Depositors with a failed institution are entitled to receive 100 per cent of the first GBP2,000 and 90 per cent of the next GBP33,000 of their protected deposits from the UK deposit protection fund, subject to a maximum amount of GBP31,700, including both principal and accrued interest. All authorised institutions are required to be members of the deposit protection scheme and are subject to a levy in proportion to their deposit base, which includes deposits in sterling, other European Economic Area currencies and Euro, to finance the deposit protection fund.

The Banking Code (the "Code") is a voluntary code agreed by UK banks and building societies which became effective in 1992, with subsequent revisions in 1994, 1998, 2001 and 2003, and which has been adopted by Lloyds TSB Group. The Code defines the responsibilities of the banks and building societies to their personal customers in connection with the operation of their accounts and sets out minimum standards of service that these customers can expect from institutions which subscribe to the Code. Compliance with the Code is monitored by the Banking Code Standards Board.

The Business Banking Code is a voluntary code agreed by UK banks which became effective at the end of March 2002, with a subsequent revision in 2003 and which has been adopted by Lloyds TSB Group. The Business Banking Code defines the responsibilities of the banks to their smaller business customers in connection with UK operation of their accounts and sets out minimum standards of service that such customers can expect from institutions which subscribe to the Business Banking Code. Compliance with the Business Banking Code is monitored by the Banking Code Standards Board.

Investment business

The FSA is responsible for the authorisation and supervision of those firms which are engaged in investment business as defined in the FSMA. As part of the authorisation process, the FSA reviews applicants to ensure that they satisfy the necessary criteria including honesty, competence and financial soundness, to engage in regulated activity. Lloyds TSB Group's investment businesses became authorised by the FSA through being "grandfathered" as having been authorised under previous legislation to carry on investment business.

The FSA's regulatory approach aims to focus and reinforce the responsibility of the management of each authorised person to ensure that it takes reasonable care to organise and control its affairs responsibly and effectively and that it develops and maintains adequate risk management systems. The FSA Handbook of Rules and Guidance ('the Handbook') sets out the principles of market conduct and the rules to which investment businesses are required to adhere.

Under the FSMA a compulsory single, industry wide, investor's compensation scheme, the Financial Services Compensation Scheme has been set up. The Scheme is financed by a levy system and the FSMA allows for the establishment of different funds for different kinds of business and for different maximum amounts of claim. The limit for investment business compensation is GBP48,000.

"Listed money market institutions" are regulated by the FSA which expects such entities to observe the "London Code of Conduct" and other regulations contained in the paper entitled "The Regulation of the Wholesale Cash and OTC Derivatives Markets" which was originally issued by the Bank of England to regulate the operation of the wholesale money markets. Lloyds TSB Bank has been granted listed money market institution status.

Insurance

The insurance companies within the Lloyds TSB Group became authorised by the FSA through being "grandfathered" as having been authorised under previous legislation. While the authorisation and supervision of insurance companies is subject to the same FSA regulatory approach as other investment companies, rules exist to:

* Restrict the carrying out of insurance business in the UK to persons authorised by the FSA.

* Require the separation of the long-term business assets of an insurance company from the assets attributable to shareholders.

* Require, and define the role of, an appointed actuary for each insurance company carrying out long-term business in the UK. The appointed actuary is responsible for monitoring the financial health of the company.

* Require the directors to prepare an annual report on the solvency position of the insurer. The valuation basis for assets is defined and there are limits on the extent to which certain categories of assets are allowable in determining the solvency position. The appointed actuary must calculate the value of long-term liabilities and details of his investigations are contained in the directors' solvency report. In determining the value of long-term liabilities the appointed actuary must use a method and valuation basis permitted by the Handbook.

* Require the maintenance of a prescribed solvency margin at all times. The amount of the solvency margin depends upon the amount and type of business an insurance company writes. Failure to maintain the required solvency margin gives the regulator grounds for intervention.

* Prevent an insurer, and its parent, from declaring a dividend when long-term business assets do not exceed long-term liabilities. Furthermore, surplus assets in the long-term fund can only be transferred out once the appointed actuary has completed an investigation.

* Prevent the use of the long-term business assets for purposes other than supporting long-term business.

The Financial Services Compensation Scheme also applies to insurance business written by an insurer authorised by the FSA or by the UK branch of an EEA firm carrying on "home state regulated activity". The limit of compensation in respect of long-term insurance contracts is 90 per cent of the value of the contract with no maximum.

Other relevant legislation and regulation

The Consumer Credit Act 1974 regulates both brokerage and lending activities in the provision of personal secured and unsecured lending. The Data Protection Acts 1984 and 1998 regulate, among other things, the retention and use of data relating to individual customers. The Unfair Terms in Consumer Contracts Regulations 1994 came into force in July 1995. These Regulations together with the Unfair Contract Terms Act 1977 apply to certain contracts for goods and services entered into with customers. The main effect of the Regulations is that a contractual term covered by the Regulations which is "unfair" will not be enforceable against a consumer. These Regulations apply, among other things, to mortgages and related products and services.

The Mortgage Code is a voluntary code followed by lenders and mortgage intermediaries dealing with customers in the UK who want a loan secured on their home. It sets standards of good mortgage practice, which are followed as a minimum standard by those subscribing to it. Compliance with the Mortgage Code is monitored by the Mortgage Code Compliance Board. A new mortgage regulation regime is currently being developed by the FSA and is expected to take effect from 31 October 2004.

The General Insurance Standards Council ("GISC") is an independent, non-statutory organisation that was officially launched on 3 July 2000 to regulate the sales, advice and service standards of its members. GISC members may be insurers, intermediaries or others involved in general insurance such as claims handlers. Members' obligations to individuals buying insurance for themselves and their families are explained fully in the GISC Private Customer Code, while the GISC Commercial Code explains members' obligations in relation to businesses buying insurance. Members are monitored to make sure they follow the standards in the Code.

In December 2001 the UK government announced that the FSA would become responsible for regulating the sale and administration of general insurance (e.g. motor, property and liability insurance) and pure protection contracts (i.e. critical illness, income protection, term assurance and long-term care assurance). The government's legislation, and the FSA's rules subsequently made under it, will, when finalised, implement the Insurance Mediation Directive ("IMD") in the UK. The regulation of insurance intermediation will commence from 14 January 2005.

The Financial Ombudsman was established pursuant to the Financial Services and Markets Act 2000 to provide customers with a free, independent service designed to resolve disputes where the customer is not satisfied with the response received from the regulated firm. The Financial Ombudsman Scheme ("FOS") was established at "N2" (30 November 2001) when the Financial Services Authority became regulator for the financial services industry. The FOS resolve disputes that cover most financial products and services provided in (or from) the United Kingdom - from insurance and pension plans to bank accounts and

92

investments. The decisions made by the FOS are binding on firms. Under section 229 of the Financial Services and Markets Act 2000, if a complaint is determined in favour of the complainant, the determination may include a money award against the firm of such amount as the Ombudsman considers fair compensation for financial loss and subject to the maximum limit of GBP100,000, or a direction that the firm take such steps in relation to the complainant as the Ombudsman considers just and appropriate or, both of these.

Rest of the world

Lloyds TSB Group operates in many countries around the world and its overseas branches, subsidiaries and associated companies are subject to reporting and reserve requirements and controls imposed by the relevant central banks and regulatory authorities.

93

LISTING INFORMATION

The information in this section has been extracted from publicly available documents from various sources, including officially prepared materials from the London Stock Exchange, and has not been prepared or independently verified by us.

The ordinary shares of Lloyds TSB Group plc are listed and traded on the London Stock Exchange under the symbol "LLOY.L". The prices for shares as quoted in the official list of the London Stock Exchange are in pounds sterling. The following table shows the reported high and low closing prices for the ordinary shares on the London Stock Exchange.

	Price per share (in pence)	
	High	Low
Annual prices:		
2002	817.0	427.5
2001	772.0	590.0
2000	774.5	517.0

1999	1,060.0	725.0
1998	1,070.5	575.5
Quarterly prices:		
2003:		
First quarter	459.0	295.75
2002:		
Fourth quarter	591.0	427.5
Third quarter	665.0	456.5
Second quarter	817.0	624.0
First quarter	775.0	680.0
2001:		
Fourth quarter	757.0	644.0
Third quarter	742.0	590.0
Second quarter	772.0	684.5
First quarter	751.0	610.0
Monthly prices:		
May 2003	454.5	405.25
April 2003	423.0	326.0
March 2003	369.75	295.75
February 2003	431.25	341.0
January 2003	459.0	370.5
December 2002	545.0	427.5

On 18 June 2003, the closing price of shares on the London Stock Exchange was 474.5 pence, equivalent to $797.07 per share translated at the Noon Buying Rate of $1.6798 per GBP1.00 on 18 June 2003.

94

Lloyds TSB Group plc's ADRs have been traded on the over-the-counter market in the US under the symbol "LLDTY" since March 2000. Since 27 November 2001 Lloyds TSB Group plc ADSs have been listed on The New York Stock Exchange under the symbol "LYG". The prices for Lloyds TSB Group plc's ADRs, as quoted below, are in US dollars. Each ADS represents four ordinary shares. The following table shows the reported high and low closing prices for the ADRs in the over-the-counter market in the US.

	Price per ADR (in US dollars)	
	High	Low
Annual prices:		
2001 (to 26 November 2001)	46.00	34.75
2000	45.27	33.50
Quarterly prices:		
2001:		
Fourth quarter (to 26 November 2001)	43.88	38.25
Third quarter	44.00	35.50
Second quarter	43.94	38.94
First quarter	46.00	34.75

The following table shows the reported high and low closing prices for ADSs on the New York Stock Exchange:

	Price per ADS (in US dollars) High	Low
Annual prices:		
2002	48.55	27.85
2001 (from 27 November 2001)	44.99	41.30
Quarterly prices:		
2003:		
First quarter	29.79	19.65
2002:		
Fourth quarter	37.75	27.85
Third quarter	41.84	28.97
Second quarter	48.55	38.30
First quarter	45.30	39.16
2001:		
Fourth quarter (from 27 November 2001)	44.99	41.30
Monthly prices:		
May 2003	30.02	26.21
April 2003	27.28	20.98
March 2003	23.61	19.65
February 2003	27.91	22.00
January 2003	29.79	24.99
December 2002	34.27	27.85

On 18 June 2003, the closing price of ADSs on the New York Stock Exchange was $32.13

95

DIVIDENDS

Lloyds TSB Group plc has paid an interim and final dividend each year since the merger of TSB Group plc and Lloyds Bank Plc in 1995. Dividends are paid in May and October and the record date for the purpose of determining the shareholders who will be entitled to a dividend is approximately 10 weeks before the dividend payment date. TSB Group plc, which was re-named Lloyds TSB Group plc after the merger, has paid an interim and final dividend every year after its flotation on the London Stock Exchange in September 1986, with the exception of 1986 when no final dividend was paid. Lloyds TSB Bank has paid a dividend every year since its incorporation as Lloyds Banking Company Limited in 1865.

Lloyds TSB Group plc's ability to pay dividends is restricted under UK company law. Dividends may only be paid if distributable profits are available for that purpose. In the case of a public limited company, a dividend may only be paid if the amount of net assets is not less than the aggregate of the called-up share capital and undistributable reserves and if the payment of the dividend will not reduce the amount of the net assets to less than that aggregate. In addition, a company cannot pay a dividend if any of its UK insurance subsidiaries is insolvent on a regulatory valuation basis or in the case of regulated entities, if the payment of a dividend results in regulatory capital requirements not being met. Similar restrictions exist over the ability of Lloyds TSB Group plc's subsidiary companies to pay dividends to their immediate parent companies. Furthermore, in the case of Lloyds TSB Group plc, dividends may only be paid if sufficient distributable profits are available for distributions due in the financial year on certain preferred securities. The Board has the discretion to decide whether to pay a dividend and the amount of any dividend. In making this decision, the Board is mindful of the level of dividend cover and, consequently, profit growth may not necessarily result in increases in the dividend. The Board recognises the importance attached by shareholders to the Lloyds TSB Group's dividend. Dividends are paid through The Bank of New York which acts as paying and transfer agent for the American Depositary Shares.

The table below sets out the interim and final dividends which were declared in respect of the ordinary shares for fiscal years 1998 through 2002. The sterling amounts have been converted into US dollars at the Noon Buying Rate in effect on each payment date.

	Interim dividend per share GBP	Interim dividend per share $	Final dividend per share GBP	Final dividend per share $
1998	0.067	0.114	0.155	0.253
1999	0.081	0.134	0.185	0.289
2000	0.093	0.136	0.213	0.306
2001	0.102	0.149	0.235	0.344
2002	0.107	0.167	0.235	0.374

There are no UK governmental laws, decrees or regulations that affect the remittance of dividends or other shareholder payments to non-residents of the UK who hold shares of Lloyds TSB Group plc.

MEMORANDUM AND ARTICLES OF ASSOCIATION OF LLOYDS TSB GROUP PLC

A summary of the material provisions of Lloyds TSB Group plc's memorandum and articles of association was incorporated into Lloyds TSB Group plc's registration statement filed with the SEC on 25 September 2001 and is therefore incorporated into this annual report by reference to that statement.

EXCHANGE CONTROLS

There are no UK laws, decrees or regulations that restrict Lloyds TSB Group plc's export or import of capital, including the availability of cash and cash equivalents for use by Lloyds TSB Group, or that affect the remittance of dividends or other shareholder payments to non-UK holders of Lloyds TSB Group plc shares, except as otherwise set out in "Taxation".

TAXATION

UK Taxation

The following discussion is intended only as a general guide to current UK tax legislation, what is understood to be current UK Inland Revenue practice and the terms of the current UK/US income tax treaty (the "Treaty") and the New Treaty (as defined below), all of which are subject to change at any time, possibly with retroactive effect. On 24 July, 2001, the UK and the US entered into a new income tax treaty (the "New Treaty"), which has been ratified by both the UK Parliament and the US Senate and will enter into force when instruments of ratification are exchanged. The UK Inland Revenue is the UK government department responsible for assessing and collecting UK tax revenues. The discussion is intended as a general guide and only applies to persons who are the beneficial owners of their ordinary shares or ADSs. References below to a US Holder are to that term as defined, and subject to the exclusions described in the introduction, below under "- US federal income tax considerations". It may not apply to certain shareholders or ADS holders, such as dealers in securities. Any person who is in any doubt as to his tax position should consult his own professional adviser.

Taxation of chargeable gains

UK residents

A disposal (or deemed disposal) of ordinary shares or ADSs by a shareholder or holder of ADSs resident or (in the case of an individual) ordinarily resident for tax purposes in the UK may, depending on the shareholder's or ADS holder's particular circumstances, and subject to any available exemption or relief, give rise to a chargeable gain or an allowable loss for the purposes of UK taxation on chargeable gains.

Persons, other than US Holders, temporarily non-resident in the UK

A shareholder or ADS holder who is an individual and who has, on or after 17 March 1998, ceased to be resident and ordinarily resident for tax purposes in the UK for a period of less than five years of assessment and who disposes of ordinary shares or ADSs during that period may be liable, on return to the UK, to UK taxation on chargeable gains arising during the period of absence, subject to any available exemption or relief.

US Holders

Subject to the provisions set out in the next paragraph in relation to temporary non-residents, US Holders will not normally be liable for UK tax on chargeable gains unless they carry on a trade, profession or vocation in the UK through a branch or agency and the ordinary shares or ADSs are or have been used or held by or for the purposes of the branch or agency, in which case such US Holder might, depending on individual circumstances, be liable to UK tax on chargeable gains on any disposition of ordinary shares or ADSs. A US Holder who is only temporarily not resident in the UK may, under anti-avoidance legislation, still be liable for UK tax on chargeable gains realised, subject to any available exemption or relief.

A US Holder who is an individual and who has, on or after 17 March 1998, ceased to be resident or ordinarily resident for tax purposes in the UK for a period of less than five years of assessment and who disposes of ordinary shares or ADSs during that period may be liable, on return to the UK, to UK taxation on chargeable gains arising during the period of absence, subject to any available exemption or relief.

Other non-UK resident persons

Subject to the provisions set out above under "- Persons, other than US Holders, temporarily non-resident in the UK", shareholders or ADS holders who are neither resident nor ordinarily resident in the UK will not normally be liable for UK tax on chargeable gains unless they carry on a trade, profession or vocation in the UK through a branch or agency and the ordinary shares or ADSs are or have been used or held by or for the purposes of the branch or agency, in which case such shareholder or ADS holder might, depending on individual circumstances, be liable to UK tax on chargeable gains on any disposition of ordinary shares or ADSs. An individual holder of ordinary shares or ADSs who is only temporarily not resident in the UK may, under anti-avoidance legislation, still be liable for UK tax on chargeable gains realised, subject to any available exemption or relief.

Taxation of dividends

UK residents

Lloyds TSB Group will not be required to withhold tax at source when paying a dividend on the ordinary shares or ADSs.

An individual shareholder or ADS holder who is resident in the UK for tax purposes will be entitled to a tax credit in respect of any dividend received from us and will be taxable on the gross dividend, which is the aggregate of the dividend received and related tax credit. The value of the tax credit will be equal to one-ninth of the dividend received (and, therefore, 10 per cent of the gross dividend). The gross dividend will be treated as an individual's marginal income. The tax credit will, however, be treated as discharging the individual's liability to income tax in respect of the gross dividend, unless and except to the extent that the gross dividend falls above the threshold for the higher rate of income tax. A UK resident individual shareholder or ADS

holder who is liable to income tax at the higher rate will be subject to tax at the rate applicable to dividends for such shareholders or ADS holders (currently 32.5 per cent) on the gross dividend. The tax credit will be set against but will not fully discharge such shareholder's or ADS holder's tax liability on the gross dividend and he will have to pay additional tax equal to 22.5 per cent of the gross dividend, being 25 per cent of the dividend received, to the extent that such sum, when treated as marginal income, falls above the threshold for the higher rate of income tax.

There will be no payment of the tax credit or any part of it to an individual whose liability to income tax on the dividend and the related tax credit is less than the tax credit, except where the individual holds the relevant shares through a personal equity plan or individual savings account and the dividend is received into such plan or account on or before 5 April 2004.

UK resident shareholders or ADS holders which are not liable to UK tax on dividends, including pension funds and charities, will not be entitled to reclaim the tax credits in respect of dividends although charities will be entitled to a payment by the UK Inland Revenue of a specified proportion of any dividend paid by us to the charities on or before 5 April 2004, that proportion declining on a year by year basis.

Subject to an exception for some insurance companies with overseas business, UK resident corporate shareholders or ADS holders will generally not be subject to corporation tax in respect of dividends received from Lloyds TSB Group, but will not be entitled to the payment of any tax credit with respect to the dividends.

US Holders

Lloyds TSB Group will not be required to withhold tax at source when paying a dividend on the ordinary shares or ADSs to a US Holder.

A US Holder is entitled under the terms of the Treaty, in principle, to receive a payment from the UK Inland Revenue in respect of a dividend from us in an amount equal to the tax credit (the "Tax Credit Amount") to which a UK resident individual is generally entitled in respect of the dividend. This is an amount equal to one-ninth of the dividend received. However, that entitlement is subject to a deduction withheld under the Treaty. The amount of such deduction will equal the Tax Credit Amount, i.e. one-ninth of the dividend. Therefore, a US Holder will not be able to claim any payment from the UK Inland Revenue in respect of a dividend from Lloyd TSB Group.

When the New Treaty comes into effect (and the Treaty ceases to apply), a US Holder will not be entitled to claim a payment from the UK Inland Revenue in respect of a dividend from Lloyds TSB Group because the New Treaty does not provide for that entitlement.

Other non-UK resident persons

Lloyds TSB Group will not be required to withhold tax at source when paying a dividend on the ordinary shares or ADSs to a holder, other than a US Holder, who is not resident for tax purposes in the UK. Holders of ordinary shares or ADSs, other than US Holders, who are not resident for tax purposes in the UK and who receive a dividend from us will not have any further UK tax to pay in respect of the dividend, but will not normally be able to claim any additional payment in respect of the dividend from the UK Inland Revenue under any applicable double tax treaty.

Stamp duty and stamp duty reserve tax

UK residents, US Holders and other non-UK resident persons

Any conveyance or transfer on sale of ordinary shares (whether effected using the CREST settlement system or not) will be subject to UK stamp duty or stamp duty reserve tax ("SDRT"). The transfer on sale of ordinary shares will be liable to ad valorem UK stamp duty or SDRT, generally at the rate of 0.5 per cent of the consideration paid (rounded up to the next multiple of GBP5 in the case of stamp duty). Stamp duty is usually the liability of the purchaser or transferee of the ordinary shares. An unconditional agreement to transfer such ordinary shares will be liable to SDRT, generally at the rate of 0.5 per cent of the consideration paid, but such liability will be cancelled, or, if already paid, refunded, if the agreement is completed by a duly stamped transfer within six years of the agreement having become unconditional. SDRT is normally the liability of the purchaser or transferee of the ordinary shares.

Where Lloyds TSB Group issue ordinary shares or a holder of ordinary shares transfers such shares to the custodian or nominee for the depositary to facilitate the issue of ADSs to him representing the ordinary shares or to a person providing clearance services (or their nominee or agent), a liability to UK stamp duty or SDRT at the rate of 1.5 per cent (rounded up to the next multiple of GBP5 in the case of the stamp duty) of either the issue price or, in the case of transfer, the listed price of the ordinary shares, calculated in sterling, will arise. Where a holder of ordinary shares transfers such shares to the custodian or nominee for the depositary or clearance service this charge will generally be payable by the person receiving the ADSs or transferring the ordinary shares into the clearance service.

A liability to stamp duty at the fixed rate of GBP5 will arise as a result of the cancellation of any ADSs with the ordinary shares that they represent being transferred to the ADS holder.

No liability to UK stamp duty or SDRT will arise on a transfer of ADSs provided that any document that effects such transfer is not executed in the UK and that it remains at all subsequent times outside the UK. An agreement to transfer ADSs will not give rise to a liability to SDRT.

US federal income tax considerations

The following summary describes certain US federal income tax consequences of the acquisition, ownership and disposition of ADSs or ordinary shares, but it does not purport to be a comprehensive description of all of the tax considerations that may be relevant to a decision to acquire such securities. The summary applies only to holders that hold ADSs or ordinary shares as capital assets and does not address special classes of holders, such as:

* certain financial institutions;

* insurance companies;

* dealers in securities or foreign currencies;

* holders holding ADSs or ordinary shares as part of a hedge, straddle or other conversion transaction;

* holders whose "functional currency" is not the US dollar;

* holders liable for alternative minimum tax;

* partnerships or other entities classified as partnerships for US federal income tax purposes; or

* a holder that owns 10 per cent or more of the voting shares of Lloyds TSB Group plc.

In addition, the summary is based in part on representations of the Depositary and assumes that each obligation provided for in or otherwise contemplated by the Deposit Agreement or any other related document will be performed in accordance with its terms. The US Treasury has expressed concerns that parties to whom ADSs are pre-released may be taking actions that are inconsistent with the claiming of foreign tax credits for US Holders of ADSs. Accordingly, the analysis of the creditability of UK taxes described below could be affected by future actions that may be taken by the US Treasury.

The summary is based upon tax laws of the US including the Internal Revenue Code of 1986, as amended to the date hereof (the "Code"), administrative pronouncements, judicial decisions and final, temporary and proposed Treasury Regulations, as well as upon the Treaty and the New Treaty, as appropriate, changes to any of which may affect the tax consequences described herein possibly with retroactive effect. Except as discussed under "-Taxation of distributions", application of the New Treaty will not affect this summary. Prospective purchasers of the ADSs or ordinary shares should consult their own tax advisors as to the US, UK or other tax consequences of the purchase, ownership and disposition of such securities in their particular circumstances, including the effect of any state or local tax laws.

As used herein, a "US Holder" is a beneficial owner of ADSs or shares that is, for US federal income tax purposes:

* a citizen or resident of the US;

* a corporation or a partnership created or organized in or under the laws of the US or of any political subdivision thereof;

* an estate the income of which is subject to US federal income taxation regardless of its source; or

* a trust subject to the control of one or more US persons and the primary supervision of a US court.
  For US federal income tax purposes, US Holders of ADSs will be treated as the owners of the underlying ordinary shares.

Taxation of distributions

To the extent paid out of current or accumulated earnings and profits of Lloyds TSB Group plc (as determined in accordance with US federal income tax principles), distributions made with respect to ADSs or ordinary shares (other than certain distributions of capital stock of Lloyds TSB Group plc or rights to subscribe for shares of capital stock of Lloyds TSB Group plc) will be includible in the income of a US Holder as ordinary dividend income. Such dividends will not be eligible for the "dividends received deduction" generally allowed to corporations under the Code. The amount of the distribution will equal the US dollar value of the pounds sterling received, calculated by reference to the exchange rate in effect on the date such distribution is received (which, for holders of ADSs, will be the date such distribution is received by the Depositary), whether or not the Depositary or US Holder in fact converts any pounds sterling received into US dollars at that time. Any gains or losses resulting from the conversion of pounds sterling into US dollars will be treated as ordinary income or loss, as the case may be, of the US Holder and will be US source.

A US Holder may, under the Treaty, elect to claim a foreign tax credit in respect of the Tax Credit Amount. A US Holder who so elects must include the Tax Credit Amount in income. Under the New Treaty no such election would be available.

The limitation of foreign taxes eligible for credit is calculated separately with respect to specific classes of income. For this purpose, any dividends paid by Lloyds TSB Group plc on ADSs or ordinary shares will generally constitute "passive income" or, in the case of US financial service providers, may be "financial services income".

Taxation of capital gains

Gain or loss realised by a US Holder on (i) the sale or exchange of ADSs or ordinary shares or (ii) the Depositary's sale or exchange of ordinary shares received as distributions on the ADSs will be subject to US federal income tax as capital gain or loss in an amount equal to the difference between the US Holder's tax basis in the ADSs or ordinary shares and the amount realised on the disposition. Gain or loss, if any, will be US source. US Holders should consult their tax advisors regarding the US federal tax treatment of capital gains, which may be taxed at lower rates than ordinary income for individuals, and losses, the deductibility of which is subject to limitations.
Deposits and withdrawals of ordinary shares in exchange for ADSs will not result in taxable gain or loss for US federal income tax purposes.

Information reporting and backup withholding

Dividends paid on ADSs or ordinary shares to a US Holder may be subject to information reporting requirements of the Code. Such dividends may also be subject to backup withholding unless the US Holder:

* is a corporation or comes within certain other exempt categories and, when required, demonstrates this fact, or

* provides a taxpayer identification number on a properly completed Form W-9 or a substitute form and certifies that no loss of exemption from backup withholding has occurred and that such holder is a US person.

Any amount withheld under these rules will be creditable against the US Holder's federal income tax liability. A US Holder who does not provide a correct taxpayer identification number may be subject to certain penalties.

WHERE YOU CAN FIND MORE INFORMATION

The documents concerning us which are referred to herein may be inspected at the Securities and Exchange Commission ("SEC"). You may read and copy any document filed or furnished by us at the SEC's public reference rooms in Washington D.C., New York and Chicago, Illinois. Please call the SEC at 1-800-SEC-0330 for further information on the reference rooms. The SEC also maintains a website at www.sec.gov which contains, in electronic form, each of the reports and other information that we have filed electronically with the SEC.

ENFORCEABILITY OF CIVIL LIABILITIES

Lloyds TSB Group plc is a public limited company incorporated under the laws of Scotland. Most of Lloyds TSB Group plc's directors and executive officers and certain of the experts named herein are residents of the United Kingdom. A substantial portion of the assets of Lloyds TSB Group plc, and a substantial portion of the assets of such persons, are located outside the United States. As a result, it may not be possible for investors to effect service of process within the United States upon such persons or to enforce against them judgements of US courts, including judgements predicated upon the civil liability provisions of the federal securities laws of the United States. Furthermore, Lloyds TSB Group plc has been advised by its English solicitors that there is doubt as to the enforceability in the United Kingdom, in original actions or in actions for enforcement of judgements of US courts, of civil liabilities, including those predicated solely upon the federal securities laws of the United States.

RISK FACTORS

An investment in Lloyds TSB Group plc's ordinary shares involves a number of risks, including credit, market, operational, regulatory, competitive and acquisition risks, some of which could be substantial and are inherent in Lloyds TSB Group's business.

Lloyds TSB Group's businesses are subject to inherent risks concerning borrower credit quality as well as general UK and international economic conditions. Development of adverse conditions in the UK or in other major economies could cause profitability to decline.

Lloyds TSB Group's businesses are subject to inherent risks regarding borrower credit quality as well as general UK economic conditions, each of which can change the level of demand for Lloyds TSB Group's products and services. Changes in the credit quality of Lloyds TSB Group's UK or international borrowers and counterparties could reduce the value of Lloyds TSB Group's assets, and increase provisions for bad and doubtful debts. Any significant increase in the UK unemployment rate would reduce profits from the insurance business. Furthermore, a general deterioration in the UK economy would also reduce Lloyds TSB Group's profit margins for both its UK banking and financial services businesses. A general deterioration in any other major world economy could also adversely impact Lloyds TSB Group's profitability.

Lloyds TSB Group's businesses are inherently subject to the risk of market fluctuations, which could reduce profitability.

Lloyds TSB Group's businesses are inherently subject to the risk of market fluctuations. The most significant market risks Lloyds TSB Group faces are interest rate risk and foreign exchange risk in its banking businesses and equity risk in its insurance businesses. See "Operating and Financial Review and Prospects - Enterprise-wide risk management" for a discussion of these risks. The Lloyds TSB Group's pension schemes are also subject to market risks, principally equity risk and interest rate risk; adverse market movements would have an effect upon the financial condition of the pension schemes which would be reflected in the Lloyds TSB Group's Consolidated Financial Statements.

Lloyds TSB Group's insurance business is subject to inherent risks concerning changing demographic developments, catastrophic weather and similar contingencies outside its control. Development of adverse conditions could reduce profitability margins.

Lloyds TSB Group's insurance business is subject to inherent risk regarding changing demographic developments, catastrophic weather and similar contingencies outside its control, both in the UK and overseas. Such contingencies can change the risk profile and profitability of such products and services.

Adverse experience in the operational risks inherent in Lloyds TSB Group's businesses could have a negative impact on its results of operations.

Operational risks are present in Lloyds TSB Group's businesses, including the risk of direct or indirect loss resulting from inadequate or failed internal and external processes, people and systems or from external events. Lloyds TSB Group's businesses are dependent on their ability to process very efficiently a very large number of complex transactions across numerous and diverse products and services, in different currencies and subject to a number of different legal and regulatory regimes. Lloyds TSB Group's systems and processes are designed to ensure that the operational risks associated with its activities are appropriately controlled, but Lloyds TSB Group realises that any weakness in these systems could have a negative impact on its results of operations during the affected period. See "Operating and Financial Review and Prospects - Enterprise-wide risk management - Operational risk" and "Operating and Financial Review and Prospects - Enterprise-wide risk management - Legal and regulatory risk ".

Terrorist acts and other acts of war could have a negative impact on the business and results of operations of Lloyds TSB Group.

Terrorist acts and other acts of war or hostility and responses to those acts, have created many economic and political uncertainties, which could have a negative impact on UK and international economic conditions generally, and more specifically on the business and results of operations of Lloyds TSB Group in ways that cannot currently be predicted.

Lloyds TSB Group operates its businesses subject to substantial regulation, regulatory and governmental oversight. Any significant adverse regulatory developments or changes in government policies or economic controls could have a negative impact on Lloyds TSB Group's results of operations.

Lloyds TSB Group conducts its businesses subject to ongoing regulation and associated regulatory risks, including the effects of changes in the laws, regulations, policies, voluntary codes of practice and interpretations in the UK and the other markets where it operates. Future changes in regulation, fiscal or other policies are unpredictable and beyond the control of Lloyds TSB Group. For additional information, see "Regulation".

The resolution of a number of issues affecting the UK financial services industry, including Lloyds TSB Group, could have a negative impact on Lloyds TSB Group's results of operations or on its relations with some of its customers and potential customers.

These issues involve the possible misselling of pension and other life assurance policies and matters arising from the treatment of guaranteed annuity options. There is a risk that further provisions may be required as a result of these issues. See "Business - Guaranteed annuity options" and "Business - Customer remediation payments".

Lloyds TSB Group's businesses are conducted in highly competitive environments and management's ability to create an appropriate return for shareholders depends upon management's ability to respond effectively to competitive pressures.

The market for UK financial services and the other markets within which Lloyds TSB Group operates are highly competitive and management expects such competition to intensify in response to consumer demand, technological changes, the impact of consolidation, regulatory actions and other factors, which could result in a reduction in profit margins. Lloyds TSB Group's ability to generate an appropriate return for its shareholders depends significantly upon the competitive environment and management's response to it. See "Business - Competitive environment".

Lloyds TSB Group is devoting considerable time and resources to securing new customers and developing more business from existing customers. If Lloyds TSB Group is unsuccessful, its organic growth prospects and results of operations may decline.

Lloyds TSB Group seeks to achieve further organic growth by securing new customers and developing more business from existing customers. Lloyds TSB Group is currently expending significant resources and effort to bring about this growth, particularly with respect to its UK retail financial services business. If these expenditures and efforts do not meet with success, its operating results could grow more slowly or decline.

Lloyds TSB Group's businesses are conducted in a market place that is rapidly consolidating, significant cross-border mergers and acquisitions may happen in the coming years and Lloyds TSB Group's ability to generate an appropriate return for its shareholders over the long term will depend upon whether management is able or permitted by either regulatory bodies or its shareholders to achieve value-creating mergers and/or acquisitions at the appropriate times and prices.

In addition to its important strategy of organic growth, one of Lloyds TSB Group's aims is to remain alert for opportunities to participate in the further consolidation of the financial services industry, both in the UK and overseas. In light of the Secretary of State's decision to prohibit the attempted acquisition of Abbey National, management believes that under current conditions Lloyds TSB Group may find it difficult to be able to make a significant acquisition in the UK in any business line where it already has a significant market share. Management also believes that domestic consolidation in many overseas markets, particularly in Europe, is entering its final phase and that, therefore, significant cross border mergers and acquisitions may happen in the coming years. Lloyds TSB Group's ability to generate an appropriate return for its shareholders over the long term may depend upon whether management is able to achieve value-creating mergers and/or acquisitions at the appropriate times and prices. Lloyds TSB Group cannot be sure that it will ultimately be able to make any such mergers or acquisitions.

FORWARD LOOKING STATEMENTS

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

Examples of such forward-looking statements include, but are not limited to:

* projections or expectations of profit attributable to shareholders, provisions, economic profit, dividends, capital structure or any other financial items or ratios;

* statements of plans, objectives or goals of Lloyds TSB Group or its management;

* statements about the future trends in interest rates, stock market levels and demographic trends and any impact on Lloyds TSB Group;

* statements concerning any future UK or other economic environment or performance, including in particular any such statements included in this registration statement in "Operating and Financial Review and Prospects";

* statements about strategic goals, competition, regulation, dispositions and consolidation or technological developments in the financial services industry; and

* statements of assumptions underlying such statements.

Factors that could cause actual results to differ materially from the plans, objectives, expectations, estimates and intentions expressed in such forward-looking statements made by Lloyds TSB Group or on Lloyds TSB Group's behalf include, but are not limited to:

* general economic conditions in the UK and in other countries in which the Lloyds TSB Group has significant business activities or investments;

* inflation, interest rate, exchange rate, market and monetary fluctuations;

* changing demographic developments, catastrophic weather and similar contingencies outside the Lloyds TSB Group's control;

* inadequate or failed internal or external processes, people and systems;

* terrorist acts and other acts of war or hostility and responses to those acts;

* changes in laws, regulations or taxation;

* changes in competition and pricing environments;

* the ability to secure new customers and develop more business from existing customers;

* the ability to achieve value-creating mergers and/or acquisitions at the appropriate time and prices; and

* the success of the Lloyds TSB Group in managing the risks of the foregoing.

Lloyds TSB Group plc may also make or disclose written and/or oral forward-looking statements in reports filed with or furnished to the US Securities and Exchange Commission, Lloyds TSB Group plc's annual report and accounts to shareholders, proxy statements, offering circulars, registration statements and prospectuses, press releases and other written materials and in oral statements made by the directors, officers or employees of Lloyds TSB Group plc to third parties, including financial analysts. The forward-looking statements contained in this annual report are made as of the date hereof, and Lloyds TSB Group undertakes no obligation to update any of its forward-looking statements.

LLOYDS TSB GROUP STRUCTURE

The following is a list of the principal subsidiaries of Lloyds TSB Group plc at 31 December 2002. The audited consolidated accounts of Lloyds TSB Group plc for the year ended 31 December 2002 include the audited accounts of each of these companies.

Name of subsidiary undertaking	Country of registration/ incorporation	Percentage of equity share capital and voting rights held	Nature of business	Registered office
Lloyds TSB Bank plc	England	100%	Banking and financial services	25 Gresham Street, London EC2V 7HN England
Cheltenham & Gloucester plc	England	*100%	Mortgage lending and retail	Barnett Way, Gloucester GL4 3RL

			investments	England
Lloyds TSB Commercial Finance Limited	England	*100%	Credit factoring	Beaumont House, Beaumont Road, Banbury, Oxfordshire OX16 7RN England
Lloyds TSB Leasing Limited	England	*100%	Financial leasing	25 Gresham Street, London EC2V 7HN England
Lloyds TSB Private Banking Limited	England	*100%	Private banking	25 Gresham Street, London EC2V 7HN England
The Agricultural Mortgage Corporation PLC	England	*100%	Long-term agricultural finance	AMC House, Chantry Street, Andover, Hampshire SP10 1DD England
The National Bank of New Zealand Limited	New Zealand	*100%	Banking and financial services	National Bank House, 170-186 Featherston Street, Wellington, New Zealand
Lloyds TSB Bank (Jersey) Limited	Jersey	*100%	Banking and financial services	25 New Street, St. Helier JE4 8RG Jersey
Lloyds TSB Scotland plc	Scotland	*100%	Banking and financial services	Henry Duncan House, 120 George Street, Edinburgh EH2 4LH Scotland
Lloyds TSB General Insurance Limited	England	*100%	General insurance	25 Gresham Street, London EC2V 7HN England
Scottish Widows Investment Partnership Group Limited	England	*100%	Investment management	10 Fleet Place, London EC4M 7RH England

Abbey Life Assurance Company Limited	England	*100%	Life assurance	80 Holdenhurst Road, Bournemouth BH8 8ZQ England

105

Lloyds TSB Insurance Services Limited	England	*100%	Insurance broking	25 Gresham Street, London EC2V 7HN England
Lloyds TSB Life Assurance Company Limited	England	*100%	Life assurance and other financial services	25 Gresham Street, London EC2V 7HN England
Lloyds TSB Asset Finance Division Limited	England	*100%	Consumer credit, leasing and related services	25 Gresham Street, London EC2V 7HN England
Black Horse Limited	England	*100%	Consumer credit, leasing and related services	25 Gresham Street, London EC2V 7HN England
Scottish Widows plc	Scotland	*100%	Life assurance	69 Morrison Street, Edinburgh, EH3 8YF Scotland
Scottish Widows Annuities Limited	Scotland	*100%	Life assurance	69 Morrison Street, Edinburgh, EH3 8YF Scotland

* Indirect interest

106

INDEX TO THE CONSOLIDATED FINANCIAL STATEMENTS

Report of Independent Accountants

To the Shareholders of Lloyds TSB Group plc:

We have audited the accompanying consolidated balance sheets of Lloyds TSB Group plc and its subsidiaries as of 31 December 2002 and 31 December 2001, and the related consolidated profit and loss account, consolidated statement of total recognised gains and losses, reconciliation of movement in shareholders' funds and consolidated cash flow statement for each of the three years in the period ended 31 December 2002 which, as described in Note 1, have been prepared on the basis of accounting principles generally accepted in United Kingdom. These financial statements are the responsibility of the directors of Lloyds TSB Group plc. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Lloyds TSB Group plc and its subsidiary undertakings at 31 December 2002 and 31 December 2001, and the results of their operations and their cash flows, for each of the three years in the period ended 31 December 2002 in conformity with accounting principles generally accepted in the United Kingdom.

Accounting principles generally accepted in the United Kingdom vary in certain material respects from accounting principles in the United States. The application of the latter, after the restatement referred to on page F-67, would have affected the determination of consolidated net income expressed in pounds sterling for each of the three years in the period ended 31 December

2002 and the determination of consolidated shareholders' equity also expressed in pounds sterling at 31 December 2002 and 2001 to the extent summarised in Note 48 to the consolidated financial statements.

PricewaterhouseCoopers LLP
Southampton, England
13 February 2003, except for the restatement referred to on page F-67 as to which the date is 23 June 2003.

F-2

Consolidated profit and loss account
for the year ended 31 December 2002

	Note	2002 GBP million	2001* GBP million	2000* GBP million
Interest receivable:				
Interest receivable and similar income arising from debt securities		567	530	443
Other interest receivable and similar income		9,982	10,834	10,611
Interest payable		5,378	6,442	6,467
Net interest income		5,171	4,922	4,587
Other finance income	43	165	307	424
Other income				
Fees and commissions receivable		3,053	2,922	2,768
Fees and commissions payable		(645)	(602)	(479)
Dealing profits (before expenses)	3	188	233	198
Income from long-term assurance business	29	(303)	(29)	443
General insurance premium income		486	428	399
Other operating income		763	708	436
		3,542	3,660	3,765
Total income		8,878	8,889	8,776
Operating expenses				
Administrative expenses	4	4,214	4,226	3,893
Depreciation	23	642	511	364
Amortisation of goodwill	22	59	39	22
Depreciation and amortisation		701	550	386
Total operating expenses		4,915	4,776	4,279
Trading surplus		3,963	4,113	4,497
General insurance claims		229	174	142
Provisions for bad and doubtful debts	14			
Specific		965	736	547
General		64	11	(6)
		1,029	747	541
Amounts written off fixed asset investments	5	87	60	32
Operating profit		2,618	3,132	3,782

Income from joint ventures	19	(11)	(10)	3
Profit on sale of businesses	6	-	39	-
Profit on ordinary activities before tax	7	2,607	3,161	3,785
Tax on profit on ordinary activities	8	764	875	1,082
Profit on ordinary activities after tax		1,843	2,286	2,703
Minority interests : equity		19	17	13
: non-equity	39	43	40	36
Profit for the year attributable to shareholders		1,781	2,229	2,654
Dividends	9	1,908	1,872	1,683
(Loss) profit for the year	41	(127)	357	971
Earnings per share	10	32.0p	40.3p	48.4p
Diluted earnings per share	10	31.8p	39.9p	47.9p

The accompanying notes are an integral part of the Consolidated Financial Statements.

* restated (see note 1)

Consolidated balance sheet
at 31 December 2002

	Note	2002 GBP million	2001* GBP million
Assets			
Cash and balances at central banks		1,140	1,240
Items in course of collection from banks		1,757	1,664
Treasury bills and other eligible bills	11	2,409	4,412
Loans and advances to banks	12	17,529	15,224
Loans and advances to customers		134,498	123,059
Non-returnable finance		(24)	(124)
	13	134,474	122,935
Debt securities	16	29,314	24,225
Equity shares	17	206	225
Interests in joint ventures:	19		
- Share of gross assets		336	281
- Share of gross liabilities		(291)	(242)
		45	39
Intangible fixed assets	22	2,634	2,566
Tangible fixed assets	23	4,096	3,365
Own shares	26	18	23

Other assets	27	5,263	4,468
Prepayments and accrued income	28	2,305	2,296
Post-retirement benefit asset	43	-	356
Long-term assurance business attributable to the shareholder	29	6,228	6,366
		207,418	189,404
Long-term assurance assets attributable to policyholders	29	45,340	46,389
Total assets		252,758	235,793

The accompanying notes are an integral part of the Consolidated Financial Statements.

*   restated (see note 1)

	Note	2002 GBP million	2001* GBP million
Liabilities			
Deposits by banks	31	25,443	24,310
Customer accounts	32	116,334	109,116
Items in course of transmission to banks		775	534
Debt securities in issue	33	30,255	24,420
Other liabilities	34	8,289	6,673
Accruals and deferred income	35	3,696	3,563
Post-retirement benefit liability	43	2,077	75
Provisions for liabilities and charges:			
Deferred tax	36	1,317	1,411
Other provisions for liabilities and charges	37	361	292
Subordinated liabilities:			
Undated loan capital	38	5,496	4,102
Dated loan capital	38	4,672	4,006
Minority interests:			
Equity		37	37
Non-equity	39	694	509
		731	546
Called-up share capital	40	1,416	1,411
Share premium account	41	1,093	959
Merger reserve	41	343	343
Profit and loss account	41	5,120	7,643
Shareholders' funds (equity)		7,972	10,356
		207,418	189,404
Long-term assurance liabilities to policyholders	29	45,340	46,389
Total liabilities		252,758	235,793
Memorandum items	44		
Contingent liabilities:			
Acceptances and endorsements		1,879	2,243

Guarantees and assets pledged as collateral security	5,927	3,789
Other contingent liabilities	2,540	1,931
	10,346	7,963
Commitments	64,504	53,342

The accompanying notes are an integral part of the Consolidated Financial Statements.

* restated (see note 1)

Other statements

Statement of total recognised gains and losses
for the year ended 31 December 2002

	2002 GBP million	2001* GBP million	2000* GBP million
Profit attributable to shareholders	1,781	2,229	2,654
Currency translation differences on foreign currency net investments	(3)	(86)	(11)
Actuarial losses recognised in post-retirement benefit schemes (note 43)	(3,299)	(2,873)	(1,452)
Deferred tax thereon (note 43)	968	863	450
	(2,331)	(2,010)	(1,002)
Total recognised gains and losses relating to the year	(553)	133	1,641
Prior year adjustment at 1 January 2002 in respect of current year changes in accounting policy (note 1)	(404)	-	-
Prior year adjustment in respect of the adoption of FRS 18	-	248	-
Prior year adjustment in respect of the adoption of FRS 15	-	-	(112)
Total gains and losses recognised during the year	(957)	381	1,529

* restated (see note 1)

Historical cost profits and losses
for the year ended 31 December 2002

There was no material difference between the results as reported and the results that would have been reported on an unmodified historical cost basis.

Accordingly, no note of historical cost profits and losses has been included.

Reconciliation of movements in shareholders' funds
for the year ended 31 December 2002

	2002 GBP million	2001* GBP million	2000* GBP million
Profit attributable to shareholders	1,781	2,229	2,654
Dividends	(1,908)	(1,872)	(1,683)
(Loss) profit for the year	(127)	357	971
Currency translation differences on foreign currency net investments	(3)	(86)	(11)
Actuarial losses recognised in post-retirement benefit schemes	(2,331)	(2,010)	(1,002)
Issue of shares	77	194	74
Goodwill written back on sale and closure of businesses	-	-	109
Net (decrease) increase in shareholders' funds	(2,384)	(1,545)	141
Shareholders' funds at beginning of year	10,356	11,901	8,829
Prior year adjustment at 1 January 2000 (note 1)	-	-	2,931
Shareholders' funds at end of year	7,972	10,356	11,901

* restated (see note 1)

The accompanying notes are an integral part of the Consolidated Financial Statements.

Consolidated cash flow statement
for the year ended 31 December 2002

	2002 GBP million	2001* GBP million	2000 GBP million
Net cash inflow from operating activities (note 47a)	5,394	9,927	7,474
Dividends received from associated undertakings	2	2	2
Returns on investments and servicing of finance:			
Dividends paid to equity minority interests	(18)	(17)	(12)

Payments made to non-equity minority interests	(43)	(40)	(36)
Interest paid on subordinated liabilities (loan capital)	(463)	(514)	(442)
Interest element of finance lease rental payments	-	(1)	(1)
Net cash outflow from returns on investments and servicing of finance	(524)	(572)	(491)
Taxation:			
UK corporation tax	(758)	(682)	(723)
Overseas tax	(193)	(147)	(141)
Total taxation	(951)	(829)	(864)
Capital expenditure and financial investment:			
Additions to fixed asset investments	(46,830)	(47,049)	(23,564)
Disposals of fixed asset investments	45,507	40,530	24,850
Additions to tangible fixed assets	(1,315)	(1,157)	(1,006)
Disposals of tangible fixed assets	359	285	78
Capital injections to long-term assurance business	(140)	(100)	-
Net cash (outflow) inflow from capital expenditure and financial investment	(2,419)	(7,491)	358
Acquisitions and disposals:			
Additions to interests in joint ventures	(21)	(44)	-
Acquisition of group undertakings (note 47e)	(117)	(180)	(5,110)
Disposal of group undertakings and businesses (note 47g)	-	40	83
Net cash outflow from acquisitions and disposals	(138)	(184)	(5,027)
Equity dividends paid	(1,903)	(1,738)	(1,522)
Net cash outflow before financing	(539)	(885)	(70)
Financing:			
Issue of subordinated liabilities (loan capital)	2,120	742	952
Issue of capital securities by subsidiary undertakings	-	-	509
Issue of ordinary share capital net of GBP62 million (2001: GBP185 million; 2000: GBP124 million) charge in respect of the QUEST (note 26)	77	194	74
Repayments of subordinated liabilities (loan capital)	(55)	(131)	(55)
Minority investment in subsidiaries	167	-	-
Capital element of finance lease rental payments	(4)	(20)	(4)
Net cash inflow from financing	2,305	785	1,476
Increase (decrease) in cash (note 47c)	1,766	(100)	1,406

*restated (see note 1)

The accompanying notes are an integral part of the Consolidated Financial Statements.

1 Accounting policies

Accounting policies are unchanged from 2001, except that:

(i) The Group has implemented the requirements of the Urgent Issues Task Force's Abstract 33 'Obligations in capital instruments'. Following its implementation the Group has reclassified Euro750 million of Perpetual Capital Securities as undated loan capital and the related cost is included within interest expense. Previously these securities were included within minority interests in the balance sheet and the cost was treated as a minority interest deduction. The effect of this change on the profit and loss account for the year ended 31 December 2002 has been to increase interest payable and reduce non-equity minority interests by GBP31 million (2001: GBP22 million; 2000: nil); there has been no effect on attributable profit. The effect on the Group's balance sheet at 31 December 2002 has been to increase undated loan capital and reduce non-equity minority interests by GBP482 million (2001: GBP451 million).

(ii) The Group has implemented the requirements of Financial Reporting Standard 19 ("FRS 19") 'Deferred Tax'. Following its implementation, the Group makes full provision for deferred tax assets and liabilities arising from timing differences between the recognition of gains and losses in the financial statements and their recognition in a tax computation. Previously provision was only made where it was considered that there was a reasonable probability that a liability or asset would crystallise in the foreseeable future. A prior year adjustment has been made increasing shareholders' funds by GBP54 million to reflect the revised policy. The effect of this change on the profit and loss account for the year ended 31 December 2002 has been to reduce the tax charge by GBP29 million (2001: increase the tax charge by GBP14 million; 2000: nil). The effect on the Group's balance sheet at 31 December 2002 has been to reduce the deferred tax liability and increase shareholders' funds by GBP69 million (2001: GBP40 million).

(iii) The Group has adopted fully the accounting requirements of Financial Reporting Standard 17 ("FRS 17") 'Retirement Benefits'. FRS 17 replaces Statement of Standard Accounting Practice 24 and the Urgent Issues Task Force's Abstract 6 as the accounting standard dealing with post-retirement benefits. The Group has decided to implement the requirements of FRS 17 in 2002 to coincide with the triennial full actuarial valuations of the Group's pension schemes and because of the significant impact that implementation has on the Group's reported results.

FRS 17 requires the assets of post-retirement defined benefit schemes to be included on the balance sheet together with the related liability to make benefit payments. The profit and loss account includes a charge in respect of the cost of accruing benefits for active employees, benefit improvements and the cost of severances borne by the schemes; the expected return on the schemes' assets is included within other finance income net of a charge in respect of the unwinding of the discount applied to the schemes' liabilities. It also includes a charge in respect of post-retirement healthcare obligations. Under Statement of Standard Accounting Practice 24 the profit and loss account included a charge in respect of the cost of accruing benefits for active employees offset by a credit representing the amortisation of the surplus in the Group's defined benefit pension schemes; a pension prepayment was included in the Group's balance sheet, together with a provision in respect of post-retirement healthcare obligations. A prior year adjustment has been made increasing shareholders' funds by GBP2,810 million to reflect the revised policy.

The effect of this change on the profit and loss account for the year ended

31 December 2002 has been to introduce other finance income of GBP165 million (2001: GBP307 million; 2000: GBP424 million), and to increase administrative expenses by GBP323 million (2001: GBP452 million; 2000: GBP327 million). Profit before tax has been reduced by GBP158 million (2001: reduced by GBP145 million; 2000: increased by GBP97 million). The effect on the Group's balance sheet at 31 December 2002 has been to reflect a net post-retirement benefit liability of GBP2,077 million (2001: a net post-retirement benefit asset of GBP356 million and a post-retirement benefit liability of GBP75 million), to reduce prepayments and accrued income by GBP928 million (2001: GBP894 million), to reduce the deferred tax liability by GBP251 million (2001: GBP268 million), to reduce other provisions for liabilities and charges by GBP76 million (2001: GBP109 million) and to reduce shareholders' funds by GBP2,678 million (2001: GBP236 million).

(iv) In December 2001, the Association of British Insurers (ABI) published detailed guidance for the preparation of figures using the achieved profits method of accounting which are published as supplementary financial information accompanying the accounts of most listed insurance companies. The ABI guidance recommends the use of unsmoothed fund values to calculate the value of in-force business. To improve the comparability of the results of the Group's insurance operations with the supplementary financial information published by listed insurers the Group has changed the basis of its embedded value calculations to use unsmoothed fund values; previously the effect of investment fluctuations had been amortised to the profit and loss account over a two year period. A prior year adjustment has been made reducing shareholders' funds by GBP67 million, to reflect the revised policy.

The effect of this change on the profit and loss account for the year ended 31 December 2002 has been to reduce income from long-term assurance business before tax by GBP104 million (2001: GBP222 million; 2000: GBP172 million). The effect on the Group's balance sheet at 31 December 2002 has been to reduce the value of the long-term assurance business attributable to the shareholder by GBP281 million (2001: GBP208 million) and to reduce shareholders' funds by the same amount.

F8

1 Accounting policies (continued)

Comparative figures for 2001 and 2000 have been restated in respect of all of the above changes.

The prior year adjustments in respect of these changes can be summarised as follows:

	Adjustment to shareholders' funds at 1 January 2000	Impact on attributable profit for year ended 31 December 2000	Actuarial losses recognised in post-retirement benefit schemes for year ended 31 December 2000	Adjustment to shareholders' funds at 31 December 2000
	GBPm	GBPm	GBPm	GBPm

FRS 19 Deferred tax (ii)	54	-	-	54
FRS 17 Retirement benefits (iii)	2,810	68	(1,002)	1,876
ABI guidance (iv)	67	(120)	-	(53)
Total	2,931	(52)	(1,002)	1,877

	Adjustment to shareholders' funds at 1 January 2001	Impact on attributable profit for year ended 31 December 2001	Actuarial losses recognised in post-retirement benefit schemes for year ended 31 December 2001	Adjustment to shareholders' funds at 31 December 2001
	GBPm	GBPm	GBPm	GBPm
FRS 19 Deferred tax (ii)	54	(14)	-	40
FRS 17 Retirement benefits (iii)	1,876	(102)	(2,010)	(236)
ABI guidance (iv)	(53)	(155)	-	(208)
Total	1,877	(271)	(2,010)	(404)

a Accounting convention

The consolidated accounts are prepared under the historical cost convention as modified by the revaluation of debt securities and equity shares held for dealing purposes (see g) and assets held in the long-term assurance business (see n), in compliance with Section 255A, Schedule 9 and other requirements of the Companies Act 1985 except as described below (see c), in accordance with applicable accounting standards, pronouncements of the Urgent Issues Task Force and with the Statements of Recommended Practice issued by the British Bankers' Association and the Finance & Leasing Association. The Group's methodology for calculating embedded value follows the guidance published by the Association of British Insurers for the preparation of figures using the achieved profits method of accounting except that tangible assets attributable to the shareholder are valued at market value. The guidance would require those assets backing capital requirements to be discounted to reflect the cost of encumbered capital, but such a treatment would be inconsistent with the treatment of capital supporting the Group's banking operations. If this treatment had been followed income from long-term assurance business before tax in 2002 would have been slightly improved. Conversely, embedded value would have been some 8 per cent lower given the size of the shareholder capital required to be retained within Scottish Widows under the terms of the demutualisation.

The Group continues to take advantage of the dispensation in the Urgent Issues Task Force's Abstract 17 'Employee Share Schemes' not to apply that Abstract to the Group's Inland Revenue approved SAYE schemes.

b Basis of consolidation

Assets, liabilities and results of group undertakings and joint ventures are included in the consolidated accounts on the basis of accounts made up to 31 December. Entities that do not meet the legal definition of a subsidiary but which give rise to benefits that are in substance no different to those that would arise from subsidiaries are also included in the conso