SUBMISSION FROM LLOYDS BANKING GROUP

We are grateful for the opportunity to make a submission to the Committee’s inquiry into the Independent Commission on Banking’s (ICB) final report.

Given the speculation of the last few months, I am sure you will agree that publication of the final report provides some welcome clarity for us all.

We have had extensive and constructive discussions with the Commission throughout its work and believe its final report sets out some important principles for how banks should be organised and how they can best protect themselves from market and economic shocks in the future.

As you may appreciate, we are still assessing the detail of the full report and look forward to further engagement with the UK Government to understand the detail surrounding some of the recommendations and how they may be implemented.

However, we thought it would be useful to offer you and your Committee colleagues our initial thoughts on some of the key elements contained in the report.

Financial Stability

As you will be aware, unlike some other firms operating in the UK, Lloyds Banking Group is primarily a retail bank. Nevertheless we have paid close interest to the ‘ring-fencing debate’. In particular, we welcome the ICB’s proposal for a wider and more flexible ring fence than the ‘narrow’ definition that some had discussed. We believe this will help protect key economic functions, including the provision of credit to businesses of all sizes.

On loss absorbency, we would note that our current 15% total capital ratio (as at June 2011) compares well with the ICB’s recommended Primary Loss Absorbing Capacity (PLAC) of 17%, which banks would have until 2019 to achieve. We also welcome the ICB’s emphasis on the need for capital buffers to be loss absorbing in a stress.

Finally, there will need to be careful debate and consultation to fully understand how the market enacts the principles on bail-ins and the implications for unsecured debt.

Competition

A key theme of the Commission’s report was on promoting competition and the creation of a strong challenger bank and increasing competitiveness in the marketplace.

You will be aware of our divestment programme, known widely as ‘Verde’. In Scotland, this includes all of the 185 LloydsTSB Scotland branches as well as Intelligent Finance (IF). This combines with a further 283 LloydsTSB branches in England & Wales as well as the Cheltenham & Gloucester business (including its 164 branches). We are very confident in the profile of the ‘Verde’ business and its capability to become a strong and viable challenger bank.
We therefore welcome the focus in the ICB’s final report on the strength of Verde as a competitor rather than on the number of branches it operates (as had been previously debated).

We have put in place measures to significantly reduce Verde’s Loan to Deposit (LTD) ratio, through the natural reduction in its assets as well as the potential growth in deposits through the IF brand. This would meet the criteria laid out by the ICB and place its LTD in-line with its peers. We have also made arrangements for there to be independent sources of medium term financing to ensure that it is fully funded at the time of its disposal. We are confident therefore that Verde will be the viable challenger the ICB seeks.

In relation to competition, the Commission also makes a number of important recommendations to make it quicker and simpler for customers to switch accounts.

We believe the UK retail banking market is internationally competitive. Customers change provider much more frequently in the UK market and often use more than one bank than is the case than in other markets. However, we also think more can be done and have led the way in putting forward proposals for achieving this.

Customers want easy-to-understand products, clear information about charges and benefits so they can compare different providers, and the ability to change provider easily and quickly if they want to. We have taken an industry lead with simple, transparent products and have improved switching through our ISA Promise. In current accounts, the industry has significantly improved the switching experience for customers in recent years, but many still think the process needs to be improved further.

We are pleased, therefore, to see the ICB has recommended the new seven-day switching process which we proposed and which is now being taken forward by the Payments Council. The Payments Council is now actively working on the implementation of a fully automated, guaranteed system to enable customers to switch current accounts within seven days. We are confident that this will be ready in time for the ICB’s deadline of September 2013 – more details can be found at http://www.paymentscouncil.org.uk/media_centre/press_releases/-/page/1618/. This is the right thing to do for customers and good for competition.

Finally, we are pleased the ICB has not recommended an immediate review of the PCA market and instead has recognised that both the switching and transparency measures along with the entrant of the new Verde challenger need time to bed in before any further review is conducted. We believe both these measures will deliver significant positive changes in the market and it is right that any future review takes place after they are fully in place.

**Timetable**

The ICB has suggested its financial stability recommendations should be in place by 2019 – this appears a sensible and realistic timetable to ensure the industry has the time to make the necessary changes once legislation has been introduced.
Again, we look forward to discussing this with the Government and other regulatory bodies to understand the key milestones the industry must achieve in advance of this date.

I hope these comments are helpful as you and your Committee colleagues consider the ICB’s final report.

Anthony Thompson
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