Lloyds Prepares to Resume Dividends as Osborne Weighs Sale (3)
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(Updates with Treasury statement in 18th paragraph.)

By Gavin Finch

Aug. 1 (Bloomberg) -- Lloyds Banking Group Plc said it will seek to resume dividends, five years after receiving a taxpayer bailout, as the government prepares to cut its stake in the British lender. The stock hit a two-and-a-half-year high.

Net income rose to 1.56 billion pounds ($2.4 billion) in the first half from a 697 million-pound loss in the year-earlier period, Britain's biggest mortgage lender said in a statement today. Loan impairments fell 43 percent to 1.8 billion pounds.

The return to profit and the possible dividend remove the final hurdles to a sale of the government's 39 percent stake in the lender as soon as this month. Chief Executive Officer Antonio Horta-Osorio said he's ready for the government to sell after Lloyds shrank assets and costs faster than planned and beat its targets to increase profitability and capital. The stock has gained 52 percent this year, surpassing the price at which the government says it would break even on its stake.

"It makes the government sale a lot easier," Colin McLean, who helps oversee 600 million pounds at SVM Asset Management Ltd. in Edinburgh, including Lloyds shares, said by telephone. "The regulator won't automatically allow dividends" and may still require the bank to set aside more capital against potential lending losses, he said.

The stock jumped as much as 6.9 percent and was up 6.6 percent at 72.98 pence as of 9:45 a.m. in London trading, above the 61 pence the government says it will break even after providing a 20 billion-pound rescue. Lloyds is the best-performing stock among its European peers in the past 12 months.

Regulator's Talks

Profit before exceptional items climbed to 2.9 billion pounds, beating the 2.34 billion-pound mean estimate of five analysts surveyed by Bloomberg.

"We're profitable, we're supporting the U.K. economy and that has enabled the U.K. government to begin the process to return the group to private ownership," Horta-Osorio, 49, told reporters on a call today. It's up to the government on "how and when to do it."

Lloyds said it plans to start talks with the regulator in the second half about the timetable and conditions for returning to dividend payments. Lloyds last paid a cash dividend in 2008,

before its takeover of HBOS Plc forced it to seek a bailout, according to data compiled by Bloomberg.
The lender booked a 450 million-pound charge in the period for compensating customers who were mis-sold payment-protection insurance. It also set aside a further 50 million pounds to cover the costs of a U.K. regulator's probe of its claims-handling practices. In total, Lloyds has set aside 7.3 billion pounds for PPI, more than any other lender and almost half of the 15.5 billion pounds total for the industry.

PPI 'Disappointing'

"It's disappointing to be having to top up the provision again," Finance Director George Culmer said on the call. "We've seen a pick-up in the amount we're paying out per case. We've also made revisions to the cost of the whole exercise."
Even after the provision, the volume of PPI complaints is falling, with the average monthly number of complaints down 12 percent compared with the first quarter and 40 below those in the second half of 2012, Lloyds said in the statement.
Horta-Osorio said he's beating his target to reduce so-called non-core assets, those that aren't designated as central to its future. They include non-performing loans, much of the lender's international operations and real estate loans. Assets at the non-core unit shrank by 17 billion pounds in the second half to 83 billion pounds. The firm said it will shrink the unit to less than 70 billion pounds by the end of 2013, a year ahead of schedule.

Paying Depositors

The lender raised its full-year target for net interest margin to 2.1 percent from a previous target of 1.98 percent. The measure, the difference between the bank's income from lending and its cost of funding, widened to 2.01 percent in the first half from 1.93 percent in the year-earlier period as it paid out less to depositors.
"These results are very strong," said Cormac Leech, an analyst at Liberum Capital Ltd. In London with a buy rating on the stock. The bank's improved net interest margin guidance "is really to do with shrinking the non-core business, which has low NIM, and they are paying depositors less and less."
Lloyds's core Tier 1 capital ratio under the full Basel III rules, a key measure of financial health, increased to 9.6 percent in the period. The bank said it expects the gauge to surpass 10 percent by the end of 2013, a year ahead of target.
Lloyds is benefiting as the U.K. economy show signs of recovery, with property prices rising and manufacturing growth

increasing. Chancellor of the Exchequer George Osborne is now accelerating plans to recoup some of the taxpayers' investment before the next election in May 2015.

Government Plans

The U.K. is considering selling as much as 5 billion pounds of Lloyds shares to money managers as a first step to reducing its holding, a person with knowledge of the plan said last week. The sale, planned for September, may come sooner if market conditions allow, said the person, who asked not to be identified because a decision hasn't been reached.
"Lloyds continues to make progress towards becoming a stronger and safer bank," the Treasury said in an e-mail today. "We have no set timetable or target share price for beginning the return of Lloyds to the private sector."
The stock price was boosted in May, when Lloyds ruled out raising additional equity to help plug an 8.6 billion-pound capital shortfall identified by regulators. It opted instead to sell assets. Since then, the bank has sold holdings of U.S. mortgage-backed securities for about $5 billion in cash and a second stake in wealth manager St. James's Place Plc. The firm is also considering a sale of Scottish Widows Investment Partnership and its unprofitable Australian business.
Horta-Osorio is also lowering expenses to strengthen the balance sheet, applying back-office efficiencies such as reducing the number of the bank's suppliers and integrating information technology. Lloyds increased its target for cost cuts this year, saying it plans to reduce expenses to about 9.6 billion pounds in 2013 and 9.2 billion pounds in 2014.

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