

To Lloyds Banking Group Shareholders

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Lloyds Bank Shareholders Action Group – Update No. 4

Meeting for Lloyds Shareholders

On the 30th/31st October 2009 we are exhibiting at the **MONEYSHOW** at the **QEII Conference Centre** in London. The MONEYSHOW event includes a **special meeting for Lloyds Bank shareholders on Saturday 31st Oct at 11.0 am**. Attendance at this event is FREE, but you do need to register for the conference to gain admission. See www.uksa.org.uk/LloydsMeeting.htm for more information.

The meeting is primarily aimed at enabling shareholders to ask questions about what this Group has been doing and the progress of the campaign to obtain some recompense for shareholders from the losses they have suffered as a result of the mistaken merger of Lloyds TSB and HBOS. It will enable those who have registered with this Group to meet the committee formed to run this Group and it will primarily be a question and answer session, but there will be short presentations at the start. UKSA will also have a stand in the exhibition area at this event (no. 413) where you can come and have a chat at any time.

In addition UKSA Director Roger Lawson will be giving a presentation on "**Shareholder Activism in the Banking Sector**" at 2.0 pm on the Saturday where he will be outlining what UKSA has been doing in this area over the last year.

There are several other events coming up in which UKSA is involved. This includes a meeting for **Bradford & Bingley Shareholders** on the morning of 10th October in London - see www.uksa.org.uk/B&B_Meeting.htm for more information. There is also a meeting for **Royal Bank of Scotland Shareholders** organised by an independent group in the afternoon at the same venue - see www.rbosaction.org/RBOS_Meeting_Notice.pdf for more information. These may also be of interest to those who have been affected by the banking crisis.

Questions & Answers

Note that the meeting mentioned above is a golden opportunity for Lloyds shareholders to ask questions. It is regrettably not possible for us to respond in writing to individual questions sent in via letter or email, or written as notes on our mailing response forms. We are very keen to control the administrative costs of this campaign, and in essence we only have one junior member of staff handling the administrative work and maintaining our contact database (all of our mailings are contracted out, even some of the response processing). We will try to answer commonly put questions in these newsletters or on our web site for those who cannot attend the above meeting. If your question is really important and is not answered on our web site, then you can call 020-8468-1027 if necessary.

One question that has arisen is regarding the legal structure of this Group. As explained on our donation forms, the Lloyds Bank Shareholders Action Group is run by a Committee within the UK Shareholders Association – the legal form of that organisation is explained on our web site on this web page: www.uksa.org.uk/Legal.htm

The Committee consists of unpaid volunteers (and they have not even been paid any expenses to date), and neither I nor any other UKSA board members are paid any salaries. All money raised by this campaign will be used to promote the interests of Lloyds Bank shareholders as explained on our donation forms.

Merger Negotiations

The Daily Telegraph ran a long article by Philip Aldrick on the 16th September on the merger negotiations between Eric Daniels of Lloyds and Andy Hornby of HBOS. In case anyone thinks that this disastrous merger was solely promoted by Gordon Brown and his friend Sir Victor Blank, the article suggests that Daniels was a key player in concluding the deal, although he seems to have negotiated the price down.

A revealing comment in the article is this: *"The strategy, it seemed, was a gamble that Lloyd's reputation as a conservative bank would reassure markets. Unfortunately, the reputational influence worked the other way. HBOS, the bigger bank, soon began infecting Lloyds with its bad commercial and mortgage lending"*. The article comments also on the failure by Lloyds to get any guarantees from the Government against the prospective losses in HBOS. The subsequent losses that have become apparent, and the need to insure against the losses on the "toxic" assets acquired from HBOS have wiped out all the synergies expected from the deal and the low price that was paid for the company. The full article can be read at: <http://tinyurl.com/kvooue>

Asset Protection Scheme

The Asset Protection Scheme still seems to be under discussion, with rumours of possible placings to raise funds to replace all or part of the insurance and associated funding. Several newspapers reported that the FSA was blocking such a move having done some "stress tests" on the prospects for the company. However, Lloyds then issued an announcement saying that they were still *"discussing possible changes to the commercial terms"* on which Lloyds might enter the scheme and that *"all possibilities remain open"*. Of course the amusing thing about any such discussions is that the Government has a financial interest in having a deal that is favourable to itself, is asking the FSA (an arm of the Government) to judge whether it is prudent for the company to enter into it, and with a 43% stake in Lloyds has very substantial influence if not effective control of the company. So you can guess the likely outcome.

Other Lloyds News

Lloyds has undertaken a u-turn over the proposed closure of the 164-branch Cheltenham & Gloucester operation. It is now to be retained, possibly so as to enable it to be disposed of in a "down-sizing" operation to meet the demands of the European Commission. But the Daily Mail reported that the more than a third of the Halifax branch network is to be closed, with many "agency" outlets among them.

Moody's Downgrades

Moody's has forecast further losses of £130bn in UK banks over the next few years as bad debts rise and profitability is squeezed. In a worst case scenario, they suggested that figure could be as much as £250bn. They also suggested that Lloyds/HBOS and the Royal Bank of Scotland were the most heavily exposed due to their high involvement in the construction and property sectors. They have downgraded or put under review the subordinated debt and preference shares of both companies, particularly bearing in mind the *"higher probability of coupon suspension on these securities as result of the ongoing discussions between the UK Government and the European Commission on the planned state aid package"*.

An example of the problems in Lloyds was the revelation that they faced the prospect of having to write off £500m on loans to Admiral Taverns as part of a restructuring of that company.

Living Wills

The Chancellor is apparently to legislate to ensure that banks have "living wills" that enable them to be dismantled if they get into difficulties. One of the problems with the Lehman's collapse was that after it was allowed to go bust (and the recent BBC television documentary gives you some idea of why), it became apparent that the complexity of the firm, and the structure of many of the deals they were involved in, means that it is going to be very complex, and take many years, to liquidate.

Of course there may be a hidden agenda here. Banks have complex financial structures for two primary reasons: 1) a long and complex history; 2) a desire to minimize tax. Mr Darling's comments suggest that he would like to see a simplification of the structures of banks. But it is no secret that until recently banks were one of the major contributors to the UK take from corporation tax and the recent financial crisis is having an impact on UK tax revenues. He seems to be wanting to ensure that if they do recover, that they pay more tax in due course. This tends to reinforce the view that the historic profitability of UK banks may never be recovered.

Book Review

There have been a plethora of books on the banking crisis and the events at Northern Rock which were the first indication of major problems in this sector in the UK. Often these tomes were rushed out and contained a superficial analysis, or even "populist" approach to the subject. As a result the underlying research was frequently inadequate and the conclusions erroneous. Now we have a publication which is more thoughtful and more comprehensive in a book by Bill Brown (*"The Decline and Fall of Banking"* by Bill Penman-Brown). Mr Brown had a lifetime career in international banking, working for several major firms, and subsequently became Financial Services Commissioner for Gibraltar responsible for regulating financial services and investment firms. So he has seen banking from both sides of the fence. His book entitled *"The Decline and Fall of Banking"* stretches to 500 pages and is a comprehensive analysis of the banking scene from a UK perspective over the last couple of years with a detailed analysis of the events at Northern Rock. If you don't understand the causes of the crisis, then this is an invaluable work as it covers the sub-prime crisis that arose in the USA, the growth of securitisation and covered bonds, the rise and fall of monoline insurers, the impact of credit rating agencies and the other factors that combined to create the crisis. Incidentally the book contains a number of references to the activities of the UK Shareholders Association (UKSA).

In summary, an invaluable work that any investor who wishes to understand the banking sector and what went wrong should peruse. The book is available at the list price of £34.95 from any good book store or direct from the publisher (Troubadour – see www.troubador.co.uk/shop.asp) but you can buy it direct from the author at a specially discounted price of only £26.95 (including post and packing) arranged by UKSA. Please send orders to Bill Brown at 79 Whitehouse Road, Edinburgh EH4 6PB (contact details in case of queries: bilbro@talktalk.net , telephone 0131 336 3131). Cheques should be made payable to W.P. Brown and please send a cheque with your order.

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Note that all previous information issued by UKSA in respect of our campaign on Lloyds Bank is present on the following web site page: www.uksa.org.uk/Lloyds.htm