

Opening Statement by Seamus Boland, CEO Irish Rural Link

Chairman and Members of the Committee. Thank you for inviting us here today.

Introduction

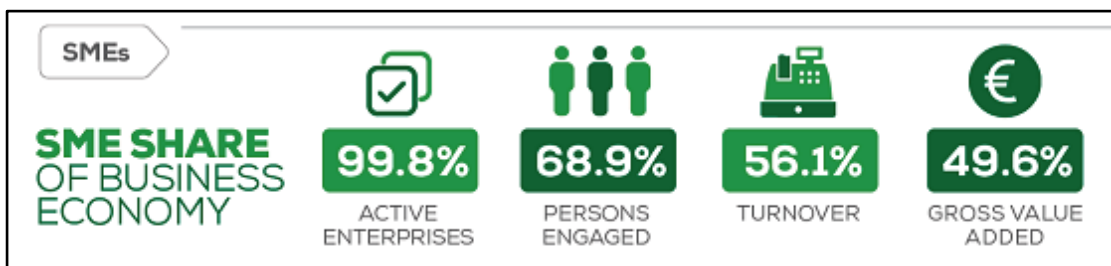
Irish Rural Link (IRL) is a national community network of local organisations dedicated to achieving sustainable rural communities. The Sparkasse Foundation (SBFIC) is the consulting arm of the DSGV (German Savings Bank Association), which advocates for the Sparkassen concept globally, and promotes core Savings banks issues.

IRL and SBFIC are working together to propose a network of Regional Public Banks that emulate the best practice as carried out by the Sparkassen banks in Germany. These banks would be focused on fulfilling the demand of SMEs for credit and promote a more even economic development across our rural communities. This policy is consistent with Irish Rural Link's vision of sustainable rural communities. It also ties into our belief that investment in rural areas must ensure infrastructure is available to companies and enterprises in these areas in order that they can create and compete for jobs.

The SBFIC are natural partners in this project as their objective is to provide proactive support to financial institutions that sustainably foster economic and social development at the local, regional or national level through needs-oriented banking services.

Background

The SME sector is the backbone of the Irish economy, comprising 99.8% of all enterprises and nearly 70% of people employed, and hence it is the engine for regional and local development.



This engine of our regions was hit particularly hard by the recession. In fact between 2007 and 2012 employment in SMEs dropped nearly 25 per cent¹. In

¹ <https://www.irishtimes.com/business/economy/smes-account-for-99-7-of-business-enterprises-in-republic-1.2035800>

rural Ireland the loss of employment was accompanied by a population decline especially of younger people, that has decimated many rural communities.

It is evident that SMEs are particularly prevalent in rural areas² and thus that rural development will depend on these enterprises being supported so they reach their potential to contribute to their local economies. The agricultural sector is, of course, almost entirely based in rural areas and the 139,100 family farms can all be considered SMEs.

Our financial institutions are not serving this key component of our economy in the way they require. We know that all the commercial banks have pulled back their branch networks significantly³, leaving many rural communities with no access to a local branch. This is a symptom of the overall trend of banks to “increasingly rigid policy-driven and automated decision making” according to the 17th Report of the Credit Review Office⁴. John Trethowan of the CRO goes on to identify the “remoteness of the relationship with borrowers” and “the increasing reliance on credit decision making software” as being of concern for SME and Farm lending. Even more worryingly Mr Trethowan notes in his latest report that “banks have generally tightened their credit policies over the past year”.⁵

Concept of Public Banking

Germany demonstrates how a banking system with three pillars provides a more stable financial support system for SMEs. The three pillars of the German banking system are made up of the Private commercial banks, the Cooperative banks and the Public Savings Banks, called the Sparkassen. The Sparkassen are most notable for the public welfare mandate they have whereby stakeholder value is the key objective not shareholder value. The Sparkassen have the lion’s share of the market for SME financing in Germany at 70% with an overall 42% market share of business financing generally.

This format of banking creates a virtuous cycle within communities and leads to balanced regional economic structures as it is guaranteed that local deposits are

² Rural Economic Development in Ireland, Teagasc, 2014, P 393, Available at https://www.teagasc.ie/media/website/publications/2014/Rural_Economic_Development_in_Ireland.pdf

³ The disappearing bank branch, available at <https://www.stubbsgazette.ie/news/the-disappearing-bank-branch>

⁴ 17th Report of the Credit Review Office, available at: <http://www.creditreview.ie/wp-content/uploads/2016/11/Seventeenth-Report-from-Credit-Reviewer-FINAL.doc>

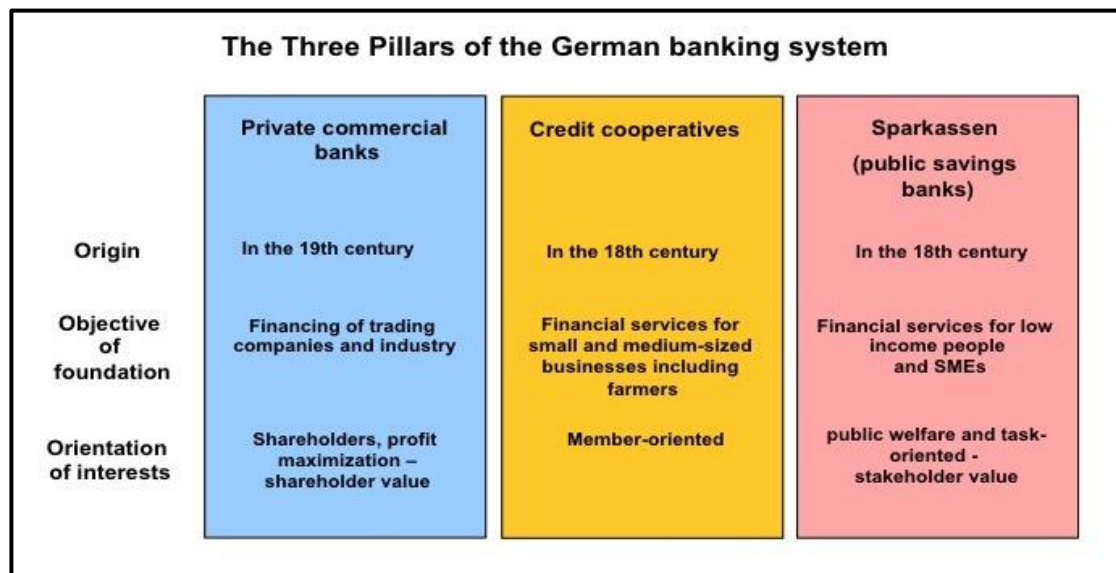
⁵ 18th Report of the Credit Review Office, available at: <http://www.creditreview.ie/wp-content/uploads/2017/07/Credit-Review-Office-Eighteenth-Report-FINAL.doc>

transformed into local loans. The regional principle establishes a strong link with the local economy where local staff uses local knowledge as a basis for risk management. Furthermore the public mandate ensures non-discriminatory provision of financial services with appropriate conditions to all citizens (especially SMEs) and reinvestment of profits for local social developments.

In Ireland we only have two pillars in existence;

- The commercial banks, who are still recovering from the financial crisis and struggling to rid their balance sheets of Non-Performing Loans (NPLs)
- The Credit Unions, similar to the Cooperative banks in Germany but catering mostly for smaller consumer loans.

We used to have banks that performed a role similar to the third pillar namely ACC and ICC. With the demise of these this has left a gap in the Irish banking sector and leaves the SME sector under-served.



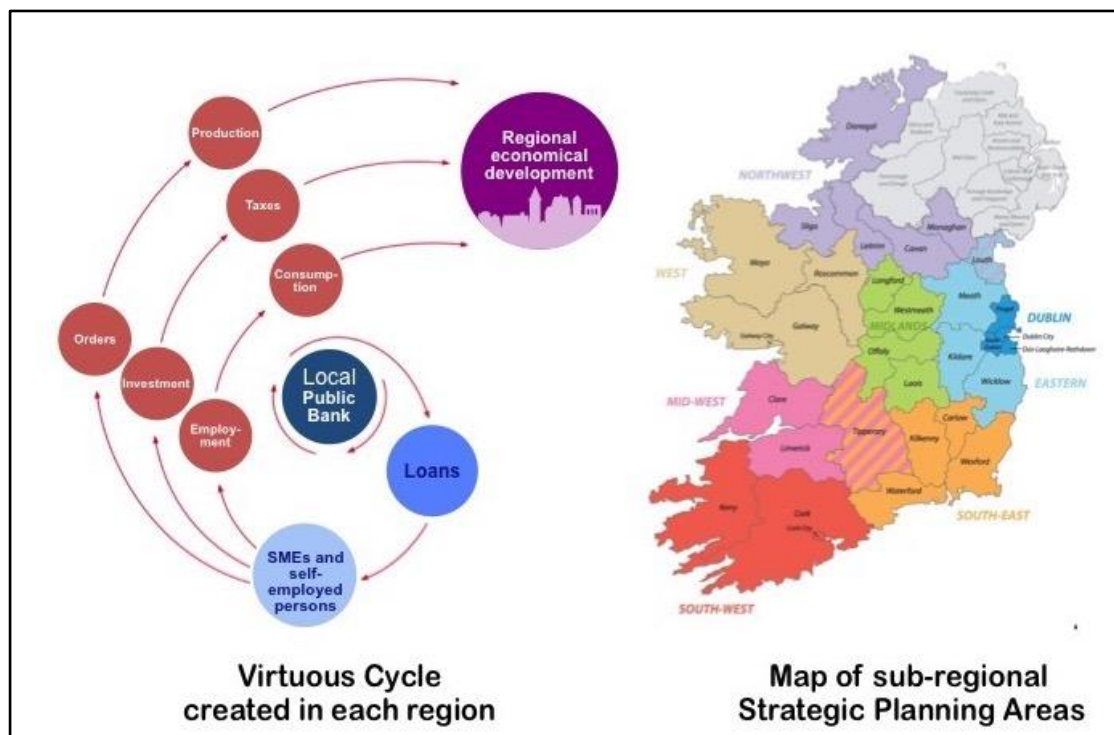
Professor Patrick Honohan recognized this gap when he said: “There should be a second tier of banking which is geared more towards local concerns, with local managers and a greater level of local awareness. This would be on a scale larger than the credit unions. They could be the nucleus of it, but the credit unions as they stand are too small individually to be really effective suppliers of services.”⁶

⁶ Speaking at Overview of Banking Sector; Joint Committee on Finance, Public Expenditure and Reform Debate 26th November 2014, available at <http://oireachtasdebates.oireachtas.ie/debates%20authoring/debateswebpack.nsf/committeetakes/FIJ2014112600002?opendocument#A00100>

The Proposal

Irish Rural Link has been working with the Sparkassen Foundation for the last 2 years to introduce the idea of a regional public banking model in Ireland. We have made a submission to the Government as part of the Consultation on Community Banking and are still awaiting this report.

In our submission we are proposing a solution to the continuing problem of accessing finance as experienced by SMEs by establishing a decentralized network of 8 to 10 regional public banks across Ireland. Each regional public bank will be an independent, fully licensed, professionally managed financial institution with its own balance sheet and responsible risk management. Through the network owning a Central Service Provider that offers administrative services, controlling and auditing functions to all the member banks of the network, efficiencies are achieved within the group.



Each Regional Public Bank will exclusively serve clientele from its defined region i.e. local private households, rural SMEs and self-employed people. This allows it to re-establish local relationship banking to Ireland's regions. Its corporate business model will focus on retail finance, finance for working capital and investment activities of SMEs and agricultural clients. Focusing on SME lending will have a direct positive influence on the level of regional employment. Finance for working capital and investment will allow indigenous SMEs to grow and attract outside investors to the region.

IRL knows that Farming and SME business is by definition local business. The business model of a Regional Public Bank offers the suitable product mix and



efficient lending procedures for rural businesses. Its credit risk management takes into account relevant local business information, including “soft” information, which enables prudent and fair risk management and allows the lender to offer start-up finance and finance for innovation.

What is now required from Government

Irish Rural Link believes that there is a strong case for Ireland to establish Regional Public Banks and we believe the 200 year old, proven Sparkasse model provides a good basis on which to shape it. IRL wants the Government to recognize the need for some kind of third pillar of banking model in Ireland and to more actively engage with parties such as the Sparkasse Foundation to fully explore how this model could be set up including any legislative or regulatory requirements.

Supplementary Information

About Irish Rural Link:

Irish Rural Link represents the interests of locally based rural groups in disadvantaged and marginalised rural areas by highlighting problems, advocating appropriate policies, sharing experiences and examples of good practice. It has a membership of over 600 rural community groups dedicated to sustainable rural development and represents rural communities at a national and international level.

www.irishrurallink.ie

About Sparkassenstiftung für Internationale Kooperation (SBFIC):

This is a not-for-profit foundation that is the consulting arm of the DSGV (German Savings Bank Association). The SBFIC advocates for the Sparkassen concept globally, and promotes core Savings banks issues e.g. financial inclusion, equal opportunities & education. It recognises that local banking serves the people and the real economy (SMEs) directly and ‘fuel’ entrepreneurs and brings this message through its work across the world.

<http://www.sparkassenstiftung.de/en/home.html>

Programme For Partnership Government 2016:

“We will thoroughly investigate the German Sparkassen model for the development of local public banks that operate within well-defined regions”

Action Plan for Rural Development 2017:

Action 23:

“Investigate the potential of the German Sparkassen model and the Kiwibank model for the development of local public banks that operate in defined regions.

National Economic Dialogue Chair's Report, 2017:

“The problem of accessing competitively priced finance among SME’s \ indigenous firms was identified as a key barrier to firm-level development and productivity growth among these firms. This constraint hampers investments in R&D, product and process development, technological adoption, workforce development and market expansion. The group felt that greater competition was needed including a regionally based SME banking model, such as the German Sparkassen model. The group urged that an appropriate banking should be implemented as soon as possible in order to address this market failure.”