



**Finance**

# **PUBLIC BANKING - A NEW CONTEXT**

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# 1 Introduction

This paper calls on the Minister for Finance to:

- Set aside the 2019 Indecon Report on Public Banking
- Begin a review of Credit Union and Post Office services
- Undertake an urgent review of:
  - a. regional access and access of underserved communities to banking services
  - b. with a view to establishing a material public banking system in Ireland
  - c. and how that public banking system might be partially or fully supported by existing infrastructure (especially Credit Unions and An Post)

As Ulster Bank announces it is to withdraw from the Republic of Ireland (and Bank of Ireland plans 88 branches closures), the requirement for a public bank has never been more keenly felt by ordinary banking customers. The moves come as a particular blow to small and medium enterprises that already face the twin challenge of Brexit and the impacts of Covid. Now 20% of SMEs will experience their bank leaving the market. It also narrows the scope and availability of banking products and services to the general public and may reduce financial inclusion for rural communities and individuals, such as those with disabilities, who already face barriers to accessing services and credit.

The Green Party believes that a public bank would be a locally focused organisation with a mandate to serve the community in its region by providing finance and other modern banking services to the real economy. Our Public Banking Policy 2019 sets out the parameters of this model.<sup>1</sup> This would fill the space previously occupied by the ACC and ICC, which were unfortunately sold to commercial banks during the Celtic Tiger years. Public banks such as these number some 1,000 and exist in 21 countries across Europe.

In 2019 an independent report<sup>2</sup> undertaken by Indecon for the government found that “*There is not a compelling economic case for the establishment of a new state-owned public banking network*” because there was sufficient competition in the banking sector and no sign of market failure. This is now no longer the case. The same report also identified a lack of trust in pillar banks and problems in the local provision of financial services. An overreliance on pillar banks is now leading to instability in the banking sector and public banking, particularly a model that accesses existing infrastructure regionally, could provide much needed confidence and access for customers.

Ireland is a small market in financial terms. We will always be at risk of a privately owned bank making the decision that NatWest/Ulster Bank has made i.e. despite being in the market for more than 160 years, and despite reporting profits, NatWest/Ulster Bank felt its capital and efforts could be deployed more profitably in larger markets. That is a decision that makes sense for Ulster Bank. It is also a decision that may make sense for any privately owned bank in the Irish market. That is one of the reasons we need a public bank.

If the aims, as set out in Programme for Government, for a more balanced economic development across all regions of Ireland urban and rural are to be achieved, the financial service requirements of this important section of the real economy needs to be fully addressed.

## 1.1 Financial Inclusion

A core element of the public banking model is a mandate to provide money and credit services to all and thus will support financial inclusion. This also allows the bank to promote savings and to support increased financial literacy among its customers. As outlined in some of the reports recently commissioned on this subject there is a segment of the population who continue to be excluded from financial services and products. While this will reflect wider societal and socio-economic issues individuals may also be financially excluded due to lack of access to internet services. Internet banking is not a viable alternative for some people who cannot access broadband but also for

<sup>1</sup> <https://www.greenparty.ie/wp-content/uploads/2018/07/Green-Party-Public-Banking-Policy.pdf>

<sup>2</sup> "Evaluation of Concept of Community Banking in Ireland", December 2019

those customers with disabilities who may need person to person assistance<sup>3</sup>. This will particularly impact low-income groups, elderly persons or people suffering from social exclusion who have no regular access to the internet. A necessity to travel to locations beyond the local community can also impact access to financial services and decrease levels of inclusion.

## 1.2 Regional Access

The announcement of the withdrawal of Ulster bank from the Irish market brought with it the closure of 22 branches. A further 88 branch closures – the majority of which are in smaller towns and villages – have been announced by the Bank of Ireland<sup>4</sup>. The banking sector in Ireland continues to suffer from the removal of local branches even in pillar banks that continue to operate in the state. The removal of banking facilities from communities has an immediate impact on financial inclusion and on the relationship between SMEs and their access to credit regionally. In a number of recent reports, outlined in more detail below, both An Post and the Credit Union sector have been identified as points of access to financial services within communities. However, a failure to expand the remit of Credit Unions' financial services and with Credit Unions currently engaged in an extremely low level of lending<sup>5</sup>, the ability of Credit Unions to offer suitable services is hampered.

The constrained nature of banking services within An Post, as service providers for pillar banks, minimises growth and profit for the organisation. In fact, the provision of the services of pillar banks through the post office network is an impediment to public banking and is keeping interest rates high. An Post already faces the possible closure of unprofitable branches in 2021 instead of realising the opportunity of community and public banking. A Public Service Obligation to keep small branches afloat is not the answer; rather the focus should be on making Post Offices profitable community-focused ventures.

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<sup>3</sup> ["Evaluation of Concept of Community Banking in Ireland"](#), December 2019, Executive Summary pg. xiv

<sup>4</sup> [Full list of Bank of Ireland branch closures](#), RTÉ, Mar 2021

<sup>5</sup> [A report by The Irish League of Credit Unions](#), July 2020

## 2 Current Political Context

In summer 2020 a new programme for government ‘Our Shared Future’ was agreed. It sets out a number of principles in which community driven, expansion of the banking sector may be achieved.

*We will support the European Central Bank and the Central Bank of Ireland’s actions to ensure stability in the banking sector. We will encourage competition within our banking sector, and develop the Fintech sector as a source of employment and competition. We do not believe that there is a long-term case for the State to remain as a shareholder in the Irish banking sector. However, we should not sell our current holdings until such a time as we are likely to recoup a significant portion, if not all, of the State’s investment.*

*We will:*

- *Introduce the Senior Executive Accountability Regime to deliver heightened accountability with the banking system.*
- *Continue working with the banking industry and non-bank lenders to support customers during and after the COVID-19 crisis.*
- *Support measures to ensure the smooth transition of ECB monetary policy for the benefit of consumers and the real economy.*
- *Implement the Finance for Ireland Financial Services Strategy to continue to deliver a competitive and resilient financial services sector.*
- *Prioritise Green Finance strategic actions that are developed in line with climate justice targets and Sustainable Development Goals.*
- *Seek to enact the Investment Partnership legislation in the Oireachtas.*

### **Credit Unions and Community Based Financial Services**

*We will:*

- *Review the policy framework within which credit unions operate*
- *Enable and support the credit union movement to grow.*
- *Support credit unions in the expansion of services to encourage community development.*

### **An Post**

- *A modernised post office network will provide a better range of financial services and e-commerce services for citizens and enterprise, as part of our commitment to a sustainable nationwide post office network.*
- *While An Post has faced significant financial challenges with a significant decline in mail volumes, they have put in place a strategic plan to transform the company. This has resulted in An Post recording an operating profit of over €41m for 2019, the third consecutive year of significant financial improvement bringing the Group out of its loss making position of 2016.*
- *This Government believes An Post has untapped potential to do more and make a further significant contribution across many areas of public, business and community life in Ireland. With an evolving mandate An Post can emerge as a central hub for a wide variety of valuable community focused services.*

The Irish state is already a significant shareholder in four commercial banks<sup>6</sup>. However, it is neither possible nor preferable to use our stake in existing commercial pillar banks to offer a form of public banking.

<sup>6</sup> [State's Shareholding in Banks](#), January 2019

Patrick Honohan described<sup>7</sup> the need for another tier of banking in Ireland when he was Governor of the Central Bank of Ireland 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.”*

We recognise that the Credit Unions’ current scale is more to do with regulatory limitations placed on them than any lack of ambition or intrinsic limitation.

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<sup>7</sup> [Joint Committee on Finance, Public Expenditure and Reform debate](#) - Wednesday, 26 Nov 2014, Pg. 10

### 3 Current Banking Sector Context

In December 2018 The Department of Finance,<sup>8</sup> published a report on public banking. It found that there is a large network of 702 commercial bank branches in Ireland. Indecon research shows that some counties including those with high levels of rural population have a high number of bank branches per capita however where the population is dispersed, local access to bank branches was restricted and there is a challenge for the banking sector to sustain the viability of the existing branches in areas of low population. It also found that the presence of higher densities of bank branches relative to number of SMEs in a number of counties where there is also a high proportion of population residing in rural locations.

There remain weaknesses in the existing banking system in Ireland as the pillar banks struggle to overcome the legacy issues they still have. This is particularly obvious in the on-going problems with the mortgage market. The banks still have higher than desirable level of non-performing loans, which increases the capital they must put aside to cover this risk and in turn feeds into the mortgage pricing. There is also a distinct lack of competition in the traditional retail banking sector in Ireland. Mario Draghi, then-President of the ECB, pointed to this as the main reason for the continuing high cost of mortgages in Ireland at a recent appearance before the Oireachtas Finance Committee.<sup>9</sup> With some of the most expensive mortgage rates in the European Union<sup>10</sup>, and now only two large lenders, the market has failed to provide adequate competition for Irish consumers.<sup>11</sup> The European Commission has defined market failure as follows: “The concept of market failure refers to non-functioning aspects of the market which result in an inefficient allocation of resources and entail the underproduction or overproduction of certain goods and services.”<sup>12</sup>

Since 2008, the Government has put in place a number of policy measures, such as the Strategic Banking Corporation of Ireland (SBCI), Microfinance Ireland and the Credit Review Office (CRO), designed to support access by SMEs to flexible, appropriately priced and sustainable finance. However, these measures have not succeeded in significantly increasing the level of credit access for small to medium enterprise and the sector continues to struggle with regional inclusion in this sector.

A distinction must be made between the various alternative non-bank finance options currently in the market and a full retail bank. On the one hand non-bank finance will offer a limited range of services addressing specific needs of the SME, mainly liquidity and risk management, finance and funding. Other fundamental day-to-day needs are still required to be provided such as Business current accounts, credit cards, foreign exchange and savings.

<sup>8</sup> [Local Public Banking in Ireland \(assets.gov.ie\)](https://assets.gov.ie)

<sup>9</sup> <https://www.independent.ie/business/irish/ecbs-draghi-blames-irish-bankmonopoly-for-high-mortgage-costs-37509130.html>

<sup>10</sup> <https://www.statista.com/statistics/615037/mortgage-interest-rate-europe/>

<sup>11</sup> [interest-rate-statistics-december-2020.pdf \(centralbank.ie\)](https://www.centralbank.ie/interest-rate-statistics-december-2020.pdf)

<sup>12</sup> European Commission and European Investment Bank, Ex-ante assessment methodology for financial instruments in the 2014-2020 programming period. April 2014. See: [https://ec.europa.eu/regional\\_policy/en/information/publications/guides/2014/ex-ante-assessment-methodology-for-financial-instruments-in-the-2014-2020-programming-period-general-methodology-covering-all-thematic-objectives-volume-i](https://ec.europa.eu/regional_policy/en/information/publications/guides/2014/ex-ante-assessment-methodology-for-financial-instruments-in-the-2014-2020-programming-period-general-methodology-covering-all-thematic-objectives-volume-i)

## 4 A New Public Banking Proposal

The Green Party contends that both the withdrawal of Ulster Bank from the Irish market and the contraction of branches available across the country by the remaining pillar banks places the need for a public Irish bank back onto the political agenda. Market conditions and competition within the sector are now insufficient for the best practice operation of the banking sector and a new consideration of public banking should be undertaken.

The core features of the model the party would seek to develop are the following:

- A business model that is profit making but not profit-maximising a public bank must have profits in order to survive and grow but the core goal of the bank is to create value and sustainability for their communities.
- A defined regional basis: a public bank has a clear geographical area within which it operates, which allows it to gain in depth knowledge of their area and build lasting relationships within their communities.
- A decentralized, network structure: Each bank would be independent with decisions taken locally. Jointly the network would own a Service Provider that would allow efficiencies and uniformity to products, costs and controls.
- A stakeholder model: the public ownership allows model to avoid focusing on shareholder value and speculation and instead focus on the real economy.

The governance model proposed is a dual board structure, based on the Sparkassen model. This comprises of a professional management board to carry out the day-to-day running of the bank and a supervisory board to oversee other functions of the bank and would include representatives of the community in the region the bank operates in. The role of the supervisory board is to ensure that the bank fulfils its public mandate. We propose that a model of public banking be developed utilising some of the following methods:

### 4.1 Banking for Micro, Small and Medium Enterprise

Small and medium enterprise in Ireland continues to struggle to access suitable levels of credit despite a spectrum of supports developed by successive governments to address this issue. A lack of credit continues to operate as a barrier to growth.<sup>13</sup>

A core driver of borrowing for SMEs is a one to one enduring relationship with a business banker who will have knowledge of the borrower's SME/farm, and of business generally.<sup>14</sup> According to the Indecon report, despite 'the overall levels of new lending there has been a decline in the application rates for bank finance by the SME sector. Application rates for bank finance were 35% in March 2014 and declined to 20% by September 2018.'<sup>15</sup> The report goes on to outline that many SMEs are choosing to reinvest retained earnings/profits or continuing to draw on existing loan facilities rather than seek finance- this may point to a gap in the availability of information amongst SMEs on how to utilise existing credit facilities.

We are in danger of moving into a situation where Ireland's two remaining pillar banks are 'too big to fail'. Many of the legacy issues of the banking system left by the 2008 recession remain, and we need resilient, community-based public banks to deliver an affordable alternative to the pillar banks.

<sup>13</sup> Gargan, E., Lawless, M., Martinez-Cillero, M., O'Toole, C., Exploring SME Investment Patterns in Ireland: New Survey Evidence.

<sup>14</sup> [19th-Report-from-John-Trethowan-2018.pdf \(creditreview.ie\)](#)

<sup>15</sup> [gov.ie - Minister Donohoe publishes independent external evaluation on Local Public Banking \(www.gov.ie\)](#)



## 4.2 Use of Existing Infrastructure

### Credit Unions

Credit Unions are looking to grow their services to small and medium-sized businesses and in doing so fulfil their role as an action group for community development through mobilising local resources for investment in the small firm economy. Such expansion will enable Credit Unions to diversify and to improve their financial health. Credit Unions are looking to play an increasing role in the Irish retail financial landscape into the future and the Central Bank is assisting credit unions in developing their business model. This may also provide a channel for increased lending to the rural SMEs in some cases, subject to the capacity of individual credit unions.<sup>16</sup>

In particular, micro firms (1-10 employees) experience significantly higher rejection rates for loans than other SME types<sup>17</sup>. Credit Unions have been seeking to fill the void of public banking in Ireland by advocating and delivering innovations to address the lack of lending to SMEs, high interest rates and rural revival,<sup>18</sup> and indeed, Ed Sibley, Deputy Governor of the Central Bank has indicated a path for credit unions to become part of a local public banking model.<sup>19</sup>

Credit Unions' new lending has increased from €1.7 billion in 2014 to €2.5 billion in 2018. This increase in lending is mirrored by the growth of larger Credit Unions, which accounted for 56% of total assets in 2018.<sup>20</sup> The network and expertise of around 250 community-based credit union branches in the Republic of Ireland could form a strong base for a local public banking model.

### An Post

There are nearly 1,000 post offices in the Republic of Ireland<sup>21</sup> and An Post is present in every county in Ireland. Analysis of An Post data by the 2019 Indecon report also confirmed that 52.7% of post offices are in geographic areas where there is no commercial bank branch within five kilometres, due to recently announced bank and branch closures this access is likely to be significantly more challenging in 2021.

An Post provides certain financial services for personal customers as well as for SMEs. These include services in the areas of savings, lending, payments and insurance. An Post also plays an important role as an agent for state savings, including for basic savings accounts and longer-term savings options. However the services offered and outreach to communities are constrained by the current model as service providers for pillar banks rather than service providers in their own right.

## 4.3 Regional Access to Banking

A principle of regional banking would see money saved in the region of the bank lent out in the same region. As part of their public mandate, these banks would aim to provide money and credit services to all and thus will support financial inclusion. This also allows the bank to promote savings and to support increased financial literacy among its customers. Countercyclical, local lending would provide a ballast during economic storms and promote economic resilience. A population in the region of 300,000 is necessary to make such a bank viable, 8 to 10 such small banks would form an Irish network.

<sup>16</sup> [Local Public Banking in Ireland \(assets.gov.ie\)](https://assets.gov.ie)

<sup>17</sup>

[https://www.oireachtas.ie/en/debates/debate/joint\\_committee\\_on\\_finance\\_public\\_expenditure\\_and\\_reform\\_and\\_taoiseach/2018-10-23/2/](https://www.oireachtas.ie/en/debates/debate/joint_committee_on_finance_public_expenditure_and_reform_and_taoiseach/2018-10-23/2/)

<sup>18</sup> <https://www.cuda.ie/blog/2018/07/11/credit-unions-will-use-a-proportion-of-e9bn-in-lending-capacity-to-reduce-sme-lending-costs/>

<sup>19</sup>

[https://www.oireachtas.ie/en/debates/debate/joint\\_committee\\_on\\_finance\\_public\\_expenditure\\_and\\_reform\\_and\\_taoiseach/2018-10-23/2/](https://www.oireachtas.ie/en/debates/debate/joint_committee_on_finance_public_expenditure_and_reform_and_taoiseach/2018-10-23/2/)

<sup>20</sup> p.14, [gov.ie](http://www.gov.ie) - Minister Donohoe publishes independent external evaluation on Local Public Banking ([www.gov.ie](http://www.gov.ie))

<sup>21</sup> <http://communityandpostoffice.ie/2020/11/postmasters-call-for-clarity-on-government-response-to-support-for-post-office-network/>

## 4.4 Costs and Benefits

The cost of implementing this will depend on the extent to which the network and expertise of Credit Unions and An Post is used, the pace of scaling up of the public banking network, and the regional context of the banks, among other factors. An independent and detailed analysis is needed. Any analysis of the costs must also feature the likely benefits to the country, such as rural revival and resilience, lower interest rates, maintaining vital jobs, and improving financial inclusion. Some of these benefits are invaluable and the cost of not doing this may be irreversible for some households and communities.

The total amount need not come entirely from Central Government. A number of options for seed financing are available, such as from the Credit Unions, the European Investment Bank and the European Central Bank.