

## **Josef Bonnici: An alternative model for banking in Malta – a case for setting up a cooperative bank in Maltese economic realities**

Address by Professor Josef Bonnici, Governor of the Central Bank of Malta, at the Seminar on “Cooperative banking”, Valletta 27 September 2012.

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Honourable Ministers, distinguished guests, ladies and gentlemen.

As the previous speakers have shown, cooperative banks, though not often in the news, in these times perhaps thankfully, have a considerable presence in most countries, particularly, but not only, in European countries. Indeed, data for 2010 show that in Europe cooperative banks hold a market share of over 20% of deposits and a similar market share for loans. Their presence is particularly marked in France, where the three cooperative banking groups (Credit Agricole, BPCE and Credit Mutuel) account for some 50% of the market share for loans and 60% of that for deposits. There is also a significant presence in Italy, where they enjoy a market share of 34% of deposits and 30% for loans; in Germany, where they have a market share of 19% for deposits and 16% for loans; in the Netherlands, with a market share of 43% of deposits and 30% for loans; and in Finland, with a market share of 34% for deposits and 32% for loans. They include, apart from the well-known French banks already mentioned, such respected names as Rabobank in Holland and the Raiffeissen banks in Germany. Cooperative banks also have a significant presence in South Korea, Japan, Canada, Morocco, Mexico and Brazil.

So the question immediately arises: how come that no such institution has ever been set up in Malta? After all one would have thought that the idea of cooperation and solidarity, and the spirit of the Seven Basic Principles of the International Cooperative Alliance (ICA) would have a strong appeal in Malta. These seven principles consist of: voluntary and open membership; democratic member control; member economic participation; autonomy and independence; education, training and information of members and employees; cooperation with other cooperatives; and, especially, concern for the community. Moreover, we do have cooperatives in other spheres of activity here, and these have been around for some time.

Indeed, the start of the cooperative movement in Malta dates back to the later years of the 19th century (around 1884), and the first form of legislation regulating cooperatives here – the Cooperative Societies Ordinance 1946 – came into effect on 12th December of that year. Initially the movement took root in the agriculture and fisheries sector, which in those times employed a significant part of the population. But later, as Malta developed socially and economically, the movement continued to flourish and to expand, and new cooperatives were set up in practically every sector of the economy. Indeed, there are currently some 60 cooperatives in Malta, with over 5000 members, spread over a wide range of activities. These include the traditional agriculture and fisheries sector, transport and media, management and marketing consultancy services, wholesale, health, maritime, archaeology, restoration, fair trade, tourism, youth services and community care. Our cooperatives are affiliated with the International Cooperatives Alliance (ICA), and so abide by the Seven Basic Principles established by the Alliance mentioned previously.

Banks too have been with us for a long time. Indeed one can trace the origins of banking in Malta to the times of the Knights of St John, though more rapid development took place under British rule, helped by the island's strategic and central position in the British Empire. In 1826, the Anglo-Egyptian Bank started operations here, and through a series of mergers and acquisitions this later became Barclay's Bank DCO (Dominion, Colonial and Overseas), which soon established an extensive branch network on the island. A number of smaller Maltese-owned banks were also established, and some of these eventually merged to become the National Bank of Malta, which also established a branch network. There followed a period when these two major banks were nationalised, but following the subsequent

liberalisation of the economy they were again privatised, with the Government retaining only a 25% share in Bank of Valletta. More banks began to operate here after Malta joined the European Union, but these were all commercial, joint stock banks. No one, till recently, seems to have thought of setting up a cooperative bank in Malta.

The distinctive characteristic of cooperative banks, as previous speakers have explained, is that they are banking entities that, for the most part, are owned by their members. The latter are both owners and customers of their bank. But this is not their only characteristic. Generally, cooperative banks are deeply rooted in their regions or communities. They are very much involved in local development and contribute to the sustainable development of their communities, because their members and officers generally belong to the communities in which they operate. Their main concern is not to make spectacular short-term gains for a small group of shareholders, but the eradication of poverty and the long-term development of the regions where they operate. Hence they are retail, not wholesale banks, and they abide by that old maxim of banking: know your customer. While helping first time buyers to buy their own homes by granting mortgages, for instance, they do not trade in mortgages.

Perhaps it is precisely because our local banks share so many of these characteristics with the cooperative banks that the need to set up a cooperative bank proper has never so far been felt here. In fact, our established banks are also – almost of necessity, given Malta's small size – deeply rooted in the local community, and are principally geared to contribute to the sustainable development of that community. They too are predominantly retail, not wholesale banks, operating a very traditional business model, one that has largely shielded them from the problems of the international financial turmoil of these last years. They take deposits from (mainly) small local savers and make loans to (mainly) small or medium-sized local businesses and help people buy their houses by providing mortgages. Their officers, like those of the cooperative banks elsewhere, belong to the community in which they operate and generally know their customers and the local environment. In addition, one of them is involved in the European Investment Fund's Jeremie programme, a programme designed specifically to help small and medium sized enterprises. The bank in question has committed over EUR 5 million over a period of three years to some 280 local SME beneficiaries under the programme.

Indeed, one could say that it is mainly in their ownership structure that the local commercial banks, which are joint stock (or "shareholder value") banks, differ from cooperative banks. In all other respects they are not very different. So that leaves us with the question: is there or is there not scope for setting up a cooperative bank in Malta? Is there or isn't there space for such an institution? Or is the local market too small, while our community is being adequately served by the banks already operating here?

I think it is not for me to answer these questions. But the point has been made, and I think it is a valid point, that competition – so necessary to ensure that customers get the best possible service at the least possible price – depends more heavily on the variety of business models rather than on having a large number of institutions giving roughly the same kind of services in more-or-less the same way. Increased competition does not result from just adding more firms with the same business model, but also, indeed perhaps more, by adding firms with different business models. Where there is more diversity, and where there are more alternatives to choose from, competition is enhanced and its benefits increased.

Perhaps I should point out that several decades ago there were many people, including many of the local business community, who were afraid to approach a bank for a loan. They were prepared to give and receive credit directly to and from each other, believing they were neither charging nor being charged interest, but not to borrow from a bank that explicitly charged interest and made a profit "at their expense". Never mind that the implicit rate of interest in the credit being given and received in this way was probably higher than that being charged by the banks. I should not be at all surprised if there were still people around, potential entrepreneurs, who still reasoned that way, and who therefore may be "financially

excluded” from the economy. Might this perhaps be a niche which a cooperative bank, setting up shop here, might be able to exploit?

Furthermore, I think that perhaps I should modify an observation I made earlier: namely, that the need to set up a cooperative bank in Malta has never so far been felt. On second thoughts, perhaps, this is not entirely true. For one of our smaller banks, one that, not surprisingly, was founded by a Jesuit priest in 1910, actually did begin life as a cooperative society. It was originally called the Lega dell' Apostolato della Pregariera, and its main aims were the setting up of a number of initiatives, all with an underlying social purpose. These included: a savings bank, intended to instil habits of thrift among the working classes; a mutual benefit society; a printing press; the publication of a Maltese language periodical; an evening school for the teaching of languages, music and crafts; an emigration bureau to help Maltese citizens wishing to settle in other countries; schemes for the free provision of food, medicines and medical care to the needy; a public lotto office; and a recreational club for members. It – or at least the savings bank part of its operations – only became a private limited company as recently as 1970, just before Malta's first Banking Act was enacted. And this, perhaps, should give us a clue as to why we do not have a Maltese cooperative bank today. Perhaps it is not because there is no scope for one, because there is no niche to be exploited, but because our legislative framework, as it has evolved so far, doesn't permit it!

For the truth of the matter is that while we have laws governing banking activities and a law governing cooperatives in Malta, we do not have laws governing cooperative banks! In our current legislative framework, the latter seem to fall between two stools. Our Banking Act envisages only joint stock banks, that is banks whose customers are not their owners, while the law governing cooperative societies in Malta, though it provides for the establishment of a fund into which all registered cooperatives are obliged to deposit 5% of their annual operating surplus to help pay for research and the education and training of their members and the general development of the cooperative movement, does not provide for the establishment of cooperative banks – that is institutions that are licensed to accept deposits and make loans. Clearly, for such a bank, or banks, to be able to be established here, either our Banking Act, or the law governing Cooperative Societies, or both, will have to be amended. But this is precisely what Minister Azzopardi said he has proposed to do in his introductory speech: to amend the relevant legislation. Then, once the amendments being proposed by the Minister come into force, we will be in a better position to judge whether or not there is scope for setting up a cooperative bank in Malta.