EACB Webinar:

8TH CONVENTION ON **CO-OPERATIVE BANKING**

Co-operative banks: A new deal for more solidarity

Tuesday, 27th October 2020

Co-operative Banks' Policy Messages

Identity card

- Co-operative banks account for about 20% of the market share of EU banks deposits and loans and so are a major player in EU banking sector. They are a main lender to Europeans SMEs and consumers and their presence is especially relevant in less urbanized areas.
- Co-operative banks are private institutions. They are owned by their members, who are also their customers, e.g. local entrepreneurs, craftsmen, farmers and households. They facilitate the channeling of funds to support local investment and development and are an anchor to prudential and financial stability and economic resilience.
- The co-operative banks' form of enterprise is enshrined in the European Treaties and is reflected in the Statute for a European Co-operative Society.
- Evidence(*) shows that co-operative banks business model are by nature long term oriented than other banks as they have :
  - ⇒ A stable deposit and customer basis;
  - ⇒ High core capital and restricted conditions for profit distribution;
  - ⇒ A conservative risk policy because maximisation of profits is not their goal but member/customer surplus;
  - ⇒ A democratic governance based on the principle of 'one person – one vote'. Diversity brought through member ownership entails a consensus -driven approach and prevents block holder in the decision process.
- Thanks to the above characteristics, co-operative banks have provided a liquidity and stability anchor to the market and in particular to SMEs throughout the Covid-19 crisis.
- Their key values are: trust between the bank and its members/clients; democratic and prudent governance; resilience to adverse market developments; close proximity to customers; social commitment; solidarity and reliance on joint liability systems.
- Co-operative Banks actively support the sustainable development of their local ecosystems by re-investing a large portion of profits back into the community. Moreover, Co-operative banks are one of the main employer for the benefit of the local economy . Finally they contribute to social welfare and take care of the impact of the climate change by taking the lead as credit provider to SME's and households
- Co-operative banks are resolutely determined to continue being a driving force for economic and societal resilience. For that purpose we would like to put forward the **following**

Views & expectations

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- **The members of EACB appreciate the actions undertaken by regulators and supervisors since the inception of the Covid-19 crisis** in order to alleviate requirements and ease processes to allow banks to focus on supporting customers and credit flow to the economy. This instance has shown that policy design should be mindful of possible procyclical effects during times of crisis and that embedding flexibility in the regulatory framework is a necessity. A pragmatic approach should also be maintained going forward, especially since the crisis will reverberate its consequences possibly for years with impacts on the amount of non-performing loans and on banks' capital requirements as well as on human resources. Regulatory requirements should be a mean to ensure financial stability not an end in itself for lawmakers and supervisors.

- **Co-operative banks have continued to support their customers and their local economies also thanks to the solidity of their solidarity mechanisms.** As companies devoted to the promotion of the economic situation of their members they consider it essential to support their customers especially in these times.

- The crisis has shown an increased use by supervisors of soft law tools, in particular Guidelines and Recommendations, as they can be adopted more swiftly than other regulatory tools. While this can have its merits, we also warn against the risks of such a tendency. Legislative mandate and democratic scrutiny should retain their primary role and authorities should not exceed the powers received from the European regulation. Also, the **cooperative specificities should be better taken into consideration as they are a factor of financial resilience.** In this vein we note that the restrictions to distributions of dividends recommended in the EU without consideration of individual profiles of institutions is excessive and risks hurting EU banks on international markets. The guidelines on Loan origination also add several obligations without a sound legal basis or are even in contradiction with the existing EU level 1 regulation and cooperative organisation. We wish that the revision of the guidelines on internal governance and fit and proper will not do the same.

- **We highlight the need for regulatory stability**. Institutions need to mobilize their resources on the financing of the economic continuity and recovery. The frequent revisions of directives and soft law by the different EU legislators and ESA's with their own requirements are extremely burdensome and require significant challenges from an operational and financial point of view with questionable results.

- **Mutual guarantee and institutional protection mechanisms among co-operative banks act as helping stabilising buffers for the sector in these times and lead to enhanced solidarity among co-operative banks.** The presence of such mechanisms should always be duly considered when reflecting on new policy in both the supervisory and in the resolution frameworks and applying existing requirements.

- **We believe that the implementation in the EU of the remaining set of Basel III reforms (aka Basel IV) should be reassessed in light of the new economic and social situation emerging from the Covid-19 crisis.** Regulatory and supervisory compliance remains very costly and burdensome, also given the many new workstreams activated at multiple levels. Covid-19 will inevitably result in an increase in credit risk in bank portfolios and higher risk weighted assets and capital requirements due to worsening credit quality of a broad range of debtors (retail as well as corporates). The expected comprehensive changes to capital requirements, the NPL backstop and IFRS 9, will affect not only banks, but

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also economies as a whole if we disregard the crisis-induced changes to the economic parameters with a serious risk of strong pro-cyclical effects. A significant increase of capital requirements will have adverse effects especially since EU banks will also have to rebuild their capital buffers due to Covid-19 in a low interest rate environment. We fear that this will seriously hamper a quick and sustainable recovery, and see the risk of undermining the resilience of the financial sector.

- We acknowledge that the pro-cyclical effect of many regulations adopted during the last decade have been in certain respects temporarily adjusted in the quick fix. We however see a need for a permanent solution which also works in an economic slump or even a crisis.

- **Co-operative banks have a key role to play at local level to accompany the green and social transition.** The recovery will pass via the financing of the transition of our economies towards a more sustainable paradigm. In this context, the integration of climate and environmental considerations in the risk management practices of banks should be pursued in a pragmatic and phased manner, avoiding sudden cliff effects on the way customers are treated and processes organised within the banks. **The focus should be on increasing the number of sustainable projects available for financing, to foster the transition of the European economy to a green future, but also avoid any disruptive effects or scenarios.**

- **We welcome the expected launch of the New Sustainable Finance Strategy**, but advise to make the new action plan workable as we are still implementing the previous one. There is a need to ensure coherence of measures both in terms of content and timeline.

- One big obstacle to the full implementation of the current action plan - that should be addressed if the EU wants to unleash the full potential of the Sustainable Finance Framework - is the lack in ESG data. Co-operative banks are mostly relying on clients' data to be able to report according to the new obligations stemming from the Taxonomy Regulation, the Sustainable Finance Disclosure Regulatio (SFDR), the possible revision of the Non-financial Reporting Directive (NFRD) and the CRR/ ESG chapter. Most of our clients are SMEs who will face challenges in reporting taxonomy aligned data at a first stage. **We believe that the revision of the NFRD and the creation of a centralised EU ESG data register would be extremely important to fill the companies' data gap.** The central data register should also collect governmental and EU environmental data already available at macroeconomic level in order to foster better assessment of physical, transtion risks and sector wide datapoints.

- **The EACB supports the new work on EU Standards for non-financial reporting.** The EACB is in favour of a standard for non-financial information that should have both a set of limited common indicators and sector specific elements. Altghough EACB Members indicated that these standards shall be based on existing standards (GRI,TCFD, , IIRF), they note that existing disclosure frameworks, whether at EU level with the NFRD or at global level all predate, by definition, the sustainable finance action plan and the EU Green Deal. Thus an alignement with the Technical Screening Criteria of the EU taxonomy is necessary. Moreover we believe that the full NFRD framework should remain to be applied to the largest and publicly listed companies, with the possibility to develop a very differentiated and simplified framework for SMEs and a less complex standard for smaller banks as Public Interest Entities (PIEs). **Inclusiveness, pluralism,**

practicability and transparency shall be at the core of the governance of the non financial reporting standard setter.

- **Europe's co-operative banks are supportive of this Commission's objective to make "Europe fit for the digital age" and strive for technological sovereignty.** The opportunities offered by technologies such as artificial intelligence, block chain and the increased computing power that has become available are plentiful. As a sector that has been among the first to automate its practices and that holds a wealth of customer data, cooperative banks clearly see the advantages they offer. But they are very prudent in using them having in mind their duty to protect not only their customers funds but also their data in line with Europe's General Data Protection Regulation. With this in mind, the EACB welcomes the different work items on the Commission's work plan in this context, notably for developing an ethical framework for the use of Artificial Intelligence and for a framework for operational and cyber resilience in the financial sector. On the topic of digital finance, open banking and retail payments, on which the Commission has released its strategies, EACB members note with interest that the Commission is starting to look at the prudential and financial stability implications of certain developments in this area. Additionally, it calls upon the Commission to firmly uphold the level playing field principles between different market players in the digital finance domain and the functions they perform and to carefully consider the pro' s and con's of using regulatory tools over market driven solutions to address these at times rather technical issues.

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(*) Tilburg University Report, European co-operative banks in 2019: a concise assessment, 2020.

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