

## European co-operative banks in 2016: a concise assessment

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*This research letter reports the performance of 17 co-operative banking groups in 12 European countries based on consolidated financial indicators pertaining to 2016.<sup>2</sup> It aims to provide policy makers, regulators and scholars with an aggregated overview of this specific sector. Collectively, these groups extended their member base by 1.6 million people and gained market share in domestic retail banking. In 2016, according to key financial metrics, co-operative banks performed differently compared to all other banks. On average, co-operative banks supplied the real economy with more new loans, improved their capitalisation and realised a higher return on their capital and reserves. Their efficiency levels deteriorated to a somewhat larger degree.*

### Background

In many respects, co-operative banks deviate from banks with other organisational structures. For instance, they do not have external shareholders. Customers of local banks can become members of the co-operative and can play an active role in the governance at the local and/or central level. Co-operative banks are characterised by a dispersed ownership and they build their equity base primarily via retained earnings. Nowadays, a customer is not obliged to become a member if he or she applies for a loan at a co-operative bank. Most co-operative banks also serve large numbers of non-members.

In this document, we concentrate on financial performance, but we acknowledge that both financial and non-financial indicators should be taken into consideration when assessing the performance of banks. This remark is particularly relevant for co-operative banks that are not just focusing on the bottom line. They also aim at social goals, e.g. contributing to a sustainable development of local communities.

Data for individual co-operative banks are taken from public sources or are compiled upon request by some banks. Simultaneously, identical indicators were gathered or constructed from various renowned data bases for national banking systems in which these co-operative banks operate. This way, the consolidated performance of co-operative banks can be put into perspective, and moreover, it can be compared to that of entire banking systems. For the non-euro countries in the sample, all figures were converted into euro at the exchange rate prevailing at the statement date.

### Sustained growth of member base

Members constitute the legitimacy of co-operative banks. In 2016, co-operative banks welcomed around 1.6 million new members. Compared to 2015, the member base grew by more than 2 per cent to 81.2 million members. This percentage increase is identical to the long term average expansion of the number of memberships (see Figure 1 on page 2). In relative terms, one can observe an upward trend. The member-population ratio displays an almost continuous rise. This ratio climbed from 15.7 in 1997 to 19.5 in 2016. Surging number of members may be due to countless factors: financial benefits, immaterial advantages, affinity with the brand, satisfaction with products and services, social goals,

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<sup>2</sup> Financial Group of the German Volks- und Raiffeisenbanken (Germany), Austrian Volksbanken Group (Austria), Raiffeisenbanken Group (Austria), Federazione Italiana delle Banche di Credito Co-operativo-Casse Rurali ed Artigiane (Italy), Unión Nacional de Co-operativas de Crédito (Spain), Banco de Crédito Co-operativo (Spain), Federação Nacional das Caixas de Crédito Agrícola Mútuo (Portugal), Rabobank (The Netherlands), Banque Raiffeisen Luxembourg (Luxembourg), Raiffeisen Switzerland (Switzerland), Nykredit (Denmark), Crédit Agricole Group (France), Crédit Mutuel Group (France), BPCE (France), OP Financial Group (Finland), Building Societies (United Kingdom), BPS Group (Poland), and SGB Group (Poland).

co-operative donations, etcetera. In fact, it is all about the ‘perceived member value’ that members derive or experience from their membership.

The number of legally independent local and/or regional banks diminished by 5.3 per cent to 3,168 in 2016. This outcome accords with the longer term trend of consolidation in co-operative banking. It is largely triggered by the need to create efficiency gains and the simultaneous shift towards digitalization and virtualization of financial products and services. In line with the cuts in branch networks, headcount at co-

operative banks contracted by 1.4 per cent. However, the number of staff in the entire banking sector fell by 2 per cent. Co-operative banks seem to acknowledge that this trend poses challenges for maintaining a sufficient degree of member engagement, commitment and involvement and their ability to participate in local networks by employees.

### Strengthened domestic market positions

In 2016, co-operative banks solidified their market position. They gained approximately 0.2 and 0.4 percentage point loan and deposit market share, respectively (Table 1). The former is currently almost 0.7 percentage point higher than the market share deposits. Five years ago, both market shares were almost similar. Hence, the loan market share has increased steadily since 2011, whereas the deposit share hovered around 21.4 between 2012 - 2015. The rise in market shares is an important demonstration of trust in these financial institutions.

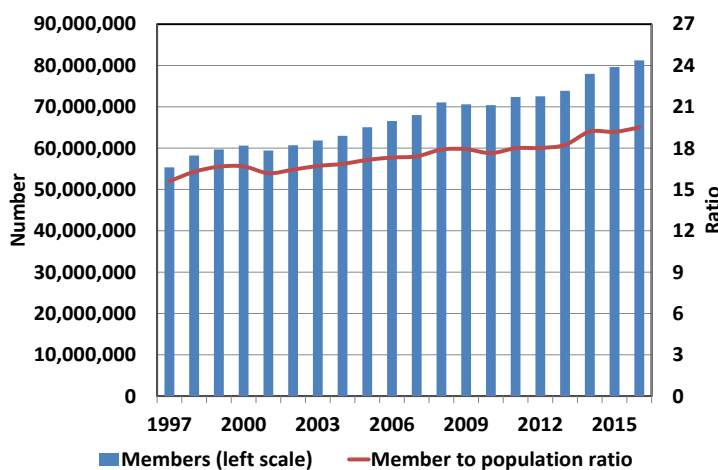
**Table 1 Average domestic market shares of co-operative banking groups**

	2011	2012	2013	2014	2015	2016	Change in percentage points (2011-2016)
Loans	21.2	21.5	21.9	22.1	22.2	22.5	+ 1.3
Deposits	20.9	21.3	21.5	21.4	21.4	21.8	+ 0.9
Branches	29.1	29.6	30.7	31.4	31.5	32.3	+ 3.1

Source: Own calculations based on data from co-operative banks, the ECB and national supervisory authorities.

The branch market share has always surpassed the loan and deposit market share. This reflects a distinct feature of co-operative banks: they operate with relatively dense branch networks and are physically close to their members. Furthermore, the share of branches owned by co-operative banks increased significantly in recent years. Their branch market share amounted to 32.3, which is more than 3 percentage points higher than in 2011. Co-operative banks closed 2 per cent of their bank offices in 2016, but all other banks cut back banking outlets by 5.5 per cent. Co-operative banks are increasingly shifting from physical to virtual distribution channels for their products and services. Hence, they invest heavily in IT technologies to offer their customers and members attractive and innovative products and services.

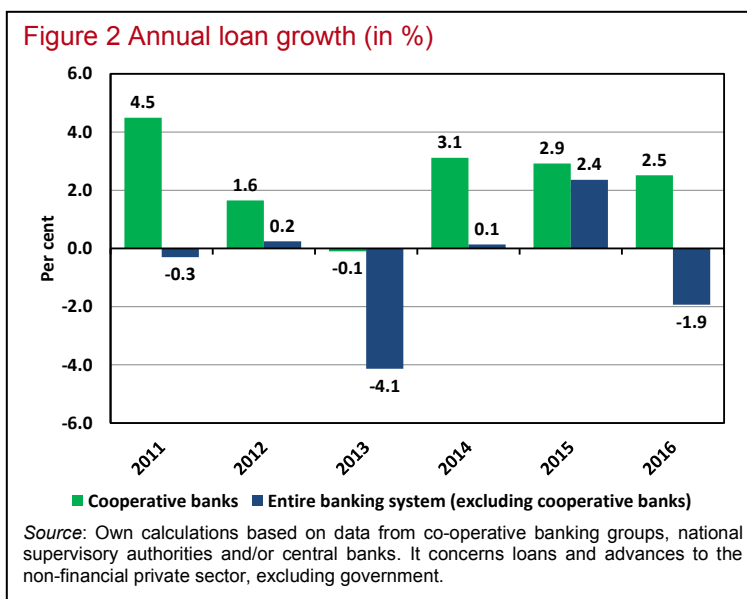
**Figure 1 Number of members and member to population ratio**



Source: Own calculations based on data from co-operative banking groups and national demographic statistics.

## Continued loan and deposit growth

The rising market shares are mirrored in dissimilar balance sheet developments between co-operative banks and all other banks in 2016. On balance, the former banks granted sizeable amounts of new loans to the non-financial private sector (+2.5%), while the loan portfolio of the entire banking system contracted by almost 2 per cent (Figure 2). It appears that both growth figures are suppressed by the fall of the British pound after the Brexit referendum in June 2016. When the British building societies and the collective U.K. banking sector are removed from the sample, the loan growth dispersion between co-



operative banks and all other banks remains significant. However, this gap narrows from around +4.4 percentage points (see Figure 2) to about +3.2 percentage points.

Statistically, lending behaviour by co-operative banks is more stable than that of the entire national banking system. Besides, credit expansion by co-operative banks outpaced loan growth of all other banks in the years reported in the Figure. Cumulatively, the loan volume at co-operative banks is more than 10 percentage points higher than in 2011, while the loan portfolio of other banks shrunk by more than 3 percentage points during this time span. This divergent development can probably be ascribed to differences in business models and strategic orientations stemming from their member-based governance.

For deposit growth, analogous conclusions can be drawn. In 2016, co-operative banks attracted a larger volume of new deposits (+2.4%) compared to all banking competitors (+0.9%). Faster deposit growth at co-operative banks has actually occurred ever since 2011, except for 2013 where deposit expansion was identical and fairly modest (just 1 per cent). The omission of U.K. figures does not alter the overall picture.

The described loan and deposit developments resulted in a small decline in the loan-to-deposit ratios. This ratio dropped to 0.96 for co-operative banks and 0.99 for all other banks. Just before the outbreak of the Financial Crisis, private savings covered around 80 percent of the private loan portfolio of the entire banking sector, whereas co-operative banks operated with a minor 'deposit gap' of 3 per cent. In a short time span, all other banks bridged their deposit gap by reducing short-term wholesale funding and restricting lending growth. They now make more use of stable deposit funding. This hints at a partial convergence of funding strategies of both types of banks, which may be partly enforced by new regulatory requirements in recent years.

## Enhanced resilience

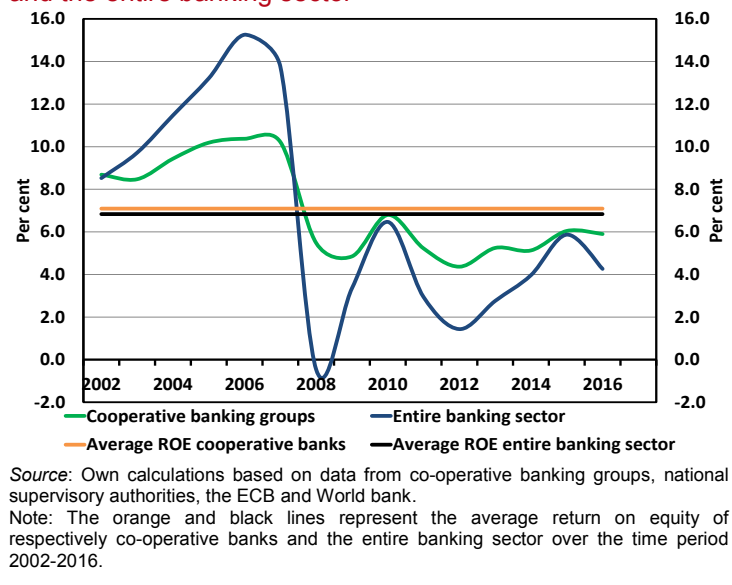
Co-operative banks boosted their capital ratios relatively fierce compared to other banks. The average Tier 1 ratio of co-operative banks rose by 1 percentage point to 15.5, whereas this ratio for the entire banking industry improved by 0.6 percentage point to 14.9. Since 2011, banking stability has clearly advanced as a consequence of stricter regulatory requirements and a cyclical upturn in the economy. Movements in capital ratios are caused by changes in the nominator, i.e. size of the capital buffers, and the denominator, i.e. volume of risk weighted assets (RWAs). Underlying data suggest that the tier 1 rise of all other banks was to a greater extent caused by a reduction of RWAs in comparison to the increase in the equity base. For co-operative banks, growth in capital and reserves seemed to

have exceeded the increase in RWAs. The latter observation suggests that co-operative banks are engaged in activities with moderate risks, as the continued growth of their loan portfolio has not led to proportionately higher RWAs. Implementation of the current proposals of Basel IV to raise the risk weights for mortgages and SME loans would, therefore, exert downward pressure on tier 1 ratios of co-operative banks.

### Stable return on equity

After a period of gradual convergence, the average return on equity (ROE) of both banking groups diverged again in 2016. The average ROE of co-operative banks ( $ROE_{COOP}$ ) remained at the same level as in 2015 (6%), while this indicator dropped from around 6 per cent to around 4.3 per cent for all other banks ( $ROE_{EBS}$ ; Figure 3). Within the context of a cyclical recovery and low interest environment, the increase in capital and reserves equalled the growth of net income at co-operative banks. For the entire banking system, the growth of net income lagged behind the rise in equity. Since the beginning of the Great Financial Crisis in 2008,  $ROE_{EBS}$  has been structurally lower than  $ROE_{COOP}$ . Over the entire depicted time span, the average  $ROE_{COOP}$  and  $ROE_{EBS}$  amounted to 7.1% and 6.8%, respectively. Finally, the volatility of  $ROE_{COOP}$  is much lower than that of  $ROE_{EBS}$ .

Figure 3 Return on Equity of co-operative banking groups and the entire banking sector



### Lower efficiency levels

The average cost-income ratios increased in 2016. The CI-ratio of co-operative banks went up by almost 3 percentage points to 64. All other banks experienced an increase in this indicator of 2 percentage points to 63. It is not easy to pinpoint the causes for the observed decline in efficiency levels, since this ratio is influenced by many factors. However, one can conclude that the ratios have hardly deviated from each other since 2012; both banking groups operate equally (in)efficient. The relatively dense branch networks of co-operative banks do not translate into a substantial higher CI-ratio.

Figure 4 Cost-income ratio of co-operative banking groups and the entire banking sector

