co-operative party

A PLAN FOR AN ALTERNATIVE FINANCIAL SERVICES SECTOR

OWNING THE FUTURE

CONTENTS

INTRODUCTION

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Our banks aren't working – at least not for the majority of us. The four largest banks that dominate high street banking have seen their share prices go up during this crisis,[1] and while they have stepped up to offer unprecedented lending and mortgage repayment holidays, they do so safe in the knowledge that the Government has stepped up further, underwriting their loans. The banks are able to profit while the taxpayer is taking on the risk with none of the reward.

Meanwhile, at least 1.7 million people don't have access to banking of any kind. Before this crisis, 40% of households had less than £100 in savings. Now, despite savings rates rocketing this trend is a deeply uneven one. The wealthiest 20% of UK households are set to have saved £23 billion thanks to reduced spending during lockdown, six times more than the savings made by the poorest.[2] So it's no surprise that the richest are saving more in the bank while lower-income households are relying on the limited savings they have while relying on often expensive debt as their only financial buffer.[3]

It isn't only individual consumers who are excluded by our banking system. The low volume of SME equity or debt finance over several years has left the bedrock of our economy vulnerable and ill prepared for crisis. With a toxic combination of banks reluctant to lend to SMEs and SMEs reluctant to borrow - only 1.7% of small firms sought new loans in the first half of 2017, down from 2.9% for the same period in 2012[4] - this is an issue in urgent need of new answers.

Alternatives already exist – for personal banking, credit unions and community development finance institutions (CDFIs) provide accessible and affordable banking, and building societies provide a service for their members rather than create wealth for external shareholders.

IT IS IN EVERYONE'S INTERESTS TO HAVE A SECTOR WHICH TACKLES RATHER THAN PERPETUATES INEQUALITIES

As we rebuild our economy after lockdown, our financial services require a rethink. It is in everyone's interests to have a sector which tackles rather than perpetuates inequalities – lower inequality means more sustained growth. And to achieve this, a more democratic, decentralised banking sector is needed. Member owned credit unions and building societies, clear responsibilities for banks to serve the public good, universal access to basic financial products and continued access to cash machines in high streets are all significant pieces of the puzzle.

A diverse banking system with many more players focused on different geographies, different sectors and different types of banking would be more supportive of the real economy, less at risk from the failure of any one institution and would likely be marked by less excessive remuneration.[5]

EQUALITY OF ACCESS TO BANKING

Covid-19 has widened the gap between those who bank online or use cards and phones to make contactless payments, and those who don't have access to even the most basic of financial products. This exacerbates other inequalities – financial tools can help you budget, access the cheapest energy tariffs or shop in places that do not feel safe accepting cash during a pandemic. They enable you to shop for groceries online if you are shielding or live too far from an affordable supermarket to make the journey.

To tackle inequality, there must also be equal access to the tools that enable you to engage in the economy – and that has to begin with a minimum level of access guaranteed for everyone, as well as the choice to be able to bank in person in a local branch or take cash out of the machine to spend.

Universal fair access

The issues of financial exclusion have been heightened during this crisis, and the greater focus on the challenges of a lack of access to basic financial products means we can have no excuse to turn a blind eye. Mutual aid groups and local councils, as well as many retailers, have found solutions for vulnerable customers stuck shielding at home so that volunteers can shop on their behalf,[6] and the Post Office has repurposed its foreign currency service to deliver cash to the homes of vulnerable customers. But it shouldn't be left to the goodwill of neighbours, and a principle of universal access along with the tools that make it a reality should be ensured.

Every adult, household and business should have access to at least a basic package of fair and affordable finance tools, including a basic transactional bank account; a savings scheme; access to affordable options for credit; physical access to branch banking facilities; insurance; and independent money management advice.

Duty to serve

The government should legislate to introduce a new 'duty to serve' that would force UK banks to demonstrate that they are serving individuals and SMEs from all backgrounds, as happens in the US under the Community Reinvestment Act. Financial institutions could also look to form a partnership with CDFIs operating in their region and commit to supporting and promoting their activities whenever possible. Data collected on this already by the Bank of England should be transparently available to enable this and create greater accountability.

Last bank in town

Bank closures accelerate the decline of highstreets, as well as leaving many customers without access to physical banking services. Whether it's local shops and businesses needing to cash up, or customers who are unable to unwilling to travel to distant conurbations, branch closures and the removal of free ATMs creates new and exacerbates existing inequalities and disadvantage.

For the 2.1 million people who still mainly use cash, many of whom don't have access to bank accounts, the use of cash must be maintained as long as it is needed. To ensure branches are not replaced by phone and internet banking only, new Access to Banking Standard should be introduced to protect the continued existence of the "last bank in town", supervised by the Financial Conduct Authority and penalised when banks fail to uphold that standard, with the funds from any fines spent on financial inclusion and development of credit unions. A review of ATM charges should take place, with a view to reforming them or abolishing charges altogether. ●

A MUTUALLY OWNED SECTOR

There is no market in greater need of reform than financial services. The Co operative Party believes we need a more diverse sector, to ensure a stable, resilient and inclusive financial system that serves us rather than the other way around.

Credit unions

The government should support the growth of the credit union movement – this was the case pre-coronavirus but even more of an urgent priority now. Credit Unions succeed in offering affordable, fair products in diverse sectors and communities. Their democratic member-owned structure means they put their people not their profits first, and everyone has a say and a stake in the system that looks after their money.

WE NEED A MORE DIVERSE SECTOR, TO ENSURE A STABLE, RESILIENT AND INCLUSIVE FINANCIAL SYSTEM

This can be kickstarted by ensuring that all public-sector employers establish payroll deduction facilities for credit unions. A credit union payroll deduction system should be a requirement for private organisations tendering for public contracts too. Funding and support should be made available for credit unions developing new products which will help cash-strapped households manage their finances more easily and avoid problem debts.

Regulatory changes, such as reforming the way capital rules for credit unions are set up, would further enable the sector to grow, and legislative reform of the Credit Unions Act is required to enable credit unions to deliver a full range of services to members.

Building societies

Building societies are a form of mutual finance, owned by their members and operating in their interest rather than for shareholders. During this crisis, building societies have stepped up to offer borrowers mortgage holidays, advice and support – but as much of their business is tied up with the housing market, lockdown has had a disproportionate impact on them. However, building societies are well placed and resilient enough to weather the storm and are preparing to restart lending now that the housing market is beginning to reopen.[7]

Even before this crisis, building societies have had a uniquely trusted position among British high street banks, and a track record of lending throughout the last financial crisis. Building societies and other financial mutuals have be shown to have taken fewer risks with their savers' money and been more resilient in the downturn, because they exist to provide a service for their members rather than to create wealth for external shareholders.

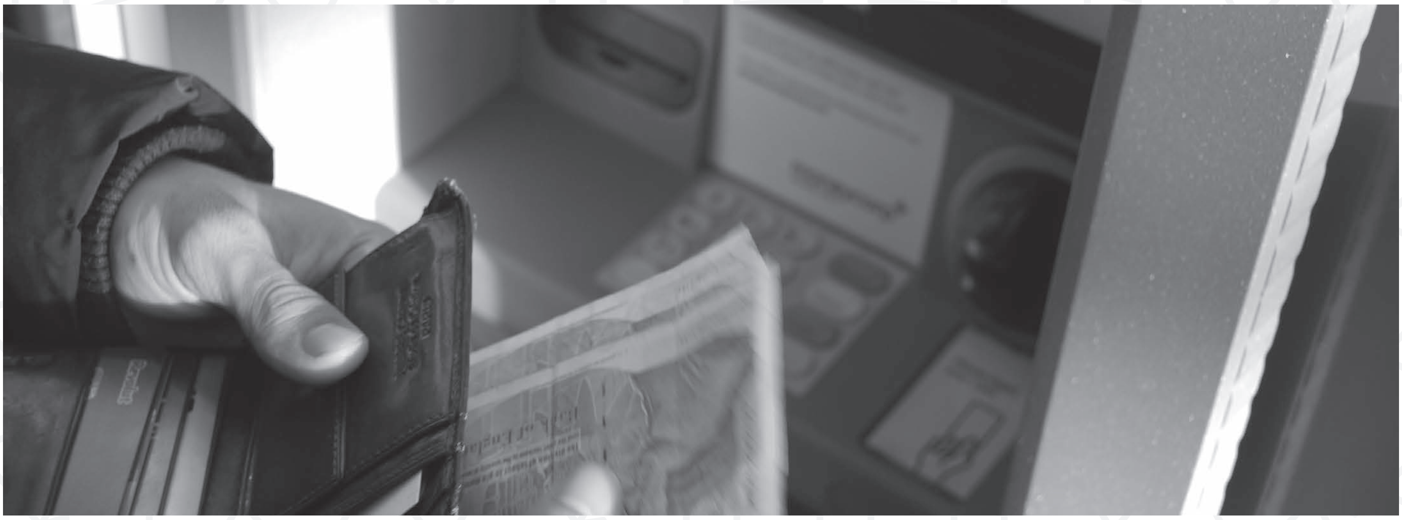
Much of the legislation governing building societies and other financial mutuals is old fashioned and in urgent need of reform. The government should modernise the Friendly Societies Act, which hasn't been reviewed since 1992. A better regulatory environment needs to be developed - one that facilitates the expansion of existing building societies as well as urgently reviewing the hurdles currently put down by government and regulators that have effectively meant no new building societies can be created.

The banking levy disproportionally hits the ability of building societies to lend and punishes them for the misdeeds of the PLC banking sector. As such, building societies should be excluded from this levy.

A regulatory refresh

Banking operates within a blunt regulatory framework that puts credit unions, building societies and other innovative banking models on the back foot. In an effort to increase competition in the financial sector, fintech start-ups have been given a degree of regulatory flexibility to enable them to innovate and grow. The same flexibility and support should be extended to proven mutual models of banking, like credit unions, and the wider co-operative banking sector to enable them to continue to grow and provide the competition desperately needed in Britain's broken financial market.

FROM CENTRALISED TO REGIONAL MODELS



Retail banking in the UK has changed – from what was once a diverse sector with a regional focus serving customers and local businesses, to one that is dominated by international and investor interests in pursuit of shareholder value, not public interest. The ownership and structure of banks has become more uniform too, with far fewer successful regional brands, smaller building societies or diverse forms. Alongside this trend, banks have gotten a bad rep, and fairly so. They have manipulated financial markets, mis-sold products, closed branches and hidden charges to make UK current accounts highly profitable.

For a resilient economy post-Covid, our banking sector needs to be reimagined. Rather than embracing and enabling the too-big-to-fail banks, seeking to curb the worst excesses of behaviour through regulation but retaining the same tired models, we should be looking to a different, decentralised and democratic way of organising the sector. A network of accountable regional banks with a stake in shaping sustainable local economies, better lending to SMEs and co-operatives as well as better access to basic banking services for local communities, and mutual ways of working that put people and place before profits.

Regional banks

Businesses that put money back into the local economy – through hiring local people, spending money in their region, and reinvesting profit instead of paying shareholder bonuses - are best placed to drive local economic growth. The UK's small and medium size enterprises employ over 24.3 million people across the UK, and the social and co operative sector has outperformed the rest of the economy in terms of growth since the financial crisis in 2008.

Despite the social, co operative and SME sectors' crucial role in our economy, they face a number of barriers to growth through difficulty in getting investment from high street lenders and a high cost of credit. And this lack of engagement from Britain's banks is hardly surprising - four of our five large banks are located within a five-square mile area of Central London.

Germany, on the other hand, has thousands of individual banks across the country, including over 400 local savings banks (Sparkassen), each independently and locally managed, as well as 1,000 co operative banks, owned by their members and run on the principle of one member one vote. The German regional banking system is run prudently, serving sub-regional areas and specialising in local SME investment. In fact, local and co operative banks have been able to continue high levels of local lending through the financial crash and beyond.

The government should work with city and local authorities to establish a network of regional mutual banks tasked with lending to co-operatives, social enterprises and small and medium sized businesses in their regions. These regional banks should be encouraged to take a co-operative form of ownership, ensuring that they are inclusive and helping them return benefits to their locality to reinforce local economic growth.

This could be funded by scrapping the Entrepreneur Tax Relief, an ineffective and unfair policy, and the £2.7 billion additional income a year as a result invested in measures which create a fairer economy – this could include a combination of creating a new co-operative investment bank and developing new regional mutual banks.

SME Lending

Mutual methods of working for SMEs across

Europe ensures that there is another avenue for attracting investment. Mutual Guarantee Societies (MGSs), which have several forms and legal underpinning, allow up to 9% of all European SMEs to work together, pay in to a MGS and more easily access banking lending.

The UK just has the one MGS – the British Business Bank – which does not allow British SMEs to be as competitive and as well placed to innovate as their European counterparts. To give the UK's SMEs the best possible support to survive this crisis, the appropriate regulatory guidance to allow MGSs to form should be updated.

Repurposing toxic debt

There have been calls for a new coronavirus toxic debt body to save the UK's small businesses.[8] The Treasury is reviewing a proposal that would see a government-owned body to manage government-backed debt given to many small businesses through this crisis.[9] It is clear that the £31.7 billion debts taken on by more than a million businesses with a 100% government guarantee, and the further £11.85 billion borrowed with 80% government guarantee will include some who will struggle to repay, and there is a challenge as to how this is managed in a way which does not cause further harm to the economy.

In a previous chapter, 'A Plan for Employee Ownership and Job Retention', our CBILs write off plan sees businesses who transfer ownership to employees having some or all of their loans written off. However, for some businesses, especially co-operatives who are already owned by their members, this won't be possible, or they simply need more time or flexibility in the way that they repay. Where these options involve equity, preferred shares schemes or profit participating debt, the design of any scheme must take into account the unique ownership structure of co-operatives and ensure products are appropriate, or that there is an equal alternative that the sector can access.

In addition, any government body which owns shares or participates in profits from companies should be accountable and transparent, with elected board members who can direct how any profit is reinvested into fair economic growth in the communities that need it most. Democratic participation provides a buffer against future privatisation – ensuring we learn the mistakes from past crises which saw the taxpayer take on all the risk of failing banks and then losing out on the profit when they were sold off cheap to private investors, and from the Green Investment Bank, a profitable government body which was privatised.

ENDNOTES

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