

The Contribution of the Credit Union Movement to the Development of Barbados.

**Access to Financial Services
For All**

Fundamental Economic Problem

- At any point in time, some Individuals, households, firms, organizations, governments experience a mismatch between:
 - Desired Expenditure
 - Income + Wealth

Fundamental Economic Problem

- Desired Expenditure = Income + Wealth
BALANCED BUDGET UNIT
- Desired Expenditure > Income + Wealth
DEFICIT BUDGET UNIT
- Desired Expenditure < Income + Wealth
SURPLUS BUDGET UNIT

Fundamental Economic Problem

- A central function of the financial system is to facilitate the movement of funds between Deficit and Surplus Budget Units.
- This movement of funds delinks expenditure from income + wealth, which plays a major role in spurring economic growth and development, and general societal wellbeing.



Fundamental Economic Problem

- What if individuals, households, businesses, organizations and governments were forced to be Balanced Budget Units?
- Financial markets are therefore critical to economic growth and development.

What Is The Role Of Financial Institutions

- Are Financial intermediaries like Credit Unions essential to the process of transferring funds from Deficit to Surplus Budget Units?
- Why not Direct Finance?

Why Financial Institutions?

- Depositor = \$10,000: Earns 0.5%
- Intermediary Accepts Deposit/ Makes loan of \$8,000.
- Household: Borrows \$8,000 at 5.15%

Why Financial Intermediaries?

Financial Market Frictions:

Search Costs;

- Maturity Matching;
- Denomination Matching;

Challenges In Financial Markets

- Imperfect / Asymmetric information
- Adverse Selection (Hidden Information)
- Moral Hazard (Hidden action)

Why Financial Intermediaries?

- Financial intermediaries in theory are an optimal solution to various financial market frictions.
- If these financial market frictions are not satisfactorily solved then the transfer of funds from surplus to deficit units is less than optimal, there is financial exclusion, and economic growth and development is retarded.

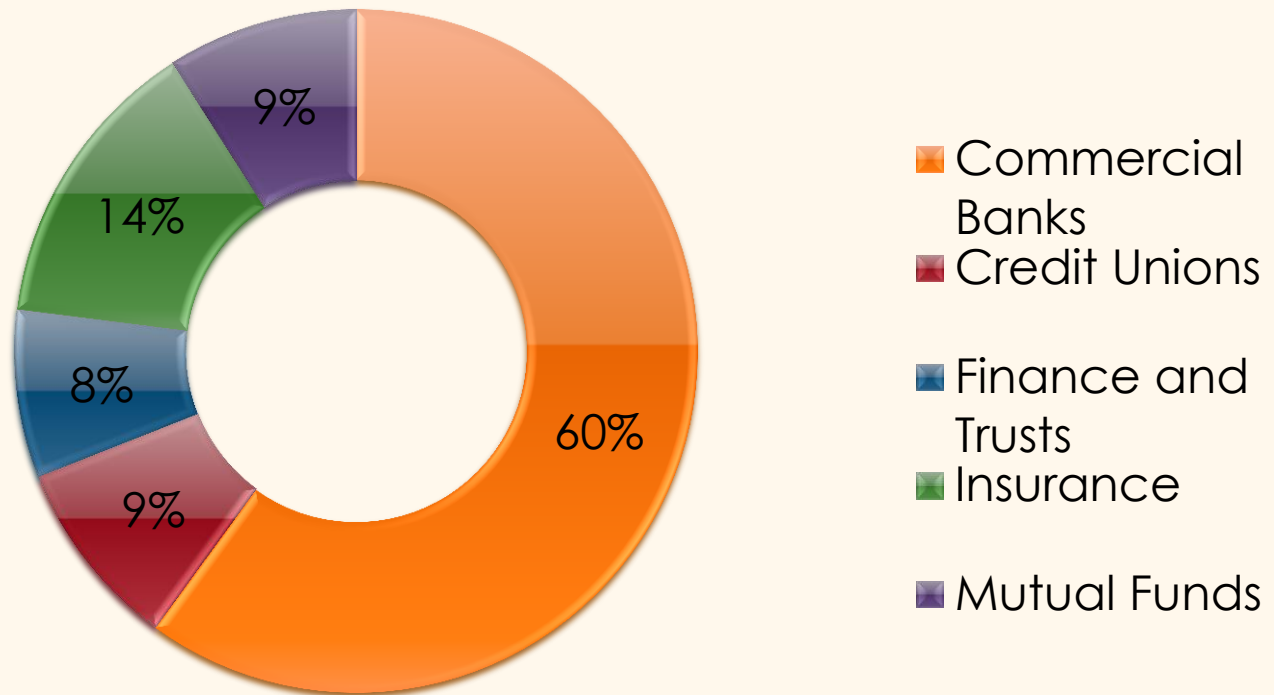
Financial Inclusion

- The World Bank Group considers financial inclusion a key enabler to reduce extreme poverty and boost shared poverty, and has put forward an ambitious global goal to reach Universal Financial Access by 2020.

Barbados Context

- For a variety of reasons (largely historical), the commercial banking sector in Barbados has been dominated by large international/regional banks.
- (The Barbados National Bank and Barbados Development Bank being important exceptions)

Structure of the Financial System 2016



Dominance of Large International /Regional Banks

- Large international/regional banks are complex organizations engaged in a wide range of activities. They provide a variety of services to their customers, but often rely on hard financial information, computer models and centralized decision making as the basis for conducting business,

Dominance of Large International /Regional Banks

- Large, international banks typically have a comparative advantage in more impersonal, transactions-based services, due to their size and access to technology (Berger and Udell).

Dominance of Large International /Regional Banks

- The local decisions of large, international banks are also influenced by standards, targets and other benchmarks set at regional and/or international headquarters.



Dominance of Large International /Regional Banks

- The presence and dominance of these large international/regional players has served Barbados extremely well in many respects.

Development of Financial Institutions

- Barbados emerges from most global financial benchmarking exercises with a relatively positive picture of its level of financial development.
- In terms of depth, access, efficiency and stability, financial institutions in Barbados are on par with Middle Income countries across the globe, and Barbados is a leader in Latin America and the Caribbean.

Table 1. Financial Institutions Depth

BARBADOS	1956-1965	1966-1975	1976-1985	1986-1995	1996-2005	2006-2015
Domestic credit provided by financial sector (% of GDP)	12.4%	35.8%	42.36	50.55	70.27	98.04
Domestic credit to private sector (% of GDP)		26.5%	2.33	36.47	53.79	76.20
Domestic credit to private sector by banks (% of GDP)		26.5%	32.33	36.47	53.50	75.96

Source: Global Financial Development Database

Table 3: Financial Institutions Access

Barbados	1986-1995	1996-2005	2006-2015
Automated teller machines (ATMs) (per 100,000 adults)	29.8	30.1	35.70
Commercial bank branches (per 100,000 adults)	19.26	18.25	19.46
% Of Firms with line of credit	42.0%	68.5%	78.8%
% Of Small Firms with Line of Credit	12.8%	35.1%	36.0%

Source: Global Financial Access Database

Table 5. Financial Institutions Efficiency

Barbados	1956-1965	1966-1975	1976-1985	1986-1995	1996-2005	2006-2015
Deposit interest rate (%)		5.94	6.63	5.03	3.84	3.13
Lending interest rate (%)		10.64	11.74	10.25	9.33	9.15
Interest rate spread (lending rate minus deposit rate, %)		4.70	4.84	5.23	5.49	6.02
Real interest rate (%)		5.56	4.22	5.83	6.02	8.38
Risk premium on lending (lending rate minus treasury bill rate, %)		3.25	3.21	3.56	5.36	5.23

Source: Global Financial Development Database

Table 9. Development of Financial Institutions

	High Income	Middle Income	Latin America & Caribbean	Barbados
Depth	148.40	98.46	54.53	80.41
Access	90.63	53.12	38.60	87.56
Efficiency	3.96	6.87	7.13	6.74
Stability	7.68	10.49	10.12	18.5

Source: Global Financial Development Database

Dominance of Large International /Regional Banks

- However, some customers (small businesses, farmers ,depositors of low to moderate wealth) require information – intensive and relationship-based and financial services, .
- International/Regional standards, targets and benchmarks may conflict with local needs.

Dominance of Large International /Regional Banks

- In a financial system dominated by large international or regional banks customers requiring relationship-based, and information-intensive financial services may be under-served.
- Customers whose needs are shaped by special features of the local market may also be underserved, if serving these needs conflict with international benchmarks.

Contribution of Credit Unions

- I want to suggest that one of the key contributions of Credit Unions to the development of Barbados is that they have filled a gap in the financial system by providing relationship-based, information-intensive financial services and meeting the needs of customers whose needs are shaped by special features of the local market.

Contribution of Credit Unions

- I also want to suggest that in Barbados, Credit unions perform the traditional role of a Credit Union, but also take on many of the functions of so called “community banks.”
- Community banks are banks that serve a limited geographical area, and are not part of a regional, national or international network.

Contribution of Credit Unions

- The available academic evidence suggests that credit unions and community based banks take into account a wide variety of factors in reviewing applications for small business loans, including the character of the borrower and special features of the local environment.

Contribution of Credit Unions

- Loan officers at large, geographically dispersed banking organizations are usually not given so much autonomy in making small business loans because it is not feasible for top managers of such organizations to review every small loan decision.

Contribution of Credit Unions

- Instead, these organizations often prefer to rely on credit scoring models – statistical models that predict a borrower's probability of repayment based on such objective characteristics such as personal wealth and past credit history (Cole, Berger et al 2002).

Contribution of Credit Unions

- While such an approach to lending may improve the flow of credit to some small businesses – those owners with substantial personal assets and long credit histories- it may also result in other creditworthy small businesses being turned down for credit.
- In Barbados Credit Unions fill a gap in the financial system by serving those without substantial personal assets or long credit histories.

Contribution of Credit Unions

- Loans to small businesses with little credit history or collateral may require the lender to carefully monitor the borrower over the course of the loan.
- To cover the fixed cost of investigating such loan applicants, the lender may also need to maintain a long term relationship with the borrower.

Contribution of Credit Unions

- Large, international banks may be reluctant to engage in such relationship-based lending because they have a comparative advantage in more impersonal, transactions-based services and because it is inefficient to provide both kinds of services (Berger and Udell).
- Credit Unions often fill this gap in the financial system in Barbados.

Contribution of Credit Unions

- Some analysts argue that credit unions and community banks are more interested than large banking organizations in providing personal service to depositors of low to moderate wealth.

Contribution of Credit Unions

- One possible reason for this difference in focus is that credit unions and community banks depend more heavily on retail deposits for their funds than large banks.

Contribution of Credit Unions

- Another possible reason is that large banks often prefer specializing in impersonal, transaction based deposit services, where they tend to enjoy a comparative advantage over credit unions and community banks due to their size and access to technology. (Hannan, Hannan and Prager)

Contribution of Credit Unions

- The central argument here is that in Barbados, credit unions play a crucial role in the economy as providers of relationship –based financial services, which is extremely important to customers without extensive credit histories and low to medium personal wealth.

Contribution of Credit Unions

- Credit unions are also extremely important to small depositors who place a premium on personal service.

Contribution of Credit Unions

- As such Credit Unions have been the critical linchpin in making Barbados a Financially Inclusive Society.
- We take this financial inclusion for granted, but it remains a major challenge around the world.



Financial Inclusion

- Financial inclusion means that individuals, businesses and Civil Society Organizations have access to useful and affordable financial services that meet their needs – transactions, payments, credit and insurance - delivered in a responsible and sustainable way.



Financial Inclusion

- While there has been progress around the world toward financial inclusion, significant challenges remain:
- An estimated 2 billion adults worldwide, or 56% of adults, do not have a basic account. Our research suggests that less than 5% of adults in Barbados do not have a basic account.

Financial Inclusion

- According to the World Bank, more than 200 million formal and informal micro, small and medium-sized enterprises in developing economies lack adequate financing to thrive and grow

Emerging Issues and Conclusion

- Digital Currencies;
- Fintech;
- De-Risking

Digital Currencies

- Bitt, is a FinTech company built around the twin pillars of global connection and financial inclusion. Bitt offers unprecedented solutions to disruptive regional issues from remittance payments to providing much-needed access to e-commerce solutions.
- With a significant multi million dollar injection from Overstock.com, BITT and its potential has been recognised by global partners. In February 2016, Bitt broke new ground by launching a digitised version of the Barbados dollar. The first ever global example of a digitised fiat currency being approved and embraced by a central bank.

FinTech

- Digital Financial Technology, or “Fintech” and particularly the global spread of mobile phones, has facilitated expanded access to many persons and small businesses at low cost and risk:

Fintech

- Digital IDs make it easier than ever to open an account;
- Digitization of cash payments is introducing more people to transaction accounts;
- Mobile-based financial services bring convenient access regardless of location.
- Greater availability of customer data allows providers to design financial products that meet the needs of users.

De-risking and the rise of Indigenous Banks?

- International regulators have been imposing more stringent anti-money laundering/countering financing of terrorism (AML/CFT) compliance requirements on correspondent banks, such as know your customers' customer (KYCC), and stiffer AML/CFT related fines.

De-risking and the rise of Indigenous Banks?

- In 2012, HSBC and Standard Chartered were fined US\$1.9 billion and US\$340 million respectively for AML failures. More recently, Standard Chartered was fined an additional US\$300 million for sanction violations, while Wells Fargo was fined US\$1.5 million for AML breaches.

De-risking and the rise of Indigenous Banks?

- These increased costs and reputational risks have led to a growing number of global banks terminating their correspondent banking relationships with some customers, business lines, and jurisdictions in an effort to better balance economic benefits relative to their potential risk exposure. This practice is referred to as “de-risking”.

De-risking and the rise of Indigenous Banks?

- Will international banks ultimately abandon the Caribbean due to an undesirable Risk / Return relationship?
- Will this lead to a rise of indigenous banks, and / or a greater role for credit unions in the financial system of Barbados?

Conclusion

- Credit Unions need to maintain their focus on providing:
- Highly personalized services in a caring and responsible manner;
- Financial services for customers who require relationship-based and information-intensive financial services.
- Financial Services for customers whose needs are shaped by the vagaries of the local environment.

Conclusion

- Large international/regional banks make for a world class financial system. However, they tend to rely on hard financial information, computerized models and centralized decision making as the basis for conducting business.
- Their local decisions may also be influenced by targets, benchmarks and standards set at headquarters.

Conclusions

- Credit Unions fill a crucial gap in the financial system by focusing more on “relationship banking,” basing decisions more on personal knowledge of members’ creditworthiness and a keen understanding of and commitment to the communities they serve.
- As such they fill a gap in the financial system and are a useful complement to banks.



Thank You

Any questions