



ICA General Assembly

Resilience of the Co-operative Business Model in times of crisis

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The recent financial meltdown and ensuing economic crisis has shown the co-operative business model to be resilient, with great potential to sustain communities world wide. This outcome has generated new and welcome interest in the model.

“The financial and ensuing economic crisis has had negative impacts on the majority of enterprises; however, co-operative enterprises around the world are showing resilience to the crisis. Financial co-operatives remain financially sound; consumer co-operatives are reporting increased turnover; worker co-operatives are seeing growth as people choose the co-operative form of enterprise to respond to new economic realities. “

Co-operatives Thrive in Times of Crisis

Research has demonstrated that co-operative businesses last longer

- More than 6/10 co-ops last longer than 5 years compared to 4/10 privately-owned firms
- More than 4/10 co-ops last longer than 10 years compared to 2/10 privately owned firms

How are Co-operative Banks and Credit Unions Faring in the Current Crisis?

At the time of the release of our report (May 2009) they had experienced an increase in almost every facet of their business:

- Assets and deposits
- Volume of lending
- Membership
- Had a better rate of interest
- Greater stability (capital adequacy ratios, loan default rates)
- Few losses on investments (at “Central” levels only)
- Few had needed government help

Strategies to counteract the Crisis

- Refocusing of business – predict sell off of non-core activities
- Mergers to increase capital base
- Cost reductions
- Rediscovery of core values as member-owned businesses –making it part of business strategy

Why are Co-operatives Good in a Crisis?

“when former US Federal Reserve Chairman Alan Greenspan went before Congress in October 2008, he told American lawmakers that the economic meltdown had revealed a “flaw in the model” that he had not expected – that banks operating in self interest would not self-regulate to protect their shareholders and institutions”

Why are Co-operatives Good in a Crisis?

• Member-Ownership

- Tend to be more risk averse
- Not driven by profits or shareholder interests
- Direct link of savings and loans acts as a moral constraint
- Losses at Central level not due to failure of governance –rated as low risk investments

• Method of Capitalization

- Funded through member deposits, not reliant on capital markets for funding
- Tend to retain profits and take fewer risks
- Higher capital reserve criteria
- Deposit guarantee schemes

• In comparison to banks, credit unions

- Have tended to not freeze credit
- Have lower increases in interest rates
- Are generally more stable due to different capitalization and lending practises

Update Since Publication of Resilience Report

Co-operatives have not been sheltered from the problems occurring globally but continue to be robust.

Credit unions and cooperative banks were not as severely impacted by financial crisis as compared to commercial banks but hit hard by “spillover” effects of unemployment, SME closures and defaults on loans and mortgages.

We see the close member-co-operative linkage—because members are struggling and in financial difficulty CU’s experience negative impacts in retail banking.

US credit union system continues to face challenges. The large wholesale credit unions (especially US Central FCU and WestCorp FCU) lost billions of dollars on the mortgage-backed securities and all CU’s had to contribute funds to replenish the deposit insurance (Rosenthal, 2009). Impact has been even worse for Community Development Credit Unions which serve low income communities. Many have experienced negative ROA, and have, or are considering, merging or liquidating (Rosenthal, 2009).

Through the end of September there have been 21 credit union failures in 2009 and National Credit Union Administration (NCUA) expects the number of troubled credit unions to increase for next few years into 2011 (Roberts, 2009).

The number of failures is still comparatively less than those of banks which have reached around 120 (of approximately 8,100) this year (Stock, 2009).

US CU’s outperformed banks in 2008 in new mortgages and loans and increases in deposits. Membership in CU’s continues to increase. “In the 12 months ended in June, 1.6 million Americans joined a credit union, boosting the industry’s assets by 8.2%, according to the Credit Union National Association (Stock, 2009).

Large credit rating agencies have shown confidence in mutual insurers. Moody’s Investor Services reported that mutual insurers have weathered the economic crisis better than publicly traded life insurance company’s. In fact, only mutual life insurers have been give the highest triple a rating. Mutuals achieved higher ratings because:

- Stronger capitalization
- Less risky business focus and products
- Less headline risk
- Less dependence on capital markets
- Greater alignment of owners, creditors and policyholders (Kuykendall, 2009)

Canadian Credit Unions had strong first half of 2009. System assets, savings & deposits, and loans all recorded gains in first six months. Five of ten provincial systems reported double-digit gains in deposits and savings over same period (Credit Union Central of Canada, 2009).

The Asian Confederation of Credit Unions (ACCU) reported that the majority of Asian Credit Unions have avoided the worst effects of the crisis. "Credit union assets have grown by 2 percent since the crisis". (CCA, 2009).

Thailand: Also see that small business owners turning to credit unions for credit (Jakarta Post, 2009).

The financial crisis appears to have raised the interest in co-ops internationally, particularly among governments. In 2008 and 2009:

- Department of Trade and Industry in South Africa encouraging unemployed to start worker co-ops
- Trade Minister of Uganda is encouraging people to use co-operatives in the recovery of the economy
- Government of the Philippines also acknowledge the importance of co-ops during economic crisis
- Malaysia looking to increase number of co-ops
- Singapore Minister of Community Development, Youth and Sports said that co-operative movement had been able to retain its workforce and even expand in some cases, while many businesses had been forced to downsize

But one thing to acknowledge but another thing to create environment for co-operative development. Also occurring:

- South Africa creating a Co-operative Bank Act which will encourage co-operatives to develop co-operative banks
- Philippines amended the Co-operative Act in 2008 which has introduced more favourable taxation for co-ops

New financial environment will be a good fit with the credit union system (Rabobank, 2009 and Rosenthal, 2009). Why? What is new for banking system has been integral part of how co-operative financial institutions (credit unions, co-operative banks, etc) have always done business.

There is going to be a push for (by governments, regulators and public):

- More transparency
- Less risk averse activities by banks
- Emphasis on customer/member based on relationship of integrity and trust
- Products designed for consumers
- More financial education for consumers
- New governance structure – elected board of directors
- Limited compensation for executives
- More emphasis on direct local control and doing banking locally (nationally)

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- Higher capitalization for larger banks (may hurt CU's depending on the regulations). In general cooperative financial institutions are well capitalized. In Europe, co-operative banks have not had to participate in government recapitalization plans for banks as CB's already had a strong solvency ratio (EACB, 2009). In US CU's have capitalization level of 10.8% compared to banks at 7.6%.

We may also expect that businesses in general will look to adapt some of these principles (insurance companies for example). The co-operative model in other sectors would be an example of how these principles can be integrated into a viable enterprise. With a shift in financial environment approaching, co-operatives will have to work harder at differentiating themselves from other banking institutions.

Considerations:

Co-operatives will still feel effects of the crisis, as unemployment levels remain high.

Rosenthal (2009) asks how can CU's insulate themselves from the financial system?

How will new regulations impact credit unions? Will CU's be differentiated from other banking institutions or be lumped in with everyone else?

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