

FIN(4)FW009  
Finance Wales Inquiry  
Response from Arian Cymru

ARIAN CYMRU - proposals for the final consultation and both parts of Dylan Jones Evans' 'Access to Finance' report for the Welsh Government.

Overview:

Prof Jones-Evans is to be highly commended for identifying the need for a new Bank in Wales. This then leaves us with the question as to what form this bank should take. We at Arian Cymru have consistently argued that what is necessary is a public Bank modelled on examples such as the sparkasse/landesbank system and KfW in Germany or the Bank of North Dakota in the USA, notwithstanding the IBFC.

To institute just another private entity simply creates the perpetuating model of the current extractive system in operation and will not be sufficiently or substantially different to the existing system needed to bring about real change. The facts drawn from around the globe is that a properly instituted public bank, with a sufficiently substantial deposit base could do much more than provide affordable finance to SME's, but could also provide an alternative to PFI's for a Welsh Government with borrowing powers - allowing infrastructure to be funded by self-liquidating loans from its own financial institution, in the same way that Germany is now funding a wholesale move to renewable energy.

We would recommend anyone interested in this idea to view the recording of Marc Armstrong's presentation on our website, from a recent Arian Cymru event [https://www.youtube.com/watch?v=NzhzK83P\\_QA](https://www.youtube.com/watch?v=NzhzK83P_QA) in which he explains the potential of such a system. Now is a time for boldness in our approach to the Welsh economy.

The example of the past five years of the virtual collapse of the existing extractive banking system needed to be propped up by the remainder of society is undeniable evidence that there is a need to do something substantially

different

To provide a concrete example of how a Welsh bank could work - for a Welsh public bank lending to a small business (where risk weighting is 100%) the bank would need to retain £10,000 for a loan of £100,000: thus providing a substantial source of liquidity to the Welsh economy through leveraging its deposit base for productive investment. Or, as another example, a £100,000,000 deposit base could leverage £1 billion pounds to the productive economy. This would also give a Welsh public bank an enormous advantage over a non-bank business lending scheme such as Finance Wales, which lacks these powers of credit creation and is also hampered by EU competition law from providing loans at a truly competitive market rate.

A public bank would, then, be able to utilise the power of money creation through credit issuance for economical improvement and benefit across society. This power over our society is currently in the hands of a very few private corporations who are able to make substantial profits through the levying of interest, as well as being granted the power to decide which sectors of the economy should be afforded liquidity. As detailed research shows the past thirty years has seen the direction of credit issuance move increasingly away from the real productive economy' towards speculative and bubble bursting banking system. With the single minded view of securing fast returns in order to generate profits for private shareholders and bonuses for bank employees at the expense of the remainder of society- with much of this non-productive profit ending up in offshore institutions, beyond the reach of the Inland Revenue and removed from any useful purpose to the remainder of society.

Also, given that a substantial part of the deposit base of private banks is the income of local and national government. We have a situation wherein private corporations are facilitated and funded by using public money as a deposit base for lending for risky speculation, allowing them to make profits from public money. This is without the seemingly endless reserves handed to these institutions through 'Quantitative Easing' and other bailout mechanisms post-2008. To which they did not use the funds provided to them by government to facilitate improvement to society. They simply used it to improve the private Banks balance sheets. We think it would prove to be safe to say, if that transaction occurred in any other business environment the recipients of the government funds would be facing serious litigation.

Any debt should be to our own bank

The reactions of the Welsh Government to the first part of the Silk Commission on Devolution in Wales, and the seeming cross-party adoption of its recommendations for borrowing powers should send alarm bells ringing for anyone in the country possessing even a passing acquaintance with the calamitous history of public borrowing by nations which, like Wales, lack monetary sovereignty. The statement of 2nd February this year by Welsh Finance Minister Jane Hutt makes clear that the Welsh Government's 'priorities' in the wake of Silk 1 are to secure 'devolution of borrowing powers to finance capital investment and to manage short term budgetary fluctuations arising from any tax devolution' and also, possibly, 'early access to borrowing powers, ahead of any tax devolution, to finance specific infrastructure projects, in line with the commitment in the joint statement on funding reform issued in October 2012'.

The joint statement states that Westminster accepts the case for devolved borrowing powers for the Welsh Government for financing infrastructure projects, 'subject to an appropriate independent stream of revenue being in place to support it. Yet real life copper bottomed alternatives to this headlong rush into the perilous embrace of the bond markets exist and there is a model which, despite its international successes, is totally ignored in the UK context: Public banking. Public banking is vital to the successes being produced by the more acceptably named BRIC nations (Brazil, Russian, India and China), as well as of the European economic powerhouse Germany through the publicly-owned Landesbanken. Together with the state-owned Bank of North Dakota in the US.

The public banking model is in essence quite simple: A nation such as Wales (together with its local government units), could use a portion, or all, of its budget as the depository base for a Wales Bank which has as a sole mandate investment in national infrastructural and in the local SME sector: taking the greatest advantage of the bank's ability to create liquidity through the issue of credit via the process known as fractional reserve banking.

A public bank allows the region or state to overcome the shortcomings of the

private banking system, wherein perverse incentives and lunatic risk models have turned banks away from investment in the 'real productive economy of society' of creating employment, via infrastructure, development and research and development, towards lending for asset price inflation, derivatives gambling and bubble creation, as can be observed in the crisis in the real estate sectors of the UK and US.

Public banking also creates the enormous advantage that profits received through arbitrage on loans, the difference between the bank's borrowing rate or depositor rate and the rate at which it makes loans (also known as the 'spread'), after overheads are met, comes back as a dividend to the bank's primary shareholder: the state. This system uses the credit creation function of banks for the good of society and to meet the needs of the broad majority, instead of perpetuating the current extractive system of private banking wherein the profits on loans to public bodies are paid out in dividends to an already wealthy class of private shareholders or in obscene bonuses to bankers, often subsequently being offshored or used as a base for further rent-seeking.

In the Welsh context the Bank of North Dakota in the model of state income as a deposit base is problematic. In that the Welsh government does not manage its own income through taxation powers, but rather draws on Whitehall-managed funds on a need-to-spend basis through the Block Grant calculated via the Barnett Formula: whether this money could be deposited in such an institution is doubtful. In this sense a putative Welsh public bank would be greatly advantaged by further devolution in taxation powers for the Welsh government and, for those in favour of a Welsh public bank, this can be seen as an argument to press all the more strongly for the implementation of the recommendations of the Silk Commission, including an extremely cautious investigation of public borrowing powers.

Any public bank of Wales would of course, as with any bank, have access to the Bank of England discount window facility, as well as to inter-bank lending and capital markets and this would be an enormous advantage of such an institution over any non-bank financing institution, such as Finance Wales, which does not enjoy this privileged access to funds.

Welsh local authorities manage their own budgets and it is possible to

use this substantial pool of funds, or a part thereof, to form a deposit base for a public/development Bank of Wales in the interim period running up to increased fiscal devolution. The disastrous experience of some Welsh local authorities during the scandalous saga of the Icelandic Banks, that example *non plus ultra* of the potential criminality and incompetence of private banking (and in once public banks), should provide councils with an added bottom-line motivation for investment in any Welsh public bank.

It is also possible to demonstrate the advantages of such an institution for the regeneration of Welsh business and industry, as well as the potential for feeding back profits into positive public uses, which will also be of great benefit to Welsh Local authorities. The Statistics for Wales report for 2011-2 shows gross revenue expenditure for Welsh local authorities of £7.7bn, with £28 million being kept in reserves for this period (which is, however, a decrease of £108 million from 2012-1): this gives some idea of the sums in circulation in Welsh local government and currently being channeled through private banks, with no benefit to the Welsh Government or the principality as a whole

The funds of Higher Education Institutions, Pension Funds and Trade Unions could also provide investment for an initial deposit base. Cardiff and Swansea Universities both have large investment funds and, along with other HE institutions can be introduced to an investment portfolio all insurance backed to take part in this innovative direction for the Welsh economy. The development of systems which would benefit the economy Wales so directly should also be something which could be explained without much difficulty to the unions and which I have no doubt would be extremely popular with their membership.

## Savings Bank Model

The Welsh public/development bank could also open its investment portfolio to taking deposits from other sources including individual savers and depositors: this would bring any Welsh public bank strongly in line with the Landesbanken/Sparkassen model in Germany. It would be wise to limit this aspect of the bank's operation to products aimed at longer-term savings investments, thus providing greater stability to the depository base.

There is much potential here to create a 'Save for Wales' system which would provide savers with competitive returns on deposits while providing genuine

benefit for the communities in which they live. It would be an added value facet for working alongside local institutions such as Credit Unions and Mutual Societies in this regard, as this would provide street level access points for the bank's products, while the Welsh public bank would provide support systems for these institutions, including providing access to short-term liquidity and fulfilling a wholesale banking role in relation to them.

Following the secure establishment of a public/development Bank of Wales, other broader scoped options could be looked at in a similar vein to the Bank of North Dakota. Future developments could include an opportunity for a Bank of Wales to offer transparent, separated (Glass Steagall) saving/deposit/transaction accounts options as proposed here:

1. A small guaranteed (full reserve) transaction account limited up to a certain amount.
2. Time deposit accounts, where only existing depositors money is loaned to borrowers (like a credit union) and hence interest paid to investors and charged to borrowers.
3. A higher risk 50/50 time deposit option account for savers, where no more than 50 % could be speculated on ethical and transparent speculations and markets.
4. A very tightly controlled and capped mortgage section and/or a capped deposit loan scheme for first time Welsh home buyers who are earning under a certain amount, with no unpredictable shared equity schemes allowed.
5. The bank itself could also be allowed to invest a limited percentage of its generated profits (no more than 10-20% say, and again, ethical and financially transparent only) and where possible, invested in Welsh companies.
6. A very tightly controlled and capped insurance section.

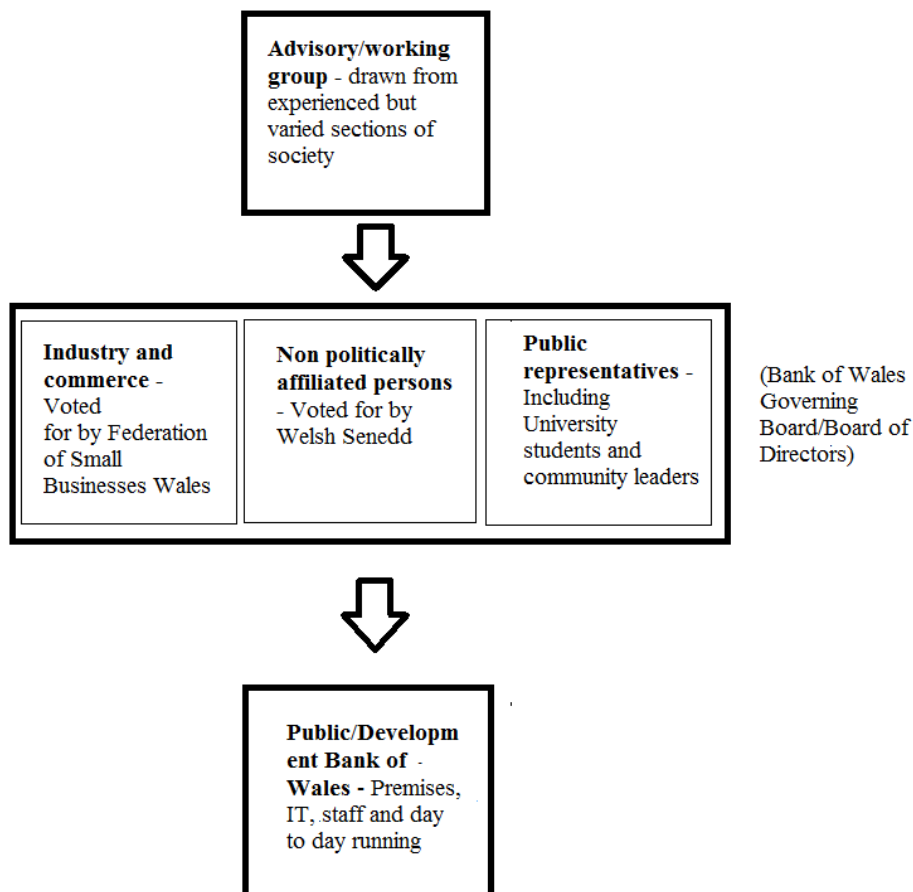
Set up/framework of The Development/Public Bank of Wales:

Arian Cymru advocate the Bank of Wales must be at arms length from direct influence by Welsh Government, with a strictly politically independent and

transparent Bank of Wales Board of Directors/Governors separate from any political influence or control but still thoroughly transparent and accountable to the Welsh Government and Assembly. The Governing Board of the Bank of Wales' remuneration would need to be set by law and directors should not be able to receive any bonuses or benefit personally from any decision made. As mentioned, the bank would have to set a yearly cap each year for all its banking sections and their Modus operandi Mandate would be an overall holistic view of the Welsh economy in order to maximise support for the whole national economy.

Arian Cymru advocate an overview management structure in line with the following graphic diagram, chosen for their variety of skills and experiences and up to a number of approximately 12 or so:

**Arian Cymru Public/Development Bank of Wales Governing Structure**



We propose that the Federation of Small Businesses Wales should choose the

chairman and three other representatives of their choice from the world of commerce and industry, that all Welsh Assembly/Senedd members vote on another four non politically affiliated/active directors of their choice and that the other four directors are made up of public representatives including University students and community leaders. More on the (as seen in the diagram) proposed Advisory Working Group below.

Arian Cymru proposal for an Advisory Working group to monitor and guide the process

Working group Dimension:

In any situation such as this it is necessary in the first part to create a working group drawn from a wide cross section of knowledge and talents as the basis of an initial step to establish a framework on which the principle of a Banking Facility for Wales can be established. This would ensure that all facets of requirement are introduced, considered, applied and knitted together in the correct cohesive and proper manner to ensure a successful product that will work in the marketplace of all sectors of society.

To this end Arian Cymru propose the setting up of a bank overview management structure. This would be a completely independent Working Group to advise and oversee to some degree the Board of Governors. Arian Cymru are already working with a number of people who are looking at the process necessary to begin to establish the foundations of a Welsh Bank and we are confident that we have a strong group of substantially knowledgeable and experienced individuals who have a shared enthusiasm and vision for a Bank of Wales and who would be happy to be part of such a group in an official capacity. We believe that this set would help to put in place a balanced, professional structure that would work for the good of all rather than for the good of the few. We would be more than happy to provide more details of our proposals and will continue to promote this crucial dialogue.

Somebody once said that "the Banks are the pillars of society". It is patently clear from the experience of the past 5/6 years that the very opposite is the case. It is our society which stands alone and holds itself and everything else up. It is the case that the Banks in their current form feed carnivorously upon society in such a manner and to such a degree that they are destructive of our society.



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