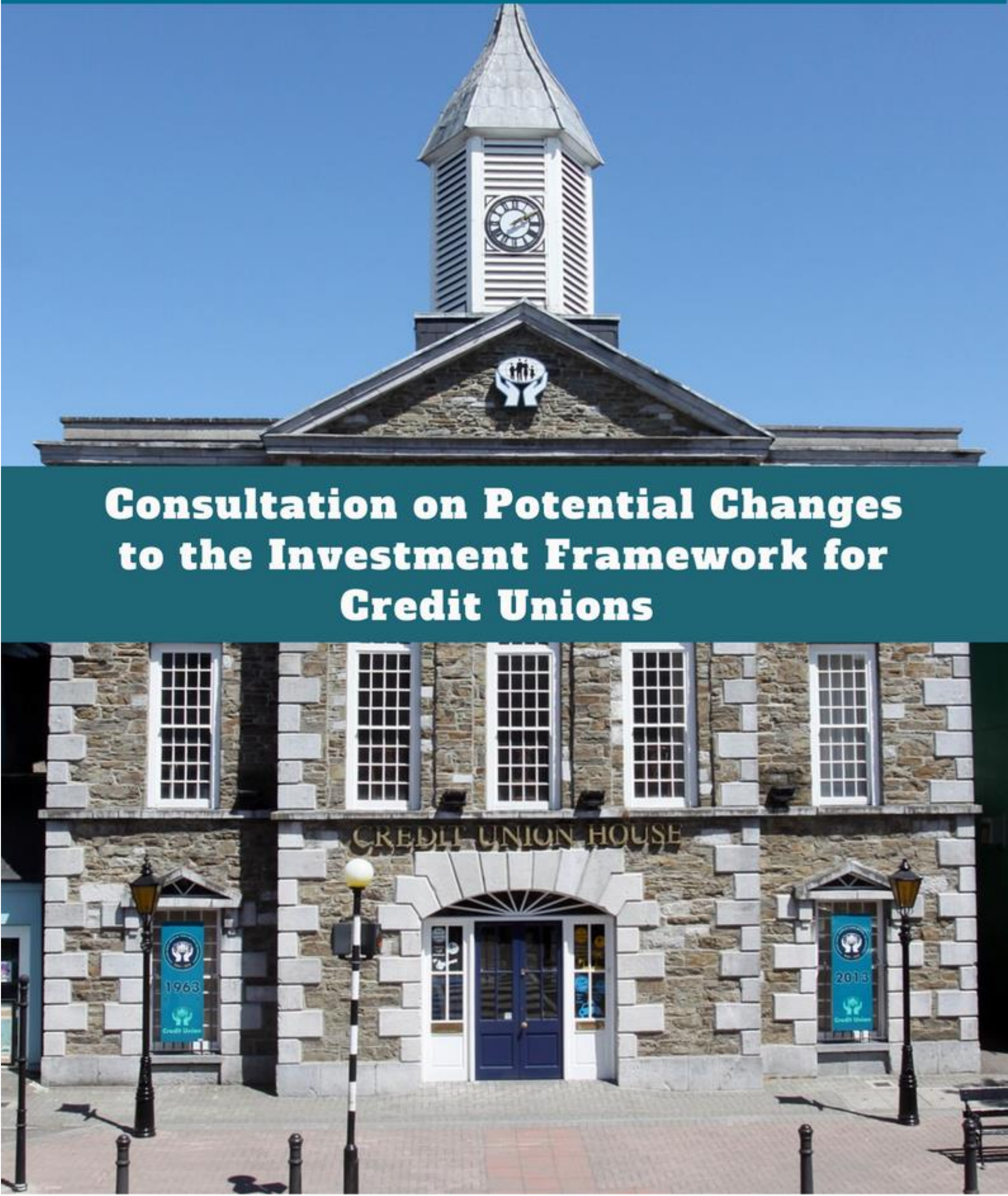
Kanturk
Credit Union
Limited

Response to CP-109



Consultation on Potential Changes to the Investment Framework for Credit Unions

About Kanturk Credit Union Limited

Kanturk Credit Union Limited is located in northwest Cork and has served the community of Kanturk and surrounding areas since 1963. Our credit union is affiliated to the Irish League of Credit Unions and has grown significantly in recent years. Our current membership is 10,000 strong with total assets in excess of €60,000,000.

Like the vast majority of credit unions, the recent financial crisis and subsequent fall out created a set of challenges that we are still tackling proactively today. Households in our community are paying down debt as quickly as possible and savings continue to grow. We have seen encouraging loan book growth over the past couple of years but the vast majority of our assets are still tied up in low-yielding deposit accounts. Our key strategic focus is to ensure Kanturk Credit Union remains a strong, financially sound business in the coming years with the aim of becoming the number one choice for personal loans in our common bond.

Overview

Kanturk Credit Union Limited broadly welcomes the consultation on potential changes to the investment framework for credit unions. The current regulatory regime governing investments for credit unions significantly limits the ability of credit unions to both diversify their investment portfolios and generate a reasonable return on members' funds. We believe that whilst some of the proposed changes represent positive developments, others will compound the current challenges faced by credit unions across the country.

We have reviewed the response made by the Irish League of Credit Unions to this consultation and agree with the main points made by the League in relation to the key proposals set out.

Observations & Comments on CP-109

Rather than respond to the wide range of questions set out in the Consultation Paper directly we would like to register our support for the League's response. We also set out some general observations and comments below in relation to some of the key proposals presented in the paper.

Supranational Bonds

We welcome supranational bonds as an additional investment class. Given that such bonds are always backed by a more than one European Government they generally have very high credit ratings and we would therefore view the proposed concentration limit of 50% of regulatory reserves as unnecessarily restrictive. Based on our most recent prudential return data this limit would result in under 7% of our total investments being permitted in supranational bonds. At this level there is little benefit in terms of investment diversification. Given that eligible instruments are likely to have the backing of European Sovereigns we believe that consideration should be given to limiting investments in the total bond universe of 70% to total credit union investments, rather than limiting certain classes to percentages of the regulatory reserve, which is consistent with the 2016 Regulations.

Corporate Bonds

The Central Bank considered permitting investments in corporate bonds in CP76 but did not include them as an approved investment class in the 2016 regulations. The benefit of corporate bonds would be in investment diversification rather than income generation as the yields on A-rated corporate bonds are likely to be in line with the yields on similar bank bonds. However, as with the proposed concentration limit for supranational bonds, the proposed concentration limit of 25% of the regulatory reserve would render corporate bonds ineffective in diversifying investment portfolios. In our case the proposed limit would result in under 4% of our total investments being permitted in corporate bonds.

We recognise that there is greater risk to capital when investing in corporate bonds when compared with bank bonds and as such we believe that such investments may be more appropriately catered for through collective investment schemes with a diversified population of such bonds.

We again recommend that a concentration limit of 70% of total credit union investments should be applied to the total bond universe (i.e. Irish and EEA State Securities, Bank Bonds, Supranational Bonds and Corporate Bonds).

Approved Housing Bodies

At present the credit union movement has c. €10 billion held in investment related products earning a low yield and put to an unproductive purpose. Under current regulations, there are limited options for the management and placement of these investments. We believe these investments could be better used to deliver key social goals, while also fully protecting those funds.

If the investment regulations were to be amended to facilitate investments by credit unions in AHBs, credit union funds currently deposited with banks, could contribute for example to assist in the provision of social and affordable housing on a basis that assures both the protection of the fund and gives a modest return. This would be in line with the principle of existing legislation and the social ethos of credit unions. This could be facilitated through the setting up of a special purpose vehicle. The details and risks associated with such an instrument would have to be worked out but this could be done in a phased basis at sectoral level with Central Bank oversight.

We refer to the League's response in relation to the possible mechanism for facilitating such investment.

Amended Definition of Bank Bonds

The proposed definition of bank bonds in CP109 is concerning. Currently credit unions can invest 70% of investments in senior bank bonds. The other proposals contained within the paper will only facilitate the addition of another 20% or so in investments and will have little to no positive impact on income especially when considered in light of the potential lost income associated with changing the definitions of bank bonds, which may have huge consequences for the viability of the sector. In ***Goodbody Stockbrokers*** response to this consultation paper they estimate that the total cost of the change in definition would be around €50 million for the sector.

The proposed change is unjustifiable as it will exclude many bank bonds from higher-rated institutions and would actually encourage investments in higher-rated bonds at riskier institutions. In our view, this would be indefensible.