Submission from Slane Credit Union on CP109

CP109 Submission

Slane Credit Union Ltd.

1. CP 109 – Comments, Observations and Responses

Please find our feedback as requested in Section 4 of CP109

5.1 Potential Additional Investment Classes

1. ***Do you have any comments on the current level of diversification in credit union investment portfolios? Are there any barriers to the use of existing diversification options within the current investment framework? If so, please provide details and any suggestions to address these.***

The restricted investment classes set out in the 2016 Regulations are the greatest threat to our investment policies.

Suggestions –

- Current liquidity ratios requirements effectively restrict investment in Bond, the definition of liquidity could be changed to allow credit unions to deem assets as liquid if they can access the funds, even if some interest may be lost or a nominal charge is applied. Such an expansion of the definition of liquid assets would allow credit unions to diversify and could promote investments in Bonds
- We believe allowable investment asset classes in Collective Investment Schemes should be expanded.
- The proposed restriction of the Bank Bonds definition will compress the investment opportunities for credit unions and therefore should be revisited.

2. ***Do you have any comments on the potential introduction of additional investment classes for credit unions and the appropriateness of the classes being considered by the Central Bank?***

We welcome the introduction of additional investment classes. The proposals in respect of Approved Housing Bodies are relevant and meets in a great part with our hopes .

Supranational Bonds and Corporate Bonds will have a very negligible impact on investment income

Over the last number of years, the loan books of Credit Unions have been diminishing. The upward trend of 2015/6 still leaves Credit Unions dependant on investment income to generate an adequate investment return on members' savings. The additional investment asset classes do not adequately recognise this fact.

3. ***Taking account of the appropriate risk profile for credit union investments, are there any additional investment classes that the Central Bank should consider? If so, please outline the investment classes and why such investment classes are considered appropriate for credit unions.***

- Investment rules should be amended to allow for centralised lending of mortgages and SME's
- Credit unions should be allowed to collectively invest in finance service organisations furnishing essential services such as data processing, liquidity management and group purchasing.
- Credit Unions should be allowed to invest in and/or purchase stock in said companies.
- Centralised Mortgage Lending – this will bring long-term lending and growth to the loan book. It will therefore bring extra income, supplementing lost investment revenue. We realise that appropriate external expertise will have to be engaged to ensure risk mitigation and operational efficiency. A central mortgage unit should be authorised by the Central bank. We believe that the Central Bank should include central mortgage lending as an investment class.
- Centralised SME Lending should be considered as a potential additional investment asset class.

- Equities, we believe the need for such investments via Collective Investment Schemes, Investment Trusts or Exchange Traded Funds are a necessity for balanced investment and growth. We would like to see the Central Bank reintroduce the eligibility of 5% of the credit union's investment portfolio being allocated to equities. It would be sensible to include a specific counterparty limit for equities whereby exposure to any individual equity would be limited.
- State Sponsored Projects such as infrastructure, schools and hospitals

4. ***Do you have any comments on the potential to include supranational bonds in the list of authorised classes of investments set out in credit union investment regulations with a minimum credit rating requirement and maturity limit?***

We see the addition of supranational bonds as an investment asset class as a move that will diversify counterparty exposure and therefore good. However, it will have very little impact on investment returns. We agree with a maturity limit of 10 years.

Do you have any comments on the suggested concentration limit for credit union investments in supranational bonds? If you have suggestions, please provide them along with supporting rationale.

- The proposed concentration limits are simply too low for credit unions to have any meaningful investment in Supranational Bonds.
- We believe that the Central Bank has not explained its rationale for proposing said concentration limits.
- If the Central Bank is insistent on applying concentration limits then investment in Irish and EEA State Securities, Bank Bonds, Supranational Bonds and Corporate Bonds should be limited to 70% of the total credit union investments, consistent with the 2016 Regulations.

5.3 Corporate Bonds

5. ***Do you have any comments on the potential to include corporate bonds in the list of authorised classes of investments set out in credit union investment regulations with a minimum credit rating requirement and maturity limit?***

- We agree that the addition of Corporate Bonds to the investment asset classes will provide credit unions with an opportunity to allocate a portion of investment portfolios to non- financial counterparties. However, yields on "A" rated Corporate Bonds currently offer very low investment return.
- We agree with a maturity limit of 10 years for Corporate Bonds.

6. ***Do you have any comments on the suggested concentration limit for credit union investments in corporate bonds? If you have suggestions, please provide them along with supporting rationale.***

- The proposed concentration limits are even lower than those proposed for Supranational Bonds.
- Any meaningful investment is restricted by the extremely low proposed concentration limits and the "A" credit ratings.
- We recommend that a concentration limit of 70% of total credit union investments should be applied Irish and EEA State Securities, Bank Bonds, Supranational Bonds and Corporate Bonds.

5.4 Investments in Approved Housing Bodies ("AHBs")

7. ***Do you think it is appropriate for credit unions to undertake investments in AHBs? If so, please provide a rationale.***

- It is appropriate for credit unions to investment in AHBs.

- We believe such investments would deliver on credit unions’ social goals, fully protecting members funds and assist civil society by contributing to social and affordable housing.

8. ***What would the most appropriate structure for investments in AHBs be e.g. investment vehicle?***

- A special purpose vehicle (“SPV”) would be the most appropriate structure for investments in AHBs.

9. ***What do you consider to be the risks associated with this type of investment and what mitigants do you feel are available to manage these risks?***

  - The key risk the AHBs’ ability to repay the money borrowed.

  Mitigation –

  - The credit union could have first charge against property where the borrowed money is earmarked for particular properties.

  - The agreement should provide safeguard for the lender to the AHB in the event of default. The Local Authority continues the Payment and Availability Agreement payments (the agreement between the Local Authority and the AHB).
  - As the de-facto counter-party to a loan to an AHB is the State, the State ultimately repays the loan.

11. How can the ALM issues associated with such investments be addressed by credit unions?

A centrally managed SPV, would have a mix of projects that give balance to the investment portfolio, in terms of length of term and a mix between acquisition and construction projects, ensuring appropriate liquidity is maintained and that risks are kept within stated parameters.

12. ***Given the existing mismatch between the maturity profile of the sector's funding and assets and the likely maturity profile of such investments, the Central Bank is of the view that the concentration limit would need to be set at a level that reflects this. Do you have any views on what an appropriate concentration limit would be for such an investment? What liquidity and ALM requirements could be introduced to mitigate these risks and potentially facilitate a larger concentration limit?***

We believe that concentration limits should be based on a proportion of investments with an acceptable range being between 10% to 20%. Credit union boards and management through their investment policy are best placed to consider and agree the specific concentration limits for AHBs

In the main credit unions already manage liquidity requirements well and will continue to do so.

13. ***Do you have any comments on the proposal to include investments in Tier 3 AHBs in the list of authorised classes of investments set out in credit union investment regulations with a 25- year maturity limit?***

We agree with the proposal and the 25 year maturity limit.

5.5 Counterparty Exposure Limit

14. ***Do you have any comments on the proposal to amend the existing counterparty limit for credit union investments? If you have suggestions, please provide them along with supporting rationale.***

- Any reduction in the counterparty limit would place additional counterparty strain on credit union investment portfolios.
- The proposed reduction may force credit unions to invest more funds in institutions outside the State
- It is strong view that the counterparty limit should be retained at 25%.

15. ***Do you have any comments on the proposed transitional arrangement to reduce the counterparty limit to 20% of total investments?***

- The proposed transitional period of 12 months post commencement of the amended investment regulations is insufficient.
- investments with fixed maturity dates should be held to maturity which is consistent with the 2016 Regulations

5.6 Collective Investment Schemes

16. ***Do you have any comments on the use of collective investment schemes for credit union investments?***

Collective Investment Schemes would provide a mechanism for credit unions to invest in a range of asset classes, across a mix of maturities. However, investments in such schemes are effectively restricted per the 2016 regulations to low yield investments in Irish and EEA State Securities etc. We therefore believe that the definition of Collective Investment Schemes should be expanded to incorporate other collective investment schemes.

17. ***Are there any barriers to credit unions using collective investment schemes in the existing investment regulatory framework?***

- The key barrier is the low yield on these investment asset classes.
- Lack of knowledge in relation to Collective Investment Schemes.

5.7 Timelines

18. ***Do you agree with the proposed timelines for the introduction of potential changes to the investment framework set out in this consultation paper? If you have other suggestions please provide them, along with the supporting rationale.***

- We need to see the Central Bank’s responses to the issues raised in our submission (and those all other contributors) before we can give a view on the timelines.
- It is important that the Central Bank meets with the ILCU to discuss the matters raised in this submission.

2. Conclusions & Next Steps

Slane Credit Union ask the Central Bank to consider the following:

(i) Active and constructive engagement with the credit union movement in respect of any proposed amendment to the definition of Bank Bonds

(ii) Review of liquidity requirements for credit unions, including additional investment asset classes within the definition of liquid assets.

(iii) Consider inclusion of additional investment classes:

- Investments in Credit Union Service Organisations;
- Centralised Mortgage Lending;
- Centralised SME Lending;
- Equities; and
- State Sponsored Projects;

(iv) Concentration limits for the bond investment, Supranational Bonds, Corporate Bonds etc. be set at 70% of the credit union investment portfolio.

(v) Minimum credit rating of Investment Grade to be applied to Supranational Bonds.

(vi) Counterparty limit should remain at 25%.

(vii) The definition of Collective Investment Schemes should be expanded.

(viii) Re-introduction of the concept that credit unions should be granted an exemption for investment limits if those credit unions can demonstrate they possess the skills and systems necessary to manage a more complex investment portfolio.