Sparkasse Aachen

Consultation by the High-level Expert Group on Reforming the structure of the EU banking sector – Questions to banks

0. Introduction to Sparkasse Aachen

The German banking market is characterized by its three pillars:

- private banks
- co-operative banks
- savings banks and state banks (Landesbanken) which as a group are known as "Sparkassen-Finanzgruppe"

Competition in the German banking industry is one of the strongest in the world. The Sparkassen-Finanzgruppe is market leader in Germany, maintaining business relations with three quarters of all households and businesses.

Savings banks are institutions governed by public law and supervised by the local municipalities. They are independent and decide locally on their respective business policy and especially on their product range and prices offered to their customers.

Sparkasse Aachen is a savings bank with total assets of € 9,5 billion by the end of 2011. It is the largest independent financial institution in greater Aachen, an area located directly at the German border to both the Netherlands and Belgium, where around 570,000 people live. Founded in 1834 Sparkasse Aachen is owned by the city and district of Aachen. As municipal welfare-oriented savings bank Sparkasse Aachen does not focus on short-term profit maximisation, but on sustainability, i. e. to strive for such a profit that the equity buffer is continuously strengthened to maintain a solid business growth rate.

Financial services for private customers and corporate clients

Sparkasse Aachen is the market leader in the region, operating a densely knit network of 94 branches and employing more than 2,000 people. Working in conjunction with its subsidiaries, Sparkasse Aachen offers private customers and corporate clients a wide range of financing, investment, real estate and insurance businesses. Access to Sparkasse Aachen's services is equally diverse; apart from visiting the local branches, customers can also avail themselves of modern online banking and brokerage services as well as a phone banking service. Sparkasse Aachen is maintaining 257,000 current accounts for private customers and 44,000 accounts for business clients.

Sparkasse Aachen's corporate banking services are geared to companies' needs. From customised lending to financial consulting, from business planning to entrepreneurial ventures - Sparkasse Aachen offers professional advice and support all the way.

Sparkasse Aachen is one of the co-founders of S-UBG (www.s-ubg.de), a private equity company, fully owned by six local savings bank. Its aim is to support newly found businesses and offer them a local alternative to rather globalised big private equity firms.

Sparkasse Aachen helps to promote regional prosperity und public welfare

Sparkasse Aachen cooperates with companies, numerous research institutions and universities in the Aachen area to promote the structural change from outdated "old economies" (coal mining, needle and cloth industries) to high-tech industries.

According to its commitment to support greater Aachen area, Sparkasse Aachen has paid out more than € 276 million to various Aachen authorities during the last ten years, such as commercial taxes to local authorities (€ 153 million), dividend payments to the city and district of Aachen (€ 76 million), donations in general (€ 29 million) and to foundations (€ 17,5 million). Not only social, but cultural and sports projects benefit from this public welfare dividend as well.

Thanks to our firm focus on local businesses and markets, Sparkasse Aachen is highly familiar with the needs and characteristics of the Aachen region. We remain committed to leveraging our regional expertise for the benefit of our customers and all citizens of greater Aachen.

1. To what extent are the current and ongoing regulatory reforms sufficient to ensure a stable and efficient banking system and avoid systemic crises?

We firmly believe that the current decentralised savings banks organisation structure already provides stability to the financial industry, a matter of fact that can easily be seen during these current months of financial turbulence.

The financial crisis has shown that the decentralised, customer-oriented networks of the savings banks and of the cooperative banks are stable in themselves and fully live up to their responsibilities to provide financial services for the economy and have even increased their lending volumes during the last five years. In the years of crises the savings banks have continued to achieve a decent business performance and – unlike other private banks - paid taxes and dividends.

This means that there is no need for any additional regulation with regard to the decentralised systems. It can certainly not be expected that the German savings bank structure serves as a blueprint to the international financial sector as there is also a need for internationally operating banks to meet globalised customers needs.

However, it is obvious that such business models pose potentially higher risks to the stability of the financial sector. Especially institutions that are "too big to fail" benefit from an implicit state guarantee, improving unfairly their funding rates which in return disadvantages regional operating banks because they lack such an implicit guarantee. Too-big-to-fail-institutions must maintain a risk-adjusted capital buffer e. g. this surcharge can be regarded as a premium for the implicit guarantee – which is a kind of subsidy – they receive.

We welcome the proposal to strengthen the equity of banks. The suggested higher equity requirements should nevertheless apply mainly to those financial institutions which, because of their size and risk appetite, pose a risk to the entire national economy if they run into difficulties.

Sparkasse Aachen's Tier I capital ratio of risk-weighted assets is 14,35 %. It should be noted that savings banks are not stock listed companies and they cannot increase their share of capital via the capital market. Sufficient equity for further lending can only be generated by the savings bank's profits. It is therefore obvious that a long-term-oriented business policy is necessary.

2. Which structural reforms would improve the safety and efficiency of the banking system in the EU in the near term? In the long term?

As outlined under 2. the German banking market is characterized by three pillars.

Small and decentralised structures are resilient to external shocks, e. g. if one bank out of 500 fails, nobody would notice, but if one bank out of three collapses the economy would be in dire straits. The decentralised German savings bank structure can be compared to a portfolio of highly diversified risks.

Some further explanations may highlight this model.

All 426 German savings banks of the Sparkassen-Finanzgruppe have strong regional roots. This is due to the so-called principle of regionalism. According to this principle savings bank shall only operate branches in their own region and shall grant loans in that region. The principle of regionalism ensures that local funds are mobilised in a given region and will be available for investment in the same region in order to strengthen the regional economy. This is a contribution towards a sustainable development. Especially savings banks focus on the business with private customers and German SMEs (“Mittelstand”). Unlike private banks, savings banks also provide universal banking services to low-income households and riskier ventures. Sparkasse Aachen has a market share of 59 % (private customers) and 67 % (business clients) respectively.

Loans to customers are therefore the largest item on the assets side of Sparkasse Aachen’s balance sheet, accounting for an market share of 68.7 %. Investments and claims on credit institutions accounted for 21.2 % and 5.4 % respectively. On the liabilities side, customer deposits and the Bank’s own securities issues traditionally constitute the bulk of the total, and account for a slightly lower share of 75.5 %. Liabilities to credit institutions accounted for 13.0 %.

Another prime motivation behind this principle of regionalism is risk mitigation. Since Savings Banks are local players, they also have profound knowledge of their local customers. This intimate knowledge allows us to get a much clearer understanding of the risks involved in extending a loan to a specific client. It is a kind of knowledge that will rarely be found in remote corporate headquarters. This knowledge may have been one of the reasons why the German economy has recovered faster than other European countries after the decline of nearly 5 % in its gross domestic product in 2009. SMEs could access loans as savings- and co-operative banks knew their customer’s business model well. SMEs in Germany rely more heavily on financing from banks than companies in other countries. This is due to the fact that Germany's economy is dominated by the Mittelstand, which accounts for two-thirds of all jobs. During the economic recovery savings banks ensured the supply of financing.

Staying in touch with reality and concentrating on real customer business rather than investing capital in international markets are a successful business model, which in a similar way is pursued by co-operative banks as well. Both pillars are fully exposed to market forces and they depend on their intrinsic capacity to generate the necessary funds for their future business operations.

The financial crisis has revealed that large parts of the financial sector are not really able to meet their customer's expectations: Instead of using the customer's deposits for reasonable “real world” investments (i.e. granting loans) they use it – unlike the savings banks – for speculative derivative trades hoping to maximise their ROE within a short term. Same players even took risks that were completely out of proportion with their own equity. In some cases this was done by making use of special purpose vehicles (SPV) with no regulation at all. These highly speculative transactions must be covered by the same set of banking regulations!

3. What are your views on the structural reform proposals to date (e.g. US Volcker Rule, UK ICB proposal)? What would be the implications of these proposals on your institution and the financial system as a whole?

As these proposals aim mainly at internationally operating banks please understand that Sparkasse Aachen as a regional operating bank does not comment in detail on this issue.

However, we assume that the Deutscher Sparkassen- und Giroverband (German Savings Banks Association, DSGV) as the umbrella organisation of the Sparkassen-Finanzgruppe will submit its views.

4. What are the main challenges of your financial institution as regards resolvability? Are you implementing structural changes to your institution in the framework of your recovery and resolution planning?

During the past years German savings banks have made numerous efforts to constantly improve their risk monitoring systems and made further developments to their instruments. This includes rating and scoring methods for the different types of customers as well as the introduction of value-at-risk-models to measure probabilities of credit and market defaults. In addition, systems have been implemented to control liquidity, operational risks and interest rate changes.

These systems and methods have been adopted by every single savings bank. Although the members of the Sparkassen-Finanzgruppe are legally and economically independent businesses, they operate under a common brand and in the case of any individual failure all other remaining savings banks are committed to safe-guard the failed savings bank, e. g. it can be seen as a mutual insurance.

The security of deposits of all customers is therefore guaranteed without any limit as to amount and far exceeds the legal requirements. All institutions have always been able to meet their payment commitments. Since the joint liability scheme was set up in 1973, no customer of a German savings bank or an affiliated institution has ever lost its deposits. Since that date, no savings bank or other member institution has ever become insolvent.

We believe that this mechanism is worth while implementing in other countries as well.

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