# German savings banks and Swiss cantonal banks, lessons for the UK

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## Foreword

We have been complaining about the shortage of finance for small and medium sized businesses (SMEs) – especially startups – for several decades. As long ago as 1931 the Macmillan committee identified a gap in the availability of investment funds for SMEs and complaints about the 'Macmillan gap', later called the 'equity gap', continue to the present day.

We decided to investigate whether or not other European countries had found solutions, and we soon found ourselves focusing on two of Europe's most successful economies, Germany and Switzerland. German savings banks (Sparkasse) hold about one-third of that country's bank assets and play a vital role in funding German industry. Swiss cantonal banks are proportionately smaller but play a pivotal role in their respective cantons. Two key features make these German and Swiss banks potentially attractive for the UK. First, they are legally restricted to operating within a defined geographical area and, second, they must function as commercially sound businesses whilst also serving the interests of the local community – especially by providing bank accounts for all and making loans and other financial services available for local businesses. This combination of aiming to be commercially viable (but not profit maximising) and pursuing social objectives is often called the 'dual bottom line'.

Until recently there were few demands for serious reform of banking, but the Independent Commission on Banking chaired by Sir John Vickers is now examining potentially radical reforms and significant change may be on the map for the first time in many years. The main strategies under discussion include the separation of 'casino' from 'utility' banking; breaking up large banks into smaller institutions that are not 'too big to fail'; behavioural regulation including limitation of bonuses; and promoting competition to stimulate the banks to reform themselves. This report argues that the localised German and Swiss banks have a lot to teach us. If we were to create a legal framework for a new style of bank – to be called a saving and enterprise bank – it would reduce the need for behavioural regulation and encourage existing institutions to fight harder to keep their customers. Wherever possible the enforcement of competition is a better

use of a government's powers than the imposition of behavioural regulation through bodies such as the Financial Services Authority.

The German Sparkasse are public-sector institutions with the typical German dual board structure: a supervisory board (in this case made up of two-thirds nominated by the local council and one-third by employees) and an executive board that runs the bank. They are regulated by the same laws as all other banks but are also subject to additional legal obligations. Any trading surplus must be ploughed back into the business and they are not permitted to make risky investments in derivatives or any of the other rarefied financial instruments that contributed to the recent financial crash. The local focus means that bank staff are familiar with local businesses and able to judge more effectively the reliability of applicants for loans.

The funds they have available for lending are primarily customer deposits which must be safeguarded. Consequently, German local banks are part of a national system that spreads risk across a system of regional banks and national institutions. Germany also has credit guarantee banks that lend within each federal region or Land. They are non-profit associations of lenders that historically provided sureties worth 80% of the loan value. Each guarantee bank would take on up to 35% of the risk, while the federal government took 40% and the Land 25%. The borrower pays a fee of 1-1.5% of the loan plus an annual commission of 1-1.5% on the amount outstanding each year. Historically borrowers were at risk for 20% of the loan value, but as a result of the recent financial crash the German government has encouraged guarantee banks to cover 90% of the risk and to take up to 50% themselves.

The report argues that we should create the legal framework for such banks to emerge in the UK. It does not argue that the government should set up the proposed banks, only that it should create the possibility that they could be established where they are wanted. Nor is it necessary for the new banks to be public-sector bodies. The Localism Bill provides a framework that would permit them to take that form, but a variety of other legal structures should also be available, including mutuals, co-ops, private limited companies, community interest companies and trusts. The presence of a supervisory board keeping a watchful eye on the executive board

is a useful constraint but it need not be made up of a mixture of local authority nominees and employees. It could comprise customers in the manner of a consumer co-op; or its members could be trustees, who are charged with safeguarding the social objectives of the bank but barred from profiting personally.

The creation of a new legal framework for saving and enterprise banks could set loose a vast pool of untapped energy that potentially holds the key to restoring our economic fortunes. In addition it would stir existing banks into new activities more compatible with the interests of the people of this country.

David G. Green

## Introduction

Britain's banks have been heavily criticised for failing to lend sufficiently to SMEs, not only recently but for many decades. German and Swiss banking is widely reputed to have a better record of financing productive industry. Here we examine the Swiss cantonal banks, an enduring component in the Swiss financial system, and the largest German banking sector, its savings banks. Are there any lessons for Britain?

## The lending problem in the UK

Using the UK survey of SME finances for 2008, Dr Stuart Fraser of Warwick Business School examined how small and medium sized firms have been affected by the credit crisis.[1] He looked at 2,500 SMEs with fewer than 250 employees and contrasted their access to finance in two periods, 2001-2004 and 2005-2008. He also contrasted firms applying for finance in 2008 with those applying in the previous three years. His most important findings were.

- Compared to 2001-04 the use of financial products (overdrafts, loans, asset and invoice finance) by SMEs fell in 2005-08;
- the use of internal finance from friends and family increased in 2005-08;
- 2005-08 saw a fall in the amount of SME deposits and an increase in SMEs using their deposits to fund working capital;
- rejection rates for overdraft requests increased in 2005-08, most dramatically in 2008;
- firms with fewer employees saw greater increases in rejection rates;
- loan margins increased for all financial products for 2005-08, with the exception of loan margins for lower risk firms which for some financial products decreased.

Holding the level of risk constant indicates that arrangement fees were 21% higher for 2008 applicants compared to previous years. Dr Fraser's analysis indicates that a firm applying for a loan in 2008 faced greater difficulties than a firm, similar in all respects, applying for a loan before 2008. Dr Fraser found that the market share of SME loans has decreased for the larger banks. Alliance and Leicester have seen their market share rise from 1% in 2001-04 to 4.8% in 2005-08 and the Cooperative Bank has seen their market share increase to 2.9% in 2005-08 from 0.5% in 2001-04. This result is echoed by figures from RBS, Barclays, Lloyds and HSBC whose combined market share fell to 71.1% in 2005-08 from 77.3% in 2001-04. Businesses' movement away from the larger banks may indicate dissatisfaction with the credit services they are supplying. Interestingly the survey found that in both 2001-04 and 2005-08 just over 7% of SMEs switched their main bank.

SMEs make up just over half of the UK economy and their success is a key element in Britain's economic growth. This is made clear in data published by the Enterprise and Industry Department of the European Commission. The contribution of SMEs to the UK's economy accounts for 54% of all employment and 52% of total value added.[2]

## Germany: a contrasting picture

**Table 1: Lending volumes of German banks**

| | Big Commercial Banks | Regional Banks | Foreign Banks | Länder Banks | Savings Banks | Cooperative Central banks | Cooperative Banks |
|---|---|---|---|---|---|---|---|
| | Overall Lending volumes every quarter (Mil €) | | | | | | |
| 2009 Jun | 183 232 | 145 706 | 42 813 | 255 996 | 303 710 | 24 554 | 166 155 |
| Sept | 189 627 | 136 888 | 41 216 | 248 104 | 305 491 | 21 779 | 168 010 |
| Dec | 177 041 | 133 620 | 38 480 | 241 857 | 306 847 | 22 849 | 169 409 |
| 2010 Mar | 173 310 | 125 560 | 36 772 | 240 306 | 309 114 | 23 339 | 171 331 |
| Jun | 179 667 | 131 470 | 37 724 | 241 437 | 313 097 | 21 065 | 174 858 |
| Market Share (%)[3] | 12 | 9 | 3 | 16 | 21 | 1 | 12 |
| | Changes in overall lending (Mil €) | | | | | | |
| 2009 Q3 | **+ 6 395** | − 8 818 | − 1 597 | − 8 192 | **+ 1 781** | − 2 775 | **+ 1 855** |
| Q4 | − 15 186 | − 3 268 | − 4 536 | − 6 247 | **+ 1 356** | **+ 1 070** | **+ 1 399** |
| 2010 Q1 | − 4 291 | − 8 230 | − 898 | − 1 551 | **+ 2 267** | **+ 490** | **+ 1 922** |
| Q2 | **+ 6 357** | **+ 5 910** | **+ 752** | **+ 1 131** | **+ 3 983** | − 2 274 | **+ 3 527** |
| Yearly + or - | - 6 725 | - 14 406 | - 6 279 | - 14 859 | **+ 9 387** | - 3 489 | **+ 8 703** |

**Source: DEUTSCHE BUNDESBANK, EUROSYSTEM, Bankenstatistik Stand vom 19.8.2010**

While credit conditions in the UK have become more constrained, some German banks have reported an increase in lending. In Germany the savings banks are the biggest providers of credit, closely followed by the Länder banks which, together with a few other institutions, form the German Savings Bank Association (DSGV). Moreover, only the savings banks and the cooperative banks saw an overall positive change in lending volume over the annual period examined.

The evidence above only covers overall lending volumes by different banks. Lending is also broken down by sector. Table 2 shows where savings banks are lending:

**Table 2: German savings banks lending by industry area**

| | *Chemicals, Minerals, Oil* | *Rubber and Synthetic* | *Glass and Ceramic Production* | *Metal Production* | *Mechanical, Engineering* | *Data Processing, Electrical Devices* | *Wood, Paper, Furniture* | *Textiles, Clothes, Leather* | *Food and Tobacco* | *Energy, Water Supply/Disposal* | *Construction Industry* |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | Lending volumes every quarter (Mil €) | | | | | | | | | | |
| 2009 Jun | 1 596 | 1 824 | 1 543 | 8 111 | 5 872 | 2 906 | 7 554 | 1 247 | 5 198 | 11 929 | 25 676 |
| Sept | 1 562 | 1 790 | 1 531 | 8 150 | 5 921 | 2 929 | 7 435 | 1 201 | 5 199 | 12 270 | 25 512 |
| Dec | 1 561 | 1 744 | 1 496 | 7 953 | 5 916 | 2 853 | 7 259 | 1 170 | 5 180 | 13 434 | 24 910 |
| 2010 Mar | 1 594 | 1 773 | 1 586 | 7 969 | 5 808 | 2 889 | 7 202 | 1 088 | 5 165 | 13 853 | 25 201 |
| Jun | 1 583 | 1 779 | 1 573 | 8 107 | 5 895 | 2 901 | 7 220 | 1 122 | 5 181 | 14 747 | 25 433 |
| | Changes in lending (Mil €) | | | | | | | | | | |
| 2009 Q3 | − 34 | − 34 | − 12 | **+ 39** | **+ 49** | **+ 23** | − 119 | − 46 | **+ 1** | **+ 341** | − 164 |
| Q4 | − 1 | − 46 | − 35 | − 197 | − 5 | − 76 | − 176 | − 31 | − 19 | **+ 1 164** | − 602 |
| 2010 Q1 | **+ 33** | **+ 29** | **+ 90** | **+ 16** | − 108 | **+ 36** | − 57 | − 82 | − 15 | **+ 419** | **+ 291** |
| Q2 | − 11 | **+ 6** | − 13 | **+ 138** | **+ 87** | **+ 12** | **+ 18** | **+ 34** | **+ 16** | **+ 894** | **+ 232** |
| Yearly + or - | - 13 | - 45 | **+ 30** | - 4 | **+ 23** | - 5 | - 334 | - 125 | - 17 | **+ 2818** | - 243 |

| | *Car trade and maintenance* | *Agriculture, Forestry* | *Transport, Storage* | *Insurance, Finance* | Building/ Housing Society | Holding/ Investment | Other Land property | Hotels and Restaurants | Information, Research | Health, Veterinary, | Removable Goods | Other Services |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Lending volumes every quarter (Mil €) | | | | | | | | | | | |
| 2009 Jun | 38 705 | 8 572 | 9 637 | 13 321 | 42 577 | 7 289 | 35 088 | 9 867 | 28 557 | 18 757 | 4 165 | 13 719 |
| Sept | 38 356 | 8 873 | 9 682 | 13 799 | 42 765 | 7 418 | 36 373 | 9 784 | 28 685 | 18 687 | 3 772 | 13 797 |
| Dec | 37 568 | 9 059 | 9 717 | 15 338 | 43 387 | 7 662 | 37 335 | 9 820 | 28 409 | 18 928 | 2 570 | 13 578 |
| 2010 Mar | 37 138 | 9 222 | 9 839 | 16 237 | 43 269 | 8 102 | 38 052 | 9 807 | 28 350 | 18 862 | 2 468 | 13 640 |
| Jun | 37 101 | 9 750 | 9 855 | 16 740 | 43 608 | 7 933 | 39 285 | 9 796 | 28 673 | 18 896 | 2 388 | 13 529 |
| | Changes in lending (Mil €) | | | | | | | | | | | |
| 2009 Q3 | − 349 | **+ 301** | **+ 45** | **+ 478** | **+ 188** | **+ 129** | **+ 1 285** | − 83 | **+ 128** | − 70 | − 393 | **+ 78** |
| Q4 | − 788 | **+ 186** | **+ 35** | **+ 559** | **+ 622** | **+ 254** | **+ 962** | **+ 36** | − 206 | **+ 241** | − 302 | − 219 |
| 2010 Q1 | − 430 | **+ 163** | **+ 122** | **+ 899** | − 118 | **+ 440** | **+ 717** | − 13 | − 66 | − 66 | − 102 | **+ 62** |
| Q2 | − 37 | **+ 528** | **+ 16** | **+ 213** | + 389 | − 149 | **+ 1 303** | − 1 | **+ 54** | **+ 54** | − 50 | − 61 |
| Yearly + or - | - 1604 | **+ 1178** | **+ 218** | **+ 2149** | **+ 303** | **+ 674** | **+ 4267** | - 61 | - 90 | **+ 159** | - 847 | - 140 |

**Source: DEUTSCHE BUNDESBANK, EUROSYSTEM, Bankenstatistik Stand vom 19.8.2010**
**Note – ‘Processing industries’ are in italics, ‘service industries’ are in regular text.**

In 13 out of 23 areas the change in lending was negative, however in the majority of these areas the negative change was relatively small. The construction industry, automotive industry, building and housing societies, land property and information/research business areas saw the highest volumes of loans.

About 20-30% of larger firms did indicate that access to credit had become restricted in 2009,[4] but the German credit market is more competitive than Britain's and it appears that those businesses that rely on the larger banks in Germany have suffered because of a reduction in lending by those banks. In contrast the businesses that relied on the smaller German banks, the savings banks and the cooperative banks did not witness a credit squeeze. Around 75% of SMEs in Germany are clients of the savings banks.[5]This is indicative of the wider commitment of German banks to provide credit for start-ups and SMEs. In Germany start-ups obtain approximately 27% of their finance from their bank whereas in Britain start-ups only obtain 12% of their finance from their bank. This means that British entrepreneurs have to use far more of their own savings or the resources of their families and friends to fund their business than their German counterparts.[6]

### German savings banks

German savings banks have been successful in continuing to increase lending volumes during the recent economic downturn. The German economy has undoubtedly benefited from this, as shown by its recent GDP growth, which was far above the European average, and even previous German performance.[7]

The DSGV group is composed of a number of different financial institutions. Below is a brief description of the main bodies in the Association:

1. **Savings Banks** – The banks that specialise in deposit taking and lending activities at the local level.
2. **Landesbanks** – Previously there was one landesbank for each German Land (German state). However there are now only 7 due to mergers and acquisitions. These are large commercial banks that provide services to customers which cannot be provided by the far smaller savings banks.
3. **DekaBank** – Is the specialist investment institution in the group, providing structured investment products to private and institutional investors.
4. **Deutsche Leasing Group** – Product and real-estate leasing services.
5. **Landesbausparkassen** – Provide home loans.
6. **Public Insurance Group** – The second largest insurance group in Germany.

The DSGV features many other institutions not listed above, offering investment, lending, and consultancy services amongst others. The strength of the group is its size, which allows it to provide an exceptionally wide range of services through a relatively decentralised structure. One of the strengths of the local savings banks is their ability to call on the wider financial resources and products provided by the DSGV group.

Savings banks are municipal bodies. They are public-sector institutions and have no owners in the commercial sense of having shareholders. Instead it is the municipality or municipalities, which may be cities or counties, in which they operate which bear responsibility for them. However it is incorrect to see municipal authorities as 'owning' the savings banks in their jurisdiction because they do not have the power to sell the banks and have very weak rights as regards profits. Each municipal savings bank has an executive board composed of executives who run the bank. These executives report to the administrative council or supervisory board of the bank.[8] Two thirds of the council's members are appointed by the municipality and the remaining third are appointed by employees. Within this

structure there is also a credit committee that reports to the administrative council, this committee is composed of three members of the administrative council and others from within the bank.

In terms of their legal and regulatory status the savings banks are regulated (like all other banks in Germany) by the Federal Financial Services Authority (BaFin) and the German Central Bank (Deutsche Bundesbank). The Banking Act of the Federal Republic of Germany (Kreditwesengesetz, KWG) decrees that only publicly controlled banks, set up by municipalities are allowed to use the savings bank name (sparkasse). Primarily, however, the savings banks are governed by the savings banks laws (sparkassengesetz) of the Länder in which they operate, and it is these laws which decree that a savings bank must pursue a 'dual bottom line' business strategy.[9] The notion of a 'dual bottom line' is meant to capture the fact that the savings bank are not solely committed to profit, but also to serving their local community and fostering sound local businesses. In some respects this latter aim is achieved through concrete stipulations, such as their obligation to open a transaction account for every applicant. In other respects the Länder laws will stipulate that the savings bank must encourage prudent and successful financial management by its customers and also satisfy the credit demands of local businesses. Linked to these goals is the further stipulation that, while the banks should not be solely concerned about profits any trading surplus should be used to pursue their wider social objectives. That is not to say that profit is not important for the banks, in many ways it is of greater importance than for some commercial banks, as the savings banks are unable to issue shares. Further restrictions, such as not being permitted to hold equity outside the DSGV and not being allowed to engage in risky trading or investment activities means that the savings banks are run on a very cautious business model. The administrative councils hold the banks to account and ensure they remain dual bottom line oriented.

The main assets and liabilities of the DSGV are the loans and liabilities to non-banks. Loans and advances to non-banks form 46% of the group's assets, and 45% of the group's liabilities are those to non-banks, mainly in the form of deposits. It is important to note that these percentages include the other institutions of the savings bank group, and the loans and liabilities to non-banks would be higher if the savings banks alone were examined. However these figures do indicate that the business model of the DSGV is one which aims at turning customer deposits into loans to firms and individuals.

This cautious, stable business model no doubt helped the savings banks emerge relatively unscathed from the financial crisis.[10] It has also meant that their main business areas, that of making loans and taking in deposits, has not severely suffered. However, the savings banks' successes in lending to SMEs

cannot solely be explained by their business model; of equal importance is the way in which they conduct their lending business.

Academic discussion of lending by banks to firms often divides lending practices between 'transactional lending' and 'relationship lending'. The former represents risk assessment conducted using quantitative methods (credit scoring, balance sheet evaluation etc) while the latter assesses risk using qualitative methods (interviews with firm executives, appraisals of business plans etc.). Above all, relationship banking implies that the bank maintains a long and pivotal role in the financing of the firm over many years. This dichotomy has been criticised, yet the distinction remains valid.[11] Savings banks tend to build up long-term relationships with businesses in their locality, as the case studies below reveal.

**Figure 1: Case studies of savings bank lending practices**

1. **The Barth Group**. The Barth group is an international leader in hops production and hops products. It is a medium sized enterprise located in Nuremburg. The firm banks with the local savings bank because the bank provides specifically tailored credit products. As the group's business fluctuates seasonally, (with the harvesting of hops) and the firm buys future harvests using commodity forwards, the firm needs a credit arrangement that takes into account such fluctuations and the risks that go with it. The group's executives found that only the local savings bank were willing to spend the time and effort involved in evaluating their business and creating a credit arrangement that suited them.

2. **SILAG Handel AG**. SILAG Handel AG is a retail company operating across the European market with Europe's largest retail groups. When the company wanted to install one of the largest solar panel systems in Germany on one of their warehouses they turned to their local savings bank for finance. The company felt that the savings bank was uniquely placed to offer credit at a competitive price because the local bank, due to a high degree of similar projects in the bank's area, employed a technology expert specializing in solar energy. The savings bank had dealt with similar requests before and because of its previous experience was able to appraise the viability of SILAG Handel AG's project. Moreover, the bank was able to more accurately evaluate the risks of the project and offer credit at an appropriate rate.

**Source: Finanzgruppe Deutscher Sparkassen- und Giroverband, Profile, 2009**

These brief case studies emphasise the long-term, tailored relationships that the savings banks can offer their customers, along with the local expertise they provide.

Their stable business model combined with their lending practices has brought the savings banks success. This is evident in the table below.

**Table 3: The profitability of German banks 2000-2008**

| | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | **Average** |
|---|---|---|---|---|---|---|---|---|---|---|
| Operating result in € million | | | | | | | | | | |
| Commercial banks | 7,974 | 3,346 | 3,472 | 4,784 | 6,744 | 19,804 | 14,905 | 14,927 | -7,768 | **7,576** |
| Savings banks | 4,055 | 3,078 | 2,641 | 4,559 | 4,329 | 4,993 | 4,638 | 4,123 | 3,685 | **4,011** |
| Return on capital as a percentage of total capital | | | | | | | | | | |
| Commercial banks | 7.31 | 4.24 | 0.04 | -6.57 | -1.42 | 15.52 | 9.12 | 15.61 | -15.11 | **3.19** |
| Savings banks | 6.02 | 5.06 | 4.65 | 4.00 | 5.03 | 5.60 | 4.95 | 4.21 | 2.15 | **4.63** |

**Source: Bundesbank, The performance of German credit institutions**

When size is held constant and the return on capital is examined, it is clear that the savings banks outperform the commercial banks with an average of 4.63 per cent compared to 3.19. Furthermore the savings banks are more stable; the standard deviation for the return on capital for the savings banks is 1.12 compared to 10.13 for the commercial banks, indicating that the performance of the commercial banks fluctuates significantly over time.

The stability of the savings banks is, in part, the result of the risk-management systems that the DSGV provides. Risk management is extremely important for small banks, a few poor credit decisions could jeopardise their financial position, however due to the DSGV the savings banks have more latitude and protection.

The DSGV has a ‘Joint Liability Scheme’ comprising 13 guarantee schemes; 11 regional guarantee schemes which cover the savings banks, the guarantee reserve of the Landesbanks and a reserve fund for the Landesbausparkassen. Importantly these guarantee schemes are interlinked and so if one is insufficient to support an institution under its remit there is the option for other schemes to contribute. This extensive system provides a good safety net for the savings banks and the Moody’s and DBRS credit rating agencies both singled out the Joint Liability Scheme as the key factor in their awards of very good ratings for the DSGV group in 2009.[12] However, one important caveat must be mentioned; the Joint

Liability Scheme is not legally binding and so the German Government may also be asked to reinforce the Scheme in the event of a risk to customer deposits. During the recent crisis the Landesbanks required assistance from the German Government, and the ratings agencies have suggested that in light of this the Joint Liability Scheme may have to be reformed. Interestingly these ratings agencies argue that the Scheme is appropriate for the savings banks and has served them well.

When a bank requires support from the Joint Liability Scheme different funds are used. First, the regional fund where the bank is located contributes, if this is not enough other regional funds contribute. Finally the reserves of the Landesbanken and Landesbausparkassen can be drawn on. This sequence ensures that there are a number of safety mechanisms in place and spreads risk across the group and in different business areas, reducing the chance that a shock in one area can destabilise the whole system. It is of interest that only the last stage of the sequence involves funds from the Landesbanks and Landesbausparkassen. The internal resources of the savings banks' regional funds in themselves provide a solid safety net for the savings banks. Arguably the banks might be better off in a liability scheme that did not include the, at present, far more risky Landesbanken. Their stability allowed them to increase lending volumes during the recent crisis. Moreover loan losses for the savings banks remained at a moderate 0.25% of average assets in 2009, suggesting that the financial support systems of the DSGV do not create moral hazard and lax lending standards.

There are a number of unique aspects of the savings banks that undoubtedly contribute to their success. First, is the 'dual bottom line' business model; second, the locally based, long-term lending strategies; and third, the support mechanisms that pool risk across the savings banks. These three elements together allow the savings banks to be both extensive in their scope whilst local in their focus, and ambitious in their lending practices while secure in their financial position.

**Credit Guarantees**

In addition to the spreading of risk across regions there is also an effective system of credit guarantees for specific loans.

In Germany, credit guarantee associations were set up soon after WWII as private self-help institutions to overcome the problem of collateral for small businesses seeking finance. The early collateral was provided by the pooled resources of members joined together in trade associations. Such institutions have remained shareholders to the present day having been joined by banks, insurance companies and

other financial backers. Since the 1980s they have organised themselves through the Association of German Guarantee Banks (VDB).

The VDB covers 18 'guarantee banks' which are based in, and confine their activities to, the specific German Länder (states) in which they operate. The banks are economically and legally independent and have different organisational and operating structures due to the fact that they arose as independent institutions and were later incorporated into the federal system of the VDB. Due to their geographic remit the banks have local and industry expertise, which is invaluable in assessing businesses within their area and their eligibility for a guarantee. The banks are not-for-profit, limited (stock institutions) whose shareholders are credit institutions (banks and investors), insurance companies and trade associations. They are regulated by the Federal Banking Act as credit institutions and so must comply with these regulations in their structure, organisational and business activities.[13] The guarantee banks issue sureties, covering loans, and guarantees, covering equity investments. In addition, unlike the British Enterprise Finance Guarantee, the system is not wholly funded by the Government. The surety covers 80% of the loan and the guarantee banks themselves take on 20-35% of the surety risk. The rest of the surety risk is borne by the Federal and Länder governments, in the form of a counter guarantee worth around 40% and 25% respectively, rising proportionally as the banks themselves take on less of the risk. There are slightly different risk distributions for guarantees.[14]

Guarantee banks issue sureties in the forms of an indemnity bond or a guarantee for an equity investor. Since the early 1990s, banks have also offered start-ups a 'surety without bank', which provides a guarantee (between €50,000 and €300,000) for a start-up before they have looked for a bank to support their business. A firm can obtain a guarantee or surety before, or after, going to the lender. However, they are assessed by both the guarantee bank and the lender. The borrower has to pay a one-off processing fee equal to 1.0-1.5% of the guaranteed credit amount and also has to pay an annual guarantee commission equal to 1.0-1.5% of the remaining guaranteed credit amount on 1 January each year, until the loan is paid off. The borrower may still have to post collateral to cover the unguaranteed part of the loan, but this is far less than would be required if the borrower had to cover the entire loan. Like the British scheme the provision of a guarantee is supposed to encourage banks to supply credit to attractive firms that do not have the necessary collateral to apply for a loan.

In its response to the problems created by the global financial crisis the German Government increased its support for the Association of Guarantee Banks by pledging to increase its share of counter guarantees by 10%, increasing the maximum guarantee amount per company from €1 million to €2

million and increasing the maximum guarantee coverage rate from 80% to 90%. The individual guarantee banks were also expected to increase their share of the total guarantee commitment to 50%. These reforms took the pressure off lenders and borrowers and placed a greater financial burden on the guarantee banks and the Government.

Two independent reports by the Institut Fur Mittelstandsokonomie an de Universitat Trier (Institute for SMEs at the University of Trier) in 2006 and 2010 found that the VDB made an important contribution to the German economy.[15] Moreover, a survey of lenders, carried out by the authors found that in 2006 only 5% of companies who had obtained a guarantee would have received a loan without the guarantee.

Between 2000 and 2009 the average annual value of loans covered by guarantees to German firms was €1.1 billion.[16] The return on the investments created with the aid of the guarantees is calculated at three times that amount (around €3 billion).[17] Aside from the quantitative benefits, the VDB also helped to promote competition by funding start-ups that otherwise would have struggled to secure credit. Between 1994 and 2004, 30% of the VDB's guarantees went to start-ups.[18] Guarantee banks in Germany play an important role in improving credit conditions for SMEs, alongside the German savings banks and cooperative banks that provided the loans for over 60% of the guarantees issued by the VDB in 2009.[19] Together these three institutions make a significant contribution to the credit provision available for SMEs in Germany. Furthermore, all three have continued their contribution through the constrained financial conditions of the last couple of years and in doing so have aided the German economy's recovery.

## Switzerland: a second contrasting picture

In the UK, the large commercial banks that dominate the market have struggled to provide credit to viable businesses. This failure to lend is also evident in the large commercial Swiss banks. However, unlike the UK, Switzerland has other banking institutions, most notably the cantonal banks, which have managed to maintain lending.

**Table 4: Credit provided by Swiss banks**

| | Credit (excluding mortgage lending) in CHF millions | |
|---|---|---|
| | UBS and Credit Suisse | Cantonal Banks |
| 2006 | 134,043 | 38,477 |
| 2007 | 174,924 | 41,119 |
| 2008 | 157,067 | 45,114 |
| 2009 | 127,778 | 46,038 |
| 2010 02 | 135,346 | 47,011 |
| 2010 05 | 136,113 | 47,595 |
| 2010 07 | 114,094 | 46,531 |

**Source: Swiss Central Bank**

The two large commercial banks lend a greater total amount of credit than the cantonal banks, because the cantonal banks hold 13% of Swiss banking assets compared to 61% for the two large commercial banks. Significantly however, the large commercial banks witnessed dramatic falls in lending in 2008 and again in 2009. In contrast the cantonal banks increased lending in 2008 and have kept the level relatively steady since then. This helped the Swiss economy during the recent economic downturn where the total output of industry never fell below 2005 levels and growth during the crisis was significantly above the OECD average.[20]

## Swiss Cantonal Banks

Switzerland is divided into 26 Cantons, highly independent federal states that have their own legislatures, constitutions, courts and governments. The Association of Swiss Cantonal Banks (ASCB) is composed of 24 cantonal banks, each of which occupies a separate canton.[21] The cantons either own the cantonal banks outright or they are the majority shareholder. Cantons are legally required to hold a minimum of one third of the bank's capital. Legally, some banks are public institutions owned by their cantonal government and some are owned jointly by private sector shareholders and the cantonal government.[22] Since a reform to the banking law in 1995 the cantonal governments no longer have to guarantee the deposits of their cantonal bank; however, most of them do provide a guarantee.[23] 14 out of the 21 cantonal banks that have a cantonal guarantee have to pay compensation for it.[24]

The cantonal banks vary in terms of size, Banque Cantonale du Jura is the smallest with assets of CHF 1,952,114,000 and the largest is Zürcher Kantonalbank with assets of CHF 115,078,590,000.[25] The differences in size are reflected in the types of activities that the cantonal banks engage in, the larger banks often compete with the large commercial banks, engage in investment banking and offer a wide range of other sophisticated banking services. In contrast, the smaller banks concentrate on savings, mortgages and local lending activities.

The 24 cantonal banks are far smaller than the two large commercial banks in terms of assets. Despite this, however, the cantonal banks are immensely important for the Swiss economy. While the two large banks orientate their business internationally, the local Swiss credit market is dominated by the cantonal banks, along with the regional savings banks and the cooperative banks. The cantonal banks redistribute credit efficiently around the Swiss economy, serving regions that are removed from the commercial centres of the country. This is especially important in the cantons of Switzerland that are not heavily urbanised, and whose businesses are not served by the large banks that concentrate their operations in the main cities. In these cases the cantonal bank is often the net capital importer into the canton, with the volume of loans to customers exceeding the corresponding volume of savings. Although far smaller in size than the two large commercial banks, the cantonal banks have a disproportionate share of the domestic market. This is evident when one examines deposits and domestic mortgages claims, shown in the table below.

**Table 5: Swiss Deposits and Mortgage Claims 2009**

| | Cantonal Banks | UBS and Credit Suisse |
|---|---|---|
| Savings and Deposits (In CHF millions) | 148,256 | 115,406 |
| Mortgage Claims (In CHF millions) | 245,803 | 231,266 |

**Source: Swiss Central Bank**

Each cantonal bank is committed to its canton. The banks, mostly set up during the 19th century, were originally created to serve industries to which the commercial banks felt were unprofitable to lend. This commitment is enshrined in Swiss Federal Law, with the Federal Constitution granting cantons the power to set up banks to serve the cantonal economy. The cantons can support the cantonal banks in activities that the bank carries out for the canton, but in all other areas the canton must ensure equal competition with the private sector. Also detailed in Federal Law is the 'factual duty' of a canton as the owner to support its bank, which many cantons promised to do during the financial crisis, although very few cantonal banks were seriously affected.[26] Some cantons have a legal ordinance which sets performance targets for the banks, often stipulating that they must ensure that they serve the needs of the local economy and population or provide viable competition for commercial banks. Consequently they have a 'dual bottom line orientation', similar to the German savings banks. Both banking groups must balance the need to generate profits with the commitment they have to their local economy. As well as having the support of their canton, the cantonal banks also benefit from being part of the ASCB. The association facilitates cooperation between the banks, this allows the banks to benefit from economies of scale in providing products such as pensions, investment advice and asset management. These services are provided by 20 network providers overseen by the ASCB, in an effort to 'produce centrally, provide locally'.[27] This local provision of services allows cantonal banks to create support schemes or products specifically tailored for firms in their local market. An example of this is given in the case studies below.

**Figure 2: Case studies of cantonal banks support for SMEs**

**1. Basler Kantonalbank (BKB) 'SME Pulse Program'.** The cantonal bank of the City Canton of Basel has a CHF 50 million finance program for start-ups, innovative companies and firms looking to finance take-overs or mergers. Firms that use BKB can apply for finance through the program. Their business plan and accounts are assessed by the bank. If successful, the bank provides credit in the form of a loan, an overdraft, a credit guarantee or a mixture of all three. The specifics of the loan depend on what it is used for, but up to 75% of the capital needed for the new venture can be provided, with funds ranging from a minimum of CHF 75,000 to CHF 3,000,000. The interest is decided on a case by case basis and the bank tries to ensure that it is manageable, while providing the bank with a sustainable return.

**2. Schwyzer Kantonalbank (SZKB) 'Innovation Foundation'.** The cantonal bank of the Schwyz Canton runs an 'Innovation Foundation' that seeks to promote innovative start-ups, SMEs and businesses looking to expand into innovative areas. The foundation is a fund of CHF 20 million which provides loans and equity investments of between CHF 300,000 and CHF 2 million to be repaid over 5 – 8 years. The fund seeks to attract companies to the canton, which does not support as much productive industry as other areas of Switzerland. The fund has provided credit to high-end manufacturing companies such as 'Dacuda' an innovative start-up that produces hand-held computer scanners that double up as mice for computers, and BoneArtis, a firm which produces artificial bone materials for medical use.

**Sources: Basler Kantonalbank, 2010, Schwyzer Kantonalbank, 2010**

Many cantons offer a range of incentives for businesses, such as subsidising the hiring of extra staff, reducing the interest on, and guaranteeing loans made by banks (in many cases the cantonal bank). The cantonal banks, work in tandem with other support schemes to ensure that businesses are supported (many under legal obligation imposed by the cantonal government). In many respects, cantons compete with one another to attract businesses so there is an incentive for all cantons, and their cantonal banks, to offer high quality, services tailored to local businesses and the local population. The cantonal banks conduct the majority of their business within their canton and this local focus is ensured by the obligation placed upon them by the cantonal government. The banks also follow a relatively conservative business model of providing credit to businesses and consumers, and taking in deposits. This business model is evident in the assets and liabilities of the ASCB. Liabilities to non-banks form 61% of the group's total liabilities, with 35% of the group's liabilities in the form of deposits from non-banks. In terms of assets, 71% are those from non-banks, in the form of loans and mortgage claims. As a result we can say that the main role of cantonal banks is to turn savings into long-term investments in the form

of mortgages and loans to businesses. This relatively conservative business model has served the cantonal banks well and more importantly provides each cantonal economy with a stable saving and investment facility. This stability is underlined by the profit and loss account figures for the ASCB group in comparison to the two large commercial banks, UBS and Credit Suisse.

**Table 6: Profit and loss account of ASCB and UBS and Credit Suisse**

| | Cantonal Banks | | UBS and Credit Suisse | |
|---|---|---|---|---|
| | Profit for the year (in CHF thousands) | Loss for the year (in CHF thousands) | Profit for the year (in CHF thousands) | Loss for the year (in CHF thousands) |
| 2003 | 1 20 7044 | | 7 053 302 | |
| 2004 | 1 576 247 | | 9 360 921 | |
| 2005 | 2 017 996 | | 17 006 760 | |
| 2006 | 2 416 175 | | 10 911 421 | |
| 2007 | 2 626 797 | | 2 847 494 | 4 251 294[28] |
| 2008 | 2 157 354 | 56 786 | | 38 185 291 |
| **Total Profit (profits-losses)** | **11 944 827** | | **4 743 313** | |

**Source: Swiss Central Bank**

The stability of the cantonal banks has benefitted the Swiss economy, providing a constant source of financial strength in contrast to the variable performance of the two large commercial banks. The annual profit of the two commercial banks is generally higher than that of the cantonal banks. This is to be expected given the fact that UBS and Credit Suisse are far larger. However, the instability of the two large commercial banks is also clear; profits range from CHF 2,847,494,000 to CHF 17,006,760,000 and in 2008 losses for the two banks reached CHF 38,185,291,000, effectively wiping out much of the profit earned in the previous five years. In contrast the cantonal banks saw steadily rising profits from 2003 and only relatively minor losses in 2008. Surprisingly the cantonal banks were CHF 7,201,514,000 more profitable than UBS and Credit Suisse during the period detailed.

Like the German savings banks the Swiss cantonal banks have proved resilient and successful during the recent financial crisis. In the period before the crisis, the majority of cantonal banks stuck to serving their canton's economy, providing credit to local businesses, rather than pursuing higher returns from innovative financial instruments. The influence of the cantonal government was important in this respect, with many of the ASCB banks legally required to serve their local economy. Furthermore, and in contrast to the large commercial banks of Switzerland, the cantonal banks did not rely on financial support from their respective canton or Swiss federal government. This was despite the fact that the majority of the banks pay an annual levy for the support of their canton, something which the commercial banks do not. Competition plays an important part in accounting for the continuing long-term success of the cantonal banks. Although the majority of the cantonal banks only have significant operations within their canton they are forced to compete with the commercial banks, the savings banks and the cooperative banks. Additionally, the cantons compete with one another to attract business and investment: so the cantonal banks indirectly compete with one another, in supporting their canton in this inter-cantonal competition. Yet a further reason for the cantonal banks' resilience is that they also cooperate with one another; this allows the group to benefit from services developed centrally, but administered locally at lower cost.

The strong competitive environment of the Swiss banking sector has helped produce efficient and successful cantonal banks. Counterbalancing this, the influence of the cantonal government has ensured that their pursuit of profit has not led the cantonal banks to stray from their common objective of providing stable financial services to their local economies.

## Lessons the UK can learn from the German and Swiss banking systems

A UK Competition Committee report in 2002 argued that a lack of competition in the UK banking industry was harming SMEs.[29]

There is some evidence of change in the UK banking system. As was noted above, some smaller banks have expanded their market share in terms of SME lending.[30] There have also been some new entrants to the sector.[31] However these changes have taken place against a trend of greater concentration in the UK banking market due to the spate of mergers brought about by the financial crisis. The problems in the UK's banking sector may have thus been exacerbated by the crisis despite some positive developments. What does seem to be clear is that the current situation does not allow the expansion of a bank or group of banks which could replicate some of the successes of the German savings banks, or Swiss cantonal banks. Could we encourage localised banking on the Swiss/German model?

In recent years British Governments have urged banks to lend more to SMEs only to find their wishes ignored. In Germany the situation is different because the savings banks are bound by the savings bank laws of the Länder. Similarly in the Swiss case the cantonal banks are owned, and in many cases set performance guidelines, by their cantonal government. The 'dual bottom line orientation' of both sets of banks is defined by local government and supported by the Swiss and German Federal Governments.

But how could the British Government create a legal framework that would support locally-oriented, savings banks? Section 40 of the Banking Act of the Federal Republic of Germany, created after WWII, sets down which banks can be set up as savings banks:

*(1) public savings banks holding a licence in accordance with section 32;*[32]

*(2) other enterprises which were legitimately using such a term under former regulations;*

*(3) enterprises which by virtue of their articles of association, display special features (in particular, business objectives geared to the common weal and a restriction of their principal activities to the economic locality in which the enterprise is domiciled).*[33]

Clause 1 defines a savings bank as publicly owned. Clause 3 decrees that a savings bank must define, in its articles of association, how it will provide services which benefit the local economy. It also requires savings banks to limit their activity to their 'economic locality'. However, as stated above it is the Länder laws which govern the savings banks and, importantly, define how the banks' articles of association must be drawn up. Each Land decrees in its savings bank law (sparkassengesetz) how savings banks in its

jurisdiction must be established, owned, managed, regulated and how it must interact with the regional and national savings bank associations. Most importantly it defines the tasks of the bank and how they should be carried out, as this excerpt from section 2, clause 2 of the Thuringian Savings Bank Act (ThürSpKG) makes clear:

*Business aims, public remit*

(1) *Savings banks are businesses serving the common good with the task to ascertain the provision of financial services within their sector, in particular to provide opportunity for secure financial investment. Savings banks strengthen competition within the financial sector. They provide services for the public, the economy, in particular the middle classes and the public services, in due consideration of the requirements of the markets. They support positive attitudes towards saving, accumulation of wealth and the monetary education of the young.*

(2) *Savings banks conduct business under the guidance of the Savings Banks Act and represent the interest of their clients. Business regarding central savings banks, mortgage banks, regarding property, investment and insurance should be pursued in collaboration with the respective branches of the Organisation of Savings Banks in Thuringia.*

(3) *Savings banks conduct their business following the principles and standard practices of business, under due consideration of their public remit. Profit is not the main purpose of their business.*[34]

Savings banks in the Thuringia Land must base their articles of association on this section, and the rest of the Thuringian Savings Bank Act. Any deviation from this must be approved by the Thuringian government.

**A British Legal Framework**

To encourage localised banking the British Government would need a similar legal framework requiring banks to serve their local economy, dedicate resources to appraising local firms and provide products tailored to the needs of their local clients. Currently, British banks see such activity as relatively unprofitable in comparison to serving large corporate clients and engaging in activity on international capital markets. One possibility could be for local authorities to create banks as public corporations. This model would be similar to the German and Swiss type where a public authority defines the remit of the bank. The German dual board structure allows each local authority to maintain a presence on the

board of the bank without participating in the daily running of the bank. As in Germany its task would be to ensure it was sticking to its articles of association and serving local industry and the local economy.

The degree of governmental involvement is not as important as ensuring that the bank or banks, are constituted and mandated to serve local industry. The British Government could ensure this directly through involvement in the bank, or indirectly by creating a legal framework that holds the bank responsible if it deviates from its prescribed mandate. In either case the bank or banks would have the following features:

1. **A dual bottom line orientation**. This should be prescribed either by law or its activities must be overseen by local representatives who ensure that the executives and the branch managers take local needs into account.
2. **No ordinary shareholders (except for local representatives).** This would ensure that it is committed to using profits to fund its operations rather than providing dividends. Like the Swiss cantonal banks, shareholders could be permitted but they would have no say in how the bank is run.
3. **Subject to the same regulatory framework as all other banks**. The banks that have direct government involvement must not receive a government subsidy, and should compete with private institutions in their local market. It may be necessary to use public funds initially but once a bank was on a stable financial footing further support would not be necessary.
4. **The individual branches of the banks should have autonomy to pursue lending strategies they deem appropriate for their local market**. This would ensure that the banks were able to create tailored credit relationships with local firms. However, this autonomy would be circumscribed by the requirement that all banks follow the dual bottom line goals of turning a profit and supporting local businesses and individuals.
5. **Operate as part of a federal system so that risks are pooled.** The central agency would be composed of representatives from local branches and representatives from local administrative councils.
6. **Not be permitted to engage in risky investment activities**. Proprietary trading, that is using the bank's profits to trade to generate further income, would not be allowed.
7. **A group liability scheme should pool resources to provide liquidity and capital in the event of a branch running into financial difficulties**. This would ensure that banks have the support they need to extend credit to companies that are attractive but which may lack collateral.

NOTES

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[1] Dr Stuart Fraser *Small Firms in the Credit Crisis: Evidence from the UK Survey of SME Finances*, Centre for Small and Medium-Sized Enterprises, Warwick Business School, University of Warwick, 2009.
[2] European Commission, Enterprise and Industry Department, *SBA Fact Sheet – United Kingdom*. Data from 2004, 2005 Eurostat SBS data base.
[3] Results do not add up to 100 because not all German lenders feature in the table.
[4] An opinion poll conducted by the opinion research firm FORSA. Quoted in R. Ayadi, R.H. Schmidt, S.C. Valverde, E. Arbak and F.R. Fernandez, *Investigating Diversity in the Banking Sector in Europe: The Performance and Role of Savings Banks*, Centre for European Policy Studies, 2009.
[5] R. Ayadi, R.H. Schmidt, S.C. Valverde, E. Arbak and F.R. Fernandez, *Investigating Diversity in the Banking Sector in Europe: The Performance and Role of Savings Banks*, Centre for European Policy Studies, 2009.
[6] According to evidence from Dr Stuart Fraser *Small Firms in the Credit Crisis: Evidence from the UK Survey of SME Finances*, Centre for Small and Medium-Sized Enterprises, Warwick Business School, University of Warwick, 2009 and KEW/KfW *Grundungspanel,* 2009.
[7] In the 2nd quarter of 2010 the German economy registered growth of 2.2%, the best performance in decades.
[8] In this structure the savings banks configure to the fundamentals of the German corporate governance system: where the supervisory board or the 'Aufsichtsrat' represents, not only, the interests of shareholders, but also that of employees and often the public interest too.
[9] A. D. Brunner, *Germany's Three-Pillar banking System: Cross-country Perspectives in Europe,* 2004.
[10] However the same cannot be said for all the members of the DSGV. The Landesbanks suffered during the crisis because they moved away from the DSGV model through their exposure to asset backed securities. The continued weakness of the Landesbanks is an issue of concern for the DSGV group, however ratings agencies, while noting this, consistently judge the savings banks to be the source of the group's financial strength and stability.
[11] See amongst others: Allen N. Berger and Gregory F. Udell, *A More Complete Conceptual Framework for SME Finance*, Prepared for presentation at the World Bank Conference on Small and Medium Enterprises: Overcoming Growth Constraints, 2004. Berger and Udell both criticize some of the simplistic assumptions of the distinction yet still use it in their study.
[12] Moody's Investors Service, Credit Analysis, *Sparkassen-Finanzgruppe'*, 2009. DBRS Rating Report, *'Sparkassen-Finanzgruppe*, 2009.
[13] Axel G. Schmidt and Guy Selbherr *Tasks, Organization and Economic Benefits of German Guarantee Banks,* Journal for SME Development, 2009.
[14] See: Axel G. Schmidt and Guy Selbherr *Tasks, Organization and Economic Benefits of German Guarantee Banks,* Journal for SME Development, 2009.
[15] Institut Fur Mittelstandsokonomie an der Universitat Trier, *Macroeconomic benefits of the German Guarantee Banks under the framework conditions of the global financial and economic crisis*, Alex G. Schmidt and Marco Van Elkan, June 30 2010 and Institut Fur Mittelstandsokonomie an der Universitat Trier, *Macroeconomic benefits of the German Guarantee Banks,* Alex G. Schmidt and Marco Van Elkan, 2006.
[16] VDB Annual Report 2009.
[17] Institut Fur Mittelstandsokonomie an der Universitat Trier, *Macroeconomic benefits of the German Guarantee Banks under the framework conditions of the global financial and economic crisis*, Alex G. Schmidt and Marco Van Elkan, June 30 2010.
[18] Institut Fur Mittelstandsokonomie an der Universitat Trier, *Macroeconomic benefits of the German Guarantee Banks,* Alex G. Schmidt and Marco Van Elkan, 2006.
[19] VDB Annual Report, 2009.
[20] OECD - http://stats.oecd.org/Index.aspx?DatasetCode=SNA_TABLE1
[21] Yet there are only 24 banks as the canton Appenzell Ausserrhoden sold its bank to UBS and the canton Solothurn privatised its bank in 1995, decisions agreed by the electorates in the two cantons.
[22] There has been talk of partially privatising some of the cantonal banks, however the problems of the financial crisis, and the positive performance of the banks, have halted any immediate plans.

[23]The cantonal bank Banque Cantonale Vaudoise does not have a guarantee and the Banque Cantonale de Geneve has only a partial guarantee, the canton of Berne plans to phase out the state guarantee by 2012.

[24] Dr. iur. Peter Hänni, LL.M., Professor University of Fribourg, Switzerland, In collaboration with MLaw Thomas Meier, *The State and the Financial Industry in Switzerland*, 2010.

[25] Swiss Central Bank - http://www.snb.ch/ext/stats/bankench/pdf/deen/BV_1_00_KB.pdf

[26] Since their creation only 6 cantonal banks have run into financial difficulty. Four were bailed out, two were liquidised.

[27] The Association of Swiss Cantonal Banks, *The Cantonal Banks, A Swiss Banking Group,* 2010.

[28] The Swiss Central Bank groups banks together and gives the profits and the losses for the banks in the group. The two big banks managed to post both a profit and a loss for 2007 because Credit Suisse posted a profit while UBS posted a loss. The same applies for the cantonal banks in 2008, when some posted a loss but the majority posted a profit.

[29] The Competition Commission, *The supply of banking services by clearing banks to small and medium-sized enterprises, A report on the supply of banking services by clearing banks to small and medium-sized enterprises within the UK*, Presented to Parliament by the Secretary of State for Trade and Industry and the Chancellor of the Exchequer by Command of Her Majesty, March 2002.

[30] See the overview of the work of Dr Stuart Fraser given in section 1, p.4.

[31] Aldermore is one new bank with 8 offices in the UK who has been offering mortgage and loan services to individuals and SMEs since 2009. Since mid-2009 the bank has lent around £300m to SMEs and processed 500 mortgage applications from companies each quarter. The bank has stated that it expects to turn a profit this year.

[32] The section of the German Banking Act which describes which institutions can obtain a banking licence.

[33] *Banking Act of the Federal Republic of Germany (Kreditwesengesetz, KWG),* Translation by Deutsche Bundesbank.

[34] Thüringer Sparkassengesetz (ThürSpKG) Vom 19. Juli 1994.