Sharon Donnery: Evolving with the times, credit unions in a changing landscape

Remarks by Ms Sharon Donnery, Deputy Governor of the Central Bank of Ireland, at the Irish League of Credit Unions (ILCU) Conference, Dublin, 19 November 2024.

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I am delighted to be here to speak to you all – in particular as I near the end of my current role, and prepare to take up my new one at the European Central Bank.[1]

As a former Registrar of Credit Unions I know the sector, and its potential, well.

And indeed in the decade since I was first appointed Registrar, about half of that time I have had responsibility for Credit Unions as some part of my role.

In my remarks today I would like to reflect a little on how the sector has developed during this time (including the legislative and regulatory framework) before looking ahead to changes to come – and how Credit Unions must continue to evolve to meet the challenges of a changing and increasingly competitive financial sector.

A decade of change

While of course maintaining its core purpose, the last 10 years has seen the sector undergo significant change – in terms of its size, shape and the services you offer.

Since 2014, the number of credit unions has halved; and the number of large credit unions[2] has more than doubled.

Total assets in the sector has grown by 50% – from €14bn in 2014 to just over €21bn in 2024.

Throughout this time, reserves have strengthened – with average reserve ratio now at 16.5%, compared to the statutory minimum of 10%.

And total loans, for their part, have grown by 73% in the last 10 years.

Interestingly, half of that loan growth has taken place in the last 2 years – with total loans rising by €1.5bn since 2022, to now stand just above €7bn.

This asset and loan growth has been complimented by a wider range of products and services that you can, and are, offering – including mortgages, business loans, current accounts and mobile banking.

Importantly, throughout this time your governance and risk management capabilities have also grown alongside your loan books – two crucial components to delivering "strong credit unions in safe hands", which I will touch on again later.

However, while all significant, with loan to asset ratios at just 33% I think we can agree that there is more to be done if credit unions are to play the role they want to play in Ireland's retail banking landscape.

This is particularly the case in the context of a rapidly changing financial services sector.

As I have said before, the last decade has seen significant changes to Ireland's financial sector – becoming larger, more diverse, more international, and more complex.[3]

Ireland's banking ecosystem has transformed, going from being dominated by largely homogenous, traditional and domestic retail-focused entities, to now being characterised by a broad range of participants – including partial service providers, value change disrupters and entities serving Europe and beyond.

This includes the rise in Payments and E-Money Institutions – with over 50 of these entities authorised now in Ireland (3 times the number authorised in 2016) – with a more than tenfold increase in the amount of customer funds held by these entities during that time, now standing at over €8bn – not to mention neobanks, and other payments and credit providers.

This reflects a financial sector that is becoming increasingly digital, driven by consumer expectations – even if the digitalisation of retail banking has so far lagged behind technological developments.

Still, 86% of Irish consumers report using mobile banking – with mobile apps now cited as the main form of contact with their providers.[4] Contactless payments now make up 85% of point of sale transactions – with half of these contactless payments done using mobile wallets.[5]

These sort of statistics were unthinkable just 10 years ago.

In addition to the development of the credit union sector and the system in which you operate, throughout the last decade there has also been significant legislative and regulatory change – much of which have been advocated for by the sector.

This includes:

- Revised lending regulations in 2019, to allow greater flexibility for Credit Unions to diversify your loan books and engage in more long term lending;

- Investment regulations, most recently updated in 2020, to introduce new investment classes in which you can invest funds not lent out to your members;

- And the Credit Union (Amendment) Act 2023 aimed at enabling greater collaboration between credit unions (for example referrals and loan participation) as well as forward looking initiatives to support further business model changes (such as corporate credit unions).

These regulations all follow the pattern of enabling you to, prudently, do more. And as we have said before the Central Bank believes the recent legislative changes in particular are consequential – and provide huge opportunities for the sector to collaborate and develop.

With some particular exceptions, which I will come to shortly, the broad regulatory framework for Credit Unions is now stable and appropriate – providing you with the means to properly and prudently develop and deliver your business models in the interest of your members.

So the Credit Union sector is moving – loan books are growing; and many of you are modernising.

The sector has also broadly maintained resilience over the last decade; and the framework has evolved to allow the prudent development of Credit Unions, including through new products and services.

These are all positives, but as I said earlier they are not enough.

Business model challenges, notwithstanding the good developments of the last few years, remain.

The evolving nature of the financial sector, and the increasing expectations of consumers around digitalisation of financial services, make the challenge to address these all the more pressing.

As you know yourselves, you must evolve further if you are to continue to sustainably serve your members into the future.

This involves delivering on the strategic vision of the retail banking review to develop a strategy to "safely and sustainably provide a universal product and service offering, which is community based, and which is offered to all credit union members, directly or on a referral basis."

For our part, as I have said, the legislative and regulatory framework has already evolved to ensure you can do more. And for the most part the challenge now is for the sector to deliver – taking opportunities in line with your strategic objectives and risk appetite.

Having said that, we have always maintained that where regulatory changes are necessary, we will be responsive. And this brings me to one area where we will be making changes in the near future, to ensure you have the scope and the flexibility to deliver on your strategic ambition.

I mentioned the lending regulations, which enabled credit unions to engage in long term lending.

These were an important set of regulations, allowing you to do more. When they were introduced they came with important guardrails, in the form of limits, as the sector re-engaged in longer term lending, including mortgages.

I have heard some criticism from the sector about these limits. But I am firmly of the view that these provided essential guardrails at the outset, given the need for Credit Unions to build the capacity and capabilities for this type of lending – a type of lending which needs different underwriting skills, not to mention more sophisticated asset and liability management.

Over the years since these lending regulations were introduced, I am happy to say that our supervisory experience tells us that many credit unions in the sector have built this capacity, and they have prudently engaged in business and mortgage lending.

11% of Credit Union loan books are now in mortgages.

And while there is still capacity within those limits, and indeed ample capacity at a sectoral level, in light of how the sector has developed in recent years – from a capability and skills perspective – and how it could develop in future years, in particular in light of recent legislation, we have undertaken a review those limits.

In early December we will publish the outcome of that review, and launch a public consultation on proposed targeted – but significant – changes to the lending framework, including changes to concentration limits and to certain underwriting requirements.

Our hope is that these changes will enable those credit unions that wish to, to undertake increased lending activity – diversifying your loan books, improving your loan to asset ratios, and better delivering for your members.

And our firm expectation is that you will continue to prudently build your books in these areas of the market, and continue to build skills, capacity and expertise in this type of lending.

This brings me to the final topic I would like to address today.

Maturing the sector

Now, it is not often you hear a regulator asking a sector to grow its loan book – to say that we are changing the rules to enable you to do more.

So you won't be surprised to hear me say that with opportunities come responsibilities.

And so while the sector continues to mature its offerings – it must also continue to mature its risk management and governance.

To be fair, this has been a focus of both the Registry and Credit Unions over the last decade.

I only say, as I have said to other sectors, that it is crucial that the development of your business models do not outpace the development of your control frameworks. And a well-resourced and effective Internal Audit function plays a key role in this regard.

A number of recent regulatory interventions should also assist, and which you need to properly adopt and implement:

- This includes the Individual Accountability Framework, which seeks to help underpin sound governance across the financial sector by setting out clearly what is expected of well-run firms;
- It also includes the minimum competency code, which should equally underpin and build on the existing high levels of knowledge and expertise in the sector.

But while the financial resilience of Credit Unions has in some ways been fortified over the last decade, resilience is not just about metrics and ratios; it is not just about regulations and rules.

Equally, while long term resilience also relies on sustainable business models, as I have said for those business models to be sustainable they must not only adapt to the changing environment, but your capabilities and controls must adapt alongside them.

This is the only way you will safely and sustainably serve your members into the future.

In that regard, the first and most important defence is always the good governance and risk management of firms themselves; and the people in this room, and Internal Audit in general, plays a crucial role in this.

One particular example of this is ICT risk and operational resilience – an increasingly fundamental focus for providers of financial services. As you rightly digitise, and as you become increasingly reliant on outsourcing, in line with the wider financial sector it is crucial that you focus on strengthening your operational resilience and disruption preparedness.[6]

This is not about regulation, this is not about compliance; this is fundamentally about ensuring you are safe and sound in a digital age – protecting yourselves and the members who you serve.

Finally, looking ahead, and as we have stated publicly before as part of our further work on the Consumer Protection Code, we plan to undertake a consideration of the full application of the revised Code to credit unions in due course.

This is simply in order to ensure your members are afforded the same protections as other consumer of financial services – something which will be particularly important as credit unions further develop the scope and depth of the services that they provide.

While I expect that the sector will not object to adopting a framework that seeks to secure the best interests of consumers, we also know it will require consideration – in particular to how it will fit with the wider framework for credit unions. And so it will take time, and is not part of the ongoing review of the Code due to be finalised and published early next year.

Conclusion

So, to sum up: the sector has changed significantly in the last 10 years. So too has the regulatory framework – with some more to come.

But regulation is not an end in itself; rather it is a means to ensuring you safety and sustainably fulfil your purpose for your members.

Furthermore while necessary for good outcomes, it is not sufficient – with a responsibility of your own to ensure good governance and risk management, with Internal Audit playing an important role in evaluating whether risks are being properly identified, assessed and controlled.

Equally, enabling regulations are not enough to deliver business model change – you have to go and take the opportunities they have enabled you to seize.

And given the increasingly competitive financial sector landscape, and the co-operative nature of the sector, I would suggest that that is best achieved through co-operation, and taking advantage of the scale collectively you can provide.

In that regard, following a series of legislative and regulatory changes to allow credit unions to do more, including proposals on lending to be published shortly, you now have to go and do it – safely and sustainably in the interest of your members.

And so from now I would suggest the focus should be on prudently growing your loan book, rather than trying to change the rule book.

Thank you

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[1] With thanks to Cian O'Laoide and Eamon Clarke for their help in preparing these remarks.

[2] i.e. with assets greater than €100m

[3] See Donnery: Banking – Past, Present and Future and also Regulatory and Supervisory Outlook 2024 (PDF 2.08MB) Section 4

[4] Department of Finance Consumer Sentiment Banking Survey August 2023 (PDF#PAGE=NULL 6.68MB)

[5] See also Madouros, The Evolving payment landscape in Ireland March 2024

[6] See also ICURN 2023 Peer Review (PDF 1.69MB)