

Dear Friends

Thank you very much for the help and support you have given to the Institute in the past year. I think it is safe to say we have both drawn on that support and built on it too. For the new year we hope to advance as a new Institute in many respects, an Institute looking to learn from its critics and one which is willing to respond to their suggestions.

I hope that together we have the élan to respond to all of the challenges present themselves in Europe: Introduction of the EURO, safe passage through the present economic crisis, reducing unemployment, development investment in Eastern Europe, an increase in homeownership, the privatisation of public bodies, structural changes in former State services, reorganisation of pension provision, massive tax reform, the opening of the capital markets for small investors, a consolidation of developments in education and training and dealing with the public debt and especially fighting discrimination and poverty.

1. Financial services are at the centre of everything. They take capital from where it is saved (private pensions) and put it to use where investment is needed (small and medium-sized businesses, self-employment, high-technology sectors, education and training, house building) to create confidence in the economy, to put incentives in place and use rational economic activity as well as new technology to achieve smooth and efficient economic communication.

The climate for those who in charge of financial services is not the best. The press and general public increasingly are losing **trust in the banks** regarding their key role in the current economic situation. Germany's big banks suffer a severe image crisis. While Deutsche Bank certainly has had to concern itself with the Schneider-Affair, Dresdner Bank is seen to be sneering over tax evasion by its directors. The discussion about „the power of the banks“ in the *Bundestag*, can be said to have left a negative feeling in its wake. Deregulation, although apparently necessary, does not address the question of bank power and responsibility.

However, in 1998 we should not wish for **banks** to have less **power** but rather as much power as is necessary for them to envisage social and economic progress and engage themselves in the search for solutions. We need banks to have this power for the following reasons: the first EU-Banking Directive gives these institutions a European wide quasi-monopoly in financial services as does the fact that know-how, infrastructure and the potential for these tasks are all concentrated in their hands. Banks and insurance companies are therefore at the centre. The second EU-Banking Directive as well as the various insurance Directives liberate them from much of the former supervision through the new principles of mutual recognition and home country control. In a democratic EU, concentrations of power should always go hand in hand with increased responsibility and public accountability.

Power means responsibility and as such it is also essential as an instrument of control in the market economy. It follows that it is not the power of banks which should be the subject of public criticism, rather any lack of responsibility in the conduct of their day-to-day business; not the number of members on the bank's supervisory board, rather what decisions are taken by it; not the level of credit advanced but to whom and for what purpose power is exercised; not merger and ac-

quisition activity in general but its effects on jobs and regional prosperity - these must all be at the centre of the discussion. Banks and insurance companies should be freed from their historical mystification as either gods or devils. Just as for any economic actor, any irresponsible conduct of business itself in the financial services sector where public scrutiny does not reach, should be monitored. The meaning of „credit“ to banks - to trust, to advance money wherever tasks present themselves, should become the yard stick for monitoring „credit institutions“. New goals such as customer orientation and regional commitment, self-employment initiatives and the advancement of SMEs, the application of new technology to customer needs, life-line basic banking services, alternative products based around solidarity in private pensions etc - all need support from the general public.

2. In this way long term reciprocal trust itself becomes a service which will have quite decisive repercussions for the economy.

In any event, this is what the English economist Paul Ormerod of the London School of Economics proposes in his refreshing book, „The Death of Economics“ (London, Faber & Faber 1994). The book deals (even with its own methodology) with the pure quantitative orientation of monetarist economic teaching, which, in its rule of success for the economy actually is „dead“ according to its ability to give predictions even though it continues to rise as the current political ideology. Ormerod queries how much credibility a bridge engineer of the same standard as our economic and political advisors would have, had he made similarly wrong prognoses concerning the steadfastness of a hypothetical bridge - as have our economic thinkers on the questions of unemployment, national disparities and the rate of growth. Economics, according to Ormerod, does not even really have a linear constitution, a basic premise - paradoxically this only appears in the mathematical formulae of the reigning economic thinking. It is much more founded in trust, politics, law and morals, equally in rate of growth, technology and unforeseen events. Accordingly, quantitative methods are applicable and very important in the short term. It is only for long-term developments that simple mathematics have little to offer and thus more open models such as chaos theory in mathematics and the natural sciences or game theory promise a better application.

The reason why we quote him here does not however lie in his exciting thoughts concerning unemployment with the refutation of the so called „natural rate“, which one must accept in an economy with low inflation.

With his theory, which proceeds from a comprehensive understanding of classical economics, Ormerod seeks to **contradict the concept of inevitability** in which politics, morals and social responsibility seem to be inapplicable, according to current thinking, to the inescapable need for the market to be left unfettered in the long-term. In this way Keynes is freed from his own followers and supported by an exciting mathematical and empirical discovery: the theory of using public spending as a market instrument and the supporting of demand through higher wages and social benefits - in contrast to the business cycle and in times of crisis - is only the (thoroughly questionable) application of a far more important insight on the importance of psychology in practical political economics on the short run. With his quotation „In the long-term we are all dead“ Keynes mocked all of the critics who wanted to believe that the market would always correct itself on a long-term view.

Our economy needs short-term improvements and the current economic situation in continental Europe certainly supports this view. Almost five million people are registered as unemployed in Germany and the growing levels of poverty are comparable with a draught, a draught where rain has been long awaited and may even come too late for certain levels of soil. Transposed from the simile, this means that for certain people, families and communities, economic recovery may come too late and we all will pay the bill through dramatically increased unproductive policing and welfare spending not to say the devastating effects on the quality of our still enviable community life in Europe.

What can be done in the short term and what does this have to do with banks? Keynes entered into this problem with his proposition of a psychological law that demand is always based around historical factors and in this way blocks recovery, which may be understood from the typical components in banks' assessments of credit worthiness. Economic recovery requires dynamic, future-looking developments. Trust and a climate for investment has to be created. To this end,

trustworthiness is required which politicians are no longer able to offer with their sneering projections of a halving of unemployment.

Keynes proceeded from the proposition that every investor is really only concerned with the money in his own pocket. What he meant by this was that the State can only trigger renewed economic confidence by giving benefit recipients more money who will in turn spend this at the baker's, the bakery will then take on another employee to ensure sufficient production and this employee will then buy himself a new suit at the tailor's. In this way the spiralling vicious circle of impoverishment is stemmed and turned into a virtuous circle

However as with Keynes' critics, Ormerod believes that ultimately this public spending process is too expensive and the long term consequences from giving false market values result in inflation, reduced productivity and backwardness.

At the end of his book he gives us the task of widening such confidence otherwise than through public spending, to use the human resources of social cohesion such as morality and solidarity which still exist in Europe and to put money into the hands of people who will invest and spend it.

This all concerns banking business and what we have described as „social banking“.

For example in Professor Leo Schuster's book (*Die Gesellschaftliche Verantwortung der Banken, Erich Schmidt, Berlin 1997 p 205 ff - The Social Responsibility of Banks*) under the title „*Social Banking - Ansätze und Erfahrungen über die Integration sozialer Zielsetzungen in privatwirtschaftlicher Finanzdienstleistungen*“ (Comments and experiences concerning the integration of social goals with private financial services). In our study on „Social Responsibility of Credit Institutions“ which we undertook together with Malcolm Lynch *Solicitors* in Leeds and Benoît Granger (EPICEA) in Paris for DG XXIII these ideas were more deeply developed in English, German and French. This study - which will be published in 1998 by Nomos (Baden-Baden) may be purchased, like all IFF studies, at our Institute. For the English speaking community we have produced essays on „Social Banking and Affordable Housing in Germany“ (Reifner/Pfau) edited by Prof. Frowen (Cambridge) in a forthcoming book on Banking and Ethics as well as an essay on „New Financial Products for Inclusive Banking“ (Reifner) in: New Policy Institute/UK Social Investment Forum (Eds) „Financial Exclusion: Can Mutuality Fill The Gap“ (London 1997). Our book on Small Business Financing (Reifner/Evers) will also be published this summer in the new IFF book series by Nomos in English and possibly in French and Italian.

Banking business which is versatile to future needs as well as ready to accept SME risks is required, in the new self-sufficiency or social context, for infrastructure and housebuilding through credit, participation and investment - **creating new hope** where what is reaped will again be sown. We need investment to a much lesser extent in large scale construction projects, tax-efficient savings schemes and money markets which only serve wealth rather than putting that money to good general use.

In this respect banks need **know-how** on how to progress and market financial services and products in these areas from the point of view of their own development. Banks must also have the desire to become pioneers who can demonstrate themselves to be specialists in creating income, where this is altogether necessary for society. This new form of commercial banking, and we are at one with Ormerod on this point, can only bring something about when it shows the highest quality standards demonstrating how profits can still be made in these areas.

There are examples of this. Ormerod shows that the extent to which unemployment oscillates and is coupled to innovation, politics and cultural phenomena. Ways to improve this environment through best practice approaches, through Community Reinvestment Act type disclosure and through political pressure have all been addressed in our above mentioned study for the Social Economy Unit of the European Commission as well as in the Micro-Finance work.

When the general public demand of banks that the latter undertake confidence creating activities - actually lending money in socially beneficial areas rather than disguising day-to-day business activity with cultural or charitable giving - we will arrive at a new state of co-operation between the banks and the people, co-operation which has the quality of a productive lending business: critical partnership and measured trust and confidence.

3. You may be interested to hear about past and future IFF projects. Please check our internet pages at the new address **www.iff-hamburg.de**

IFF has started a **series of books** published by Rowohlt giving the general public a new form of financial advice which is independent, responsible and critical. Seven financial advice books on various contemporary issues in financial services have already been published and another five are at the printers for 1998. Our debt advice program **CADAS for Windows** - which we have been able to develop further and distribute thanks to a grant by the German Savings Bank Association - has, with the help of DG XXIV, been translated into English and French and will hopefully enable international cooperation in this field following its overwhelming success in Germany. We are already working on the next improved version. Similar projects are underway on our other software which can analyse and calculate any financial product in consumer credit (CALS), defaulting credit relations (FOAB) as well as housing finance, life insurance and investment (BAUFUE) are in the pipeline - CALS is now available in English, French and Italian.

Much of our work has been in **debt advice** support, proposals for out-of-court settlements in bankruptcy cases (for the German Ministry of Justice), on the situation of overindebtedness in Germany as well as APR legislation in Europe (for DG XXIV). Another important project concerned a legal and factual analysis of combined endowment insurance with fixed **mortgage loans** (for the German magazine *Stiftung Warentest*).

Our ideas on how **private law** may incorporate and reward socially responsible behaviour by financial institutions have been presented at different international conferences and will lead to English language publications on the use of „Good Faith in Financial Services“ (published in Sheffield by G. Howells and R. Brownsworth) and approaches of contract interpretation where socially embedded claims are at stake („The Lost Penny“ published by T. Wilhelmsson in Helsinki)

In the field of **social banking** and regional responsibility we have developed ideas and contributions on **micro-lending, small business financing, low income housing finance** in various projects for banks and public institutions especially in cooperation with the German Savings Banks.

Our most important international project is still the FIS-database. With the help of DG XXIV we look forward to presenting a user-friendly and comprehensive CD-ROM resource where our partners in seven countries of the EU will present their work and data on financial services issues in their respective countries. This unique data base has more than 20,000 full text data sets covering legal and factual information on all issues that especially relate to consumer and client orientation in financial services. Under the new brand name of **FIS-Money Advice** the data is already available on the Internet at our new address www.iff-hamburg.de - where all of us at IFF may also personally be reached directly by e-mail in the format [first name].[second name]@iff-hamburg.de. By June 1998 the combined

system will be technically complete with the CD-ROM, an HTML-Database with (selected and commented) links to other sources in the Internet (both in five different languages), a separately available Access-Database for decentralised input of data by all collaborating organisations. We have asked the European Commission DG XXIV to support the further development of its contents and towards the goal of making the project self-financing. For 1999 we hope to be able financially to support our partners as far as the input of data relating to the EURO (legal, economic, consumer advice, newspaper articles etc.) is concerned. A special edition of the CD-ROM will be presented to the broader public. Our network is changing and improving and new partners are joining us. Particularly in the Mecca of financial services in Europe, the UK, the London based **Policy Studies Institute** intends to build up a similarly rich database as has been done in Germany in collaboration with the National Consumer Council, the Social Investment Forum and with the support of the Office of Fair Trading. This all promises a breakthrough on the international level with further developments hopefully arising soon in France and Belgium, where data on credit law are also rather complete.

The revised concept of FIS-Money Advice envisages vast distribution and easy access in the whole of Europe through the Internet and a low price CD-ROM for consumers, consumer organisations, the media, financial advisers and financial institutions. The partners in the FIS Network who will organise the information input appear as the main organisation responsible in the national context. Also, on the Internet FIS-Money Advice will become an independent address. A decentralized cooperative group of organisations able and willing to build up their own national data base in their respective language focused on issues of interest for „stake holders“ in financial services will show that international cooperation can provide exciting tools for all of us to be kept in the information loop as much as we need in the 21st century.

The main **financial resources** will stem not from users but from suppliers of information such as state agencies and commercial financing institutions. We hope that each partner can levy enough national support for the own input and up-dates costs. In Germany we will seek to „rent out“ space to banks and other financial institutions as well as commercial advisers and lawyers where they may introduce themselves in a special section under our choice of headings. This will help to get additional information from financial industries closer to the needs of the public on one hand and on the other further comparative information. Besides this new source of income we invite all other bodies concerned with financial information to use our product to convey their work to a general European and world wide public. Such proposals have been discussed with ILO officials in Geneva for their intended data base on best practice examples in social investment and development banking and has been equally proposed to DG XXIII. Regarding the multitude of failed data bases in consumer protection and social investment all parties should think twice before they invest into a separate undertaking. The enormous cost cannot be underestimated as we have experienced in the last 10 years. It is comparatively easy and cheap to create databases, but it is extremely difficult and costly continually to update them and ensure continued usage.

This new year letter can also serve as the starting point for the preparation of the fifth conference on financial services which, if our Swedish colleagues can make it possible, will be held in **Göteborg from September 23 to 25, 1999**. The issue of the conference will be **Access to Financial Services**. As has already been the case in Hamburg 1989, Birmingham 1992, Bergamo 1993 and Strasbourg 1996 it

will seek to bring together researchers, consumer organisations, debt advice organisations, trade unions, social investment activists with bankers, insurers, politicians and development agencies. „Access“ will cover such issues as basic bank accounts and new products for high risk clients, new forms of demand and marketing as well as legislation and jurisprudence concerning the transparency of financial markets and institutions and their connection to the goals of social banking in job creation, community development and the improving of housing conditions. In the winter of this year we would like to arrange a preliminary meeting for those who will actively participate in the national or sectoral preparation of the conference. We especially would like to have confirmed cooperation from banking organisations and other financial institutions who are very welcome to join us at this early stage. We hope too that organisations such as the European Savings Bank association, INAISE and some other interested commercial or coop banks will join us this time, especially after they participated in such numbers at our last conference in France. We see it as a good sign that a high-ranking official at DG XXIV has asked us to reflect precisely about exactly this issue.

- 4. IFF** has recently enjoyed a turn-over of more than half a million ECU but with additional staff we expect an ever growing budget for 1998. Our new manager is Martin Jung, an economist who joins us from ISA Consult, a trade union-connected research agency. He is also leading the project on new opportunities for jobs in the financial services sector where trade unions and some major financial institutions cooperate. Stephanie Jack, who studied Chinese and worked on a management project for SAS for some years in China before returning to Germany to organise conferences in collaboration with a leading German journal is now heading our department for international affairs. Her experience in marketing and organisation will help us to put FIS-Money Advice on a firm financial footing and will equally add to the increasing success of our seminars and international conferences. Marco Habschick, a broadcast journalist whose work may be known by some from the daily program „Telebörse“ on n-tv (German CNN) and who for years has managed our BankWatch Internet journal joins us too and will help us to become more professional in our services for the press. A fairly new experience for the Institute is the collaboration by two economists, Juliane Pfau and Torsten Peters who work part time in two important German banks. Their presence is undoubtedly enriching our discussions on possibilities to improve banking services for people.

I hope that we can keep in contact and improve our efforts to built up a cross-partisan approach to make banks and other financial institutions ever more responsive to the needs of modern society.

We wish you and ourselves a successful New Year that will bring self-confidence and social justice in Europe, an economy and society which will become increasingly open to the rest of the world.

Yours sincerely

Professor Udo Reifner

INSTITUTE FOR FINANCIAL SERVICES (IFF)