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2008

Governance, Diversification and Performance: The Case of Italy's Banche Popolari

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Governance, Diversification and Performance: The Case of Italy's Banche Popolari

by

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Abstract

The paper has two objectives both pertaining to the specific corporate governance model of Italy's Banche Popolari. First, we aim to disentangle to what extent the observed lower profit volatility for such class of cooperative banks – vis-à-vis other joint stock banks – depends on their lower revenue diversification and/or on their governance setup. Specifically, less diversified banks – i.e., those relying less on noninterest income – tend to enjoy greater profit stability. While exhibiting lower revenue diversification, Banche Popolari groups also show an additional feature possibly conducive to lower profit volatility, namely they have more stable boards of directors, thereby focusing on longer-term business horizons. To test the relative explanatory power of these two hypotheses, we use data referring to the mid-1990s, before a big wave of consolidations that changed the Italian banking landscape.

Secondly, we investigate more up to date evolutions across the Banche Popolari groups. In recent years, some of these banks grew quite rapidly, while others were less dynamic. Growth of the former banks generally materialized via expanded holding group structures controlling several acquired banks, where the target banks featured both other Banche Popolari as well as some joint stock banks. On the contrary, the less dynamic Banche Popolari typically continued their business as standalone banks. Within this scenario, we study whether the peculiarities of their cooperative structure allowed the fast-growing Banche Popolari to cope with the more complex governance requirements implicit in such expanded holding group structures.

As to the first point, across Italian banks, we find that lower profit volatility associates with more stable boards of directors and not with less diversification (i.e. less reliance on noninterest income). Thus, the governance model of the Banche Popolari may be held responsible for the lower profit volatility of these banks. Regarding the second point, we found that the fast growing Banche Popolari groups: i) exhibit performances that are no worse than at other less dynamic BPs, and ii) are substantially as effective as joint stock banks in mastering post-acquisition performance improvement at the acquired banks. Thus, the governance specificity of the Banche Popolari seems to be still effective and the current proposals by some experts to transform the BPs into joint stock banks appear largely ill grounded.

(*) Paper prepared for the SUERF Seminar on Corporate Governance in Financial Institutions, jointly organized with the Central Bank of Cyprus. Thursday, 29th March – Friday, 30th March, 2007.
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1. Introduction

By 2005, the Banche Popolari¹ covered 22% of bank deposit taking in Italy, doubling their 1971 market share. This was achieved owing to better performance than at the other Italian banks, mostly belonging – directly or indirectly – to the state until fifteen years ago. A notable strength of the Banche Popolari is that their profits exhibit lower volatility over time than at joint stock banks.

Over the past decade, participating in the intense bank consolidation wave in Italy, some of the Banche Popolari moved on a path of rapid change. By 2004, the five largest banks held almost 80% of the total assets of the entire category. Consolidation continued in more recent years. The typical growth mode has been through acquisitions, without mergers. Rather, the acquired banks have been generally kept operating, even though within the control of the acquiring bank holding group. While most of the target banks were Banche Popolari themselves, some of the BP groups made also a number of acquisitions of joint stock banks. On the contrary, the reverse cases – i.e. a joint stock bank acquiring one of the BPs – happened only very seldom. This has led to a – still open – debate on whether the alleged low contestability of the ownership of the BPs is, *de facto*, preventing takeovers on them, possibly leading to management entrenchment and inefficiency. Furthermore, there is also debate on whether the complex bank holding group structures are posing threats to the governance of the Banche Popolari.²

Indeed, the Banche Popolari have a cooperative nature featuring some differences – e.g. the one vote per capita, irrespective of the number of shares held by the shareholder – with respect to the joint stock banks. This notwithstanding, the Banche Popolari seek profit as much as the joint stock banks do. So, we should think of them as cooperatives with a limited propensity to mutuality. As we will see briefly, this status did not happen by accident but was enshrined in the inspiring plan at the foundation of the Banche Popolari. Nevertheless, their cooperative nature makes the governance structure of the Banche Popolari somewhat diverse *vis-à-vis* that of the joint stock banks. On the positive side, thanks to their governance setup, the Banche Popolari have a higher stability of their boards of directors. Supposedly, this allows these banks to keep their business with a longer term focus, which might account also for their lower profit volatility. On the negative side, common wisdom and the theory of the cooperative firm suggest that the governance of the Banche Popolari may become increasingly difficult the farther out they venture from their original set up – one cooperative bank, one local community – into complex bank holding groups.

The aim of this paper is twofold. First, looking at the status prevailing before the great consolidation of the recent years, we investigate whether and to what extent the lower profit volatility of the Banche Popolari depended on two concurrent factors: their governance specificity *vis-à-vis* their productive specialization. On one hand, their cooperative governance could grant BPs higher stability of board directors and a longer term business approach which, in turn, would lower profit volatility. On the other hand, the Banche Popolari have lagged at expanding their business into non-intermediation services, which resulted in a lower reliance on noninterest income, where the literature points to a positive link between higher noninterest income shares and bank profit volatility. Hence, we wish to verify whether the positive side of BPs' governance effectively contributed to their performance.

Second, focusing on more recent years, we intend to shed light on whether the rapid growth of the large BP holding groups has weakened their performance with respect to the less dynamic BPs as well as to the joint stock banks. Here, a relative worsening of performance might depend on the negative side of BPs' governance.

¹ We will sometimes use the acronym BPs instead of the full name Banche Popolari.

² The cases of two large BPs suffering distress in recent years – Banca Popolare di Brescia and Banca Popolare di Lodi – rekindled criticisms of this type. However, each one of these crisis episodes was due to very specific circumstances. In addition, these crises do not overshadow the progress achieved by the entire BP category.

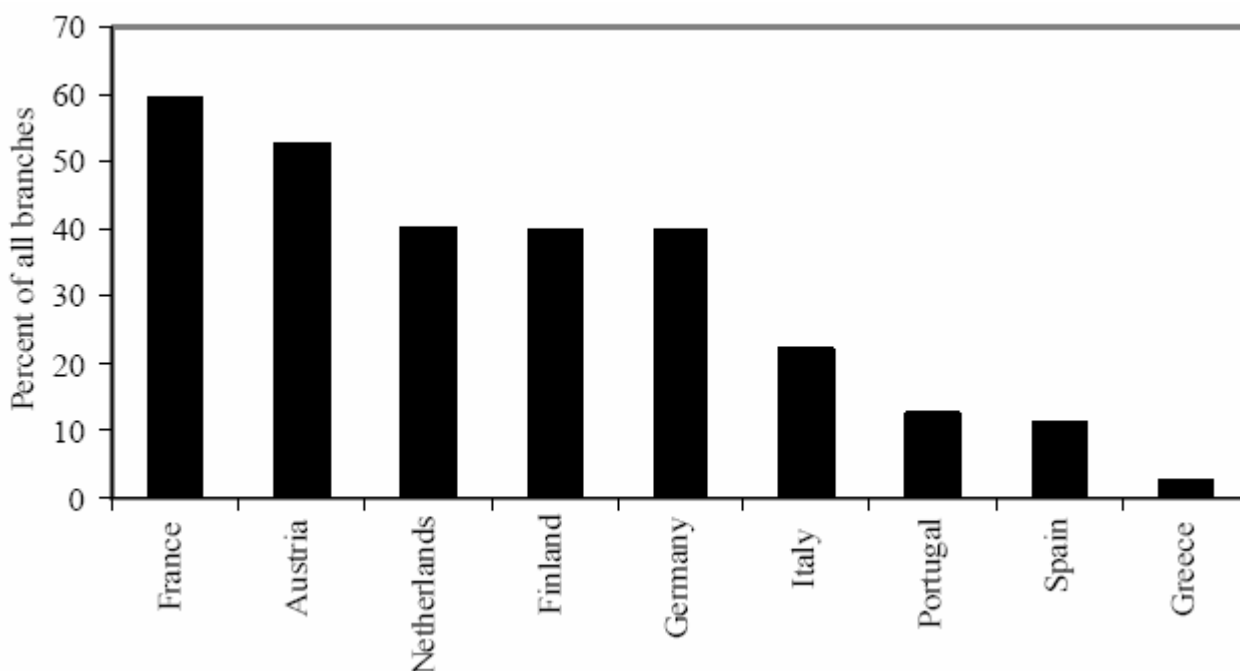
In the remainder of the paper, Section 2 provides the basics on the role and the specificity of the Banche Popolari within Italy’s banking landscape. Section 3 is devoted to outline and test econometrically whether the main factor behind BPs’ lower profit volatility was board stability or income diversification. In Section 4 we study the evolution of the Banche Popolari in more recent years, with a particular focus on the largest BP holding groups, examining whether they exhibit a governance-related worsening of performance, benchmarking them on less dynamic BPs as well as on joint stock banks. Section 5 draws conclusions and policy implications.

2. Increasing Role and Specificity of Italy’s Banche Popolari

2.1 The current role of the Banche Popolari in Italy’s banking

Although little studied by scholars, cooperative banks enjoy a significant market share throughout most of continental Europe. In terms of branches, the share of cooperative banks reaches almost 60% in France, above 50% in Austria, around 40% in the Netherlands, Finland and Germany, with Italy at 20% circa, Portugal and Spain around 10% and Greece below 5% (Figure 1). Thus, studying cooperative banks does not mean dealing with a marginal segment of banking in Europe, but rather the contrary.

Figure 1. Cooperative Banks: Retail Market Shares in Selected Countries

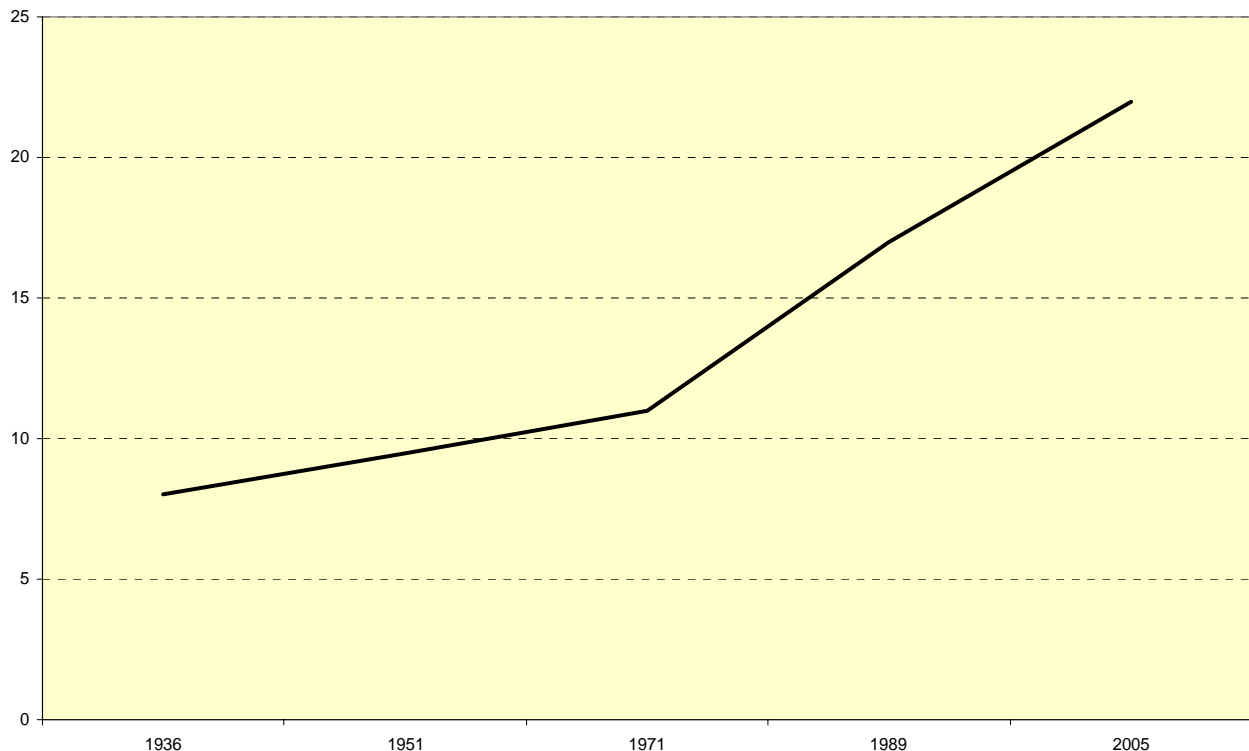


Source: OECD’s *Bank Profitability Report*; and authors’ calculations. Figure taken from Hesse and Čihák (2007).

Presently, the Banche Popolari hold some 22% of Italy’s bank deposit market. Most of these banks were established in the three decades following 1865. By 1895 there were 720 of these banks and their number peaked at 800 before the Great War. Thereafter, three crises – one immediately after the First World War; another one in 1927-28 following the deflationary shock from the overvalued return to gold of the Italian Lira; and the final one with the Great Depression – sentenced many Banche Popolari out of the market. Between 1910 and 1936 – the year in which the country regained its banking stability – the ratio of the total assets of the joint stock banks to the

total assets of the Banche Popolari more than quadrupled, also due to the disfavor by the Fascist regime against the Banche Popolari catering for the local elites antagonist to Fascism (Conti et al., 2002). With the end of the Fascist era, the Banche Popolari gained once more a constantly expanding role in Italy's banking system. This surge was subdued until 1971 – up to an 11% circa market share of deposits from just 8% in 1936 – accelerated greatly during the 1970s and 1980s – up to a 17% market share – and continued over the latest 15 years – up to 22% in 2005 (Figure 2).³

Figure 2. Deposit Market Share (%) of the Banche Popolari in Italy (selected years)



Source: authors' calculations on Bank of Italy data.

Beside the growing market share of the entire category, the largest BP groups stand out as intermediaries of noticeable size. Listing the ten largest banking groups in Italy we find that three are BP groups – and one (Banca Antonveneta) was a BP until it converted to joint stock bank just a few years ago (Figure 3).

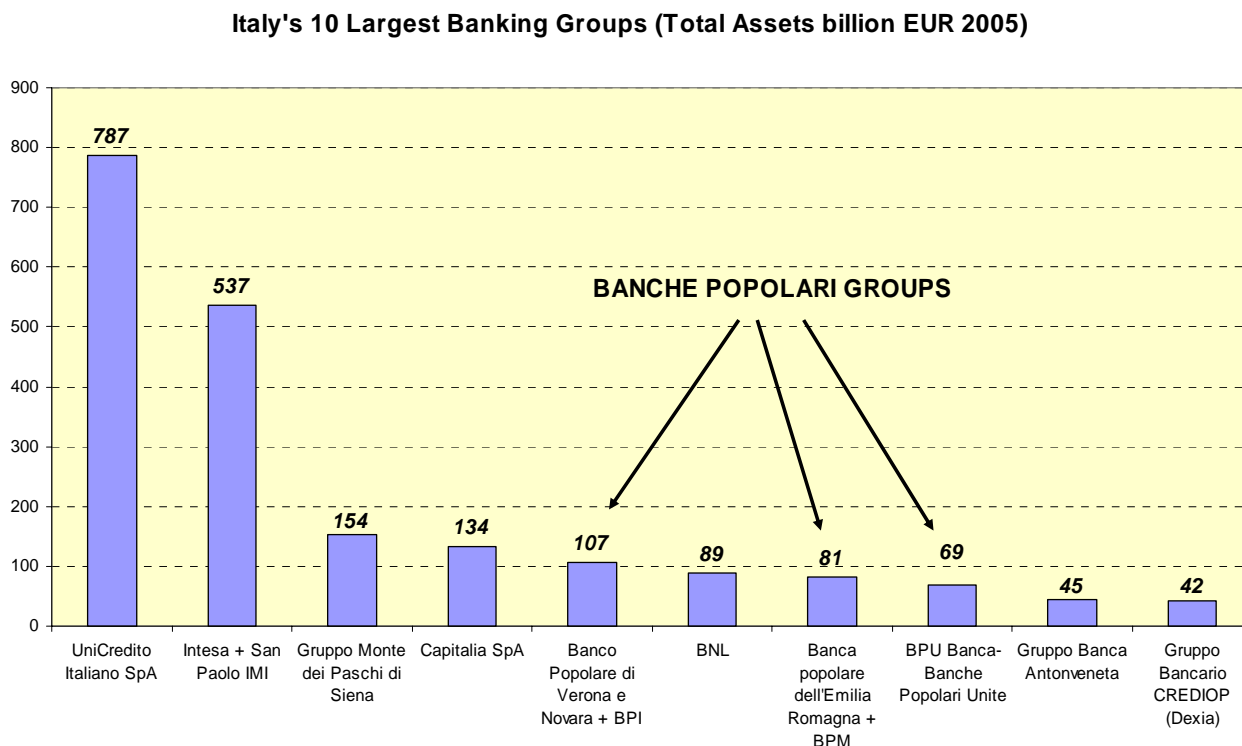
2.2 The current status of the Banche Popolari

The drive to establish the Banche Popolari was ignited in 1865 when the influential figure of Luigi Luzzatti promoted the adoption of Germany's model of cooperative banks suggested by Schulze-Delitzsch. Luzzatti deemed that in the pre-capitalist economy of – the then just unified – Italy it was crucial to support the growth of the urban productive middle class and saw the establishment of the BPs as a key passage in that direction. Using Luzzatti's own words in the occasion of his commemoration of the death of Schulze-Delitzsch: "He [Schulze-Delitzsch] rekindled the hope of more cheerful days for the artisans, the small entrepreneurs and the merchants

³ Some authors associate the surge in the business of the Banche Popolari to their link with the – then buoyant – industrial districts (Conti and Ferri, 1997).

– left with many ambitions but disillusioned by the 1848 revolution –, a positive evolution which they will owe neither to the state nor to private pity, but rather to the free association of their will. To the slaves of usury he points to the Banche Popolari ...” [in Levi (1886), p. XX].

Figure 3. The Ten Largest Banking Groups in Italy (2005)



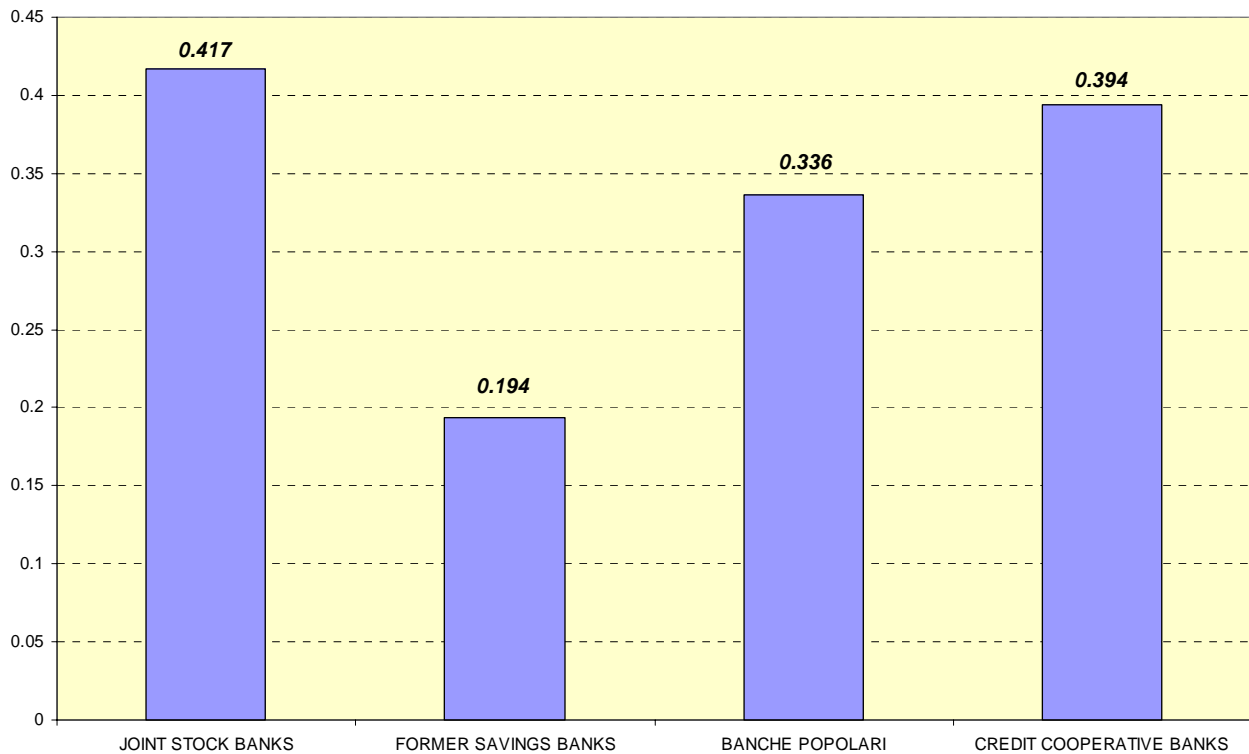
Source: authors' calculations on Bankscope data.

Since the status of cooperative firms was not yet embodied in Italy's law, Luzzatti promoted the Banche Popolari as a special branch of the joint stock banks. In particular, the statutes of the BPs prescribed two main limitations. First, BP shares could not be purchased by non-members and membership was to be granted only to “desirable” individuals. Second, irrespective of the number of BP shares he held, each member had right to one vote (the one-head-one-vote principle) and stringent limits to proxy voting were introduced. While the former limitation has been phased out, the latter still holds.⁴

This special set up seems conducive to a longer term business focus by the Banche Popolari (De Bruyn and Ferri, 2005). This does not show so much in profit – average 2004-2006 ROE was 9.8% for the entire Italian banking system vis-à-vis 6.7% for the BPs – as much as in profit volatility, which is somewhat lower for the BPs, even though it is even lower for the former Savings Banks (Figure 4). And, on passing, this is not a peculiarity of Italy as Hesse and Čihák (2007) find similar patterns for cooperative banks in their international comparison.

⁴ For more details on the specificity and the recent trends of the Banche Popolari, those who can read Italian are also referred to De Bruyn and Ferri (eds.; 2005).

Figure 4. Profit Volatility by Category of Banks in Italy (1995-1998)



Source: authors' calculations on a sample of individual banks' balance sheets.

Which factors account for this lower profit volatility of the BPs? Or, otherwise stated, if it is the different business focus of the BPs that accounts for this, through which channel does this materialize?

One of the differences with respect to joint stock banks delivered by of the special governance set up of the Banche Popolari is the longer tenure of board members. Ferri, Masciandaro and Messori (2001) constructed an indicator of board stability defined as:

$$STAB_i = \frac{\text{number of directors of bank } i \text{ in year } t_0 \text{ still in office in year } t_1}{\text{number of directors of bank } i \text{ in year } t_0}$$

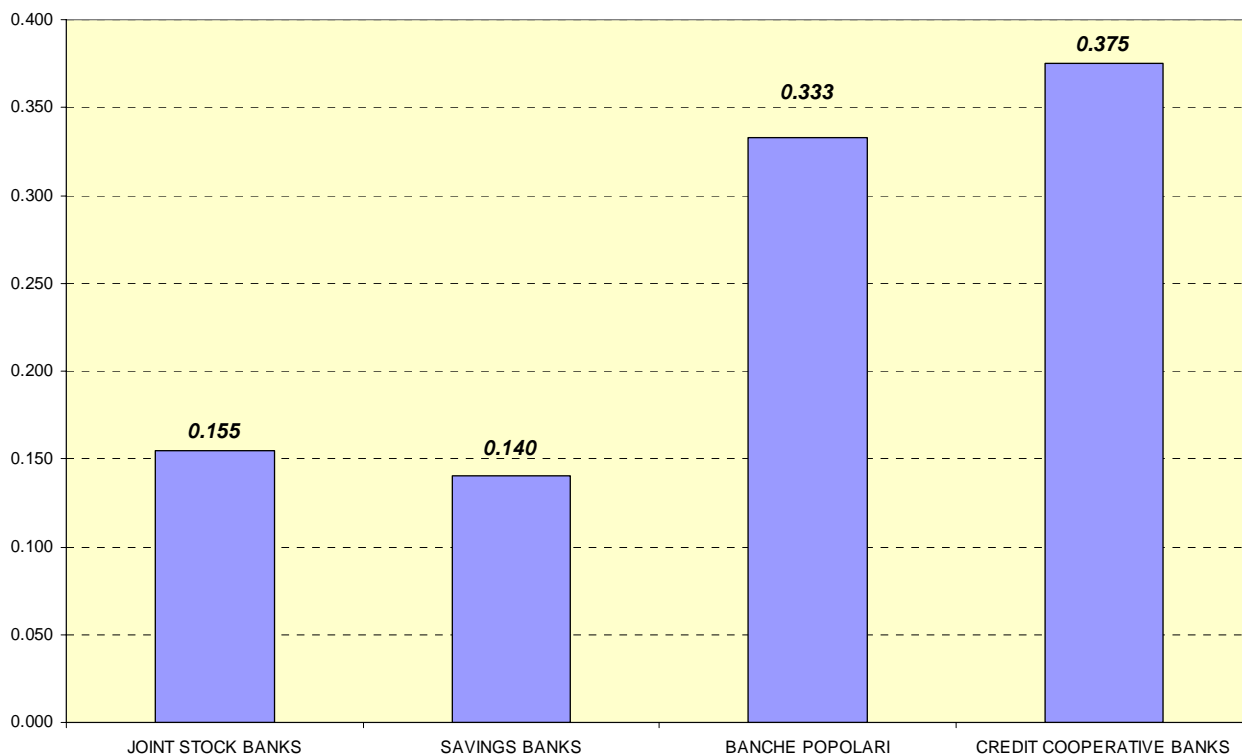
where t_0 is the base year and t_1 the end year.

They adopted 1990 as the base year – a year of great discontinuity in the Italian banking system, featuring extensive liberalization measure (e.g. branching and capital movements) and the start of the transformation of public-sector banks (including savings banks) into joint stock banks and the beginning of their privatization – and 1999 as the end year. They calculated $STAB_i$ on the basis of the names of the directors published in the yearbooks of the Italian Bankers' Association. The average value they calculated for the index, distributed by category is shown in Figure 5.

Clearly, stability is much higher for the two categories of cooperative banks – the BPs and even more so for the Credit Cooperative Banks (CCBs, formerly rural and artisan banks) – than for the joint stock banks and for the savings banks – also transformed into joint stock banks in the early 1990s. Going beyond this descriptive evidence, Ferri, Masciandaro and Messori (2001) run a tobit estimate of the determinants of STAB and find that – after controlling for bank size and other bank specific features – only for the BPs (not for the CCBs) the difference in terms of STAB with respect

to the other banks is statistically significant. Thus, their econometric evidence confirms the specific situation of BPs in terms of the stability of board directors.

Figure 5. Stability of Board Directors by Category of Banks in Italy (1990-1999)



Source: calculations by Ferri et al. (2001).

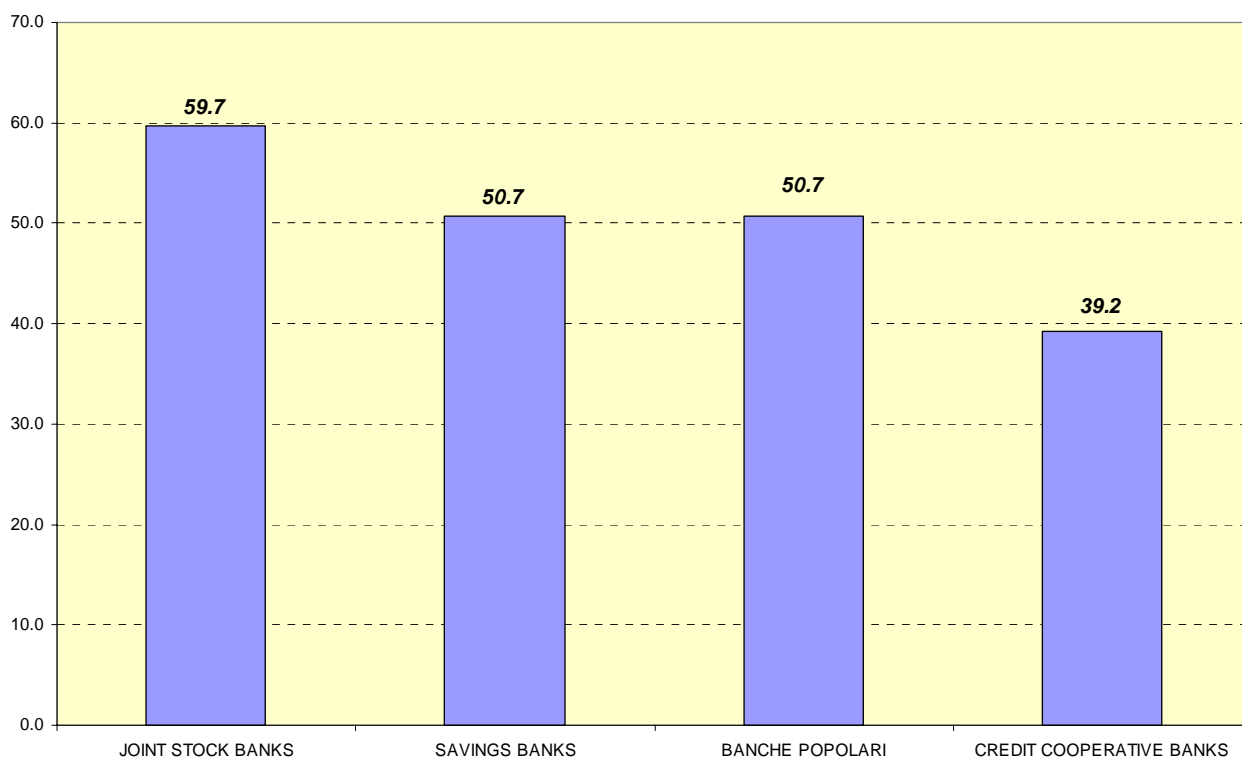
However, the Banche Popolari also show another difference with respect to joint stock banks which might have implications for their lower profit volatility. Namely, they rely less on noninterest income. Figure 6 reports the share of noninterest income in total income over the period 1995-1998: while the share reaches 59.7% for joint stock banks, it is 50.7% for BPs (and also for Savings Banks) and only 39.2% for CCBs.

Indeed, a strand of the literature is now casting doubts on the tenet that an increasing diversification of income sources, associated with higher noninterest income shares, may reduce bank profit volatility. This belief was widespread until a few years ago based on the conventional wisdom that, since interest income was traditionally the bulk of bank total income, a diversification enlarging the share of noninterest income could only lower profit volatility. However, a few studies find opposing evidence. Regarding the US, initial doubts on the hypothesis were raised by Roland (1997) and De Young and Roland (1999): the main idea is that traditional relationship lending activities tend to generate more stable revenues because switching and information costs tend to reduce the likelihood that either the borrower or the lender will terminate the relationship. Borrower are less prone to shop around in search for better prices, a behavior that, viceversa, characterizes trading activities. Besides, as Berger and Mester (1999) highlight, the expansion towards fee-based activities requires substantial fixed investments (particularly those related to the information technology) with negative effects on the reduction of operating costs, and therefore on the benefits of economies of scale and scope⁵, let alone on the level of operational risk taken on by the bank.

⁵ Berger and Mester (1999).

Considering that until the recent proposal by the Basle Committee no request for capital was made with respect to operational risk, the final effects of diversification could result in an incremental risk not associated with an increase in the level of capital.

Figure 6. Share (%) of Noninterest Income in Total Income (average 1995-1998)



Source: authors' calculations.

More recently, Stiroh (2004) assessing the potential diversification benefits of noninterest income finds that, in the aggregate, declining volatility of net operating revenue reflects reduced volatility of net interest income, not diversification benefits from noninterest income, which is quite volatile and increasingly correlated with net interest income. In addition, at the bank level, greater reliance on noninterest income is associated with lower risk-adjusted profits and higher risk. Thus, Stiroh (2004) concludes that the diversification benefits from the ongoing shift toward noninterest income are not obvious. Regarding Europe, Staikouras and Wood (2003) bring evidence in favour of diversification observing that, with the single exception of large German banks, there exists a positive correlation of noninterest income with bank profits. However, the study also demonstrates that the positive effects of diversification, in terms of profit stabilization and risk reduction, are somewhat limited.

All in all, there seems to be evidence of a positive – not a negative – link between growing reliance on noninterest income and bank profit volatility. In the jargon of the Capital Asset Pricing Model, one could argue that noninterest income is an aggressive asset – with $\beta > 1$ – and, thus, since it implies higher volatility, it should also require higher return.⁶

⁶ Among the other related literature on income diversification and profitability levels, adopting a comparative approach that focuses on the level of revenue diversification for a sample of European and US banks, Bongini, Di Battista and Nieri (2000) confirm the positive effects of diversification on bank profitability levels; the study, however, is limited to the period 1993-1998; therefore it doesn't completely capture the effect of heavier reliance on trading revenues and its

Accordingly, we seem to have two alternative hypotheses to account for the lower profit volatility of the Banche Popolari. On one hand, we have their governance-related higher stability of board directors. On the other hand, we have their business-practice-related lower reliance on noninterest income. In the next Section, we will try to disentangle between these two hypotheses.

The second issue we aim to address pertains to the current possible problems for the large BP bank holding groups which have experienced an incredibly fast growth over the past ten years. Namely, is the specific corporate governance mode of the Banche Popolari still effective under this rapidly changing scenario? There appear to be two reasons to worry. First, as the Banche Popolari move on from single standalone banks to complex banking groups, they may undergo a worsening of performance, as pointed out by some papers on the inefficiencies of bank holding groups. Various studies, on either theoretical or empirical grounds, conclude that bank holding companies often show evident organizational inefficiencies (e.g., Berger and Mester, 1997; Stein, 2002). Second, as they grow larger, the Banche Popolari may face specific governance problems related to their cooperative structure. For instance, Hart and Moore (1998), by means of their analysis of voting mechanisms, conclude that cooperative enterprises are better than joint share companies when the interests of the members of the cooperative are relatively homogeneous but the opposite holds when members' interests become heterogeneous and/or when competition increases. As argued by Pittaluga et al. (2005), it is possible that, with the passage of time and the enlargement of the number of members, different objectives among members surface, along with a conflict between cash flow and control rights. In turn, this may lead the institution to relinquish its cooperative structure and/or to experience growing governance problems. Furthermore, still related to the specific cooperative structure, the likelihood of management entrenchment is higher when BPs become larger. This depends on the fact that forming alternative coalitions to force manager change – at member annual meetings – may become more and more difficult as the number of members increases.

This problem will be addressed in Section 4. Before doing that, we now turn to testing whether stability of board directors or income source diversification explain better the lower profit volatility of the Banche Popolari.

3. Lower Profit Volatility: Testing Board Stability vs. Income Diversification

In this section we analyse the determinants of profit volatility for a sample of Italian banks, comprising both joint stock, savings and cooperative banks (BPs and CCBs), over the period 1995-1998. Our testing hypothesis is that profit volatility is mainly determined by two concurrent factors: governance specificity and productive specialization. Hence, we wish to verify whether the positive side of BPs' governance effectively contributed to their performance. Profit volatility is calculated as the standard deviation of ROA during the sample period.

First, we posit that the cooperative governance could grant BPs (and CCB as well) higher stability of directors and a longer term business approach which, in turn, would show a positive effect on the stability of their profits (i.e. lower profit volatility). We refer to Ferri, Masciandaro and Messori (2001) for the index of board stability (see previous Section).

Second, following the recent empirical works that point to a positive link between higher noninterest income shares and bank profit volatility, we conjecture that a lower reliance on noninterest income should help reduce profit volatility. As explained in the previous section, the Banche Popolari have lagged at expanding their business into non-intermediation services, in particular with respect to their joint-stock competitors; this might explain their lower profit

impact on profits when markets rallies to a downturn. More recently, Baele, Van der Venet and Van Landschoot (2004) observe that market participants perceive functionally diversified banks as being better protected against a deterioration in money and credit market conditions compared to their more specialized competitors).

volatility. Differences in the structure of banks' income are detected by a measure of income diversity that is defined as follows:

$$\text{Income diversity measure} = 1 - \left| \frac{(\text{net interest income} - \text{other operating income})}{\text{total operating income}} \right|$$

Higher values of the variable correspond to a higher degree of diversification.

In addition to these key variables of interest, the regression includes a number of other control variables. First, we control for size and size growth during the sample period. Indeed, a large increase in size tends to show a direct and potentially immediate impact on banks' profits. However, the increase in size, with its potential for economies of scale and scope, may also imply a positive effect on profit volatility, e.g. lower volatility. Second, the ratio of total expenses to total assets is inserted to control for banks' cost structure: the higher the operating costs the lower the bank ability to adjust the cost structure to income shocks. Third, we also control for the institutional type of bank, namely a categorical variable taking value 1 if a bank is a cooperative, 2 if the bank is a saving bank, 3 if the bank is a popolare and 4 if the bank is a joint stock bank, is inserted.

Our calculations are based on individual bank data drawn from the Bankscope database. We use data on all joint stock, cooperative and savings banks in the database for which the board stability index by Ferri, Masciandaro and Messori (2001) was available. In total, we have data on 211 banks from 1995 to 1998, comprising 61 Credit Cooperative Banks (CCBs), 61 (formerly) savings banks, 46 banche popolari (BPs) and 43 joint stock banks.

Variable definitions are summarized in Table 1, Table 2 provides summary statistics and Table 3 presents the OLS estimation results.

Table 2 confirms that with respect to joint stock banks: i) profit volatility is visibly lower for BPs and CCBs (though it is even lower for savings banks); ii) STAB is higher for BPs and CCBs; iii) income diversity is lowest for CCBs but somewhat low also for BPs (and also for savings banks); iv) operating costs are a little higher for CCBs and BPs (though they are highest for savings banks); v) size is smallest for CCBs but somewhat small also for BPs (and also for savings banks); vi) growth is largest for CCBs but somewhat high also for BPs.

Table 1. Variable definitions

| <i>Variable name</i> | <i>Variable definition</i> | <i>Potential effect on profit volatility</i> |
|-----------------------------|--|---|
| Profit volatility | ROA standard deviation over the sample period | - |
| Income diversity measure | $1 - \frac{(\text{net interest income} - \text{other operating income})}{\text{total operating income}}$ | Positive: the higher the diversification the higher the profit volatility |
| Index of director stability | see Ferri et al (2001) for complete definition the index lies between 0 and 1, higher values corresponding to higher governance stability | Negative: the higher the stability the lower the profit volatility |
| Size | Logarithm of Total assets | Unknown, control for differences in bank size |
| Size growth | % change of total assets during sample period | Negative |
| Operating costs | Ratio of total expenses to Total Assets | Positive: higher operating cost ratios imply lower ability by banks to adjust the cost structure to income shocks |
| Institutional type | Categorical variable which takes the value 1 if a bank is a cooperative, 2 if the bank is a saving bank, 3 if the bank is a popolare and 4 if the bank is a joint-stock bank | Unknown |

Table 2 Summary statistics

| <i>Variable</i> | <i>Overall mean</i> | <i>Mean if BCC</i> | <i>Mean if Popolare</i> | <i>Mean if savings bank</i> | <i>Mean if joint stock bank</i> |
|--|---------------------|--------------------|-------------------------|-----------------------------|---------------------------------|
| Profit volatility | 0.33 | 0.39 | 0.33 | 0.19 | 0.42 |
| Index of director stability (STAB) | 0.29 | 0.35 | 0.36 | 0.16 | 0.29 |
| Income diversity measure (%) | 33 | 39 | 51 | 51 | 60 |
| Operating costs (% of Total assets) | 4.00 | 3.93 | 3.94 | 4.3 | 3.81 |
| TA (in log) | 13.59 | 11.84 | 14.13 | 14.20 | 14.61 |
| Size growth (% change between '95-'98) | 5.43 | 7.56 | 5.72 | 3.33 | 5.10 |

Table 3 OLS robust estimation results⁷

| <i>Variable</i> | <i>Initial Specification</i> | | <i>Preferred Specification</i> | |
|--|------------------------------|---------------------------|--------------------------------|-------------------|
| | <i>coefficient</i> | <i>Std errors</i> | <i>Coefficient</i> | <i>Std errors</i> |
| Index of director stability | -.2146364 | .1120185 (*) p value 5,7% | -.2788811 | .1037078 (***) |
| Income diversity measure (%) | .000212 | .2505155 | .0552092 | .2906788 |
| Operating costs (% of T. assets) | .17928 | .0491425 (***) | .2016106 | .0653928 (***) |
| TA (in log) | .0184313 | .0235234 | - | |
| Size growth (% change between '95-'98) | -.0129743 | .0108429 | - | |
| Dummy CCB | -.0546926 | .0943234 | .020384 | .0844842 |
| Dummy BP | -.1252217 | .0875999 | -.0621983 | .0785981 |
| Dummy savings bank | -.4041361 | .0813652 (***) | .020384 | .0844842 (***) |
| Constant | -.3645814 | .4013308 | -.3232203 | .3417811 |
| Adjusted R- squared | 33.81% | | 30.05% | |
| N. observations | 211 | | 211 | |

The results in Table 3 corroborate our expectation that directors' stability associates significantly with lower profit volatility. On the contrary, although the coefficient of income diversity is positive, as expected, its link with the dependent variable is not significant. It is also confirmed that banks with higher ratios of operating costs to total assets experience higher profit volatility. Size and growth turn out not significant. As to the bank type dummies, only the savings banks one turns out significant, telling us that profit volatility is lower for savings banks.

⁷ Since the Breusch-Pagan/Cook-Weisberg test suggests the presence of heteroskedasticity, we compute robust standard errors via White's correction.

Thus, since both BPs – and also CCBs – have higher stability of board directors, our results suggest that their cooperative governance set up is the distinguishing factor behind their lower profit volatility.

4. Challenges Posed by the Cooperative Governance to Growing Banche Popolari

A key question is whether Italy's Banche Popolari still preserve the specific cooperative and local traits that made them successful through some 140 years. The various contributions in De Bruyn and Ferri (2005) seem to suggest that little has changed over the years for the Banche Popolari in terms of their cooperative corporate entity and governance. In spite of the rapid consolidation affecting the banking industry, the Banche Popolari are still to all intents and purposes cooperative entities governed according to the democratic principles of their blueprint. It is true that, with high growth and consolidation, the once very simple structure of these banks has significantly grown in its organizational complexity. In lieu of the hundreds of tiny banks they once were, today's Banche Popolari feature a bimodal distribution. On the one side, a few of them (prevalently originating from Northern regions) have reached a national scale or beyond and are structured in composite banking groups. On the other, a certain number of small BPs continue to operate in a narrowly delimited environment. Both still abide, however, by their cooperative principles.

Something has instead changed as regards the second initial trait – namely, their essential focus to support the local communities from which they originated – for the Banche Popolari that have grown big: of course, they cannot focus just on the local community of inception. Nevertheless, the evidence collected by De Bruyn and Ferri (2005) supports the view that the “updated mission” of the big Banche Popolari is to continue being “community-based” banks servicing now all the local communities where they operate and catering specifically for small and medium-sized enterprises (SMEs) and family businesses.

The tendency for the Banche Popolari to keep doing business largely based on relationship banking and the changes in this respect induced by consolidation within the BPs may be underscored by looking at two specific dimensions:⁸ i) the degree to which the Banche Popolari have directors who are rooted in the local communities where they do business (a proxy for BPs' local business focus), and ii) the turnover of branch managers (a proxy for BPs' reliance on relationship banking).

A larger recourse to locally rooted directors is suggestive of a stronger focus to service local communities.⁹ Recent evolutions within the BP category might have weakened these banks local business focus. Firstly, the growing BP groups have considerably expanded their business in areas far away from their community of origin. Furthermore, many Banche Popolari, especially in Southern Italy, have become part of the large BP groups, generally originating from distant areas. Both these evolutions might have weakened the rooting of directors in local communities. Our aim here is to gauge whether, and to what extent, this happened between end 1995 and the beginning of 2003. Our analysis takes into account the possibility that the intensity of the phenomenon could be different between, on the one side, the subset of the still independent BPs¹⁰ and, on the other side, the acquired BPs.¹¹

⁸ The evidence reported here is taken from De Bruyn and Ferri (2005).

⁹ This must be interpreted as a proxy. To be sure, in fact, having directors belonging to the local communities where BPs do business is neither a necessary condition for the BPs to have a local business focus – directors coming from outside the local community might not be an obstacle to local business focus – nor a sufficient condition to it – locally rooted directors might even obstruct the local business focus.

¹⁰ The first subset includes: Banca Agricola Popolare di Ragusa, Banca Popolare Commercio e Industria, Banca Cattolica Popolare, Banca Popolare del Lazio, Banca Popolare di Valsabbina, Credito Popolare, Banca Popolare di

The local rooting of BP directors is measured by an indicator of the distance between the province where the BP is headquartered and the province of birth of each director.¹² The indicator takes value 1 if the two provinces coincide. If, instead, the province of birth of the director differs from that of the BP headquarters, the indicator is valued: 2 when the two provinces belong to the same region;¹³ 3 when the two provinces do not belong to the same region, but belong to the same territorial area;¹⁴ 4 when the two provinces belong to different territorial areas; 5 if the director was borne abroad. Finally, the value the bank level indicator takes for each BP is the simple average of the value of each distance indicator for all the directors in charge at the BP at that moment.

The change in the indicator gives some interesting insights. Across all the Banche Popolari – both independent BPs and BPs group controlled – between 1995 and 2003 the distance indicator increases from 1.60 to 1.99 (Figure 7). In other words, from the initial situation in which almost half of the directors had province of birth coinciding with the province of the BP headquarters, the Banche Popolari move on to a new configuration where the distance has significantly increased. However, it is worth noting that, as expected, the change radically differs between the subset of independent BPs and the others. As to the former (the group heads) the indicator records only a very small increase (from 1.57 to 1.63), while the index jumps from 1.63 to 2.29 for the subset of the acquired BPs. Such a jump was partly to be expected, as it seems natural that acquiring banks appoint a new class of trustworthy directors. At the same time, however, this might indicate a weakening of the local rooting of the BP.

The second dimension of our analysis regards the length of stay of branch managers at the same branch of the bank. A long stay may be desirable to improve relationship lending. Longer stays may, in fact, reduce the degree of asymmetric information for the bank – since the branch manager cumulates more information on borrowers, particularly soft information which are hardly transferable when he moves on to a different assignment)¹⁵ and, hence, improving banks' allocative efficiency. However, various papers reach the conclusion that long stay of branch managers is unlikely feasible for large banks. Ferri (1997) argues that as such stay lengthens, the probability increases that the branch manager is captured by and/or starts colluding with local entrepreneurs.

Piacenza, Banca Popolare di Lodi, Banca Popolare di Verona e Novara, Piccolo Credito Valtellinese, Banca Popolare di Lajatico, Banca Popolare Pugliese, Banca Popolare di Fondi, Banca Popolare del Frusinate, Banca Popolare Cassinate, Banca Popolare Puglia-Basilicata, Banca Popolare dell'Emilia-Romagna, Banca Popolare dell'Etruria e del Lazio, Veneto Banca, Banca Popolare di Bari, Banca Popolare di Bergamo, Banca Popolare di Cortona, Banca Popolare di Cremona, Banca Popolare di Intra, Banca Popolare di Milano, Banca Popolare Vesuviana, Banca Popolare di S. Felice sul Panaro, Banca Popolare di Sondrio, Banca Popolare di Vicenza, Banca Popolare S. Angelo, Banca Popolare di Valconca, Cassa di Sovvenzioni e Risparmi tra il Personale della Banca d'Italia, Banca Popolare dell'Alto Adige.

¹¹ The second subset includes (we also consider the small Savings Banks, CRs, and the CCBs acquired by BPs): Banca Popolare di Augusta, Nuova Banca Mediterranea, Banca Popolare della Penisola Sorrentina, Banca Popolare della Calabria, Banca Popolare di Ancona, Banca Popolare di Todi, CR di Fano, Banca Popolare di Luino e Varese, Banca Popolare di Cividale, Banca Popolare di Crotona, Banca Popolare dell'Irpinia, Banca Popolare del Materano, Banca Popolare di Aprilia, Banca Popolare di Castrovillari, Banca Popolare di Lanciano, Banca Popolare di Ravenna, Banca Popolare di Sassari, Banca Popolare di Salerno, CR dell'Aquila, CR di Vignola, Banca del Monte di Foggia, Banca Popolare di Roma, Banca Popolare di Sesto S. Giovanni, Banca Popolare di Monza, Banca Popolare della Romagna, Banca Valori, Banca Popolare di Mantova, Banca Popolare di Crema, Banca Popolare del Trentino, BPL Network, CR di Livorno, CR di Imola, CR di Lucca, CR di Pisa, Banca Popolare di Rho, BCC S. Elisabetta, Banca Meridiana, Banca Nuova, Banca Popolare di Novara.

¹² In the relevant period of observation, Italy could be subdivided into 103 provinces.

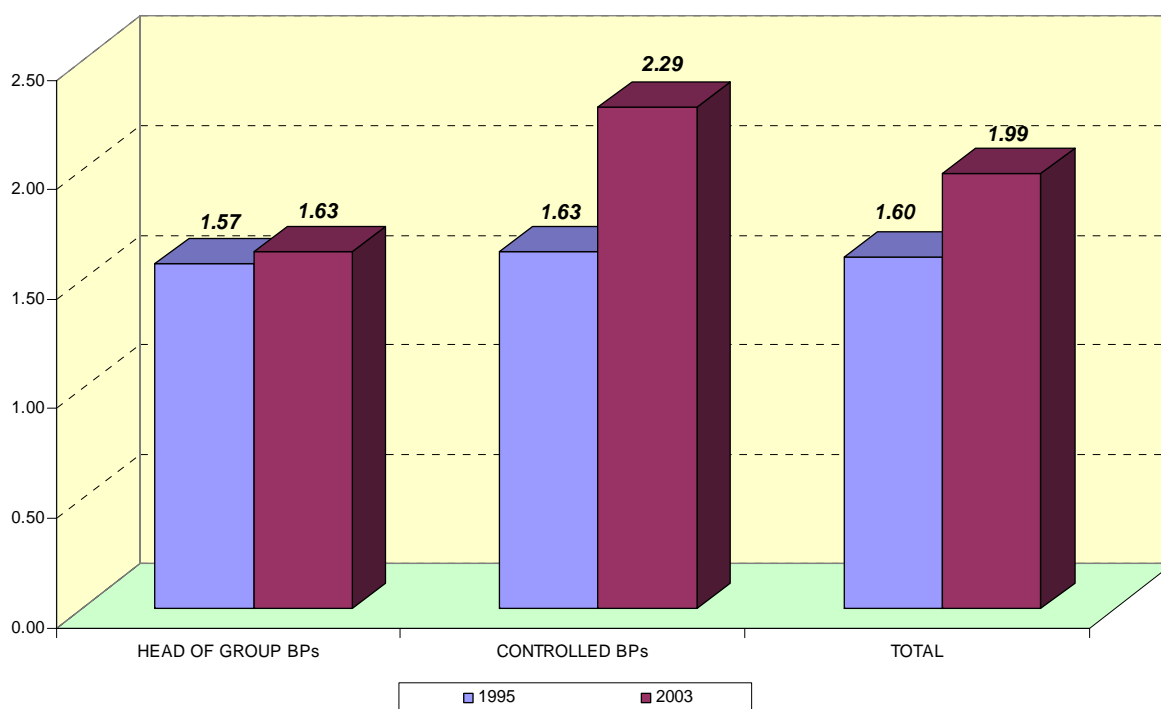
¹³ Italy is subdivided into 20 regions.

¹⁴ Italy is subdivided into 5 territorial areas: North-West, North-East, Center, South, Islands.

¹⁵ For example, Ferri (1997) shows that a longer stay by branch managers associates with lower NPL ratios for individual banks. Scott (2004) finds that a lower turnover of branch managers and frequent social contact with borrowing firm owners strengthen *relationship banking* giving benefits to borrowers in terms of both availability and cost of credit.

Stein (2002) remarks that, given the hierarchical context of large banks, local credit managers would be led to underinvest in costly operations such as gathering soft information – typically governing the bank-SME relationship – to avoid that the bank headquarters restrict resources assigned to their branch.

Figure 7. Distance Indicator of Board Directors: 1995 vs. 2003



Source: De Bruyn and Ferri (2005).

Nevertheless, it is possible that its lower hierarchical complexity (according to Stein) or its higher ability to control local managers (according to Ferri) allow local banks to grant longer branch manager stays. In turn, this could improve the loan allocation, thereby benefiting the bank and/or its borrowers. Indeed, referring to 1992 data for Italy, Ferri (1997) showed that branch manager stay was significantly longer for those bank categories populated by local banks vis-à-vis what observed at national-level banks: the average stay was 43.5 months for the Banche Popolari and 43.3 months for the then Savings Banks, as against 30.4 months for the larger public sector banks then denominated Istituti di Credito di Diritto Pubblico, and 32 months for the large joint stock – also state owned – banks then called Banche di Interesse Nazionale.¹⁶

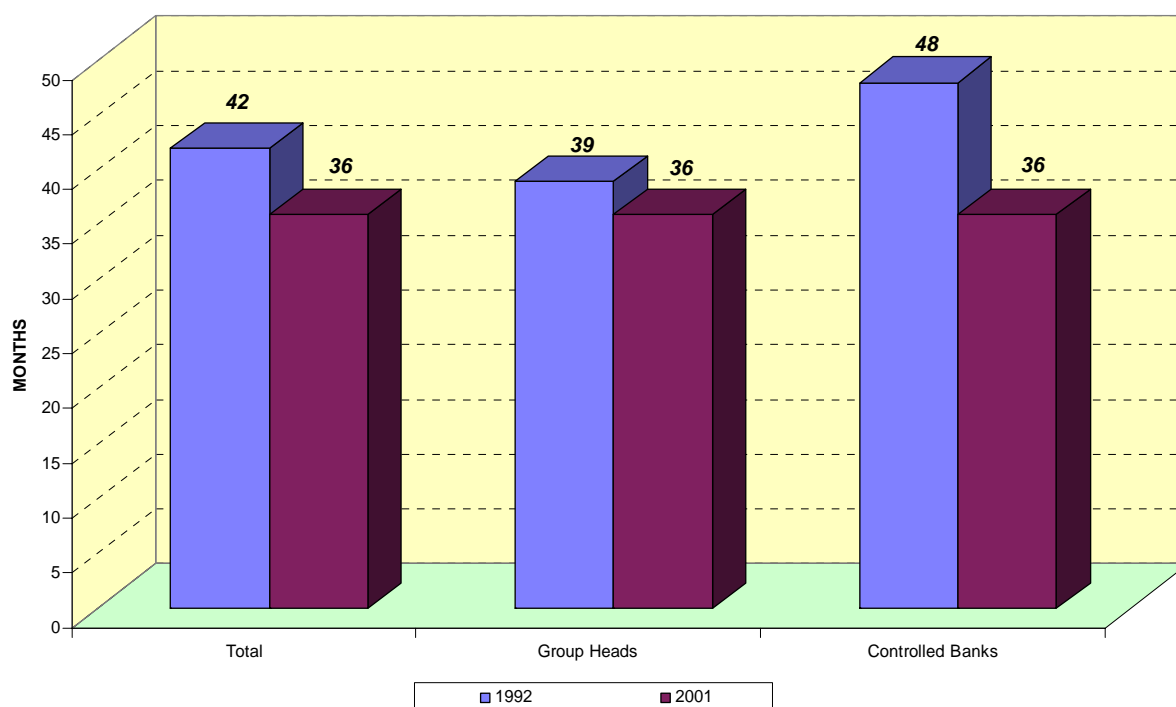
Following the 1992 survey, we have access to new survey data for 2001 on the sole Banche Popolari. This allows checking whether – in conjunction with the intense changes during this period – their far reaching reorganization led the Banche Popolari to shorten branch manager stay. A positive answer to this question might point to a lower BP reliance on relationship banking.

¹⁶ Istituti di Credito di Diritto Pubblico included: Banca Nazionale del Lavoro, Banco di Napoli, Banco di Sicilia, Banco di Sardegna, Monte dei Paschi di Siena, Istituto Bancario San Paolo di Torino. Banche di Interesse Nazionale included: Banca Commerciale Italia, Banco di Roma and Credito Italiano. While the survey data excluded CCBs, the other included joint stock banks – then denominated Banche di Credito Ordinario – had intermediate values (38.4 months).

Furthermore, we would like to tell apart whether this descended from lower BP ability to control branch managers or from the increasing hierarchical complexity of the BP holding bank groups.

Between 1992 and 2001 the average stay of branch managers – at the 21 Banche Popolari for which we have data for both years¹⁷ decreased by 6 months: from 42 to 36 months (Figure 8). In addition, from the same figure we can see that the decrease was much stronger for controlled banks than for head of groups banks. The average reduction for the latter banks was only 3 months (from 39 to 36) while the decrease was 12 months (from 48 to 36) for the controlled BPs. The marked drop in branch manager stay at controlled banks seems, thus, an impact of consolidation, implying their convergence to the head group banks practice: in fact, the difference was noticeable in 1992, when the now controlled BPs were still independent, and it had vanished by 2001.

Figure 8. Average Stay of Branch Managers at BPs: 1992 vs. 2001



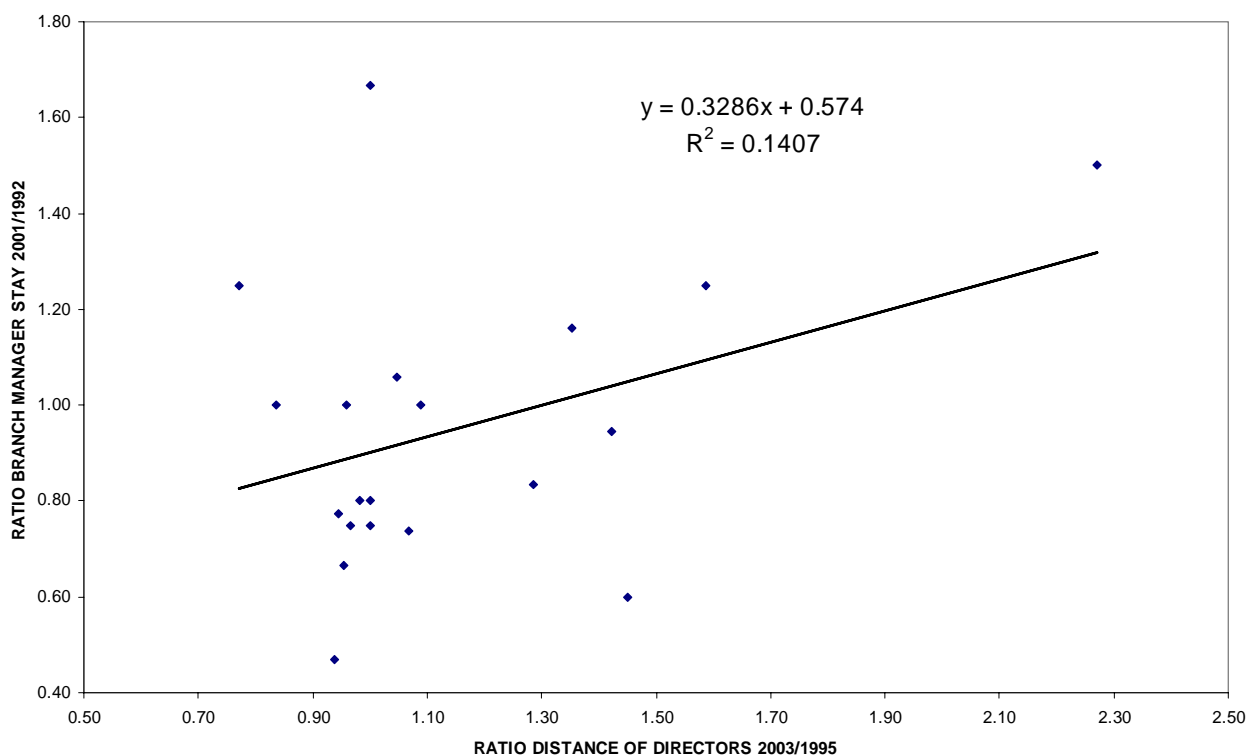
Source: De Bruyn and Ferri (2005).

Then, the following question is key. What induced the decrease in the branch manager stay at the head of group BPs? Specifically, is this decrease related to a weakening local rooting of the Banche Popolari or to the growing complexity of their group structures? Indeed, the introduction of the group organizational structure – virtually non-existent at the beginning of the 1990s – gives rise to new decision levels. This, in turn, may render more complex the governance within the BP category.

¹⁷ The Banche Popolari included are: Banca Agricola Popolare di Ragusa, Banca di Credito Popolare, Banca Popolare di Lodi, Banca Piccolo Credito Valtellinese, Banca Popolare di Lajatico, Banca Popolare di Crotone, Banca Popolare di Puglia e Basilicata, Banca Popolare dell'Emilia Romagna, Banca Popolare dell'Etruria e del Lazio, Banca Popolare dell'Irpinia, Banca Popolare del Materano, Veneto Banca, Banca Popolare di Bari, Banca Popolare di Bergamo-Credito Varesino, Banca Popolare di Cortona, Banca Popolare di Cremona, Banca Popolare di Luino e di Varese, Banca Popolare di Marostica, Banca Popolare di Milano, Banca Popolare di Ravenna, Banca Popolare di Sondrio.

We gather supportive evidence to this hypothesis observing the correlation between change in the indicator of distance of board directors – as measured above – and change in branch manager stay. Figure 9 plots on the horizontal axis the ratio of the distance indicator in 2003 to its own value in 1995: values above one point to an increasing distance of board directors, possibly identifying a lower local rooting of that BP. The scatter plots on the vertical axis the ratio between branch manager stay in 2001 and branch manager stay in 1992: here, values above one indicate a lengthening of the branch manager stay. If the reduction in branch manager stay were, in effect, related to lower local rooting by the BP, we should expect finding a negative link prevailing in the scatter: i.e. more distant directors should associate with lower branch manager stay. However, on the contrary, the scatter gives a positive correlation: as signalled by the interpolating line. Thus, we may conclude that the decrease in branch manager stay relates more likely to the growing organizational complexity of the BP groups than to lower local roots of the Banche Popolari.

Figure 9. Change in Branch Manager Stay vs. Change in Distance of Board Directors



Source: De Bruyn and Ferri (2005).

It is now time for us to address whether large and fast growing BP holding groups are experiencing governance-related performance problems.

We address this question analyzing two issues. First, we illustrate the recent performance of the entire BPs' sector, distinguishing between listed groups, unlisted groups and individual BP banks. As the financial institution moves from a simple organization – like the individual bank – to reach a group structure and to obtain the status of listed company, i.e. being subject to market discipline,¹⁸ then the growing organizational complexity, implicit in such an evolution, might create a weaker intermediary, unable to completely lever on the advantages of a cooperative nature, while being refrained in the pursue of shareholders wealth maximization because of its cooperative structure. In

¹⁸ In general terms, market discipline is positive; however market objectives, say for instance the shareholders wealth maximization goal, to be daily pursued, may not perfectly conform to the cooperative nature.

other words, by changing organizational nature, the cooperative status might represent a restraint, in terms of performance, rather than an *atout*. Second, we investigate the performance of target banks involved in recent M&A operations, distinguishing between operations where the bidder was a BP and deals where the bidder was a joint stock bank. The main idea is that, owing to their governance model, BPs might be refrained in their task of restructuring the target bank and extracting value from the acquisition, at least in the short term. Indeed, a recent study on M&A operations in the Italian BP sector has highlighted that acquisitions of control by a BP generally comes with a set of governance agreements favouring the target bank, aimed at opening up the market for corporate control and at offering minority shareholders some guarantees of partial autonomy aimed at guaranteeing the maintenance of their local roots (Finmonitor, 2004). The same does not apply when the bidder bank is a joint-stock: governance agreements with the target are unlikely to occur. Such a different behaviour might differently influence the success of the M&A operation.

Table 4 Recent performance of the Banche Popolari sector

| Variable | | listed group | unlisted group | Individual banks |
|--------------------------------|--------|--------------|----------------|------------------|
| Total assets (th. €) *** | Mean | 27,500,000 | 4,420,830 | 845,148 |
| | median | 11,400,000 | 2,301,830 | 383,845 |
| Total assets 04 (th. €)*** | Mean | 29,840,245 | 5,798,250 | 1,038,933 |
| | median | 14,947,150 | 2,667,700 | 491,900 |
| income diversity measure *** | Mean | 0.76 | 0.74 | 0.61 |
| | median | 0.79 | 0.62 | 0.64 |
| income diversity measure04 *** | Mean | 0.76 | 0.76 | 0.55 |
| | median | 0.80 | 0.58 | 0.56 |
| NPL/LOANS (%)* | Mean | 6.77 | 6.94 | 8.36 |
| | median | 4.67 | 5.42 | 9.09 |
| NPL/LOANS 04 (%) | Mean | 6.57 | 6.62 | 7.54 |
| | median | 4.92 | 5.14 | 8.79 |
| Total capital ratio (%)** | Mean | 9.49 | 14.50 | 17.91 |
| | median | 10.00 | 13.50 | 17.50 |
| Total capital ratio 04 (%)** | Mean | 9.78 | 13.83 | 16.18 |
| | median | 10.00 | 12.00 | 16.50 |
| ROA(%) | Mean | 0.42 | 0.73 | 0.57 |
| | median | 0.50 | 0.49 | 0.65 |
| ROA 04 (%) | Mean | 0.54 | 0.79 | 0.67 |
| | median | 0.60 | 0.47 | 0.66 |
| ROE (%) | Mean | 6.05 | 7.16 | 5.30 |
| | median | 5.67 | 6.56 | 5.74 |
| ROE 04 (%) | Mean | 7.44 | 7.99 | 6.01 |
| | median | 7.21 | 5.84 | 6.27 |
| Cost income (%) | Mean | 71.60 | 72.87 | 71.75 |
| | median | 73.75 | 68.40 | 70.24 |
| Cost income 04 (%) | Mean | 67.84 | 72.15 | 66.52 |
| | median | 72.12 | 63.98 | 65.84 |
| LOANS/Tot. Assets (%) | Mean | 64.36 | 60.03 | 59.30 |
| | median | 65.14 | 66.75 | 60.52 |
| LOANS/ Tot. Assets 04 (%) | Mean | 68.14 | 68.07 | 60.63 |
| | median | 68.05 | 69.85 | 58.43 |

A *k* sample test for statistical significance of differences in medians is performed and statistical significance at the 10%, 5% or 1% level are reported by *, **, *** respectively

Table 4 presents a selection of ratios for the entire Banche Popolari sector (36 institutions in total), over the period 2000-2004 and distinguishing among the three different organizational models adopted by the BPs: listed banking groups, unlisted banking groups and individual banks. For each variable and cluster the mean and the median values over the sample period and for the very last year under investigation (2004) are reported. A *k* test for differences in medians is also performed. More organizationally complex BPs, e.g. listed groups, are more than six times and 30 times larger than, respectively, unlisted groups and individual BP banks. Indeed, these nine groups cover more than 80% of total assets pertaining to the entire BP sector, present relatively more diversified income sources, bear lower credit risks, are less capitalized and show a higher propensity to lend with respect to the other BPs, i.e. vis-à-vis unlisted BP groups and individual BP banks. However, they do not show any specific ability in controlling costs/efficiency and, above all, notwithstanding their lower capital base, these groups are less profitable, although the 2004 figure shows some improvement. Their lower profit and efficiency profiles are most probably the consequence of their recent M&A campaign. As we will see in the next exercise, during the sample period large listed groups were involved in many M&A operations, which were, for most of the times, rescue operations of low performing BPs or joint stock banks: acquirors' cost-income ratios and profits became immediately worse after such operations and it takes some time to digest a rescue. This could be the worrisome aspect of the specific corporate governance of large and listed BPs, whose management, enjoying large amounts of free capital and seemingly being less subject to shareholders' control, notwithstanding the listed status, have been able to pursue dimensional increase goals with relatively less attention to cost control and profit maximization.

Our final empirical investigation deals with M&A operations completed in recent years, namely over the period 1999-2003. The main goal is to investigate the effect of different governance models on the success of the acquisition. The analysis concentrates on the profitability, efficiency, risk, capital adequacy and operational profiles of target banks before and after the acquisition, distinguishing between banks acquired by BPs and banks acquired by joint stock banks.

Table 5 Sample composition

| Bidder: Joint Stock Banks | | | Bidder: Banche Popolari | | |
|---------------------------------|--|------|---|------------------------------|------|
| Acquiring bank | Target bank | Year | Acquiring bank | Target bank | Year |
| Banca Regionale Europea | Cassa di Risparmio di Tortona | 1999 | BPL (then BPI) | Banca Federale Europea ICCRI | 1999 |
| Credito Emiliano | Banca del Garda | 1999 | | Banca Popolare del Bronte | 2002 |
| Monte Paschi | Banca del Monte di Parma | 1999 | ICCRI-Banca Federale Europea | Cassa di Risparmio di Imola | 2000 |
| | Banca del Salento | 1999 | Veneto Banca | Banca Italo-Romena | 2000 |
| Carige | Banca Agricola Mantovana | 1999 | BPER | Meliorbanca | 2000 |
| | Banca del Monte di Lucca | 1999 | | Banco di Sardegna | 2001 |
| Banca Intesa | Cassa di Risparmio di Parma e Piacenza SpA (Fondazione Cassa di Risparmio) | 1999 | | Banca Popolare dell'Irpinia | 2000 |
| CARIPLO | Cassa di Risparmio di Terni e Narni SpA (Fondazione Cassa di Risparmio) | 2002 | | Banca Popolare di Salerno | 1999 |
| Cassa di risparmio di Firenze | Cassa di risparmio di Orvieto | 2000 | Banca popolare di BG - Credito Varesino | Centrobanca | 2000 |
| Banca Lombarda e Piemontese SpA | Banca Regionale Europea | 2000 | | | |
| Rolo Banca | Banca dell'Umbria | 2000 | Banca Popolare Commercio e Industria | Carime | 2001 |
| Banca di Roma | Banco di Sicilia | 2002 | Centrobanca | IMI WEB | 2002 |

For each target bank we gathered financial statement information pertaining to –3 years before the deal and +3 years from the deal. Deals were included in the sample according to three criteria: a) the deal must be an acquisition, in order to obtain the relevant information about the separate performance of the target bank after the consolidation process; b) the deal delivers a relevant stake to the bidder, so that it can perform an influential if not a controlling role in the target’s board (Acquisition of at least 30% of target voting rights are deemed as controlling stakes); c) target banks’ financial statements are available for at least one year before and after the operation. Twenty-three operations satisfy the above mentioned criteria and are summarized in Table 5: 12 pertain to joint stock banks as bidders and 11 have BPs as bidders. We gathered information on M&A operations from the database Thomson Deals, while financial statement information is taken from the Bankscope database.

Table 6 shows financial ratios of targets before acquisition while Table 7 illustrates financial ratios after the completion of the acquisition, distinguishing deals according to whether the bidder is a BP or a joint stock bank. A t-test for statistical significance of differences in means is performed and statistical significance at the 10%, 5% or 1% level are reported by *, **, *** respectively.

Table 6. Ex-ante financial ratios of target banks

| | When bidder is a BP | When bidder is a joint stock | p values |
|---|---------------------|------------------------------|----------|
| ROA % | -1.87 | 0.53 | |
| ROE % | -5.28 | 6.12 | **** |
| Net interest margin % | 3.30 | 3.91 | |
| Operating income/total assets% | 5.84 | 4.95 | |
| Equity/total assets % | 13.53 | 9.97 | |
| NPL/Loans % | 20.82 | 17.82 | |
| Loan Loss Reserve / Gross Loans (%) | 7.81 | 5.22 | |
| Total capital ratio % | 17.19 | 12.76 | ** |
| Net interest revenue/total operating income % | 75.04 | 68.65 | |
| Net Loans / Total Assets (%) | 51.46 | 52.12 | |
| Net Loans / Tot Funding (%) | 63.99 | 64.43 | |
| Cost to Income Ratio (%) | 102.85 | 71.32 | |
| Personnel costs/Tot operating income % | 43.61 | 41.60 | |
| Operating costs/Total Assets % | 5.70 | 4.08 | |
| Personnel expenses /n. employees | 61.55 | 55.67 | |
| Loan/n.employees | 3,016 | 1,454 | |
| TA/ n.employees | 6,102 | 2,793 | |

t test for differences in means is performed and statistical significance at the 10%, 5% or 1% level are reported by *, **, *** respectively

The following outcomes stand out. The analysis of the pre-acquisition situation shows that BPs tend to acquire banks characterised by lower profitability ratios, lower revenue diversification and higher operational and credit risk with respect to those banks targeted by joint stock banks. Notwithstanding negative profits, targets tend to have stored up a larger amount of capital, which is a typical mark of BPs. After the acquisition, all targets show a general improvement in performance, although banks targeted by BPs keep having lower profitability (ROE) and efficiency ratios (cost-income) while higher capital availability (total capital ratio) as BP bidders tended to finance acquisitions through capital increase. Such differences may be attributable to the governance model adopted by BPs in M&As, which – via bilateral clauses conditioning the deal – may have limited their ability in restructuring the target bank and extracting value from the

acquisition. An alternative explanation highlights that the worst initial ROE e cost-income levels could justify the lower post acquisition performances: indeed, BP bidders had to put more efforts in “working out” low performing targets as the differences, in percentage points, between ex-ante and ex-post ratios highlight (col. 5-6 of Table 7). To be sure, targets of acquisitions by BPs show a more intense improvement after the deal in terms of increase of ROA and ROE.

All in all, the recent wave of acquisitions does not suggest that the governance specificity of the Banche Popolari renders them ineffective at restructuring the acquired banks. We gather some indications that the restructuring may have a lower pace for acquisitions by BP groups but the overall results improve visibly also in these cases.

Table 7. Ex-post financial ratios of target banks

| | When bidder is a BP | When bidder is a joint stock | p-value | % pt change after acquisition when bidder is a BP | % pt change after acquisition when bidder is a JS | p-value |
|---|---------------------|------------------------------|---------|---|---|---------|
| ROA % | 0.51 | 0.72 | | 2.39 | 0.20 | |
| ROE % | 5.01 | 9.49 | * | 10.29 | 3.37 | |
| Net interest margin % | 3.76 | 3.40 | | 0.46 | -0.52 | |
| Operating income/total assets% | 3.64 | 4.47 | | -2.17 | -0.48 | |
| Equity/total assets % | 12.55 | 8.25 | ** | -0.98 | -1.72 | |
| NPL/Loans % | 17.38 | 6.21 | | -3.12 | -10.12 | |
| Loan Loss Reserve / Gross Loans (%) | 6.90 | 3.56 | | -0.83 | -1.66 | |
| Total capital ratio % | 24.67 | 11.53 | *** | 6.80 | -0.17 | |
| Net interest revenue/total operating income % | 69.13 | 67.26 | | -5.91 | -1.39 | |
| Net Loans / Total Assets (%) | 49.48 | 63.50 | | -1.98 | 11.37 | ** |
| Net Loans / Tot Funding (%) | 61.20 | 77.38 | | -2.80 | 12.95 | |
| Cost to Income Ratio (%) | 95.11 | 70.87 | ** | -7.74 | -0.45 | |
| Personnel costs/Tot operating income % | 48.02 | 38.11 | | -2.73 | -3.49 | |
| Operating costs/Total Assets % | 3.63 | 3.62 | | -2.06 | -0.46 | |
| Personnel expenses /n. employees | 60.18 | 56.92 | | - | - | |
| Loan/n.employees | 3,900 | 2,209 | | - | - | |
| TA/ n.employees | 7,183 | 3,405 | | - | - | |

t test for differences in means is performed and statistical significance at the 10%, 5% or 1% level are reported by *, **, *** respectively

5. Conclusions

This paper focused on one of the two segments of Italy’s cooperative banks: the Banche Popolari (BPs). Even though featuring a cooperative set up, the BPs seek profit as much as the joint stock banks do. So, we should think of them as cooperatives with a limited propensity to mutuality. Nevertheless, the specificity of their corporate governance seems to favor the adoption of a longer term business focus by the Banche Popolari – vis-à-vis joint stock banks – which may benefit small business and the local communities they serve.

In particular, we investigated two governance-related issues. First, we assessed that the lower profit volatility of the BPs is to some extent accounted for by the higher stability of their board directors, as against the alternative factor identified in BPs’ lower reliance on noninterest income – where the literature points to high noninterest income as a source of profit volatility. Second, we found that the fast growing BP groups – contrary to the belief that their governance might make them less efficient as they grow – exhibit performances that are no worse than at other less dynamic BPs. In addition, examining the outcome of the numerous acquisitions made by the fast growing BP

groups, we found that the post acquisition performance improvement of target banks is not significantly worse with respect to acquisitions made by joint stock banks.

Thus, the governance specificity of the Banche Popolari seems to be still effective and the current proposals by some experts to transform the BPs into joint stock banks appear largely ill grounded. It seems that the transformation under discussion might disfavor the small businesses and the local communities served by the BPs as the Banche Popolari could then lose the long term business focus due to their specific governance set up.

Regarding the large listed BP groups, it is true that their contestability may be lower in the short term than that of (some) joint stock banks. However, the fact that they are listed may be strengthening their traditional cooperative governance mode. Namely, shareholders can more quickly – and in continuous time – observe the market assessment and, possibly, this promotes more (not less) activism on their part at the annual members' meetings. In turn, this mechanism likely increases the medium-long term contestability also for the Banche Popolari and, thus, introduces incentives to proper behavior on the part of BP directors and top managers also for the short term.

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