Mini Review
Volume 11:8, 2022

Business & Financial Affairs

ISSN: 2167-0234

Open Access

Public Banking: From Feasibility to Implementation

Curtis J. Gregory*

Temple University, 1801 Liacouras Walk Alter Hall, Room 542, Philadelphia, PA 19122, USA

Abstract

The purpose of this study is to explore the obstacles towards implementation of a public banking system within the United States through a review of the literature on public banking. A review of the literature on public banking demonstrates fluidity in the definition of public banking as legislative efforts attempt to take the path of least resistance towards implementation. This study provides macro and micro benefits and challenges for formation. Global examples of public banking systems are reviewed along with political challenges in coordination and cooperation learned from the COVID-19 pandemic. This literature review concludes with practitioner observations at the micro level on the potential impact in forming a public bank.

Keywords: Public banking • Implementation • Macro and micro benefits • Banking systems • Public policy • Money • City of Philadelphia

Introduction

On March 10, 2018, in Loveland, Colorado a retreat on the topic of Public Banking was convened through an anonymous donation to the Public Banking Institute. This small group consisted of scholars, bankers, elected officials, public servants, and activists from all over the United States. The objectives of the retreat were to share best practices, identify strategies, and discuss potential obstacles towards implementation of public banks throughout the United States of America (USA). As a participant in the retreat, the experience provided foundational context, varied perspectives on the obstacles for implementation, and incentive towards future research opportunities. The strategies regarding implementation of a public bank require proficiencies in public policy, money, and banking, along with political savvy and/or agility.

Public banks are different from private banks as their mandate begins with the public's interest and are owned by the public since their funds come from a state or local governing body [1]. This concept of placing value in stakeholder's interests over shareholders' interests is also referenced as a stakeholder management theory [2]. Stakeholder theory is defined by assigning an economic unit of measure to stakeholders such as employees, customers, suppliers, financiers, and even competitors [2]. Although there is agreement that public banks are publicly funded and therefore publicly owned, there are discrepancies around whether the bank is controlled by a municipality, city, or state or run privately through a holding company [3,4]. In a feasibility study for the City of Philadelphia, HR&A Advisors [3] provided a comprehensive list of resources for financial services divided by commercial banks, non-traditional banking services, mission driven institutions, and city efforts of programs and services. Even with the acknowledgement of a long list of resources for access to capital, demand for capital in underserved communities continues to be elusive [3,5].

There are 32 states with active legislation around public banking and four pieces of legislation at the federal level being given consideration in the USA [1]. Additionally, eighteen public bank bills were introduced in 2021 [6]. These legislative efforts center around the feasibility of a public bank at a city or municipal level or at the state or commonwealth level [1]. Despite the recognized financial success and community impact of the Bank of North Dakota that has been in existence for over 100 years, no city or state has implemented a public bank in the USA [3,1]. The Bank of North Dakota remains as the only state-level public bank in the USA [7].

The creation of the Bank of North Dakota (BND) initially was a strategy to address access to capital for the underserved agriculture industry but evolved over time to become an economic development strategy with the first transfer of funds to the State's General Fund occurring in 1945 [8]. The history of BND is a compelling one as examples of the bank focusing on their stakeholders as opposed to their shareholders is prevalent. From recovery funding during the floods of 1997, participations loans for development in 1967, to paying teachers during the Great Depression, BND has been a resource for North Dakota [8]. The passion of activists eager to find resources for the underserved communities of minority and women owned businesses is easy to understand, as public banking as seen through the BND model, appears to be a viable solution to the problem of access to capital. Why are cities and states still conducting feasibility studies instead of implementation plans? Does an environment of where the old economy is preventing a new economy from emerging exist? Why is there belief that a Public Bank will meet the demand of access to capital over existing financial resources such as community development financial institutions (CDFI)? This review of the literature will explore public banking from a global perspective to see if there are lessons to be learned from the success or failure of public banks outside of the USA.

Problem or Challenge

There is empirical analysis around three different countries that share the commonality of a significant public sector in banking [4]. Brazil, Germany, and India have significant differences with India having significant numbers of unbanked households, and Germany representing a mature financial market and one of the places where public banking started [4]. Brazil provides an opportunity to research how public banking can provide stabilization to a financial market through anticyclical interventions [4]. Most of the activist driven research and narrative around public banking looks to solve the challenges of access to capital in underserved or unbanked communities [9,3], but there is research that demonstrates an opportunity for public banks to play a role in macroeconomic policies or economic development strategies [4].

Flögel F and Gärtner S [10] in their qualitative study found significant differences between banking systems in the United Kingdom (UK), Germany, and Spain. Of particular interest is the elimination of savings banks in 2017 along with failures of small and regional banks in the UK [10]. Comparatively, 3,400 U.S. based financial institutions have failed since the mid-1980s as of 2012 with 457 representing community banks [11]. The study by Flögel and

***Address for Correspondence:** Curtis J. Gregory, Temple University, 1801 Liacouras Walk Alter Hall, Room 542, Philadelphia, PA 19122, USA, E-mail: curtis.gregory@temple.edu*

Date of Submission: 22 August, 2022, Manuscript No: jbfa-22-72532; **Editor assigned:** 23 August, 2022, PreQC No: P-72532; **Reviewed:** 29 August, 2022, QC No: Q-72532; **Revised:** 27 September, 2022, Manuscript No: R-72532; **Published:** 03 October, 2022, DOI: 10.37421/2167-0234.2022.11.415.

Gärtner [10] is a focus on centralized banking systems vs decentralized banking systems with a recommendation for the UK to consider a network of local and public banks. Restructuring of the Royal Bank of Scotland into a network of local and public banks is mentioned in the article as a potential strategy [10]. One of the challenges in implementing a public banking model in the U.S. is that a considerable number of feasibility studies are predicated on creating and starting a public bank as opposed to restructuring an existing bank [3,1]. There is also the challenge of cooperation among all the states and municipalities. The COVID-19 pandemic illustrated the need for political cooperation as members of the World Health Organization (WHO) experienced difficulty in coordination problems and cooperation problems [12]. Benvenisti [12] articulates lessons learned from the SARS outbreak and the COVID-19 pandemic in terms of the effectiveness of the WHO and calls for the need to refit this organization with the power to secure interstate cooperation. This presents a possible need for an umbrella organization that ensures coordination and cooperation among a network of local and public banks as public bank by definition would be outside of the Federal Reserve Banking System.

Uğurlu and Epstein [7] point out that the BND model of public banking is a partnership model between the state funded bank and other financial institutions. A feature worth noting is that in the partnership model the public bank does not compete with private banks for retail deposits and relies primarily on interest and fees associated with lending activities [7]. HR&A Advisors [3] project a return on assets (ROA) of 1.42% to 1.46% in their feasibility study for a public bank in the City of Philadelphia if the city were to incorporate a small business lending component to their small business support model. This ROA aligns with research from the Roosevelt Institute's 1% projected ROA [9]. This conservative estimate of a 1% ROA translates into $15 million in profit for a $15 billion portfolio, provides context on why elected officials are investing time and energy on public banking [9].

The worldwide public health emergency of COVID-19 has emerged as a global economic crisis as countries continue to struggle with the socioeconomic challenges in the short-term and long-term objectives of macroeconomic policies [13]. Consumers have had firsthand experience with the USA's weaknesses in healthcare, supply chain management, economic development, and access to capital. "Change happens when the pain of staying the same is greater than the pain of change" [14]. The economic and social disparities that have been highlighted by the COVID-19 pandemic have activists re-energized around the role public banks can play as new economic policies start to emerge. One of the topics from the 2018 public banking retreat in Loveland, Colorado was on the need for banking services for the emerging cannabis industry. Medicinal and recreational cannabis is still considered illegal at the federal level but as more states and municipalities move towards the legalization of cannabis, the industry has been limited by having to do business on a cash basis only. The majority of merchants that provide credit card services and cash management services are part of the Federal Reserve Banking system thus creating legal challenges for cannabis distributors to accept credit cards. The strategic solution is that a public bank can be set up to receive deposits from the cannabis industry and in return provide access to credit and merchant services enabling them to receive credit and debit card transactions.

Solution/Results

The recession of 2017 demonstrated the cyclical behavior of markets and the corresponding regional or sector inequalities that could be reduced through the alternative of a public bank [4]. The definition of what constitutes a public bank appears to be fluid as control of the bank fluctuates depending upon the audience or legislative steps required for implementation [3,1]. There is agreement among the eighteen public bank bills that the bank is publicly funded [6], but inconsistency as to the control of the bank. Feasibility studies fluctuate as to whether the proposed public bank be privately run, under government control, or a quasi-government agency. There is research that suggests the answers to these questions depends on whether the objective of the bank is to allocate resources to segments of the economy that will generate income and employment, or to meet the credit demands in underserved economic segments and geographical areas [4].

A considerable number of feasibility studies and research around public banks focuses on the impact of a public bank from a macro perspective. Missing from these feasibility studies is the potential impact of a public bank at the operational or micro perspective. In conversations with small business lenders or commercial lending officers there are often references to the credit policy of a financial institution. The credit lending policy determines a financial institution's standards, objectives, and risk parameters for lending activity and there is an opportunity to manage credit risk on the national financial system of the bank [15-18]. When I was a Senior Vice President in banking I would ask to review the credit lending policy during the exploratory phase of an interview and selection process for jobs in commercial lending. What I learned from working for 4 top 10 US based financial institutions is there is consistency if not duplication of the credit policy from one institution to another. Furthermore, the credit policies of financial institutions still are weighted towards an industrial or manufacturing based economy. Typically, within the credit lending policy is a list of cautionary industries or industries that a commercial lender should proceed with extreme caution in advancing capital Over the years of leading various commercial lending teams it became apparent that the majority of growth in our (USA) economy was within the service or knowledge based industries and or credit policies leaned in favor of a manufacturing based economy.

Conclusion

A public bank with a credit policy designed and written to the satisfaction of stakeholders as opposed to shareholders offers an opportunity to impact underserved communities and socio-economic objectives. In my 9 years of public service within the Commerce Department for the City of Philadelphia it was common to see CDFI underwriting and credit policies that were synonymous if not identical to the credit policies of privately owned banks. The formation of a public bank has the potential for positive economic impact as demonstrated by the BND, but attention needs to be given to the design of the public bank from a micro-perspective focusing on the credit policy of the proposed bank. Imagine a bank with a credit policy that focuses on the community's infrastructure, educational, or affordable housing needs and shifts the objective from the needs of the shareholder to the needs of the stakeholders.

Acknowledgement

None.

Conflict of Interest

None.

References

1. https://publicbankinginstitute.org/
2. Parmar, Bidhan L., R. Edward Freeman, Jeffrey S. Harrison and Andrew C. Wicks, et al. "Stakeholder theory: The state of the art." *Acad Manag Ann* 4 (2010): 403-445.
3. https://www.phila.gov/media/20200930101919/Philadelphia-Public-Bank-Feasibility-Study_-FINAL_Sept-2020.pdf
4. Scherrer, Christoph, ed. Public banks in the age of financialization: A comparative perspective. *Edward Elgar Pub* (2017).
5. Wiersch, Ann Marie and Scott Shane. "Why small business lending isn't what it used to be." *Econ Comment* 10 (2013).
6. https://publicbankinginstitute.org/
7. Ugurlu, Esra Nur and Gerald Epstein. "The Public Banking Movement in the United States: Networks, Agenda, Initiatives, and Challenges." (2021).
8. https://bnd.nd.gov/history-of-bnd/
9. Beitel, Karl. "Municipal banking: An overview." *Roosevelt Institute* (2016).

10. Flögel, Franzand Stefan Gärtner. "The banking systems of Germany, the UK and Spain from a Spatial Perspective: The German Case." (2018).
11. Parsons, Richard J. Broke: America's Banking System. *Risk Manag* (2013).
12. Benvenisti, Eyal. "The WHO—Destined to fail?: political cooperation and the COVID-19 pandemic." *Am J Int Law* 114 (2020): 588-597.
13. Loayza, Norman and Steven Michael Pennings. "Macroeconomic policy in the time of COVID-19: A primer for developing countries." *World Bank policy res work* (2020).
14. https://www.goodreads.com/quotes/7957460-change-happens-when-the-pain-of-staying-the-same-is
15. Cociug, Victoria and Victoria Postolache. "The essence of credit policies and methods for perfecting this from the prudential perspective." (2019).
16. Bhatti, Saqib and Renaye Manley. "Dirty deals: how Wall Street's predatory deals hurt taxpayers and what we can do about it." *J L Soc'y* 17 (2015): 65.
17. Parekh, Sandeep. "Disclosure duplication a waste of time and money." *Int'l Fin L Rev* 24 (2005): 47.
18. Bolton, Patrick and Joseph Farrell. "Decentralization, duplication, and delay." *J Political Econ* 98 (1990): 803-826.

How to cite this article: Gregory, Curtis J. “Public Banking: From Feasibility to Implementation.” J Bus Fin Aff 11 (2022):415.