

# **RISK MANAGEMENT IN LITHUANIAN AND IRISH CREDIT UNIONS: TRENDS AND IMPACTS ON CREDIT UNION DEVELOPMENT**

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## **Abstract**

The goal of this paper is to examine the Irish and Lithuanian credit union movements in terms of risk management and risk performance and to discuss credit union risk regulation. Risk management in credit unions often closely relates to credit union development stages so that as credit unions mature, higher standards of risk management should be implemented. In some cases these changes are accompanied by shifts in the regulatory framework. A comparison of the situations in Lithuania and Ireland offers some interesting and sometimes unexpected contrasts in the levels of credit union regulation. Despite the comparatively advanced stage of development of the Irish movement, key aspects of risk regulation are considerably more lenient than in Lithuania, where the credit union movement is far smaller and less developed, yet at the same time, more tightly regulated. This comparison demonstrates that the regulatory regime is not always aligned with the stage of credit union development and may, indeed, reflect the economic policies of the country in which they operate.

## **Introduction**

Risk management in banking has always been an issue for State regulators and management bodies in banks. Risk is the major factor influencing the value of a bank and the effectiveness of its activities. Though credit unions are acting in the same retail banking market as conventional banks, they are often excluded from the State regulation of banking performance because of the differences in their structure and activities. Internal procedures for credit union risk management also differ from those in commercial banks. Market laws that set the value of capital (shares) do not influence credit unions as they have a limited number of member-owners and as their shares are not traded in the market. As credit union members are also owners of credit unions, corporate management problems (arising from the interrelationship between owners and managers) do not exist. Because of these reasons, the board of directors in a credit union often avoids pressure to develop risk management procedures and to control the risk of credit union activities. In some cases, inadequate management of risk may lead to the bankruptcy of individual credit unions or the entire credit union network.

Risk management in credit unions often closely relates to credit union development stages. As credit unions develop, the professionalism and high standards of risk management in credit unions should develop. Along with the expansion in credit union services and activities and the introduction of central financial services for credit unions, this often leads to an increase in the regulation of credit union activities.

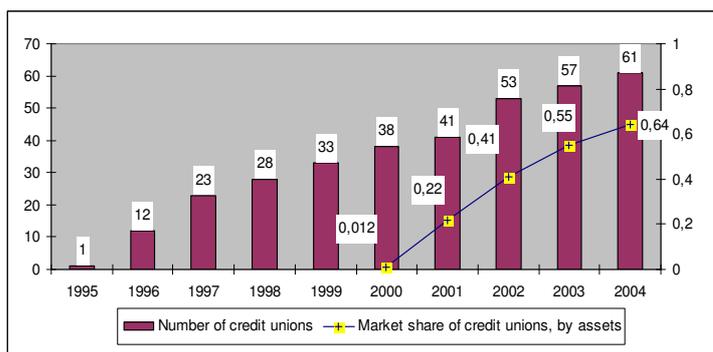
Mature cooperative banking systems in most countries in the EU are regulated by the same rules as their competitors, conventional banks, although credit unions in most European countries (including new entrant countries in the EU) have exemptions from banking regulations. Increasing competition in the retail banking sector raises the question of whether credit unions, acting in the same retail banking market, should enjoy such exemptions and or should have the same standards of risk management as conventional

**The goal of this paper** is to analyze risk management and risk performance indicators in the Lithuanian and Irish credit union movements and to discuss credit union risk regulation and its impact on further credit union development in the single European market. A comparison of the situations in Lithuania and Ireland offers some interesting and sometimes unexpected contrasts in the levels of regulation of credit unions in both countries. Despite the comparatively advanced stage of development of the Irish movement, key aspects of risk regulation are considerably more lenient than in Lithuania, where the credit union movement is far smaller and less developed. This comparison helps to show that the regulatory regime is not always aligned with the stage of credit union development and may, indeed, reflect the economic policy of the country in which they operate.

### Credit Union Development in Lithuania and Ireland

Lithuania and the Republic of Ireland are of similar size and have similar size populations (3.5 million in Lithuania and 4 million in Ireland). Following the restoration of independence from Soviet rule in 1990, Lithuanian governments have worked to establish a sound institutional and regulatory framework and an economy built on free-market principles. Success is evident in high growth rates in Gross Domestic Product (GDP), and significantly lowered rates of inflation and unemployment. Weakness in the banking sector was one particular challenge facing the country. Lithuania’s banking reform program has strengthened risk management in the banking sector to ensure compliance to international standards.

In 2005, 61 credit unions were active in Lithuania. Total assets of credit unions were 185 million Litas (1 Lt = 3.4528 Euro). Loans to credit union members form the majority of credit union assets. The total loan portfolio is 132 million Litas. Members’ deposits form the majority of credit union liabilities (148 million Litas). Although market share of credit unions, at 0.64 percent of the total banking assets, in Lithuania is still very small, it is increasing rapidly (for example, in January 2000, it stood at 0.09 percent). (See Figure 1)



**Figure 1** Number of credit unions and credit union market share by assets in Lithuania for 1995-2004  
 Source: Compiled by authors based on various materials of the Association of Lithuanian Credit Unions

This is explained by higher credit union growth rates when compared to the conventional banking sector: bank assets during 2004 grew by 32.3 percent while credit unions grew by 50.6 percent; bank loans grew by 39.7 percent while those of credit unions grew by 51.6% (Lithuanian Central Bank, 2004).

According to the Ferguson & McKillop (1997) typology of credit union development, credit unions in Lithuania are in the *transitional* stage of development. In order to reach the highest (*mature*) level, credit unions should experience large asset size, deregulation, a loose common bond, a competitive environment, highly developed information technology networks, professional management, well-developed central services, diversification of products and services, products and services based on market rate structures, and rigorous financial management of operations.

Ireland, too, has experienced impressive economic growth, with low rates of inflation and extremely low unemployment. The credit union movement in Ireland, being much older than the Lithuanian movement, is considered to be far more developed than the Lithuanian movement. It demonstrates many of the characteristics of this *mature* stage of development. There are currently approximately 600 credit unions on the island of Ireland. 531 of these are affiliated to the Irish League of Credit Unions (ILCU) and a further 60-70 are affiliated to other umbrella organizations, such as the Credit Union Development Association (CUDA) and the Ulster Federation of Credit Unions (UFCU)<sup>1</sup>. Total assets of the movement in Ireland reached €12.5 billion by the end of 2004, total lending was in excess of €5 billion, and total savings were almost €11 billion.

A comparison of the credit union movement in Ireland and in Lithuania is interesting because it reveals that, despite the fact that the Irish movement is more developed than the Lithuanian movement, it faces more lenient regulation. This is likely to be the result of strict economic reform of the banking sector in Lithuania, which incorporates credit unions, and a more *laissez-faire* approach to credit union regulation, at least until more recently, in Ireland.

Table 1 shows a comparative analysis of various indicators of credit union penetration in Ireland and in Lithuania.

**Table 1**  
**Comparative analysis of credit unions indicators in Ireland and Lithuania for 31<sup>st</sup> of December, 2003<sup>2</sup>**

	Ireland (ILCU)	Lithuania
<b>Relative indicators per 1000 inhabitants:</b>		
Members/1000 inhabitants, North and South of Ireland (approx)	526	9
Assets, EUR/1000 inhabitants	1,599,000	9,899
Total amount of members' savings, EUR/1000 inhabitants	1,427,806	7,509
Total amount of loans, EUR/1000 inhabitants	902,957	6,995
<b>Relative indicators per 1 member of credit unions:</b>		
Assets, EUR/ per 1 member	3319.14	1113.98
Total amount of loans, EUR/ per 1 member	1894.56	845.07
Total amount of savings, EUR/ per 1 member	2962.96	787.18
<b>General indicators</b>		
Average membership in a credit union	5075.19	551.72
Market share (comparing by personal savings, %)	14.6%	1%
Market share (comparing by personal credit, %)	27.4%	3.55%

Source: Lithuanian Central Bank (2003), Department of Statistics in Lithuania (2003), Irish League of Credit Unions (2003), Irish League of Credit Unions (2004).

<sup>1</sup> For accuracy, figures presented in this paper refer to ILCU-affiliated credit unions only.

<sup>2</sup> For Ireland, we use the 2002 figures.

The Irish credit union movement has been in operation for more than 45 years and Table 1 shows that Irish credit unions are now very widespread. 526 inhabitants out of every 1000 in Ireland (Republic of Ireland and Northern Ireland) are members of a credit union, that is, one half of the population is a credit union member. In Lithuania, 9 people per 1000 are credit union members.

The table also shows that credit unions in Lithuania are, on average, three times smaller in assets, loans and savings per member when compared to credit unions in Ireland. In comparing market share, Lithuanian credit unions have the smaller market share, in terms of personal savings, at only 1 per cent. Credit unions in Ireland have 14.6 per cent of the total market for personal savings. In terms of personal credit, Lithuanian credit unions have 3.55 per cent of the market share, while credit unions in Ireland have 27.4 per cent market share. From the comparative analysis we see that credit unions in Lithuania (in comparing relative indicators per member) are quite well developed, even when compared to Ireland. But Lithuanian credit unions have a very small level of penetration.

### **Credit union risk regulation**

Supervising institutions set certain standards and regulations for credit union activities that define risk and specified limits for credit union risk exposure. Prudential regulations are extremely important and establish minimum operational requirements. Rules and regulations should be drafted specifically to address credit union operations and their mutual-based ownership structure. Regulators should ensure:

- That adherence to the rules and regulations is not overly burdensome for the credit unions or their members;
- That rules and regulations are appropriate to the size of the institutions regulated.

To effectively regulate and supervise credit unions, prudential regulations should be developed to address, at a minimum, the following areas: capital adequacy, asset classifications/allowance for asset losses, licensing and entry requirements, liquidity risk, investments into fixed assets, member loans and portfolio diversification, calculation of loan delinquency, external credit, investment activities, standardized accounting, external audits, nonmember deposits, and voluntary and involuntary liquidation and merger (Regulatory Standards, 2002).

Lithuanian credit unions act under the Amendment Law of the Lithuanian Credit Union Law, 2000. The Law sets certain risk limitations: credit union membership is limited by the common bond – members of credit unions may be persons of the same occupation, working at the same enterprise, living in a ward or belonging to the same non-governmental organisation (NGO); the minimum shareholding of a member is 100 Lt; 50 persons are required as a minimum number of members to start a credit union; minimum share capital is set at 15,000 Lt. The Law describes and sets limits for the extent of credit union activities (for example, credit unions can take deposits from their members, governmental organisations and NGOs and grant loans only to their members, with limited possibilities to invest elsewhere (except government bonds and deposits in the Central credit union); the maximum amount of a loan to one member must not exceed 10 percent of total deposits, and the size of the loan should not exceed 10 times that member's share. The Law also regulates the credit union governing bodies and sets their responsibilities. The Lithuanian Central Bank acts as a Supervisory Institution for credit unions. It has rights to set prudential standards for credit union activities. The Lithuanian Central Bank regulates credit union liquidity by setting minimal liquidity ratios at 30 per cent or greater and capital adequacy ratios at 13 percent or greater. It holds an open position on foreign currency and also sets standards for bad debts and bad debts provisions.

The State regulation of Irish credit unions in the Republic of Ireland is the responsibility of the office of the Registrar of Credit Unions (RoCUs), a distinct entity operating under the Irish Financial Services Regulatory Authority (IFSRA)<sup>3</sup>. This is a relatively new regulatory body established by the Irish government in May 2003. Prior to this, credit unions were regulated by the Registrar of Friendly Societies (RoFS) who also regulated the activities of all co-operatives. However, in the wake of a series of banking scandals (in conventional financial institutions), IFSRA, a new regulating body was set up to regulate and control the activities of all financial institutions in the Republic. Recognizing the unique nature of credit unions and their need for a distinct regulatory style, the office of the RoCUs was established to regulate credit union activities alone within IFSRA. Prior to May 2003, credit unions were required to submit annual returns only to the RoFS. Monitoring, in terms of risk management, was more rigorously carried out by the Irish League of Credit Unions (on a non-statutory basis) as part of its savings protection scheme. The ILCU used the CAMEL (Capital adequacy, Asset Quality, Management Quality, Earning and Operating Efficiency, Liquidity) ratios until 2003 and then changed to the PEARLS (Protection, Effective financial structure, Asset quality, Rates of return and cost, Liquidity, Signs of Growth) ratios as advocated by the World Council of Credit Unions (WOCCU). Under the new regulatory regime, the precise nature of regulation is still somewhat uncertain. The Regulator has drawn up a quarterly prudential return, having consulted with the credit union movement on its layout and contents. At present, only an approximate 60 credit unions must submit this return to the Regulator. All ILCU-affiliated credit unions must submit this return to the ILCU from which the ILCU calculates the PEARLS ratios. It is unclear to date what use the Regulator makes of the return. It is likely that issues such as liquidity and bad debts are monitored but this has not yet been communicated to credit unions. Since taking office, the Regulator appears to have placed an emphasis on checking breaches of legislation by credit unions rather than on financial ratios. The ILCU continues to produce the PEARLS ratios but one could speculate that at some point in the future there will be some merging or takeover of monitoring activity. This all remains very uncertain, however.

Credit union regulation in the Republic of Ireland is governed by the Credit Union Act (1997), which gives substantial powers to the Regulator. Under Section 84.1 of the Act, the Regulator must

- a. ensure that credit unions protect the funds of the members
- b. maintain the financial stability and well-being of credit unions generally.

In so doing, the Regulator has the *'power to do anything which, in his opinion, is necessary to facilitate the exercise of his functions'* (Section 84.2). The Act contains similar clauses to those in Lithuania – membership is confined to those holding the common bond, services are confined to members, the minimum number of members is 15, and so on. There are also prescribed limits on the amount of loans and savings held by any individual member: members can be in debt to the credit union for a maximum of €39,000 or 1.5% of the total assets of the credit union, whichever is the greater; members can hold a maximum of €26,000 in deposits and a total savings (shares and deposits) of €64,000 or 1% of the total assets of the credit union, whichever is the greater. Additional services (other than those currently provided) must receive the prior approval of the Regulator before they can be offered to the members.

Table 2 shows aspects of credit union risk regulation for the three major risk areas – capital adequacy, liquidity and loans (or credit risk). Lithuanian credit unions have the more strict regulation in terms of capital adequacy – 13% of risk-weighted assets, where the calculation of capital is based on Basel

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<sup>3</sup> Regulation of credit unions in Northern Ireland does not fall within the remit of IFSRA because they operate within a different jurisdiction. However, ILCU-affiliated credit unions operate in both jurisdictions and must meet ILCU requirements.

requirements. Comparing Irish and Lithuanian credit unions, Lithuanian credit unions also have stricter provisions for bad debts. In Lithuania, loans have to be written-off if they are overdue by more than 181 days. In Ireland the same requirement comes into force for loans that are overdue more than 53 weeks (371 days). It is difficult to compare liquidity requirements, as the basis for the obligatory reserves calculation is different.

**Table 2**

**Comparison of Risk Regulation in capital adequacy, liquidity and bad debts provisions for credit unions in Ireland and Lithuania**

ASPECTS OF REGULATION	Republic of IRELAND	LITHUANIA
<b>1. CAPITAL ADEQUACY</b>		
Does regulatory agency intend to accept Basel II?	No, although there is one regulatory agency	Yes
Possible influence of Basel II on capital	Uncertain	Yes
Minimum ratio of capital to assets	There is no minimal requirement, PEARLS standard is applied	13 percent of risk weighted assets
How capital is calculated	Reserves are obligatory. No less than 10 percent of surplus funds to be allocated each year.	A percentage of risk weighted assets
<b>2. LIQUIDITY</b>		
Risk evaluating components and changes	There are none. Irish law does not classify loans. ILCU recommends that loans due more than 12 months should be written off.	Overdue loans are classified according to the requirements of Central Bank.
Does National regulator regulate liquidity?	No, but this may change.	No
Who is responsible for maintaining liquidity in the system?	Irish League of Credit Unions, for affiliated credit unions	Lithuanian Central Credit Union
Is the size of the liquidity reserve required the same as for banks?	No	No
Obligatory reserves ratio	Must maintain liquidity reserves of at least 20% of total unattached / uncommitted savings	1.2 percent of total liabilities
<b>3. PROVISIONING/ CHARGE OFF SCHEDULES</b>		
Provisioning/Charge-off Schedules	Irish League of Credit Unions AGM Resolution 49: 0-9 weeks – 0% 10-18 weeks – 10% 19-26 weeks – 20% 27-39 weeks – 40% 40-52 weeks – 60% 53 weeks and over – 100%	Lithuanian Central Banks sets the following standards for bad debt provisions, calculated on the net loan balance: 0 - 60 days – 0 % 61- 90 days – 20 % 91- 180 days – 40 % > 181 days – 100 %

Source: Compiled by authors using data provided by Irish League of Credit Unions (2004), Prudential Standards (2003) and Evans & Richardson (1999)

The results of the analysis show that although Lithuanian credit unions are at a less developed stage than Irish credit unions, the requirements, at least for capital adequacy and loan provisions, are higher than in Ireland. Lithuanian credit unions have to follow the standards that are applied to the banking sector, or even more strict standards. For example, the minimum capital adequacy requirements for Lithuanian banks are 10 percent and are soon to be decreased down to 8 percent, while the minimum capital adequacy ratio for credit unions is 13 percent. This situation may also indicate that the regulation of Lithuanian credit union activities is stricter than it should be for their stage of development. We may also make an assumption that strict regulation influences the development of credit unions in Lithuania and, in some cases, becomes inappropriate considering the changing requirements caused by credit union development.

Credit unions in Lithuania offer a far broader range of financial services in comparison to Irish credit unions. At the end of the first half of 2005, Lithuanian credit unions offered their members share accounts, current accounts, and savings accounts (for children and pension savings) as well as short term and long term deposits. Lithuanian credit unions offer their members loans of one month to twenty years' duration. Loans are granted for personal and business purposes (including small and medium and agricultural businesses) as well as for mortgages. Together with loans, credit unions offer credit lines and overdrafts for the short term borrowing needs of their members. In the next two years, Lithuanian credit unions plan to implement credit and debit cards and internet banking services.

In some respects, the kinds of services provided by Irish credit unions are more limited in scope, primarily because the enabling technological infrastructure is not fully in place to offer services involving Electronic Funds Transfers (EFT). Credit unions in Ireland provide savings and lending services, budgeting services and financial counselling, as well as life savings protection and loan protection. Through various agency agreements, they also offer insurance services, foreign exchange and money transfer, for which they receive commission. Until Irish credit unions can network more closely together, technologically speaking, they will be unable to expand their services very much. This is being impeded by the wide range of software systems already in place in credit unions, the cost involved in networking, and a general reluctance and fear to network with other credit unions. Furthermore, the Regulator has, to date, refused to give permission to a number of initiatives designed to enable credit unions to offer more technologically-based services, further impeding the efforts of credit unions to develop their range of services.

### Risk indicators in Ireland and Lithuania

For a more thorough analysis of credit union risk exposure in Lithuania and Ireland, the authors focus on a number of risk indicators that provide information about the size and quality of the loan portfolio (bad debts provisions and loans/total assets ratio), the proportion of investments (investments to total assets), and also growth ratios such as growth of loans, investments and members shares.

In Lithuania, bad debts provisions are calculated under the regulation of the Lithuanian Central Bank. The regulation sets the following provisions for overdue loans:

- 20% for loans overdue more than 2 months (60 days)
- 40% for loans overdue more than 3 months (90 days)
- 100% for loans overdue more than 6 months (180 days).
- Loans for which 100% provisions have been made should be written-off within two months (For grouping doubtful assets and provisions for doubtful assets, 2003).

Loans overdue as a % of total loans	00.03.31	00.09.30	01.03.31	01.09.30	02.03.30	02.09.30	03.03.31	03.09.30	04.03.31	04.09.30	05.03.31
up to 30 days	6,7	11,93	9,5	9,92	9,58	10,25	10,74	12,58	10,59	13,1	12,12
30 - 60 days	2,34	1,88	1,33	1,01	2,23	1,65	2,21	1,53	2,88	2,29	2,6
61 - 90 days	0,74	1,18	1,79	0,58	0,96	0,66	0,89	0,79	1,28	0,63	0,53
91 - 180 days	1,69	1,06	0,55	0,84	0,71	0,8	0,92	1,08	1,2	1,16	0,44
more than 180 days	0,29	0,52	0,58	0,43	0,39	0,25	0,24	0,33	0,31	0,41	0,44
	00.03.31	00.09.30	01.03.31	01.09.30	02.03.30	02.09.30	03.03.31	03.09.30	04.03.31	04.09.30	05.03.31
Provisions for bad loans, % of total loans	1,23	1,35	0,89	0,76	0,63	0,43	0,5	0,59	0,62	0,8	0,72

**Table 3 Loans overdue and provisions for bad debts as a % of total loans 2000-2005 in Lithuanian credit unions**

Source: Compiled by authors based on various material of the Association of Lithuanian Credit Unions

As we can see from the analysis, the quality of the loan portfolio in Lithuania has not changed dramatically over the last five years (see Table 3).

In Ireland, bad debts provisions laid down by the Irish League of Credit Unions are as follows:

- 0-9 weeks – 0%
- 10-18 weeks – 10%
- 19-26 weeks – 20%
- 27-39 weeks – 40%

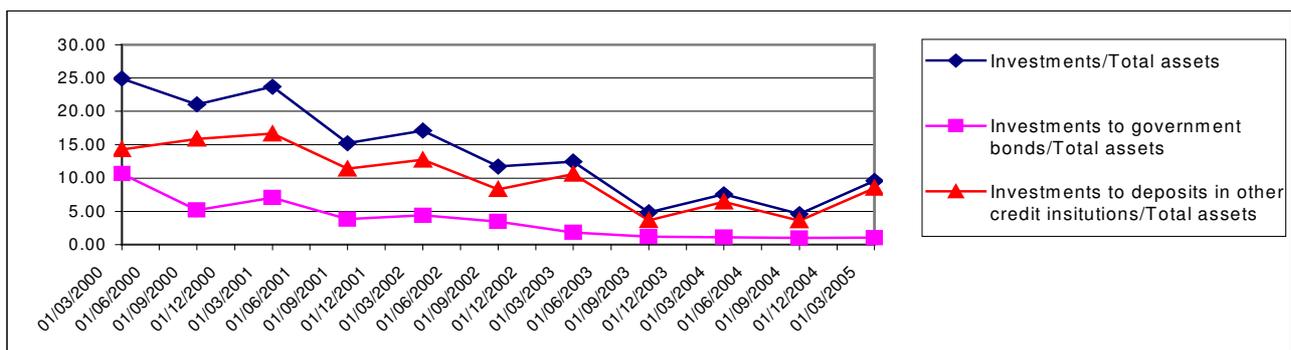
- 40-52 weeks – 60%
- 53 weeks and over – 100%

Bad debts provision ratios have been in operation for many years in the Irish credit union movement as part of its Savings Protection Scheme, which set basic requirements for provisions by all affiliated credit unions. More strict provisions were put in place in October 2004. According to the PEARLS ratios, bad debts provisions for affiliated credit unions were 129.5% in March 2005, where the minimum requirement is 100%. Therefore credit union risk in terms of bad debts is well-covered according to PEARLS in Ireland.

The other ratio we have analyzed is the ratio of loans to total assets. The loans to total assets ratio is a very important indicator of credit union competitiveness in the market. The ratio recommended by PEARLS is in excess of 70%. In March 2005, the ratio was 56.06% in Lithuania and 49.56% in Ireland. These ratios are low in comparison with the PEARLS recommendations. In Lithuania, this can be explained by the fact that most Lithuanian credit unions are owned by farmers. In the months prior to March, demand for loans is low. If we were to look at the same ratio at the end of June, the average would be much higher (e.g. loans to total assets ratio at the end of June 2004 was 77.27 %). In Ireland, the low ratio is explained by the intense competition in the market for personal loans all year around, and not by seasonal fluctuations. New entrants into the lending market, such as supermarkets, and a far greater number of banks, have made it more and more difficult for credit unions to sustain lending. One might be tempted to speculate that the increasing affluence of Irish people is another explanation for decreased levels of borrowing. However, considering that personal debt has grown by 300% in the past 3-4 years, it is clear that credit union members are accessing credit from other financial institutions.

The ratio of total loans to total assets has been declining for a number of years (for example, in 2003 it was 54%, and in 1999 it was 64%). This has been a key concern for credit unions resulting in reductions of loan interest rates in order to sustain competitiveness.

The authors have also analyzed the dynamics of investments by credit unions. In Lithuania, the Law on Credit Unions limits the potential of credit unions to invest. Credit unions may invest in government bonds and deposits in banks or they may invest with the Lithuanian Central Credit Union. Before the Lithuanian Central Credit Union was founded, credit unions could invest money as deposits in other credit unions. As the interest rates for government bonds and deposits in other credit unions were very high in the year 2000 and 2001 (from 12 to 18 %), credit unions preferred to invest in low-risk investment rather than grant loans to their members. As the situation in the market has changed (now credit unions earn only 1-2.5 % from investments in government bonds), more credit unions have switched to granting loans to their members or, in some cases, do not invest, and instead maintain greater liquidity reserves (see Figure 2).



**Figure 2 Investments, investments in government bonds and investments in deposits in other credit institutions in Lithuanian credit unions 2000 – 2005 as a % of total assets**

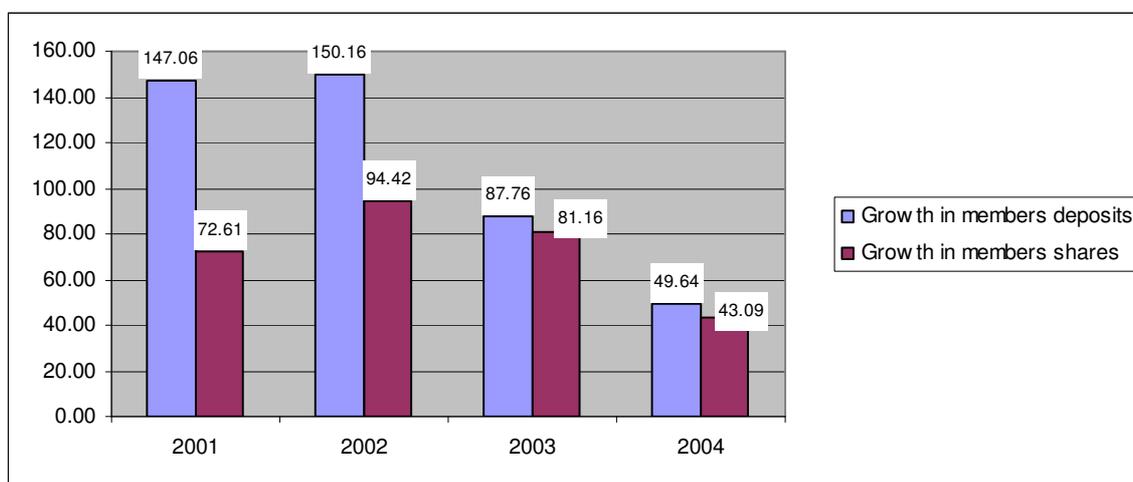
Source: Compiled by the authors based on various materials of the Association of Lithuanian Credit Unions

In the Republic of Ireland, according to Section 43.1 of the 1997 Credit Union Act, credit unions may invest surplus funds in

- a. securities in which trustees are for the time being authorized by law to invest
- b. the shares of or deposits with or loans to a credit union
- c. the shares of a co-operative society
- d. such other manner as may be prescribed by the government

Given the increasing competition in lending and the consequent reducing proportion of loans to total assets, many Irish credit unions find they must invest more and more of their surplus funds in order to achieve a return for their members. Lending to members is still preferable to investments given the higher returns gained from lending. Credit unions can invest funds for an average return of between 1% and 5%, depending on the duration of the investment. Longer-term investments attract higher returns. Lending rates, on the other hand, vary between credit unions, from approximately 6% APR (Annual Percentage Rate) minimum, to 12.67% APR maximum.

Ideally, according to the PEARLS ratios, investments to total assets in Irish credit unions should be less than 30%. The figure, however, is far higher and growing. In March 2005, it stood at 46.12%. This has increased from approximately 32% in 1998. Investments by credit unions in the ILCU Central Investment Management fund have quadrupled in the past 6 years, from €420 million in 1998 to €1.9 billion in 2004. This growth in investments is indicative of the competition in the market for loans, rather than a high return on investment.



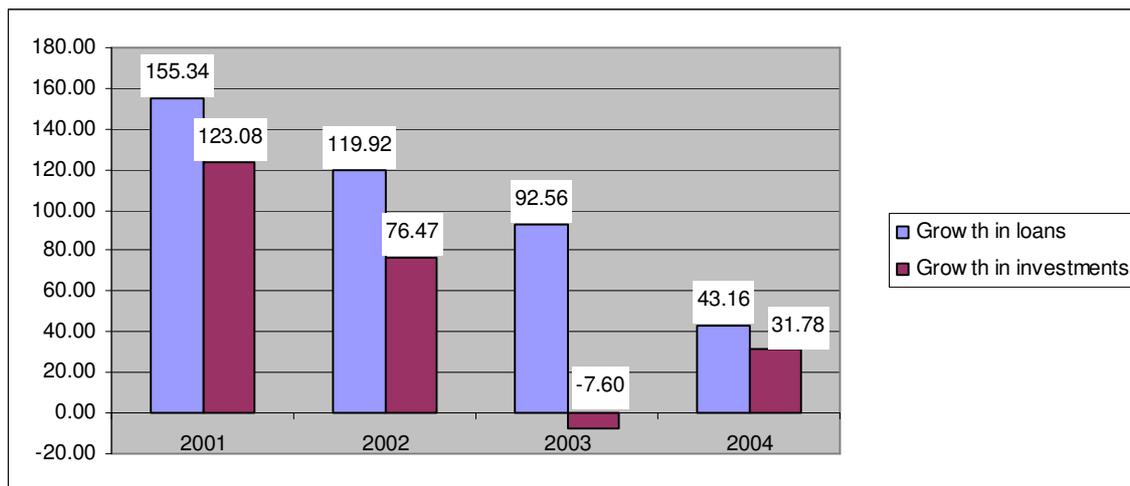
**Figure 3 Growth rates of members' deposits and shares 2001-2004 in Lithuanian credit unions, in percent**

Source: Compiled by authors based on various materials of the Association of Lithuanian Credit Unions

We also analyze growth ratios in Lithuanian and Irish credit unions. The analysis of growth indicators show that credit unions in Lithuania have maintained quite steady and fast growth rates over the last 4 years, as might be expected in the early stages of development. The average growth rate in loans and member deposits is about 80 percent per year. For example, loans in credit unions increased by 155.34% in 2001 and 43.16% in 2004. Deposits in credit unions increased by 147.06% in 2001 and 49.64% in

2004. Growth in member shares almost mirrors the growth of membership in credit unions – the rates here are a little bit lower in comparison to growth rates in deposits and loans (see Figure 3 and Figure 4).

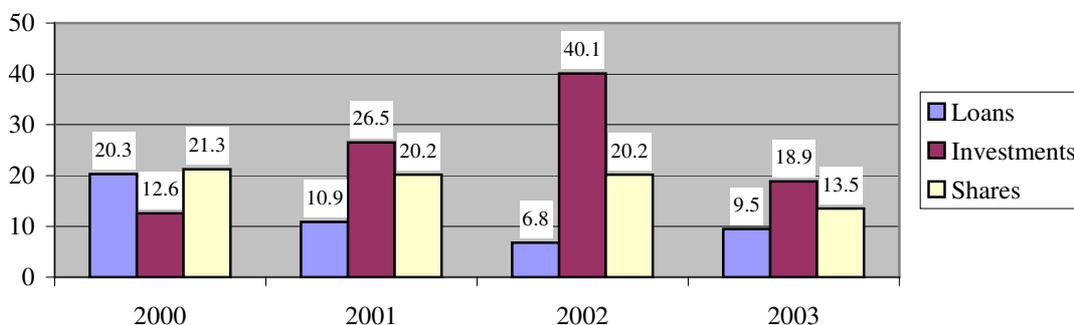
It is important to note that shares and deposits are considered as separate parts of the balance sheet under the Lithuanian Law of Credit Unions. Deposits are liabilities that may be redeemable after a certain time period. Shares are considered as capital, and play a major role in calculating capital adequacy ratios and measuring the solvency of credit unions.



**Figure 4 Growth rates of loans and investments in 2001-2004 in Lithuanian credit unions, in percent**

Source: Compiled by authors based on various materials of the Association of Lithuanian Credit Unions

Figure 5 shows the rates of growth within the Irish credit union movement. In Ireland, growth in lending and savings is much slower, as one might expect in a more developed movement. At the same time, we can see that growth in investments far exceeds growth in lending, reflecting the difficulties faced by Irish credit unions in competing in the lending market. In 2000, lending grew by 20.3% while investments grew by 12.6%. This situation was reversed by 2003, where lending grew by 9.5% and investments grew by 18.9%. Growth in shares was stable from 2000-2002 but dropped somewhat in 2003.



**Figure 5 Growth rates of loans, investments, and shares 2000-2003 in Irish credit unions, in percent**

Source: Compiled by authors based on various materials of the Irish League of Credit Unions

The indicators clearly show a maturing credit union movement in Ireland, where growth in lending and savings is slowing down, and growth in investments is increasing. It is clear from the discussion that Irish credit unions are reasonably well-covered in terms of risk, particularly from a bad debts perspective. Bad debts provisions are well in excess of the PEARLS requirements. On the other hand, Irish credit unions are competitively weak, particularly in terms of lending.

## Conclusions

To date Irish credit unions, as they have matured, have controlled their own standards of risk management by monitoring CAMEL and now PEARLS ratios within the monitoring scheme of the Irish League of Credit Unions. It is the understanding of the authors that credit unions which are not affiliated to any central body, currently face no requirements for risk management. The new regulatory regime under IFSRA has yet to announce how the finances of Irish credit unions in the Republic will be regulated by the State. Regulation will, no doubt, increase, but it is hoped that there can be some partnership between the ILCU and IFSRA in this regard. As the Irish movement has matured, monitoring standards have developed, but not, perhaps to the same extent as in Lithuania, nor, perhaps, to the extent that might be appropriate to their stage of development.

The results of the analysis show that although Lithuanian credit unions are at a less developed stage than Irish credit unions, they have, in most cases, higher requirements for risk regulation. Lithuanian credit unions have to follow the standards that are applied to the banking sector, or even more strict standards. Under the recent regulations, Lithuanian credit unions have to maintain higher operating standards that, in some cases, do not help credit unions to compete in the banking market with the commercial banks. We may presume that the regulation of Lithuanian credit union activities is stricter than it should be for their stage of development (in comparison with the regulation of Irish credit unions to date). We may also make an assumption that strict regulation influences the development of credit unions in Lithuania and, in some cases, becomes inadequate considering the changing requirements caused by credit union development. On the other hand, the changes to Irish credit union risk regulation might cause a set of problems for credit unions in adapting to the new regulatory environment while, at the same time, decreasing their competitiveness and increasing risk exposure in some areas, such as profitability.

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