An Interview with Professor Giulio Sapelli On the Italian Banking System

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According to Edward W. Said, an intellectual is an exile, ostracized by definition. An intellectual needs to be free to tell the truth. She or he does not defend any personal power and is not interested in following mainstream ideology. Professor Giulio Sapelli is indeed an intellectual. He has never been afraid to express controversial positions going against orthodox ideas. He is a polyhedral thinker, integrating several disciplines including economics, history, and philosophy in his thought.

Professor Giulio Sapelli has had an outstanding academic career. He is currently Professor of Economic History at Università degli Studi di Milano and he has been a fellow and visiting professor at several international universities. For five years, he was Director of Ecole des Hautes Etudes en Sciences Sociales in Paris. Sapelli has also had an excellent non-academic career. Among numerous experiences, we can note that between 1996 and 2002, he was a member of Eni's Board of Directors and in 2000-2001 he was President of Fondazione Monte de Paschi. He has written more than 400 publications.

Sapelli has extensively written on the international financial market and its degeneration. His studies have focused on the role of cooperative banks in financial capitalism. Nicola Bilotta had a discussion with Giulio Sapelli about the Italian banking system and its structural weaknesses. As Sapelli said: "Italian capitalism is a capitalism without capital." This statement is the first step to understanding the Italian banking system's development.

The Italian banking system has three main peculiar features. (i) Italy has one of the highest rates of private savings in the world. (ii) Italy has many more small- and mid-size banks compared to other European countries. (iii) There is a close relationship between banks and enterprises; the Italian stock market is not well developed, so companies raise funds from bank loans. In light of these features how can we explain the issues of the Italian banking system?

The origins of the weakness of Italian banking trace back to the 1980's. When Carlo Azeglio Ciampi was Governor of Banca d'Italia (1979-1993), the Italian central bank encouraged banks to both compete amongst themselves and consolidate. These two processes are impossible to implement simultaneously. Thus, banks preferred to consolidate, but their mergers were not well supervised either by Banca d'Italia or the banks' management.

The Italian banking system changed its structure too quickly. It promoted processes of privatization and consolidation while simultaneously abolishing the legal separation between commercial banks and investment banks. The reform allowed banks to increase their functionalities; they were not only lenders to enterprises, but traders of derivatives and financial products. From a system based on three big public banks, Italy became a system in which there were many banks working as universal banks.

Consolidation and privatization were the two principles which led Italian cooperative banks (Banche Popolari and Banche Credito Cooperativo) to change their nature. Cooperative banks normally work on the relationship-oriented principle. Relationship banking looks to reduce information asymmetry by building a relationship with the customer. This strategy assumes that knowing your customer and being involved as an advisor help to reduce the risk. Universal banks instead base their strategy on the transaction principle.

Italian cooperative banks were forced to change from relationship-oriented banking to transaction-based banking. Their increased functions and added dimensions forced cooperative banks to work as universal banks. It is not always good to have bigger banks. Especially in a country like Italy in which there is not a strong stock market, small- and mid-size companies need to be supported by local banks.

In a capitalist society, there is a need for different types of banking. Different economic-social actors need different kinds of banks.

Yes, commercial banks need to be separate from investing banks. Italy is the only country in which the state has not protected its cooperative banks. Obama appointed a representative of the American credit unions to the Federal Reserve Board. Germany protected its Sparkasse during the economic crisis.

And there are several cases of big banks which are successful cooperative banks. Dejardin Group for example.

Well, that is true. One time I was talking to a famous Bocconi Professor. I asked his opinion about Dejardin Group and he answered that he did not like gardening! (*In Italian, "gardens" has a similar sound to Dejardin*). Cooperative banks are a valuable commodity all over the world. The abolishment of any form of cooperative banking just helps universal banks to expand their markets and to leave many clients without proper financial help.

Can cooperative banks be properly managed when they get bigger? Many people think that once a cooperative bank gets too big, it loses its relationship with its local territory.

Yes, of course! There are several books which clearly explain how to solve the issue of cooperative bank governance. The answer is simple. We need to go back to the original theories on the strengths of a cooperative bank: limited eligibility for management, transparency, and division between ownership and management.

Minsky extensively studied the degeneration of financial capitalism. His lessons are still crucial to understanding how we can mitigate the influence of the financial market over the real economy. Minsky argued there are two main constraints, which can reduce the risk of financial degeneration: (i) moral disapproval and (ii) state intervention. How can we apply Minsky's principles in handling the cooperative banks' crisis?

Minsky's principles are eternal. But to implement them in cooperative banks, we need to balance them with the issue of governance. As management is elected, there is a high risk of creating excessive concentration of power in a single person. Studies indeed show that any cooperative business form is dominated by managers who remain for at least 20 years.

Regarding the problem of governance, how have stock option schemes affected banks?

As proposed by Peter Drucker, the founder of the Modern Management School, managers should not earn more than 20 times than the amount the poorest worker of the company earns. Nowadays, managers can earn 2000 times more than the average worker. Recently, Italian cooperative banks have introduced a stock option scheme for their managers. These schemes improve opportunistic behaviours favouring short-term profits rather over serious industrial plans.

Cooperative banks were superior to universal banks because they separated management and ownership. Personal power and stock option schemes negated the positive factors of cooperative banks' business strategy. We need to go back to original forms of cooperative banking through a clear separation between employees and members. Those original forms contain the basic rules of cooperative banks which cannot be changed or cheated. We need to avoid creating conflicts of interest inside cooperative banks. If governments do not impose basic cooperative rules on these banks, members of cooperative banks need to self-impose a moral regulation to avoid personal power.

Of course, a moral fine needs to be implemented, and should be recognized by most members of a banks, as well as society. As none would be happy to see his daughter getting married to a Mafioso, none should be happy to see his/her daughter getting married to [former President of Banco Popolare di Vicenza, Giovanni] Zonin. There should be the same moral condemnation of financial violations as there is for criminal organizations.

The economic crisis hit Italy. But it cannot explain alone the amount of (non-performing loans) NPL which Italian banks have accumulated. What is the role of bad management in Italian NPL?

Banking managers do not know industries and factories. They do not know how to value risks nor how to manage access to credit. In addition, several small- and mid-size companies falsify their balances. Everyone knows it. However, the high level of NPL is due not to small- and mid-size companies, but to a few big corporations. There is no ethical code inside cooperative banks. In the end, NPLs are caused by the technical ignorance of bankers and by excessive credit lending.

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