Review of Banking Services in the Falkland Islands

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Queenstown Strategic Advisors

Contents

Section 1: Executive summary

Queenstown Strategic Advisors (QSA) is delighted to have been selected by the Chamber of Commerce to undertake a review of the banking provision in the Falkland Islands. This report represents the main artefact which arises from the review. This part of the report seeks to set out the background and rationale for this piece of work, the approach and methodology adopted by the review team, and summarise the key findings and recommendations of the review.

Context and rationale for the review

The Falkland Islands is a remote, self-governing British Overseas Territory situated in the South Atlantic spread across an archipelago comprising two large islands and 776 smaller islands. It stretches across 4,700 square miles and is home to a permanent population of ~3,500 people. In the late 1970's there were well founded concerns that the economy was becoming moribund amidst depopulation.

The Falkland Islands is subject to a longstanding irredentist claim by Argentina which came to a head with the United Kingdom in the short military conflict of 1982. Since liberation, and with initial rehabilitation funding and support from the United Kingdom, the economy of the Islands has undergone a remarkable transformation. Powered by a thriving and entrepreneurial business community, the transformation in its economic fortunes is stark; public finances are in comparatively rude health, there is virtually full employment and judged on a GDP per capita basis it often ranks in the top fifteen most prosperous places to live.

There is one bank operating in the Islands with Standard Chartered Bank ("**SCB**") having opened and maintained a branch since December 1983. Government and a number of larger firms also benefit from commercial banking relationships with clearing banks in the UK in addition to maintaining local banking relationships with SCB. Some businesses and individuals also have legacy arrangements with UK clearing banks; existing accounts are maintained, but they have been unable to access new products.

Many businesses and individuals have to find creative solutions to work around the challenges created by the rudimentary nature of the current banking proposition in the Islands. These include using neo-banks (digital challenger banks such as Monzo or Starling) if they have a UK address and an increasing use of non-bank financial institutions such as Wise (nee Transferwise). Some businesses have also put in place banking arrangements with Gibraltar International Bank – an initiative established in conjunction with the Chamber of Commerce in order to enable Square to offer the ability for smaller businesses to accept credit and debit card payments.

There is widespread frustration amongst the business community with the current range of banking services provided in the Islands. The Falkland Islands Chamber of Commerce with the support of key stakeholders including the Falkland Islands Government ("**FIG**"), the Development Corporation and SCB, commissioned QSA to undertake a comprehensive review of banking services to assess the historical and current landscape, to consider how the Islands benchmark against other small island jurisdictions and to identify initiatives which could be pursued by stakeholders to improve the current arrangements.

Approach and methodology

Given the nature of the assignment and the unique circumstances of the Islands it was considered that a deep dive on the history of banking in the Islands was an essential component of the review in order to understand why things are as they are today. A significant level of qualitative and archival research has been undertaken to develop the historical context.

Field interviews with a cross section of the business community across the Falkland Islands, including with those based in Camp, have been an important component in facilitating the development of a series of profiles which set out the differing needs of different types of businesses.

To undertake the benchmarking of banking services in the Falkland Islands a peer group of comparable jurisdictions has been developed. This cohort of peers has been assembled using a filtering process in order to ensure that the final peer group have a broadly similar range of characteristics.

The benchmarking exercise was completed using a comparative study approach. This has been largely completed on a desktop basis albeit the project team have endeavoured, where practicable, to validate the desktop research with sources on the ground in each peer country.

Input received

Members of the project team were warmly welcomed to the Falkland Islands in early January for a field trip in order to hold interviews with a range of businesses across a breadth of sectors based in both Camp and Stanley.

The project team would likely to record their gratitude to the following businesses and organisations who were generous with their time – the insights around their current banking experience have undoubtedly added significant depth to the research:

- Coast Ridge Farm, Camp
- Wild Falklands, Camp
- 60 South, Stanley
- Beauchene Fishing, Stanley
- Falklands Legal, Stanley
- Government of South Georgia & South Sandwich Islands, Stanley
- SG Accounts, Stanley
- Waverley Law, Stanley
- Seafish, Stanley
- Falkland Islands Company, Stanley
- Fortuna, Stanley
- Stanley Services, Stanley
- Shorty's Diner, Stanley

In addition to members of the Falkland Islands business community, the project team met with the following key stakeholders to understand their perspectives on the banking provision in the Islands which include their views as a consumer of banking services where appropriate:

- Falkland Islands Government
- Falkland Islands Development Corporation
- Standard Chartered Bank

The project team have not been able to substantively explore the extent of any technical challenges associated with operating digital banking services in the Islands due to internet or communications constraints. Despite extensive efforts by both the Chamber and QSA, Sure - the telecoms provider which enjoys a monopoly in the Islands - did not respond to numerous invitations to organise a face to face meeting or video conference.

The project team have also either conducted meetings via videoconference or entered into correspondence with the following organisations:

- Gibraltar International Bank
- The Bank of St Helena
- Niue Development Bank (Kiwibank agency)
- Issuing Institute for Overseas Departments (IEDOM, France)
- Government of St Helena
- Bank of International Settlements
- Bank of England

The project team would also like to express their appreciation to the Chamber of Commerce and their team who assisted greatly with logistical support and co-ordination during the project and field trip in particular.

Please refer to Appendix 2 for a schedule of sources used in undertaking the review and preparing this report.

Summary of principal findings

The extent of integration of small island territories with their 'metropolis' country appears to heavily influence the plurality of banking providers and breadth of services available.

Based on the academic literature reviewed, smaller, non-sovereign territories tend to be at an advantage as they are able to leverage both greater resources and political influence compared to their small yet sovereign counterparts. However, amongst the peers surveyed it is also clear that those countries who are more constitutionally integrated (e.g. Easter Island, St Pierre & Miquelon) tend to have a greater number of banking providers present and a broader range of products available than those with greater autonomy (e.g. Falkland Islands, St Helena & Ascension Islands).

The size and lack of scale of the market constrains the breadth of products and services available – stakeholders should focus on securing and sustaining access to a core range of essential services.

Banks, particularly large international banks, need to operate in scaled markets in order to generate acceptable and sustainable returns on equity. Creating sustainable returns which surpass the cost of equity has been challenging in the recent era of prolonged ultra-low interest rates and in the face of stiff competition from fintech firms. In response, banking groups have had to curtail their operating expenses which has led to greater levels of product commoditisation with less scope for customisation in markets with smaller scale. Investment budgets have also been squeezed with the inevitable consequence that investment allocations will be directed at projects / geographies which offer the 'biggest bang for the buck'.

In a Falkland Islands context this means there needs to be an acknowledgement that not all banking products can be offered in a sustainable or cost-effective way – particularly those which might only have utility for small portions of the local market. Instead, the focus should be on securing and sustaining access to a core range of essential services focused on the ability to do three things: (i) help businesses and individuals safely store money (deposits and savings), (ii) enable credit worthy businesses and individuals to easily borrow money (mortgages, working capital and funding growth), and (iii) facilitate businesses and individuals to effortlessly move money (online banking and payments). Having the ability to do just these three things will meet the vast majority of banking needs in the Islands market.

Standard Chartered Bank deserve significant credit for taking the risk of setting up and persevering to support the economic development of the Islands over the last forty years.

The bank, largely motivated by political pressure from then Prime Minister Margaret Thatcher, took the gamble of opening a branch in Stanley to support the rehabilitation and development of the Islands economy. Other UK clearing banks were not prepared to offer support and there can be no question that SCB's ongoing presence has contributed to the prosperity the Islands now enjoy.

Their ongoing commitment to the Falklands in the face of a very challenging operating environment for banks following the 2008 financial crisis is arguably even more remarkable. Practically all international banking groups have exited smaller markets citing a lack of scale and a need to prioritise higher growth markets.

SCB's current operating model and the lack of digital/mobile channels is a core driver of the Islands benchmarking unfavourably relative to its peers in terms of breadth of banking services available.

The Falkland Islands is a prosperous country notwithstanding its relatively small sized population. However, the review reveals that the Islands compare unfavourably to the cohort of peers identified in terms of the range of banking services available. To a significant degree this can be attributed to the operating model of SCB which does not presently offer any digital/mobile channels in the Falkland Islands.

All of the businesses interviewed as part of the review cited the lack of digital/mobile channel as their biggest frustration with the banking service in the Islands. The manual nature of the service creates a drag on their productivity. The other issue called out by many businesses is the cost and time it takes to transfer money to and from the Islands as a result of it operating on the SWIFT network.

In addition to the poor customer experience, the resilience of the operating model appears to be increasingly fragile with businesses reporting a rise in the number of errors being made in terms of payment processing. In the run up to the recent Christmas period the bank had a significant number of staff absent owing to Covid and because customers cannot self-serve it was necessary to reduce the opening hours of the branch. A number of firms reported they had payments made a number of days late including wages for their employees.

It is worth noting that Niue and St Helena and Ascension Islands, which are less well developed and remain dependent on direct aid payment from their respective 'metropolis countries' have access to a contemporary digital/mobile banking capability. In both cases the banks are government owned and therefore it is acknowledged that investment decisions may not be necessarily made on a wholly commercial basis.

The operating model when the branch was originally established was no doubt fit for purpose and it is acknowledged that internet bandwidth constraints would have hampered the ability to draw investment funding from the wider bank to introduce digital/mobile banking historically. However, internet bandwidth has much improved over the last five years and St Helena which has poorer internet connectivity has had digital banking for some time.

SCB acknowledge there is widespread frustration from the community about the continued lack of digital/mobile access. The bank has sought to innovate to improve the customer experience including the introduction of contactless debit cards, bulk payment instructions, an online mortgage calculator, email payment instructions. However, these innovations improve things around the edges but do not address the fundamental challenges with the operating model. It is acknowledged that SCB recently migrated the Stanley branch to the wider bank's core banking platform – this is an important enabler to introduce digital/mobile banking but as yet no firm funding or delivery date is in place to deliver this much anticipated improvement.

The commercial lending market is not functioning effectively with the Development Corporation having a commercial loan book nearly five times the size of the SCB commercial lending portfolio.

The commercial lending marketplace in the Falkland Islands is considered not to be functioning effectively. This can be observed through a comparison of the FIDC and SCB commercial lending portfolios. FIDC has a total lending portfolio of ~£2.5 million whereas SCB has a commercial lending portfolio of £600,000 or just 0.4% of its total deposit base. It would be typical to expect commercial banks to have a far larger share of the lending market relative to a development agency.

It has not been possible given the time constraints involved with this review to undertake a deeper dive on this topic. It is also acknowledged that not all businesses will qualify for lending support because of their own idiosyncrasies. However, a number of key themes emerged during the course of the interviews with the business community, FIDC and SCB which reinforces the need for further work to overcome the current market dislocation.

Established businesses with a profitable track record and acceptable collateral appear to be struggling to secure access to bank lending to fund working capital and their growth plans. A number of businesses, perhaps unjustifiably, expressed a view that SCB are not open for business and based on their past experience they would not approach the bank for working capital or growth financing. Whereas other firms noted that they would look to approach FIDC first as they tended to be more proactive, offered finer pricing and more flexible borrowing terms.

SCB advise they have lost business to FIDC based on both deal structure and pricing terms. There is also little incentive for businesses which benefit from FIDC support to transition to SCB for their lending needs if the commercial pricing and terms are going to be less attractive.

FIDC take the view that they will offer loan support to viable businesses which meet their lending criteria – ultimately, they do not wish to see businesses with credible lending propositions not receive the working capital / growth funding they require.

Addressing this multi-layered issue will, in all likelihood, require collaboration between Government, FIDC and SCB in order to properly understand the issues in play and to develop proposed solutions. SCB have confirmed they do have positive appetite to lend to businesses in the Islands that meet their lending criteria.

Having an international bank in the Islands brings a range of wider benefits – setting up a domestically owned bank is unlikely to be a panacea, solving current challenges in terms of service proposition.

There is extensive research which sets out that having international banks in smaller and developing markets brings a host of benefits. Larger banking groups can bring about improved financial stability given they have larger balance sheets and a diversity of revenue streams – they can also tap support from central banks during times of market dislocation. Larger banking groups are also able to transfer their knowledge and experience from across their network to the benefit of smaller territories – there is evidence of this in the Falklands in terms of risk management and effective governance frameworks.

Community banks, particularly given the evolution of 'bank in a box' technology can tailor their product range and services to reflect the specific needs of their local community. However, community banks tend to be most effective when they are part of a wider eco-system and complementary to larger financial institutions. Small island-based economies without international banks increasingly struggle with international connectivity particularly as access to correspondent banking relationships can be difficult to secure and maintain in the face of a wider de-risking by correspondent banks.

The regulatory framework and architecture for banks should be updated to reflect developments over the past thirty years. Government also needs to lean into digitisation with delivery of its services.

The current banking legislation and architecture has not been updated for some considerable time. To a large extent this reflects the longstanding arrangements in the Islands with SCB being a branch of a British bank which is supervised by the UK regulators. However, it is recommended that the Government develop a plan to bring forward an updated package of banking legislation. This should be considered a foundational element which might support an alternative financial institution operating in the Islands.

A refreshed banking regime would not only ensure that the Islands are keeping pace with international standards and best practice but also affords an opportunity to consider introducing elements which might help improve the current levels of service provision. By way of example, the revised regime could include provisions regulating how consumer credit is provided. It could also seek to embed similar Consumer Duty principles being introduced in the UK which seeks to ensure that banks put their customers interests first and that their products/services are operated in a fashion which do not provide poor customer outcomes.

The Government and SCB together sit at the heart of the Islands community and inevitably as a result they play a key role in setting the tone in certain areas including innovation and digitisation. Both institutions need to set out how they plan to embrace and embed the digital economy in the Falkland Islands.

The challenges facing the Falkland Islands in terms of banking provision are not unique to them – this creates opportunities to collaborate with other territories to pool expertise and resources.

Many small island countries face broadly similar issues to the Falkland Islands. Addressing some of the longer-term issues will be difficult to achieve on a solo basis and therefore efforts should be explored to partner with other territories in order to pool expertise and resources. Developing common legislative frameworks or sharing regulatory architecture might represent a more cost-effective way of addressing these shared challenges.

Collaboration with other island territories could also usefully boost the prospects of attracting alternative service providers by deepening the potential market and associated value pools. It might also usefully increase the effectiveness of any influencing strategy by creating a 'louder voice' for the territories.

Conclusions and key recommendations

As part of the review three broad options have been identified for the stakeholders to consider in order to improve the provision of banking services in the Islands:

(i) Work with SCB to facilitate improvements to their existing service provision – including considering whether there needs to be financial support/incentives for addressing specific shortcomings;

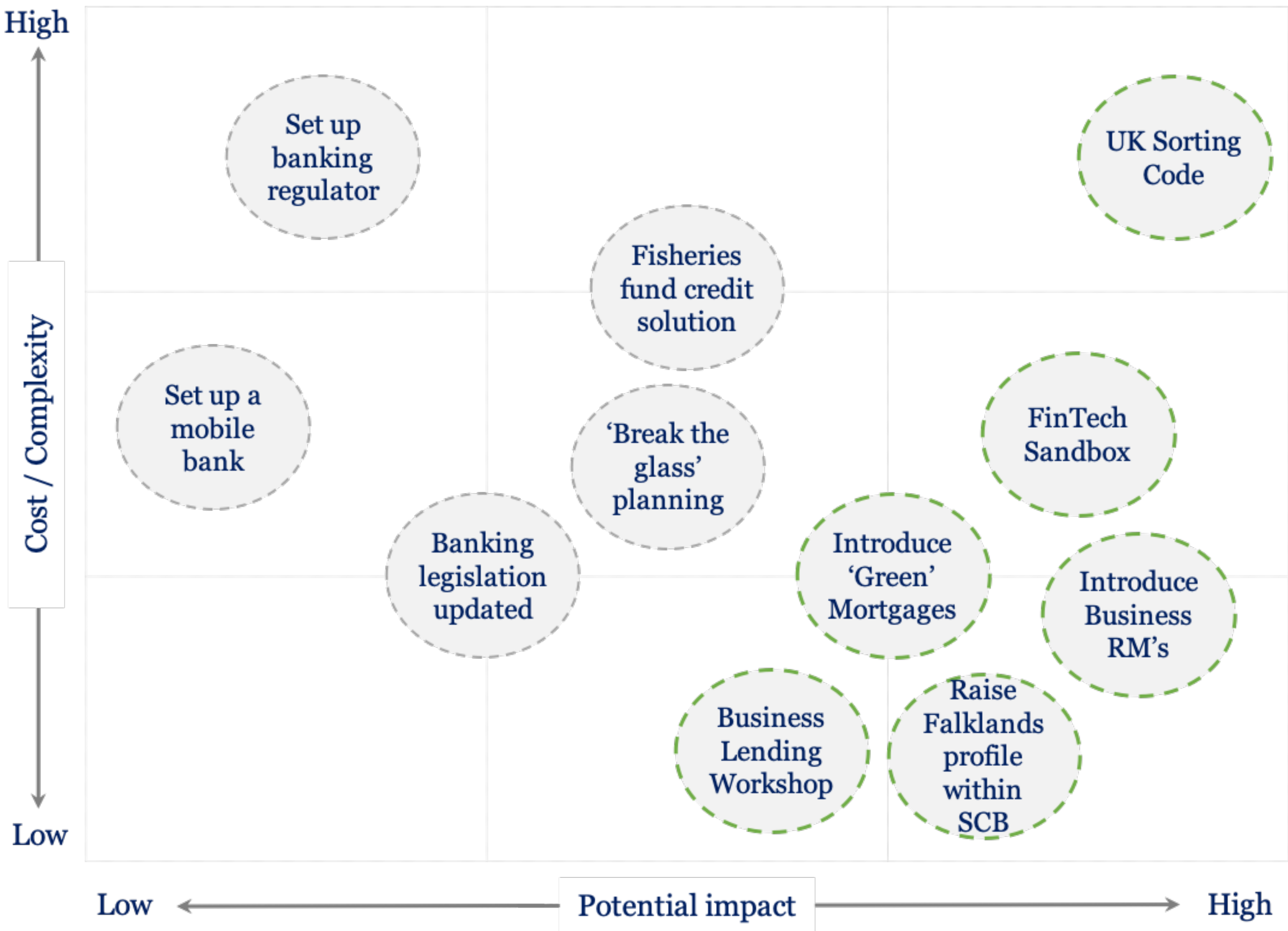
(ii) Seek to bring in another financial institution either physically or virtually to compete with SCB; and

(iii) Establish a domestically owned and operated national bank to either compete with or replace SCB.

Based on the work and analysis undertaken it is recommended that the stakeholders pursue the first option. Working with SCB to improve their current operating model retains the presence of an international and systemically important financial institution in the Islands. It leverages the wider SCB capabilities including risk and balance sheet management expertise. Much of the foundational build to enable digital/mobile banking is already now in place albeit the funding and project resources to deliver it are not yet lined up.

The other options considered would potentially offer a greater level of scope to customise the products and services to meet the specific needs of the Falkland Islanders. However, it is considered highly improbable that there is a sufficiently deep market to support two banks operating in the Islands. The Islands risk losing the presence of an international bank which may have wider consequences for the reputation of the Islands and its international connectivity. Establishing and operating a domestically owned bank is an endeavour that requires both deep pockets in terms of funding and is not for the faint of heart.

A portfolio of initiatives which could improve the banking proposition in the Islands have been identified and are summarised in the schematic overleaf.



A fuller discussion of the structural options and initiatives can be found in Section 8 of the report. It is recommended that consideration be given to setting up a working group to explore the priority initiatives further.

Section 2: History of banking in the Falkland Islands and an overview of Standard Chartered Bank

This section provides an historical overview of the evolution of banking in the Falkland Islands. It orientates the reader around how the Falkland Islands has arrived at the position it finds itself in today and how this has shaped the current range of service providers and the proposition available to individuals, businesses, government and non-government organisations.

Shackleton Economic Survey recommends a commercial bank is set-up

In 1976, the Labour government published an Economic Survey of the Falkland Islands which was led by Lord Shackleton in association with the Economist Intelligence Unit. It sought to set out a series of initiatives and the UK investment required to reduce the outflow of resources from the Islands and declining population with a view to boosting the long-term economic prosperity of the Islands.[1]

The survey noted that rudimentary banking facilities had hitherto been provided by the Falkland Islands Company ("the **FIC**"), the Estate Louis Williams ("**ELW**"), and the Falkland Islands Government ("**FIG**"). The FIC acted as a banker to many of the farming companies, partnerships and wider community. It offered current account facilities which customers could draw cheques on and it maintained a banking relationship with a UK clearing bank to facilitate a remittance service together with foreign exchange. The Estate Louis Williams provided a very similar service.

For its part, FIG operated a Government Savings Bank in the Islands along similar lines to that of the UK's Post Office Savings Bank. It paid an interest rate of 3.50% per annum on a tax-free basis whilst making a return on the rate it received from its commercial bank in the UK where it would place the deposits. FIG had also made a moderate number of loans, typically for agricultural purposes.[2]

Shackleton's survey called for, amongst other recommendations, the expansion of key sectors of the economy by: (i) expanding the airport; (ii) addressing the problem of absentee landowners and facilitating the sub-division of farms; (iii) the development of the fisheries industry; and (iv) the creation of a development agency which would go on to become the Falkland Islands Development Corporation. The survey team also believed establishing proper commercial banking facilities including the provision of overdrafts and loans was key to boosting the economic output of the Falkland Islands.[3]

1980 Banking survey ruled out the possibility of attracting a UK bank and recommended instead setting up a domestically owned bank

In response to the Shackleton report the Overseas Development Agency ("**ODA**") undertook a deep dive of the banking sector in March 1980 led by Robin A.V. Benbow with a view to evaluating how commercial banking facilities might be established in the Islands.

The Benbow report first reviewed who was licensed for banking activities. It validated the role the FIC was playing in providing banking services. It recommended that the licence for ELW be removed as they had ceased to offer banking services.[4] It also identified the Stanley Co-operative Society as providing interest-bearing deposit accounts up to a maximum amount of £1,600 per member of which there was approximately 300. The deposits financed the trading of the Society, which provided competition in the supply of general

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[1] Foreign & Commonwealth Office, *Volume 1: Economic Survey of the Falkland Islands – July 1976* (London: Foreign & Commonwealth Office, 1976), i-vii, accessed December 5, 2022, https://www.nationalarchives.gov.fk/jdownloads/Trade%20and%20Industry/R-TRA-ECO-1-7.%20Economic%20Survey%20of%20the%20Falkland%20Islands%20Volume%201%20of%202%20Resources%20and%20Development%20Potential%20July%201976%20-%20The%20Rt%20Hon%20Lord%20Shackleton.pdf

[2] Ibid, 260.

[3] Foreign & Commonwealth Office, *Volume 2: Economic Survey of the Falkland Islands – July 1976* (London: Foreign & Commonwealth Office, 1976), 22, accessed December 5, 2022, https://www.nationalarchives.gov.fk/jdownloads/Trade%20and%20Industry/R-TRA-ECO-1-10.%20Falkland%20Islands%20economic%20survey%201982.pdf

[4] Overseas Development Agency, *Banking Facilities in the Falkland Islands – March 1980* (London: Overseas Development Agency), 1, accessed January 9, 2023, http://www.nationalarchives.gov.fk/jdownloads/Utilities%20-%20General/R-UTI-GEN-1-2.%20Report%20by%20Robin%20A%20V%20Benbow%20Overseas%20Development%20Agency%20on%20banking%20facilities%20in%20the%20Falkland%20Islands%20-%20March%201980.pdf

goods. Benbow recommended that the licence be maintained albeit it might be restricted to the taking of deposits to members only.

Benbow noted that all of the organisations with a banking licence had been granted exemptions from various sections of the Banking Ordinance – which meant they did not have to maintain the minimum levels of capital of £250,000 and were not required to publish audited accounts.[5]

In terms of FIG banking activity, Benbow observed that the Government Savings Bank provided not only deposit accounts but also accepted currency deposits, effected wire transfers to third parties and also introduced a cheque system. In addition, the Treasury department also provided foreign exchange services through the purchase and sale of currencies – mainly Argentine Pesos, US Dollars and Sterling. They also issued drafts and effected wire transfers through the Crown Agents.

Treasury was also engaged in providing mortgages for house purchases at favourable interest rates and with repayment terms of up to 25 years. They also provided loans for property improvements, extension of tourist facilities. Finally, Treasury was responsible for issuing all bank notes and coins in the Falkland Islands.

Once banking services were reviewed, Benbow noted Shackleton's recommendations that improved banking services would be provided by the setting up of a commercial bank. However, he believed that the Islanders already enjoyed a range of banking services from a number of different sources but the objective was to co-ordinate this service provision into one organisation which could be scaled as demand dictated.

The report outlined the following services were required: (i) current and savings account in local currency; (ii) payments to third parties mainly by cheque; (iii) money transmission through drafts, mail transfers, and wire transfers; (iv) mortgages – longer term facilities of 20/25 years for house purchases albeit restricted in number given the short-term nature of the deposit base; (v) short term overdrafts and medium term loans for financing cars or home improvements; (vi) working capital facilities for businesses; (vii) travellers cheques issuing and encashment facilities in both Sterling and overseas currencies; (viii) collection and payment of bills of exchange in Sterling and US Dollars to include cheques; (ix) investment advice and investment dealing through brokers or correspondent banks; and (x) safe custody of documents.

Benbow articulated three principal methods to achieve this:[6]

(a) An international or UK bank to establish a branch or a new subsidiary in the Falkland Islands;

(b) A new bank is established in the Islands with local shareholder which might include FIG; or

(c) A new Government-owned bank.

This was accompanied with narrative and analysis about the prospects of each option:

- **Establishing a branch or new subsidiary of an international or UK bank:** Both Barclays and Lloyds (through their Bank of London & South America subsidiary) were approached and declined as they considered it was not a viable proposition. They believed that the investment required to set up premises, provide a strong room, provide staff including expatriates could not be commercially justified. Benbow concluded there was little merit in considering this aspect further and it was not desirable to have a non-UK firm operating in the Islands.

- **A new bank owned by local shareholders:** The report concluded, based on discussions undertaken in the Islands that it would be difficult to find Falkland Island shareholders who would wish to capitalise a new bank. In addition, a new bank of this nature would not have the benefit of the Savings Bank's funds. Therefore, it was not considered a viable option.

- **A new Government-owned bank:** Benbow concluded that in order to make the optimum use of the funds available in the Islands as a deposit base, any commercial bank would need to utilise the funds presently kept within the Government Savings Bank. Therefore, it recommended that the Government be involved in setting up a new bank on a wholly owned basis.

[5] Ibid, 2.
[6] Ibid, 4-6.

The Benbow report recommends that the Executive Council consider whether it wishes to undertake this type of venture, establish whether it is legally possible for FIG to own a commercial bank, and also to ensure that the Foreign & Commonwealth Office ("**FCO**") has no objection.

By way of second order actions, the report recommends that the legal method of creating the new bank and transferring the Savings Bank should be explored. The report goes onto provide further considerations about the proposed customer proposition, the capital levels anticipated, and other arrangements which will need to be arranged e.g. premises, correspondent banking arrangements and so on.

The final part of the report discusses whether the Falkland Islands should consider embracing offshore banking. It reaches the conclusion that this line of business should not be pursued given the Islands would be somewhat "late to the party" with many other countries already well established and more accessible. It would mean the Falklands would likely only attract banks of a more "dubious element".[7]

The Executive Council agreed to progress further work on establishing a government owned national bank. Councillor Bowles, speaking in the Legislative Council in August 1980, refers to the promising prospect of the first 'National Bank' being established. The Dependent Territories' desk at the Bank of England was tasked to draft a more detailed business plan which was forwarded to the FCO and FIG in November 1981. Then the war came.

Post 1982 - Shackleton redux, the plan to rehabilitate the Falkland Islands and enter Standard Chartered Bank

In May 1982, as the British Task Force had landed on the Falkland Islands and it was clear that the retaking of the Islands was only a matter of time, the Prime Minister asked Lord Shackleton to update his 1976 Economic Survey. He was able to get together most of his former team and within just two months published an updated survey with recommendations as to how the prosperity of the Islands could be improved.[8]

In terms of banking provision - the updated Shackleton report re-affirmed its earlier conclusion that proper commercial banking facilities needed to be established with a particular need for overdraft and loan facilities. The presence of a commercial bank would be a much-needed catalyst in the economic development of the Falklands.

The Shackleton team re-affirmed their earlier recommendation that the Falkland Islands should not seek to become an offshore finance centre. They also welcomed the interest which was being shown by an international bank to set up a branch in Stanley and noted discussions were well progressed with FIG and the FCO.[9]

As the war came to an end in June 1982, the focus of Westminster turned towards rehabilitation. Lord Anthony Barber, the Chairman of Standard Chartered Bank ("**SCB**") and former Chancellor of the Exchequer under Ted Heath's Conservative administration, attended a meeting with Prime Minister Margaret Thatcher in Downing Street. At this meeting Mrs Thatcher lamented the lack of commercial banking facilities in the Islands. Barber conveyed an immediate assurance that his bank would address this issue and returned to his offices in the City to set the ball rolling.[10]

SCB moved quickly. By the end of June their Executive Committee had given its approval in principle to establish a branch in Stanley.[11] This new branch was contingent on four principal conditions:

(a) that SCB would be appointed as FIG's bankers and handle all their cash and payments;

[7] Ibid, 13.
[8] Foreign & Commonwealth Office, *Economic Survey of the Falkland Islands – September 1982* (London: Foreign & Commonwealth Office, 1982), 1-4, accessed December 5, 2022, https://www.nationalarchives.gov.fk/jdownloads/Trade%20and%20Industry/R-TRA-ECO-1-10.%20Falkland%20Islands%20economic%20survey%201982.pdf
[9] Ibid, 39-40.
[10] Duncan Campbell-Smith, *Cross Continents – A History of Standard Chartered Bank* (London: Allen Lane, 2021), 496.
[11] Michael McWilliam (SCB) to R. Fearn (FCO), 30 June 1982, FCO7/4680, Falkland Islands Rehabilitation: Banking Services, National Archives, Kew, London.

(b) that the new branch would absorb the business of the Government Savings Bank which would be subsequently wound up;

(c) that the Ministry of Defence would agree to open accounts with the new branch to hold their main funds for the Falklands in and would make maximum use of the new bank's facilities; and

(d) that the FIC agree to end its banking services to the wider community and agree to conduct their banking with the new branch and to make full use of the bank's services.

All the parties concerned agreed to the conditions proposed by SCB. There is an exchange of letters between SCB and FIG in October 1982 agreeing to this new arrangement. The Ministry of Defence agreed to open accounts and make use of the bank's new facilities. An agreement was also reached between the FIC and SCB about the withdrawal of FIC from banking activity in the Islands.

In January 1983, an application for a new banking licence was submitted for consideration by the Governor. With board approval at SCB granted, a formal agreement is drafted between FIG and SCB which appointed the bank as its sole banker and stipulated the terms of the transfer of the Government Savings Bank. It also stipulated that all existing banking licences save for that granted to the Stanley Cooperative Society will be surrendered by the end of December 1983.[12] SCB placed their order for their building materials and pre-fabricated structure and intended to open the new branch in Stanley by mid-1983.

There were concerns in some quarters that SCB were driving a tough bargain with their conditions for setting up the new bank. However, the Bank of England expressed genuine surprise that SCB had opted to set up in the Falkland Islands. They observed in correspondence with the FCO that:

> Standard Chartered will be placing some reliance on future economic expansion, backed by a commitment to the Islands by HMG in the shape of a long-term development plan. Nevertheless, their hope of increasing business will relate to normal short-term bank financing and a growing level of deposits, not to long-term development loans.[13]

The hopes of the Falkland Islands attracting a commercial bank would soon be realised but the Bank of England remained somewhat perplexed – "I do not understand fully why a bank should be so interested in a small and still troubled territory when others, under more peaceful conditions, have found the prospective cost prohibitive … Perhaps they are betting on a major exploitation of the whole region at a later date."[14]

The official handling matters at the Bank of England notes a "decision to withdraw would have major political repercussions since, having achieved a monopoly of banking in the Islands, they would leave a political vacuum. It does not take much imagination to foresee the political rumpus this would cause. It must be assumed that Standard Chartered appreciate this point." This would prove to be prescient in the months and years to come.[15]

An early case of 'buyer's remorse' at SCB?

Six months later, by July 1983, SCB's set up of the new branch had already run into challenges. Implementing the agreement regarding the transfer of the Savings Bank was proving to be more complicated than envisaged. The physical building of the new branch was also delayed – the materials had arrived from Scandinavia but the contractors to build it had no spare capacity as they were fully engaged on other rebuild projects.

It was becoming apparent that SCB's lack of market research before deciding to establish a branch was an issue. Archie Mitchell, SCB's first manager for the Falklands, only heard about his appointment through the

[12] A. J. Mitchell (SCB) to A. E. Palmer (FCO), 26 January 1983, FCO7/4680, Falkland Islands Rehabiliation: Banking Services, National Archives, Kew, London.
[13] P. N. Hayes (Bank of England) to P. R. Fearn (FCO), 26 July 1982, FCO7/4680, Falkland Islands Rehabilitation: Banking Services, National Archives, Kew, London.
[14] Ibid.
[15] P. N. Hayes (Bank of England) to P. R. Fearn (FCO), 19 August 1982, FCO7/4680, Falkland Islands Rehabilitation: Banking Services, National Archives, Kew, London.

newspapers. In addition, all the decisions about taking over the Savings Bank as its operating base and becoming banker to FIG were all taken before he even arrived in the Islands.

Mitchell felt it was increasingly unlikely that the branch would deliver even a moderate return on its significant investment. In particular he felt that the enthusiasm in London about SCB setting up in the Islands was not reflected locally. M. F. Smith, writing from Government House to the FCO, did not fully share this view albeit he accepted that some Islanders were wary of SCB's motives in setting up in the Islands. Smith acknowledged that FIG's legal team and treasury, have been at best lethargic in their support of the mobilisation of the bank; the Financial Secretary was refusing to even share the books of the Savings Bank and the draft legislation necessary to implement the transfer.[16]

Meanwhile, back in London, much soul-searching and finger pointing was abound about who was responsible for the miscalculation on the prospects of setting up a profitable business in the Falkland Islands should the issue come into the public domain. Mitchell was logging of all his correspondence and telephone calls with FIG together with their replies in order to demonstrate to his management that he had been following up and applying as much pressure as possible to move things along. Ultimately, SCB were committed to the endeavour but the episode emphasised the need for any new enterprise setting up in the Islands of doing detailed preparatory work, market research, and the need for a reasonably long field trip to size things up.[17]

The branch opens in December 1983 but frustration soon builds about the perceived lack of a full-service banking proposition

The new branch opened for business in December 1983. The Chairman of SCB invited Baroness Young, then a Foreign Office Minister to formally open the branch in Stanley in January 1984 whilst on a visit to the Falkland Islands. The Government Savings Bank was transferred shortly afterward.

In September 1985, the Managing Director of the Falkland Islands Development Corporation ("**FIDC**") wrote to SCB setting out proposals for SCB to support both the FIDC and FIG by lending to some of the newly sub-divided farms and to provide finance for house purchases. Both FIDC and FIG were unable to meet the demand, given constraints on their finances, which had been generated post liberation. The matter was referred to London but SCB concluded they would only entertain lending with the benefit of a full guarantee from the UK government.[18] SCB appeared to have reservations about the long-term future of the Falkland Islands and wished to have a guarantee from the UK to demonstrate the UK's political commitment to the Islands.

FIG, working in concert with the FCO, made representations to the senior management of the bank in London in an effort to break the impasse albeit without success. The FIDC switched tack and proposed that SCB instead provide them with a £1.2 million overdraft facility to acquire the farming land and subsequently repay in tranches as each sub-divided parcel of land is sold. SCB agreed to advance facilities but insisted on a 'letter of awareness' being issued by the UK government which in effect amounts to a letter of comfort. This is considered unacceptable by the UK Treasury.[19]

Governor Jewkes, whilst in London, met with the Chairman of SCB and senior executives to raise concerns about SCB's lending practices. During lunch, Lord Barber confessed that it was he alone that felt that SCB should open a branch in the Falkland Islands – against the advice of his senior executives. This added to a growing sentiment within the Islands that SCB are operating in the Islands as just a "Savings Bank" and not making as broad and positive a contribution to the local economy as it could. They were deemed "out of step with most of the British clearing banks" given their refusal to entertain domestic mortgage financing.[20]

[16] M. F. Smith (Government House, Stanley) to A.E. Palmer (FCO), 21 July 1983, FCO7/5518, Falkland Islands rehabilitation: Banking, National Archives, Kew, London.
[17] Ibid.
[18] John H. Cosson (SCB, London) to Simon Armstrong (FIDC), 19 September 1985, FCO7/5518, Falkland Islands rehabilitation: Banking, National Archives, Kew, London.
[19] Gordon W. Jewkes (Governor) to D. Broad (FCO), 27 March 1986, FCO7/5518, Falkland Islands rehabilitation: Banking, National Archives, Kew, London.
[20] Ibid.

The matter was raised at ministerial level in the FCO who were keen that FIG and the FCO explore with SCB senior management in London whether an accommodation could be reached. It was felt that all avenues should be exhausted before asking Lady Young to raise these issues with her fellow peer and the Chairman of the bank Lord Barber. A series of follow up meetings were held over the next year including with the General Manager of the bank Peter Weller. He had strident views that it would not be in the interests of the bank shareholders to make available long terms loans for house purchases against a short-term deposit book. The bank also had concerns about the viability of the newly created sub-divided farms and the ability for any bank lending to be repaid.[21]

By autumn 1986, it was apparent that SCB would not shift their position in terms of their restrictive lending policy in the Falkland Islands. It was felt that there was no alternative other than for the Foreign Minister to intercede with the Chairman of SCB as the rationale for establishing a commercial bank in the Islands was for it to provide much needed additional funding which would boost the growth prospects of the Islands. The resources of both FIG and FIDC were already stretched.

Lady Young was briefed ahead of a meeting in the House of Lords with Lord Barber and Peter Wells at SCB in October. The briefing revealed that SCB had "been doing good business. Deposits taken over from Government Savings Bank have provided good basis for expansion. Islanders' savings ratio are high."[22] This business also included the provision of short-term lending and working capital facilities. The original fears about the viability of the new Stanley branch appear to have been misplaced.

In the meeting with Lady Young, Peter Weller provided a useful and reasonable context about SCB's stance in relation to residential mortgage lending. They had, unlike the UK clearing banks, ceased mortgage lending in the UK and as the Islands came under the jurisdiction of the UK they were being treated in the same way. He also explained why SCB was not a typical high street bank given its strategy was largely focused on facilitating international trade in the emerging markets of Africa and Asia. Lord Barber undertook to look into the perceived restrictive lending practices personally to see whether this was true and what could be done.[23]

The meeting provided some useful insight and understanding into SCB and how the Falkland Islands fits (or does not fit) within its wider corporate strategy. The archive material suggests that they are supporting local businesses and providing a level of short-term business lending in the Falkland Islands. However, it also confirms FCO suspicions that SCB's concerns about extending longer-term credit are not framed just by commercial considerations. Notwithstanding the extensive assurances from the FCO including at ministerial level about the UK's political commitment to the Falklands, and in particular to the principle of self-determination for the Islanders, the SCB executives still held a view that only short-term financing be considered because a future deal on sovereignty with Argentina might lead to them incurring bad debts. Islanders may, in those circumstances, decide to just leave the Islands without repaying their borrowing.[24]

SCB approach their tenth anniversary in Stanley and seek a long-term licence but has planning permission for a new branch refused

When SCB established their branch in Stanley they were granted a banking licence which was renewable on an annual basis. In reality, there was little prospect of the licence not being renewed at each anniversary given the desire to retain a commercial bank in the Islands. However, SCB felt that the short tenor influenced the way in which it would provide products and services – particularly lending facilities.

In January 1990, its banking licence was extended for a longer period of six years. In May 1992, SCB wrote to the Financial Secretary seeking a banking licence with no expiry date – thus matching the practice in their other jurisdictions. The bank were cognisant that there had been doubts in certain influential quarters about their commitment to the Islands and their willingness to commit further capital and expertise to develop

[21] Christopher Hum (FCO) to Peter Weller (SCB, London), 5 March 1986, FCO7/5518, Falkland Islands rehabilitation: Banking, National Archives, Kew, London.
[22] Briefing Note – Falkland Islands : Standard Chartered Bank by David Broad (FCO), 3 October 1986, FCO7/5518, Falkland Islands rehabilitation: Banking, National Archives, Kew, London.
[23] Record of Call by Lord Barber on Lady Young in the House of Lords, 22 October 1986, FCO7/5518, Falkland Islands rehabilitation: Banking, National Archives, Kew, London.
[24] Ibid.

their proposition further. SCB had somewhat eased on their previous reluctance to lend for longer term periods with business lending increasingly structured over 5 years and residential mortgage lending up to 25 years. The bank was also being asked to consider larger lending transactions over longer periods but the restrictions on the licence meant they were unable to meet these customer requests. Another consequence of the short-dated licence is that they could not place branch deposits on longer maturities with their head office. This had an impact on the rates they could pass on to customers and limited their lending capacity.[25]

FIG agreed, having taken advice from the Bank of England, to remove the expiry date of SCB's banking licence subject to SCB providing a greater level of statistical information to FIG which could in turn be shared with the Bank of England. Both FIG and the Bank of England had some concerns that granting an unlimited licence to a firm with a de-facto monopoly might cause indigestion for some stakeholders. This was resolved by considering it a factor of the small market as opposed to the characteristics of the licence itself.[26]

SCB understandably felt frustrated that their commitment to the Islands continued to be questioned in certain quarters. They even went as far as providing a fairly detailed memorandum, on some considerations, for the Treasury if FIG should wish to explore replacing them with a domestically owned bank.[27] As a tangible sign of their ongoing commitment, SCB was keen to improve the proposition and services provided to customers. They had earmarked over £500,000 of investment to move to an improved premises across the road however planning permission was refused on a number of occasions due to concerns about the loss of recreational amenities. Eventually, planning permission was granted and SCB operate today from this site on Ross road.

A public – private innovation is launched with SCB in 1996 which boosts access to mortgage funding in both Stanley and the Camp area

In 1996, SCB partnered with FIG to launch the Joint General Mortgage Scheme ("**JGMS**") which significantly boosted the availability of mortgage funding for borrowers in both Stanley and Camp. Under the scheme, FIG guarantee the 'top-slice' of a mortgage thus providing additional security for SCB in addition to the usual deed security and enables buyers to borrow up to 95% of the value of the property whereas lending is restricted to 80% on the variable rate mortgage scheme.[28]

The scheme was revised in March 2001, July 2003, July 2007, March 2019 and in December 2020 to increase the maximum thresholds to reflect the increase in house prices. In the most recent scheme revisions SCB agreed to not only increase the maximum level of borrowing provided under the scheme but also agreed to reduce the maximum guarantee component required from FIG. For properties in Stanley, it has reduced from 20% to 16% whilst the guarantee component for properties in Stanley now ranges from a maximum of 50% to 16% whereas previously it was set as a fixed guarantee of 50%.[29]

The JGMS has particularly helped first time buyers get onto the property ladder and also provides the peace of mind of having a fixed interest rate throughout the duration of the loan which can be up to a maximum of 25 years. It is noteworthy that SCB has never experienced a foreclosure or significant mortgage delinquency in the Falkland Islands. This reflects the prudence amongst members of the community but also is a testament to the sound underwriting framework of SCB.[30]

Launching a credit union was explored in 2014 but did not proceed

In 2013, the FIDC working in collaboration with the World Council of Credit Unions, undertook an in depth feasibility study to explore whether a credit union should be established in the Falkland Islands. The aim was to introduce greater plurality into the lending market. The feasibility study included public consultations

[25] Norman Black (SCB, Stanley) to Derek F. Howatt (FIG), 6 May 1992, FCO7/9459, Falkland Islands: Standard Chartered Bank, National Archives, Kew, London.
[26] Richard Wagner (FIG) to Graham Bradshaw (Bank of England), 7 September 1992, FCO7/9459, Falkland Islands: Standard Chartered Bank, National Archives, Kew, London.
[27] Normal Black (SCB, Stanley) to Richard Wagner (FIG), 27 August 1992, FCO7/9459, Falkland Islands: Standard Chartered Bank, National Archives, Kew, London.
[28] Executive Council Paper – Amendment to Joint General Mortgage Scheme, 9 December 2020, Falkland Islands.
[29] Ibid.
[30] Ibid.

which found there was a very high level of public support for such an institution in the Islands. However, the project did not progress as with the relatively small size of population the credit union was forecast to make a loss of £750,000 over a 5-year period and it was not considered financially sustainable. It would have also necessitated FIG to contribute start-up capital, overhaul the banking legislation and to appoint a banking regulator.

A brief history of the Standard Chartered Bank – not your typical British high street bank

SCB can trace its heritage back to the commanding heights of the British Empire. In order to fund further overseas expansion, specialist banks were set up to facilitate trade. One such bank was the Chartered Bank of India, Australia and China – which was focused on serving the markets of those countries albeit it did not receive a charter in the end for Australia. Its business model was based on being an 'exchange bank' with capital raised in the City of London and then shipped out as bullion to support the foreign currency transactions of British companies in Eastern ports stretching from Bombay to Shanghai. By the late 1920's, Chartered Bank was equal in size to HSBC as a large British bank focused on foreign exchange and trade.[31]

The Great Depression triggered a collapse in international trade and Chartered Bank's access to its core markets became heavily restricted, particularly in China following the rise of the Communist Party after the end of the Second World War. The bank retreated to Hong Kong and built a lucrative business by pivoting to lending to local companies as opposed to firms of the Empire. It opened a network of retail branches to raise deposits and, come the 1960's, it was opening up to 3 new branches per month in the territory. Its reliance on the remnants of the Empire was diminishing fast.[32]

The Labour devaluation of Sterling in the 1960's ended its role as an official reserve currency and led to the dismantling of the UK overseas banking model. As the era of Empire was drawing to a close and with fierce competition coming from American banks, Chartered Bank merged with Standard Bank of South Africa. The aim was to create a more balanced firm with operations stretching across Asia, the Middle East and Africa.[33]

Standard Bank had a similar backstory to Chartered. It was conceived to facilitate trade albeit in Africa with the burgeoning diamond industry supporting over 100 branches across South Africa giving it a quasi-central bank role. But geopolitics also played a role in its evolution – as South Africa became more isolated because of Apartheid, it spun off a chunk of its South African operations and ventured into other African markets through the acquisition of the Bank of British West Africa.

Both banks had courted suitors. Barclays held a 14% stake since the late 1950's and there was a clamouring within its international division to bolster its shareholding ahead of a full-blown merger. Midland (now HSBC) also floated the idea of a merger in 1963. The Chartered chairman rejected these overtures having also turned away Australia & New Zealand Bank ("**ANZ**") as well as an American outfit. Over at Standard Bank, Chase Manhattan (now JP Morgan) had accumulated a 15% stake and the two bank's African operations were well integrated. Chase and two other firms declared an intention to increase their holding to 40%. Standard's board was not impressed neither too was the Bank of England. Their preference was to merge with another overseas bank with links to Asia to create a global business – this triggered the merger with Chartered Bank.[34]

The newly combined firm was large and very complex. Getting approval from the minority bank shareholders and the full array of regulators was no mean feat and integrating the two firms with very different cultures was challenging. The market signalled that the integration was not going well – the share price had fallen from 267 pence to 160 pence within the year. The task of merging the two banks was put into the 'too difficult' box and the two banks were run separately for years to come.[35]

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[31] Duncan Campbell-Smith, *Crossing Continents: A History of Standard Chartered Bank* (London: Allen Lane, 2021), 2-4.
[32] Ibid, 5-12.
[33] Ibid, 431-432.
[34] Ibid, 438-440.
[35] Marc Rubenstein, "The Bank that Never Sold," Net Interest (substack), 13 January 2023, https://www.netinterest.co/p/the-bank-that-never-sold

A strategic review was launched in the mid 1970's by a new CEO with the aim of diversifying the bank's international revenues. The idea was to have a quarter of assets in North America and to build a business in Europe which would account for another quarter of its assets. At the time assets were split roughly 50:50 between Africa and Asia with a very small presence in the UK. Over the next decade it pushed for global expansion. It bought a bank in America and tried to buy the Royal Bank of Scotland. By the time it opened the branch in Stanley, the group was riding high - reporting a £405 million profit with just over a quarter of revenues coming from South Africa and ~ £50 million from Hong Kong and Singapore.[36]

But the bank soon hit the rocks. The geopolitical situation in South Africa turned sour and the banks reputation, because of its association with the country, was damaged. Combined with heavy losses on its loan book, the share price fell to levels where it yielded 9.5%. Trading at a 50% discount to book value bidders, sensing an opportunity, began to circle. Senior management mounted their defences including evaluating innovative solutions including taking the bank private through a management buy-out. Amidst rumours of potential bids, Lloyds sprung the first hostile takeover bid of a British bank valuing the bank at £1.2 billion. A hurriedly assembled and eclectic mix of 'white knights' blocked the Lloyds bid. It worked in the near-term but left SCB with a register of new shareholders with sharply differing interests. Some wanted to focus on how the bank's position in Hong Kong could be exploited to capture growth in China whereas others were urging a tougher focus on profitability and the disposal of marginal business lines including the US bank.[37]

Respite from bid distractions did not last long. SCB, as had all the other British banks, piled into the syndicated lending market in the early 1980's building up an imprudent level of exposure to Latin American sovereign debt. It triggered a wave of defaults and SCB were forced to take over US$600 million of write downs which plunged them into a loss. Shareholder reserves declined sharply from £1.3 billion a year earlier to just £717 million. Vultures circled once again but were ultimately rebuffed. A new management team embarked on a heavy restructuring and cost-cutting plan which saw the American operations sold. This refocused its strategy on gathering funds in Africa and Asia to facilitate international trade and institutional business.[38]

The Asian Financial Crisis in late 1997 engulfed SCB given its pivot to Asia. This led to more internal soul-searching. The stock price collapsed by 50% over just five months and the merit of exploring tie-ups as a way of shoring up the business was broached. Barclays, like a phoenix rising from the ashes, emerged as a potential partner. They were keen on internationalising their business but again a deal did not materialise.[39]

SCB, along with HSBC, were the British banks who fared best during the Financial Crisis of 2008. The pivot Eastwards and decision to exit the US market shielded SCB from the sub-prime mortgage write downs which holed many peers below the waterline. Perhaps, finally the value of its global network would start to shine?

Alas, another crisis would soon afflict the bank. In 2011, it was charged in the US with engaging in a criminal conspiracy to bust sanctions imposed against Iran. The bank paid significant fines and a new CEO, Bill Winters was hired. Since this time, Winters has overhauled the risk culture, bolstered the compliance function, exited high-risk business lines including a number of countries and regions – all against a backdrop of ultralow interest rates in the era of quantitative easing. SCB was hit with another round of enforcement action and fines as recently as 2019 relating to earlier money laundering and sanctions breaking.[40]

Is SCB destined to always be the bridesmaid but never the bride?

Winters took up the reins at SCB when it was in midst of a crisis and no one should doubt the size of the task. The restructuring has seen the loss of ~15,000 jobs and over US$5.1 billion of fresh equity was raised in 2015. It needed to shed risky emerging markets loan assets, introduce an effective financial crime/money laundering framework and overhaul its risk culture. Growing revenues and boosting shareholder returns is a tall order against that backdrop.

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[36] Ibid.

[37] Duncan Campbell-Smith, *Crossing Continents*, 534-547.

[38] Ibid, 558-568.

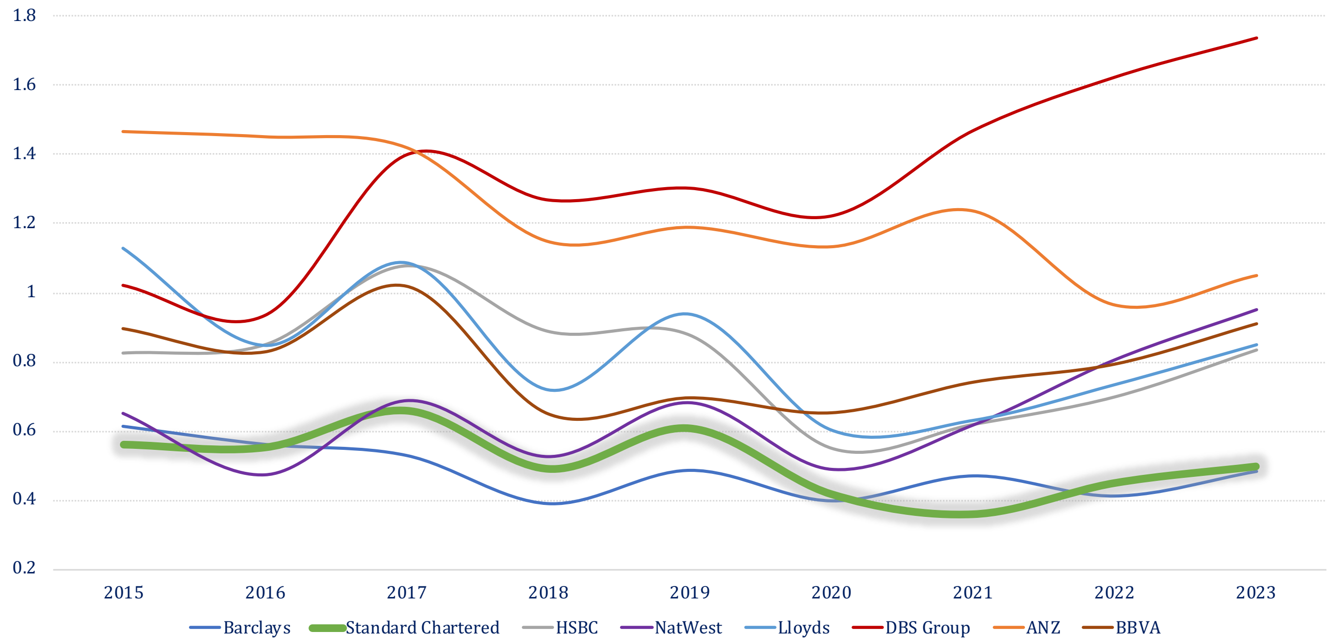
[39] Ibid, 620-625.

[40] Frances Coppola, "Standard Chartered Bank's Long History of Financial Crime," *Forbes*, 10 April 2019, https://www.forbes.com/sites/francescoppola/2019/04/10/standard-chartered-banks-long-history-of-financial-crime/

On the face of it SCB should be an attractive opportunity. It has a 150-year heritage, is well positioned in a number of attractive markets and should be positively geared to benefit from rising interest rates. But, why do so many firms appear to walk away after taking a closer look at the business? In 2014 and 2015 alone – ANZ, JP Morgan, Santander and Scotiabank were linked to potential transactions attracted by its international reach. In 2018, Barclays rekindled its long-standing interest but chose again not to proceed with a bid.[41]

SCB's longer term shareholders are nursing significant paper losses with the share price having dropped by a third during Winters custodianship. The first 9 months trading of 2022 saw underlying income rise by 10% to US$12.5 billion and pre-tax profit jump 17% to US$3.2 billion. Return on equity also moved into double digits to stand at 10.1% up from 6% a year earlier. The *Financial Times* also reports they have returned US$1.4 billion to shareholders via dividends and buybacks in the first nine months of 2022. However, the shares are not enjoying the same re-rating as peers with a marked gap developing as shown in Figure [1] below.[42]

Figure 1: Mind the gap – SCB price to book ratio vs. a selection of peers



Source: Refinitiv

SCB remains one of the cheapest banking stocks in Europe. The recent softening in Sterling may also stimulate further take-over interest as the buying power of foreign suitors is boosted. In early January 2023, First Abu Dhabi Bank confirmed to the market it had mulled a takeover of the bank but was not progressing with an offer. Perhaps, the near 50% discount to book value is not considered to represent sufficient value bearing in mind the complexity of integrating SCB and the extent of regulatory approvals which would be required.

[41] Stephen Morris & Emma Dunkley, "Why Standard Chartered remains a target despite its latest suitor walking away," *Financial Times*, 6 January 2023, https://www.ft.com/content/77c5e742-fc3c-4fdd-a5d1-96865e5cccb9.
[42] Ibid.

Section 3: Review of the Falkland Islands

Country overview

The Falkland Islands is a remote British Overseas Territory ("**BOT**") positioned in the deep South Atlantic Ocean. Its ties with the UK can be traced back to the seventeenth century when the first British landing was made. The relationship with the Crown formalised in 1843 with an Act of Parliament that enabled the British government to conduct civil administration on the Islands. A local government was soon established with a Governor, Legislative Council and Executive Council to assist the governor. Initially, suffrage was limited but became universal in 1948 alongside changes to have elected members of the Legislative Council.[43]

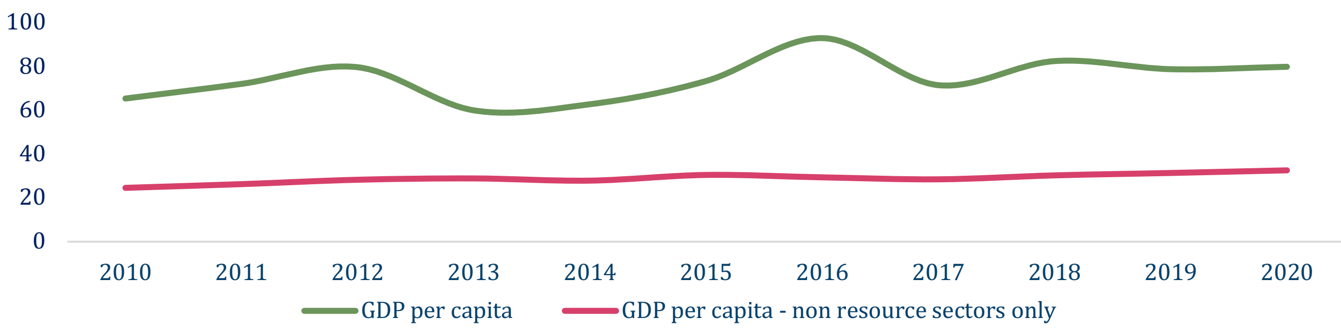
Further changes were made in response to the recommendation contained in the Shackleton report that greater autonomy be granted to the Islands. A new constitution was enacted in 1985 which shifted the decision-making away from the Governor towards the elected legislative council members. There were further constitutional changes introduced in 2008 which incorporated a broad range of fundamental rights and enshrined self-determination in the constitution itself. The Legislative Assembly was created to replace the old Council. Under these arrangements the Governor, representing His Majesty the King, has responsibility for external affairs, defence and police. Whilst, the government directs the economy, health, education and immigration. The Governor retains a right of veto but in reality, this is seldom exercised.[44]

The Falkland Islands operates in a uniquely complicated geopolitical context because of the continuing irredentist claims from Argentina. This can create logistical challenges in areas such as communications, airlinks and so on however the Islanders are highly resourceful and have found ways to work around these challenges to build a prosperous economy.[45]

Economic overview

By the late 1970's, Shackleton found the economic situation of the Falkland Islands troubling – it was a 'quasi-colony' manifesting a dependency culture with significant depopulation, deteriorating public finances and a political class who lacked confidence to arrest its decline. After the liberation in June 1982 and after a follow up report from Shackleton, the UK committed significant funds to the rebuild of the Islands. A good many initiatives identified in the Shackleton report were implemented. These included the setting up of the Falkland Islands Development Corporation which spear-headed a series of economic changes including land ownership reform, projects to diversify the economy and the declaration of a fisheries zone around the Islands. The Falklands, in just 40 years, has gone from being on the verge of economic peril to becoming financially independent of the UK in all matters save for defence. Public finances are in rude health and offering a high standard of living for residents as evidenced below in terms of GDP per capita.[46]

Figure 1: GDP per capita (FK£)

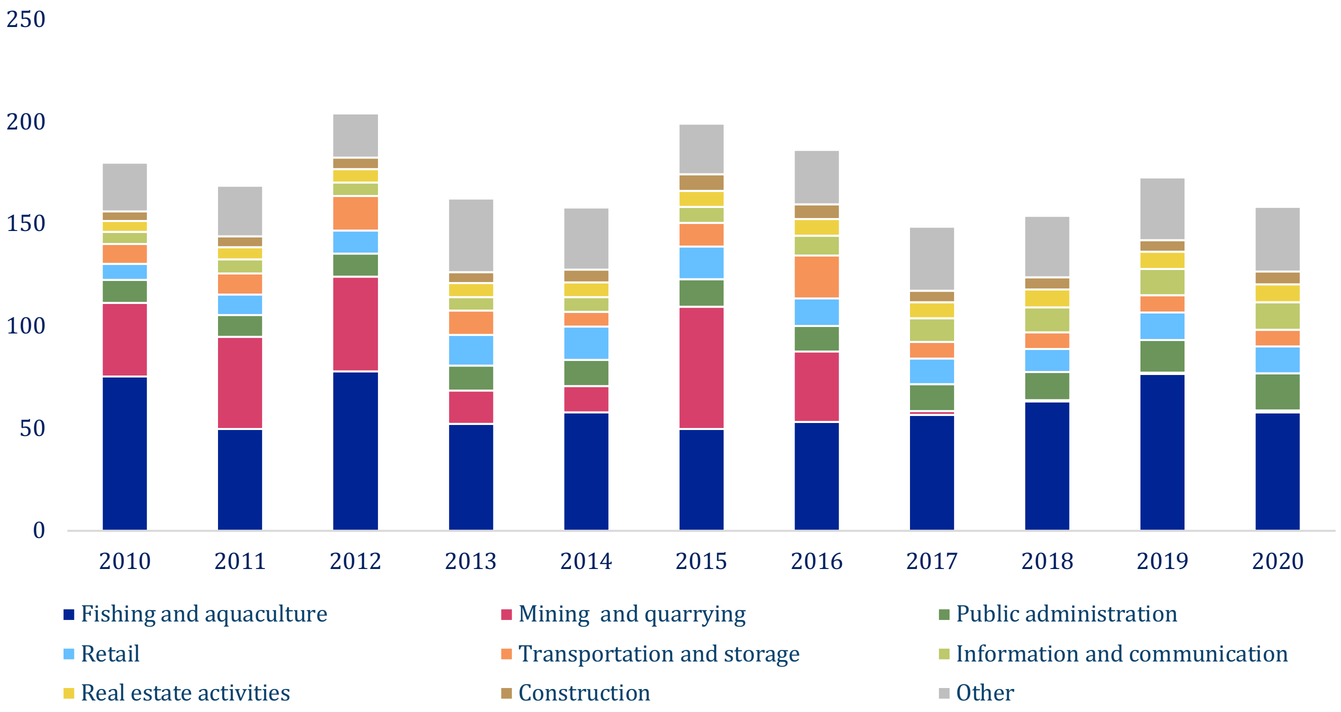


Source: Falkland Islands Government

[43] Peter Clegg, "Political and constitutional issues for the contemporary Falkland Islands," March 2022, *The Round Table – The Commonwealth Journal of International Affairs*, 2-4.
[44] Ibid.
[45] Sarah Tudor, "Sovereignty since the ceasefire: The Falklands 40 years on," 2022, *House of Lords Library*, https://lordslibrary.parliament.uk/sovereignty-since-the-ceasefire-the-falklands-40-years-on/#heading-3
[46] Clegg, "Political and constitutional issues for the contemporary Falkland Islands," 2-5.

As Figure 2 demonstrates, the fisheries industry dominates the economy of the Islands and also drives other sectors such as transport and storage, administrative and support services. Investments made by the fisheries companies in other sectors including retail and real estate are also present in an effort to diversify. Efforts are underway to try to reduce the reliance on fishing, as it can lead to volatility linked to fish stocks and annual catch. Tourism is considered to be a driver of future growth in the Islands however its development was retarded by the pandemic.

Figure 2: Sector drivers of economic performance (FK£)



Source: Falkland Islands Government

There has been widespread speculation for some time that the Falklands is on the verge of largescale hydrocarbon extraction. It is important to note that currently this sector is a relatively small contributor to national income albeit it has boosted economic output in previous years. Should extraction become a reality it is likely to have a significant influence on the future development of the Falklands albeit it may potentially introduce a greater level of volatility into the public finances.

Overview of the banking sector

Standard Chartered Bank

Standard Chartered

Standard Chartered Bank ("SCB") is an emerging markets focused global banking group, headquartered and listed in London. The bank opened a branch in the Falkland Islands in December 1983, on the initiative of its Chairman Lord Barber, in response to urgings from then Prime Minister Margaret Thatcher.

The branch operates with an FTE of 21 people from premises on Ross Road in the centre of Stanley. The branch is fairly characterised as being 'traditional' in terms of look and feel with a number of tellers and an enquiries desk sitting front of house. Behind which sits the machine room and strong room with a suite of management offices on the upper floor.

Until recently the bank operated on its own servers situated in the Falkland Islands but recently migrated to the wider SCB back office platform; the implementation of which took place in November following five months of delay owing to challenges identified in the User Acceptance Testing ("**UAT**"). It is understood the delay stemmed partly from a review by the UK regulator but also due to extended UAT connected to the internet bandwidth challenges in the Islands. Data continues to be stored locally and transmitted at various points during the course of a working day as opposed to operating purely on the cloud given the broadband challenges in the Falkland Islands.

The branch provides a range of rudimentary money transmission (current) and savings accounts. Payments can be made via debit card, cheque or funds transfer slips. Payments in and out of the account electronically can only be made by SWIFT as the branch does not form part of the UK banking network. The bank does not provide an Automated Teller Machine (**"ATM"**) and neither does it issue credit or charge cards. Customers can choose to receive e-statements by email on a daily, weekly, monthly or quarterly basis. There is no online, digital or mobile banking for customers to access their accounts to view information or to originate payments. Funding for this project was previously allocated but was subsequently cancelled owing to the Covid-19 pandemic. There is no confirmed date or funding allocated for the delivery of this capability.

SCB have banking relationships with ~3,000 individuals and ~500 businesses albeit it should be noted that nearly 50% of these business relationships have balances of <£15,000. They have issued ~2,000 debit cards across these accounts. The SCB branch has total deposits ranging between £150 million and £180 million with the majority of these being on sight or short dated tenors. They are laid off with other SCB offices in Jersey and London.

The bank has a total loan book of ~£21 million. Residential mortgages comprise ~£17.5 million of this loan portfolio of which ~£14 million is underwritten through the Joint General Mortgage Scheme and benefiting from the 'top-slice' guarantee from FIG. There is a commercial lending book of ~£600,000 and the balance of loan book comprises other personal lending (e.g. car finance loans and so on). SCB in the Falklands will not lend to businesses which have not been operating for less than three years. SCB operates with a loan to deposit ratio of between 11 – 13% in the Falkland Islands.

The SCB business is led by current Local CEO Sarfraz Rao who joined the business in 2021. The Local CEOs are rotated in from the wider SCB network for terms of between 3-5 years and they lead a team of 21 branch colleagues including 14 in operations. There are 5 colleagues who provide support with customer due diligence and credit management and a finance officer. The Stanley branch is also supported by functional Subject Matter Experts in Jersey in areas such as compliance and financial crime. The Stanley branch reports to SCB in Jersey which focuses on international personal banking.

The Falkland Islands Development Corporation

The Falkland Islands Development Corporation ("**FIDC**") was setup in 1983 following on from the Shackleton Report which saw an important role for a Development Corporation on the Islands. The FIDC was charged with spearheading a number of initiatives including the reform of the farming land and also attracting to the Islands missing skills and expertise which would support the wider development of the economy.

Its mandate is to act as a partner to business, helping to develop and execute strategies for the improvement of the Islands' rural, tourism and wider business sectors. The FIDC is managed at arm's length from the government by a Board of Directors. It receives its budget from the FIG which currently sits at ~£1 million per year.[47]

FIDC provides loan and grant funding to businesses. It presently has a loan book of £2.5 million although in the past it has on occasion provided equity financing. There is a formal loan approval process with FIDC staff having a delegated authority for smaller loans and larger loans requiring sign-off from a credit committee, the Board or Executive Council.

FIDC support, in loans or grants, are always made on the basis they support its core mission to boost the economic development of the Islands. Loans will be considered for start-up ventures and established businesses for a variety of purposes including working capital, growth funding or the acquisition of land and property. Loans will be provided either on a concessionary basis or at commercial rates of interest. Loan

[47] Falkland Islands Development Corporation. 2021 Annual Report, https://www.fidc.co.fk/about-us/annual-report

terms of up to 5 years are available for financing plant and machinery or up to 25 years for financing land and property.

In addition to its role as a development lender, FIDC also plays a critical role in helping businesses develop business plans and strategies to grow, advice and support including training and skills seminars. These additional services are provided free of charge.

Wise (previously Transferwise)

Wise functions like a digital bank for many Falkland Islanders, although it is not authorised as a bank by the UK regulators. Instead, it is authorised an electronic money provider and is subject to placing customer funds on safeguarding bank accounts with established banks.

Wise offers a multi-currency bank account for both individuals and businesses with a UK sorting code and account number. Its services are delivered entirely digitally through an intuitive and simple to use mobile app. It offers the ability to make international and domestic payments at competitive rates compared to SWIFT.

Wise also issues a multi-currency debit card which allows Falkland Islanders to spend their money both at home and abroad. These accounts are increasingly being used by businesses using the Square card merchant service as an alternative to Gibraltar International Bank because of the faster account opening service.

Wise have announced they are applying for authorisation to become a regulated bank in the UK. This would benefit their customers by also providing coverage under the Financial Services Compensation Scheme for deposits held with them.

Square

Square is a payment processing platform that charges a flat 2.5% transaction fee. It allows businesses to accept card payments from all major debit, credit and charge cards, this was particularly helpful to businesses which relied on the custom of tourists who have increasingly not wanted to use cash. A trend which has accelerated following the pandemic. Many businesses who have adopted Square payments note that the 2.5% transaction fee is more than offset by an uplift in the total customer spend.

The business is owned by Block Inc. which is a multinational technology conglomerate, owning a suite of payment related platforms, including in the buy-now pay-later sector.

It is important to note that Square have declined to roll-out the service to St Helena, Ascension Islands and Tristan de Cunha at the current time. They have cited technical difficulties with the roll-out of the service to the Falkland Islands.

Gibraltar International Bank

Gibraltar International Bank ("**GIB**") is a Gibraltar based full-service bank, wholly owned by the Gibraltarian Government. It was setup following the Barclays withdrawal from Gibraltar and the concerns which arose around the competitive landscape of the remaining banking sector.

GIB have been providing bank accounts and digital banking to businesses in the Falklands to allow them to operate the Square payment platform which cannot run using SCB's existing infrastructure. Each transfer payment back to bank accounts held at SCB is charged at ~£30 as it has to be routed via the SWIFT network which means businesses have to plan carefully to minimise the number of payments. Some businesses noted that the on-boarding process with GIB can be a little protracted and the recent introduction of text messaging as a means of secondary authentication for online banking / payments has caused issues given challenges with the mobile signal in Camp.

GIB is not a full-service bank in the Falklands but they have offered a much needed solution and access to the UK banking network. They do not provide any credit facilities in the Falklands given they do not have a physical presence. Without their support the roll-out of Square would not have been possible.

The Falkland Islands Company

The Falkland Islands Company ("**FIC**") is the largest business on the Islands and has approximately 25 business units including a car retail outlet. FIC provides credit accounts to customers in its retail stores and also provides car financing including hire purchase loans. It is understood that the loan financing book is in excess of £1 million.

FIC are also heavily involved in the building of new properties in the Islands and offers a turn-key solution to prospective buyers which affords them a level of certainty in terms of the price and enables them to continue renting whilst the house is being built. At completion the property is typically financed by SCB through the JGMS scheme.

FIC are also act as agents for the Caribbean Alliance Insurance Company who provide a range of insurance for residents of the Islands including personal, property, vehicle, employer and cargo insurance.

Stanley Services

Stanley Services is one of the larger corporations on the Island owned by a consortium of stakeholders including FIG and two other institutional shareholders. The primary business of Stanley Services is oil import, storage and distribution. As well as the civilian petrol station, the business provides commercial refuelling including marine bunkering and aviation fuel.

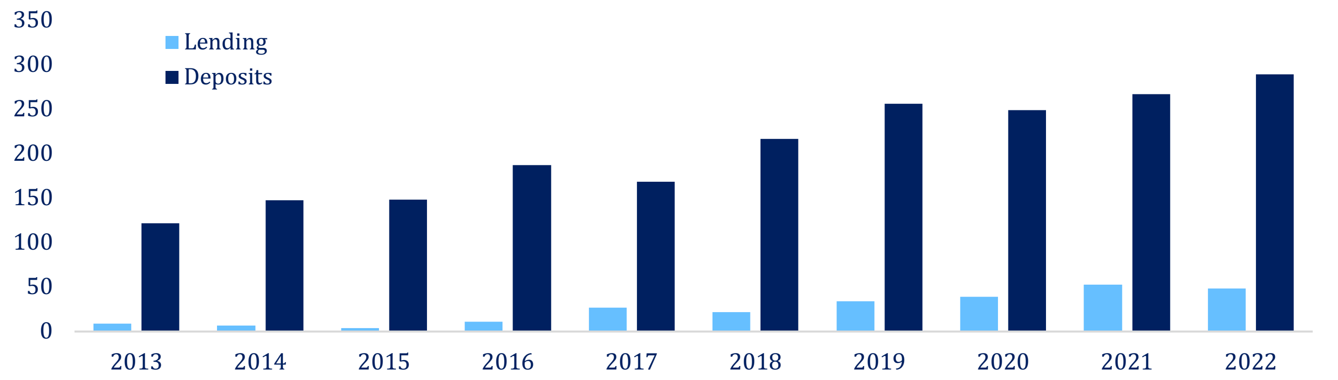
In terms of financial services there is a modest car finance portfolio. More recently Stanley Services has become well known for their ATM service which is on the Visa/Mastercard network. As the only ATM on the Island, it dispenses cash of £100,000 and £150,000 per month. It is understood this service is operated on the basis it 'washes its own face' as a community service as opposed to being a for-profit endeavour.

Service provision ex-Falkland Islands

It is noted that a number of the larger organisations and FIG have arrangements with UK banks some of which are very long-standing in nature. Some firms which were interviewed indicated that whilst these UK banks were comfortable in maintaining their existing arrangements they were not open to extending further services including the opening of additional accounts.

These arrangements are in addition to maintaining accounts with SCB in Stanley which are typically used for settling local wages/salaries and suppliers. All of the firms interviewed with UK accounts of this nature have access to them via digital or mobile banking including the ability to originate payments. A number of those undertaking retail operations also benefited from card merchant services to accept debit and credit cards.

Figure 3: Lending & Deposits to Islanders by banks without a physical presence (£m)



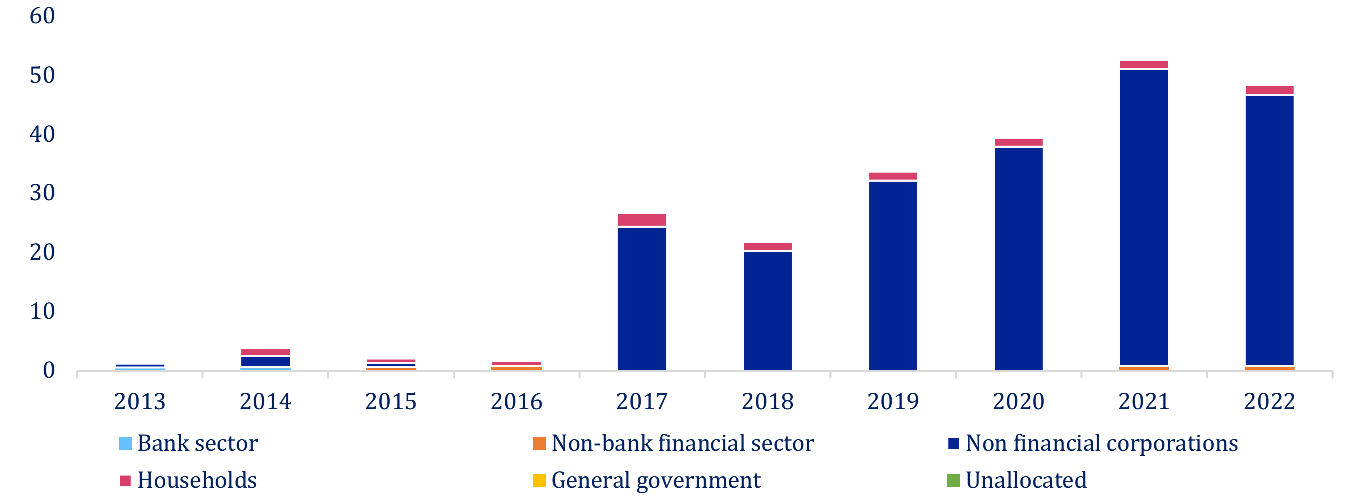
Source: Bank of International Settlements, Bank of England

Figure 3 shows the level of deposits and loans for Falkland Island residents with banks outside of the Falkland Islands. As at June 2022, there is £49m of lending – almost entirely from Spanish banks and likely to one of the fishing joint venture companies – and over £280 million of deposits. This suggests that the total size of the banking market in the Falkland Islands for deposits stands in the range of £430 million to £450 million.

Over the past decade deposits outside of the Falkland Islands have grown 238%, with a compound annual growth rate of 9%, lending has grown 538% which corresponds to an 18% compound annual growth rate. Whilst deposits have grown at a slower rate than lending, it is important to note deposits started at a far higher level relative to lending (£121m compared to £9m).

This is greater than the total amount of deposit and lending book held by SCB at present and represents a significant value pool which is being lost by the Islands. Some of these deposits will be placed with banks other than SCB because of the requirement to have counterparty diversification however it is not unreasonable to assume that a significant proportion of these deposits might be repatriated to sit within the Falkland Islands should the range of services be expanded.

Figure 4: Analysis of lending to Falkland Island residents from outside of the country (£m)



Source: Bank of International Settlements, Bank of England

Figure 4 shows the lending to Falkland Island residents from outside of the country. The overwhelming majority of lending takes place in € to non-financial corporations, most likely the joint venture fishing companies which have started a significant fleet renewal programme.

Understanding the banking needs of Falkland Islanders

The Falkland Islands has a diverse range of businesses operating in Stanley and Camp which were interviewed as part of this work in order to get a clear picture of the breadth of the banking needs on the Islands. It is not considered appropriate to profile specific businesses in this report – instead a range of generic profiles have been developed to articulate the characteristics and needs of a typical retailer, hospitality business and so on. These are set on the following pages together with a short narrative summary.

Families and households

Name: Sally & Jason Smythe **Occupations:** Doctor & Teacher
Location: Stanley

Sally and Jason moved to the Falkland Islands from the UK about two years with their work – Sally is a GP and Jason a primary school teacher.

As young professionals with two small children they lead extremely hectic lives and have decided to make the Falkland Islands their long term home. They are actively looking for houses and are looking to purchase within the next twelve months.

Needs

- Sally and Jason both have everyday banking needs for receiving their salaries, paying their bills and making savings. They also receive rental income from their investment property in the UK and also contribute to investment plans and their own pension funds.
- They are also both keen to save for their children's longer term education needs including a university fund.
- Sally and Jason are also looking to finance their house purchase in the Falkland Islands with a mortgage.

Challenges

- They both lead busy lives revolving around their children's extra curricular activities – they want to be able to do their banking at a time that suits them.
- They were very accustomed to doing all of their banking in the UK via their mobile apps – not being able to do this with their accounts in the Falkland Islands is very inconvenient.
- They would also like some more innovative savings products to encourage regular savings for their two young children.

Key Product Requirements

Banking	• Current and Savings Accounts • Fixed Term Deposits • Online / Mobile Banking • Money Transmission
Financing	• Overdraft / personal loans • Credit Card • Mortgages – home purchase and investment property
Other Products	• Share dealing • Investment products • Insurance (Car / Home / Travel)

All individuals have day to day banking needs for receiving their salaries, paying their bills, and making savings. Many also require lending facilities, this might be an unsecured personal loan, an overdraft, a mortgage, a car loan or a secured personal loan. Many individuals, particularly expats from more connected countries, expect to be able to do their primary banking through either an app or an internet portal. Families, particularly those who live far away from Stanley and those who are time-poor, would benefit from a means of doing their banking online.

The Falkland Islands has a relatively young and able population relative to the UK, however there is a substantial number of vulnerable individuals. Greater levels of digitisation may adversely affect the service proposition for those who prefer the highly personal and traditional banking process that currently exists. Any service changes must consider this vulnerable sector of the Falkland Islands, ensuring that there is a degree of financial inclusivity maintained. This could come by way of greater promotion of financial education tools online.

Fishing industry

Name: Philip Agnew
Location: Stanley
Position: Owner & Managing Director
Sector: Fisheries

Philip's fishing business is one of the many SME's engaged in deep sea fishing with most of his catch exported overseas.

Based out of Stanley with cold storage facilities, an office and a leasehold on a dock Philip runs the business with a workforce of around 30 people. He is keen to expand the business through the purchase of an additional vessel and is keen to hire more people to support this growth.

Needs

- Access to day-to-day banking services with the ability to connect them to accounting and invoicing applications.
- A banker with broad experience managing international networks, trade finance transactions.
- Access to a Foreign Exchange and Money Market dealing desk together with research insights.
- Structured Asset Finance to fund the acquisition of a new vessel in order to support the growth of the business.

Challenges

- There is increasing reliance on foreign banks given the lack of services available locally in the Islands.
- Not being able to integrate the banking with accounting and invoicing software is inefficient and time consuming.
- Limited options for funding the growth of the business.
- Lack of experience in international trade and foreign exchange means most business is conducted off island.

Key Product Requirements

Banking	Current and Savings Accounts Online Banking Foreign exchange Business accounts
Financing	Business Credit Card Asset financing Trade finance
Other Products	Treasury services Business Insurance / Employers Liability Cover

The Falkland Islands rapid economic growth since the 1980's is largely attributed to innovations in the fishing sector. Fishing businesses have distinct asset finance needs, many of which a high street bank branch would not have the expertise to offer. This has led most fishing companies to establish a relationship with overseas banks for both making payments and facilitating lending.

Larger fishing companies often have more complex structures owing to their presence in overseas markets, primarily Spain which is the predominant export market for squid. This has contributed to prominent partnerships with Spanish banks who have better knowledge of the risks posed by fishing related asset finance. This will be particularly relevant over the next few years, owing to the need of several businesses, which are renewing their fleets at the cost of several million pounds. The terms offered by Spanish banks have tended to be reasonably generous owing to the strength found in the relationships they have with Spanish partners of Falklands fishing companies.

Fishing companies often employ expats in their ship's crews, and thus some require a means of paying wages in several currencies, or to several different bank accounts in different countries. It is understood that SCB have only minimal involvement with local fishing companies. The only significant involvement is where SCB Jersey provide investment services for companies with excess cash.

Tourism

Name: Greg & Jamie Thomas
Location: Camp
Position: Owners
Sector: Tourism

Greg and Jamie set up their rib tour and charter business three years ago to take advantage of the growing number of tourists visiting the Falkland Islands. They specialise in sight seeing and wildlife watching tours for visiting cruise ship passengers.

The business was severely impacted by the Coronavirus pandemic as tourists and cruise ships had been restricted from visiting the islands. However, forward bookings have rebounded strongly which is improving the outlook for the business.

Needs

- A core need of the business is the ability to accept international credit and debit cards from tourists.
- Having a modern and reliable vessel is essential and access to asset finance means is therefore important to enable the latest equipment to be used.
- Working capital facilities are also useful given the seasonal nature of the business.
- It is difficult to get to the bank during the day as we are out on the water which means having online access is crucial.

Challenges

- The arrival of Square in the Islands is a real gamechanger for the business as they can now accept credit and debit cards from cruise ship passengers. Previously everything had to be handled in cash and we lost business as a result.
- The lack of online banking access is a major issue – it means we have to organise ourselves around the bank's opening times.
- Accessing asset finance secured against the boats would be a sounder way to fund the growth of the business.

Key Product Requirements

Banking	Current and Savings Accounts Fixed Term Deposits Online / Mobile Banking Foreign Exchange Services
Financing	Overdraft / Working Capital Finance Commercial Payment Cards Asset Finance
Other Products	Merchant Services Business Insurance Public Liability Insurance

The tourism sector of the Falkland Islands is growing quickly, notwithstanding the negative impact of the Covid-19 pandemic. Tourism activities largely revolve around the unique environment and history of the Falklands and as a result are geographically diverse, some businesses even basing themselves overseas.

The core banking needs of tourism businesses include asset financing, commercial mortgages, business lending, accounts from which to pay bills/wages (both domestically and internationally). The lack of digital banking services has been subject to a wide range of workarounds including using Wise, utilising overseas accounts, at times even resorting to posting cash to the branch for deposit.

Hospitality

Name: Sabrina Elliot
Location: Camp
Position: Owner
Sector: Private sector

The Falkland Islands has a growing tourism sector which has provided additional trade for the Falkland Islands hospitality sector. Sabrina owns and works for her own café serving breakfast and lunch in near a beach in Camp. She has 3 employees (2 FTE) and is open 6 days per week.

The clientele for the business are evenly split between locals and tourists, since introducing card payments with Square Sabrina has observed a significant uptick in the amount of trade done each month.

Needs

- The business needs a means of accepting card payments.
- There is some need for debt financing whether its commercial mortgages and/or asset financing.
- Business banking allowing Sabrina to pay her three employees and her suppliers in a timely fashion.
- Ability to do transactions with overseas suppliers and customers paying in USD, which requires some limited foreign exchange services.

Challenges

- Moving money from overseas to a local account is expensive.
- Access to commercial credit is limited and Sabrina has had to approach the FIDC to help finance some kitchen upgrades.
- Employees have reported delayed wage payments due to bank system outages. Despite Sabrina sending timely payment instructions to the Bank.
- The lack of online banking makes managing cashflows challenging.

Key Product Requirements

Banking	▪ Current and Savings Accounts ▪ Money Transmission ▪ Online Banking
Financing	▪ Commercial mortgages ▪ Asset financing
Other Products	▪ Foreign exchange

The hospitality sector is strongly linked to tourism, albeit there are notable differences in their banking needs. The most obvious need for hospitality businesses is the ability to take card payments, and whilst the Square solution has improved this aspect of business it is by no means without significant drawbacks. The most crucial shortcoming is the fee associated with getting money back into the Falklands which hospitality businesses must do more frequently than most in order to meet local suppliers bills and to pay wages. This requires careful planning of their cashflows.

Conglomerate

Name: David Cullen
Position: Managing Director
Location: Stanley
Sector: Conglomerate

David is the Managing Director of a mid-sized corporate operating in a number of sectors including transport, fisheries, farming and retail. The business has ~115 employees, albeit this changes seasonally in each business. It is always looking for projects to expand its footprint both on the Island and elsewhere.

Initially a farming and retail business the conglomerate has grown rapidly since its founding 15 years ago, and has accessed capital from its shareholders to fund various acquisitions and investment projects.

Needs

- Conglomerates require a means of managing cash flows between businesses.
- There is some need for debt or equity capital, to help fund investment. As well as asset and trade financing.
- With greater fixed cost bases than the typical business, conglomerates require a means of paying wages and other costs.
- Larger conglomerates may require some corporate advisory services.
- Currency exchange services to help businesses trade internationally

Challenges

- There is a significant reliance on overseas banks for core banking needs, there is a preference for this to be facilitated locally.
- There is limited relationship management services provided by the bank locally. This limits the access to products across the wider SCB Group.
- The manual nature of the current local banking proposition creates inefficiencies within the business, complicating cashflow management.

Key Product Requirements

Banking	Current and Savings Accounts Money Transmission Foreign exchange Online Banking
Financing	Business / Purchasing Cards Working Capital / Liquidity Lines Trade finance
Other Products	Treasury Services Money Market services Investment products Corporate advisory

There are several businesses on the Islands which function like old fashioned conglomerates, with operations in multiple sectors. This creates more complex requirements from a banking provider, which has led some in the sector to partner with UK banks. The complexity relates to the greater scale of the businesses, often managing over a dozen business units each with their own unique needs and risk profiles.

Agriculture

Name: Jennifer Smithels
Location: Camp
Position: Farm owner/manager
Sector: Agriculture

Jennifer, along with her husband Tim, own and operate a sheep farm in the Falkland Islands. This farm has six thousand sheep and is run with the help of seasonal staff during the "lambing season."

The primary export market is the UK where the sheep are bought through an intermediary. The business owns the land on which the sheep graze, a warehouse and its farming equipment including a number of farm vehicles.

Needs

- As a small farm it requires an easily accessible source of working capital. There is an ongoing requirement to fund new business assets through secured asset finance.
- The business has extensive international trade requirements both importing and exporting activities.
- Access to foreign exchange services both spot and forward in order to protect against fluctuations in currency markets.
- Everyday banking services including online banking.

Challenges

- The current service provision does not include any form of business asset financing which increases costs and complexity of doing business.
- Foreign exchange and international trade have to be facilitated by off island providers as SCB have a very limited proposition presently.
- The lack of online access to bank accounts also makes administration of the business more time consuming.

Key Product Requirements

Banking	Current and Savings Accounts Online / Mobile Banking Money Transmission
Financing	Overdraft / working capital facilities Business Credit Card Asset financing Trade finance
Other Products	Investment / Retirement Savings Business Insurance

The agricultural sector in the Falklands is dominated by sheep farming for wool exports. Although there is some modest cattle farming on the Islands. These businesses are generally smaller in scale and have reasonably straightforward needs from a banking perspective. They require asset financing for farming equipment, commercial lending, and international transaction services. There is a perception from the agricultural community of the Falkland Islands that there is too limited lending from SCB than is warranted by the sectors risk profile. SCB indicate that the nature of many farms financial reporting is not sufficient for SCB to properly assess the credit proposition.

Retail

Name: Samantha Greer
Location: Stanley
Position: Owner
Sector: Retail

Samantha owns and operates a convenience store in Stanley which employs two other people. This store provides basic goods to its community and relies heavily on tourists. This has resulted in a significant decline in retail sales over the past year and a half as tourism numbers have declined steeply.

The business owns it premises as well as a van. The business imports all that it sells and relies heavily on a domestic wholesaler for these goods.

Needs

- A core need is to accept payments by both debit and credit cards. Accepting cash only can lead to a loss of business particularly from visiting tourists.
- Ready access to working capital to fund the advanced purchase of stock and to cover short term daily expenses.
- Access to online banking is essential as it is difficult to visit the bank during their business hours.
- Insurance against potential property or stock damage.

Challenges

- There is a lack of access to domestically provided merchant services which have to be set up through Gibraltar International Bank in partnership with Square. This increases complexity and cost for the business.
- There is no local provision of business credit cards by SCB.
- The lack of online banking access is frustrating and means the business cannot link its book-keeping software.

Key Product Requirements

Banking	Current and savings accounts Fixed term deposits Merchant Services Online / mobile banking Money Transmission
Financing	Overdraft / personal loans Business credit card Asset financing
Other Products	Share dealing Investment products Business insurance

There are several boutique retailers in the Falklands servicing both locals and tourists with a range of products and services. These businesses have modest financing needs, perhaps a commercial mortgage and a small amount of working capital finance for the purchasing of stock or productive capital. Most significantly these businesses require a means of making and receiving payments. These businesses have similar issues relating to making and receiving card payments through Square. Any improvements which reduce the cost of transferring money back into the Falkland's would benefit retailers.

Government

Name: Rose Henderson
Location: Stanley
Position: Treasurer
Sector: Public Sector / Government

The government of the Falkland Islands is a British Overseas Territory with a devolved legislature which is responsible for rising taxes and providing the full range of public services to residents of the Islands.

The government prides itself on being financially independent of the UK and also operating with budget surpluses and low levels of debt which has supported the growth of strong reserves. There is a need to upgrade the infrastructure of the Islands including the building of a new port in Stanley.

Needs

- The government needs to raise and collect taxes, rates and charges for services – it therefore has a large need for efficient money transmission capability.
- It's Treasury function is also responsible for managing the reserves of the Islands, including Government Pension, and therefore needs to access Money Market desks and investment products.
- The government also has infrastructure financing needs and will need to access syndicated borrowing markets.

Challenges

- The manual nature of the current local banking proposition creates inefficiencies within the Treasury department in managing the cash flows of the government.
- There is a significant reliance on offshore providers for certain products including the ability to accept debit / credit cards.
- The government also faces the possibility of having to arrange its syndicated borrowing from offshore providers whereas it would prefer to arrange this locally.

Key Product Requirements

Banking	Current and Savings Accounts Money Transmission Foreign exchange Online Banking
Financing	Business / Purchasing Cards Infrastructure Financing Working Capital / Liquidity Lines
Other Products	Treasury Services Money Market services Investment products

Broadly speaking, FIG is responsible for taxation and the provision of public services. In this regard they help to administer and improve all aspects of economic and social policy on the Islands. Their financial needs are relatively complex and require a variety of providers in the interests of diversification. Government requires a means of making and receiving payments, and facilitating investments.

Overview of available services

Below is an overview of banking services and the respective providers. Green shows availability, red shows unavailability, and grey is partial or unknown. This approach is also used in the peer-group case studies. It should be noted that it does not include situations where Falkland Islanders have access to other banking products and services through other providers outside of the jurisdiction.

Personal Banking

		Standard Chartered		wise	Gibraltar International Bank	Stanley Services	Falkland Islands Company
Money Transmission Accounts (inc. Debit Card)	Red	Green	Red	Green	Green	Red	Red
Savings Accounts	Red	Green	Red	Red	Green	Red	Red
Online/Digital/ Mobile Banking	Red	Red	Red	Green	Green	Red	Red
Share dealing & Investments	Red	Green	Red	Red	Red	Red	Red
Lending	Green	Green	Red	Red	Red	Green	Green
Mortgages	Red	Green	Red	Red	Red	Red	Red
Credit & Charge Cards	Red	Red	Red	Red	Red	Red	Red
Insurance	Red	Red	Red	Red	Red	Red	Green
Foreign Exchange Services	Red	Green	Red	Green	Green	Red	Red
Asset Finance	Red	Red	Red	Red	Red	Red	Red
ATM	Red	Red	Red	Red	Red	Green	Red

Commercial Banking

		Standard Chartered		wise	Gibraltar International Bank	Stanley Services	Falkland Islands Company
Money Transmission Accounts (inc. Debit Card)	Red	Green	Red	Green	Green	Red	Red
Savings Accounts	Red	Green	Red	Red	Green	Red	Red
Online/Digital/Mobile Banking	Red	Red	Red	Green	Green	Red	Red
Markets / FX	Red	Green	Red	Green	Green	Red	Red
Lending	Green	Green	Red	Red	Red	Green	Green
Commercial Mortgages	Green	Green	Red	Red	Red	Red	Red
Real Estate Finance	Red	Red	Red	Red	Red	Red	Red

Asset Finance							
Credit & Charge Cards							
Trade Finance							
Business Insurance							
Card Merchant Acquiring							
Support Services							
Relationship Manager Service							

Climate change resilience

The Falkland Islands, along with the United Kingdom, have a strong commitment to fight climate change. In its 2021-2040 Environmental Strategy, the Falklands set out the principles and commitments that would guide government action going forward. Among others, the government is committed to; running Stanley entirely off renewable energy, plan for the potential impacts of climate change, reduce pollution through improved waste management. These strategic objectives will have to be followed by a comprehensive programme of both public and private investment. The nature of green public investment is currently in flux, with greater clarity likely to come following the discovery work currently planned or underway.

The private sector in the Falkland Islands has not shown significant appetite to undertake green investment projects. Albeit, owing to the dominance of sectors depending on a stable relationship with the natural environment there is a powerful incentive to reduce environmental degradation.

Summary

The Falkland Islands has a solid economic and fiscal position. However, there are core banking needs for both businesses and individuals which are currently not being met by the existing bank in the Falkland Islands.

Indeed, some of these needs which are not being met might be retarding the overall development of the Islands. This is because deposits which would otherwise be with SCB locally, improving their profitability, and thereby contributing more by way of tax revenue to the FIG, are with other overseas providers. This is largely due to the isolation of local SCB accounts from the wider financial system, and the challenges caused by the lack of internet banking. Indeed, offshore deposits amount to ~£289 million which if a reasonable proportion was brought back to the Falklands would increase the deposit base and boost profitability for SCB. Insufficient service provision could be a contributory factor to this capital flight.

Section 4: Peer group cohort case studies

This section devises a cohort of jurisdictions which share similar characteristics to the Falkland Islands. These jurisdictions are used for comparative analysis in order to assess and determine what banking provision should reasonably be expected. Based on the review of the Falkland Islands found in the previous section, unique factors can be identified that have informed the selection of the peer cohort.

The Falkland Islands are a unique jurisdiction – a self-governing British Overseas Territory comprised of an archipelago of islands located in the South Atlantic Ocean. Notwithstanding its remoteness it enjoys a high level of development as exhibited by its high Human Development Index rating and robust economic performance. It is financially independent of the United Kingdom save for the matters of defence and foreign affairs.

Methodology

The following factors are unique to the Falkland Islands and have been considered in the selection of the relevant cohort. These factors were chosen to reflect those things which determine the viability of certain banking propositions and represent key factors determining the level of banking services the Falkland Islands should expect.

- **Sovereignty Status:** The Falkland Islands are a British Overseas Territory ("**BOT**") meaning it is self-governing, yet non-sovereign; depending on Britain for its foreign affairs and defence. Whilst the Falkland Islands is a self-determining territory, it does not have representation within international bodies such as the United Nations or International Monetary fund.
- This is an important consideration as non-sovereign territories tend to lack the full policy flexibility of sovereign states. Notably they lack the ability to effectively conduct monetary policy as they often have pegged currencies (as is the case with the Falkland Islands Pound which is pegged to Sterling). The interaction between the jurisdictions and their 'metropolis country' is important in the final analysis as public policy decisions at a metropolis level have the potential to significantly impact banking provisions overseas.
- **Population and Population Density:** Population is directly relevant to a bank's considerations as to whether to serve a market in any given jurisdiction as the scale of market opportunity directly affects their profitability. Population size and density also affect customer needs. The Falkland Islands requires banking products which cater to the diverse needs of the agricultural, fisheries, retail and tourism sectors in addition to the personal banking products each Islander would require.
- Population size also influences how small states navigate their integration into international trade and what kind of industries they can adopt into their macro economy (e.g. human capital restraints and so on).[48] The Falklands is a territory with a comparatively small population of ~3,600 permanent inhabitants although its population density is just 0.3 people per km^2 which places it firmly within a low-density subcategory of jurisdictions.
- **Remoteness** – Located in the South Atlantic, remoteness is a key feature in the economic development of the Falkland Islands. It therefore is prudent for this case study to use distance from the 'metropolis country' as an indicator of remoteness, as non-sovereign states tend to be reliant on support from the metropolis for certain decisions. Greater proximity can mean a more straightforward path for material support, as well as greater ease in providing technical support and advice. For the private sector remoteness can affect the feasibility of ventures by adding geographic obstacles such as poor internet connection and limited physical connectivity. This largely affects the service proposition but may also impact profitability. Given the centrality of this issue the project will look to compare the Falkland Islands against other jurisdictions which have similar levels of remoteness as measured by their distance from their metropolis.

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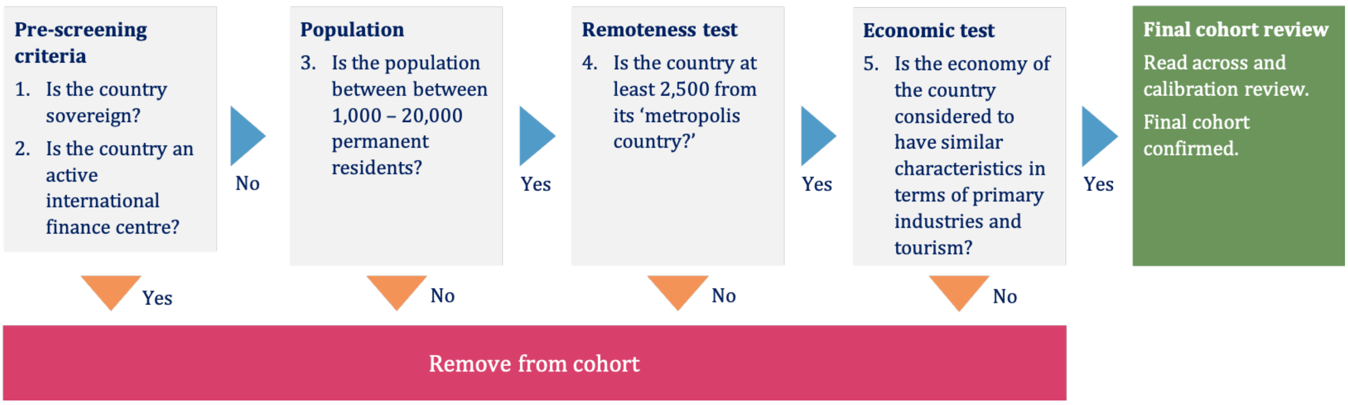
[48] Harvey W Armstrong et al, "The non-sovereign territories: Economic and environmental challenges of sectoral and geographic over-specialisation in tourism and financial services," *European Urban and Regional Studies* (2021): 3-5.

- **Economic Composition**: The Falkland Islands is a small but comparatively wealthy jurisdiction that was resilient during the pandemic. Its economy is primarily driven by the primary industries of fishing and agriculture, yet oil exploration and tourism have also supported it and show viable prospects for development.[49] A broadly similar economic composition is a necessary component for the cohort in order to compare the needs of each local jurisdiction and each strategy they found to cater to these needs. It is acknowledged that this is a relatively unique economic composition, thus some jurisdictions may only be compared in those areas where similarities exist.

Filtering criteria and process

The following criteria have been used in selecting the cohort of peer jurisdictions:

- **Sovereignty Status:** Only those jurisdictions/territories which are not considered to be sovereign territories in their own right have been selected. It should be noted the legal status and constitutional position of each jurisdiction with its 'metropolis country' within the cohort differs.
- **International Finance Centres:** Countries with active international finance centres have been excluded for the purposes of this exercise. Domestic residents and businesses are likely to be over-served in international finance centres as banks are not operating there on the strength or size of the domestic market.
- **Population and Population Density:** With the Falkland Islands population of ~3,600, this metric should only be stretched to consider jurisdictions with a population less than 20,000 to ensure comparable scale.
- **Remoteness**: Jurisdictions have been selected based on their remoteness from their 'metropolis country' e.g. the United Kingdom. With the Falkland Islands being significantly distanced, anything closer than 2,500km ought to be considered too close for comparison.
- **Economic Composition** – Peer group countries have been selected with a view to ensuring they have similar economic characteristics i.e., a dependency on primary industries such as fisheries, agriculture and with tourism representing an increasingly important component of economic output.



The following academic comparative research has been used to inform the starting point of the cohort selection: Ferdinand, Oostindie and Veenedaal,[50] and, Armstrong and Read.

Limitations

Factors of GDP per capita and the Human Development Index have not been included in terms of screening as to do so would likely constrain the ability to develop a meaningful peer group for this exercise. They are, however, important markers and have been included within the overview and consideration of each case.

The overall approach is more qualitative than quantitative. Availability of robust and granular quantitative data is challenging for small island countries. A comparative and qualitative approach was therefore

[49] Standard and Poors, "Falkland Islands assigned 'A+/A-1' long- and short-term sovereign Credit Ratings," *S&P Global Ratings* (2021).
[50] Malcolm Ferdinand et al, "A global comparison of non-sovereign island territories: The search for 'true equality,'" *Island Studies Journal* (2020): 15(1), 43-66.

considered to be the most sound approach to develop a cohort of peer countries. It is also acknowledged that each island jurisdiction is unique in its own right with a wide range of factors (heritage, culture and history) that have shaped their economic development.

Lastly, quantitative comparisons across jurisdictions run the risk of a lack of available or accessible information. Only official documents have been digitally translated and follow up phone calls / emails have been used where possible to endeavour to get an 'on the ground view' as opposed to what a purely desktop exercise may reveal.

Final cohort selection

After carefully considering a range of countries using the above selection criteria, the final cohort of peers was determined as: **Niue, Cook Islands, St Pierre and Miquelon, Easter Island, and St Helena**. A brief overview of each country is detailed below:

- **Niue:** A self-governing territory part of the Commonwealth which is in a free association with New Zealand. Major industries are tourism and fisheries with significant foreign aid from New Zealand also featuring. Tourism sector has been heavily impacted by the Coronavirus pandemic. The New Zealand Dollar is its currency.
- **Cook Islands:** A self-governing territory and part of the Commonwealth, which is in a free association with New Zealand. Heavily dependent on foreign aid from New Zealand. Agriculture and tourism are dominant economic contributors. Running down its nascent offshore finance industry after political pressure from New Zealand. Uses the New Zealand Dollar as is its currency.
- **St Pierre & Miquelon:** A devolved parliamentary dependency of France (Overseas Collectivity) which is represented in the French legislatures. The Euro is the official currency but Canadian Dollars are also widely accepted. Fishing and agriculture were historically a very dominant component of the economy however this has significantly reduced and they now stand at ~15% of total economic output.
- **Easter Island:** A Chilean Special Territory which has its own set of additional legislation due to its unique demographic and history. Its formal economy is relatively new and largely dependent on tourism. The Chilean Peso is the currency in use.
- **St Helena & Ascension:** A British Overseas Territory who receive substantial funding from the UK's development budget. St Helena's economy is geared to growing coffee, fishing, tourism and the exporting of alcohol. The airbase on Ascension is the focal point of the economy there. The local currency is pegged to the British Pound.

These countries fit within the core criteria outlined above but there are also differences. It is deemed valuable to have a range in GDP per capita, population, and population density. The most notable difference is that of the Cook Islands, with a population comparatively much higher than the Falklands. Nevertheless, it still fits within each metric, and conversely has a much lower GDP.

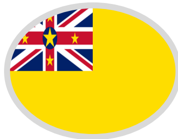
Comparatively, the Falkland Islands has a much higher, even unusually high, GDP per capita for such a small and remote jurisdiction – with global rankings placing it between the 9th and 13th most prosperous. It was therefore unlikely to find other jurisdictions that were comparable in this regard, albeit one could assume that banking provisions with such a high GDP p/c would be comparatively better – this may benefit the comparative study also.

A one page overview of each peer group country with key information is attached overleaf.

Peer group at a glance

	Population	Area (km^2)	Density	Distance to Metropolis	GDP per capita (US$)	Human Dev Index	Credit Rating	GDP per capita rank
Falkland Islands 	3,662	12,173	0.3	12,660	65,350	0.874	A+	9
Niue 	1,719	260	6.6	2,862	16,551	0.794	Not rated	120
Cook Islands 	17,459	236.7	73	3,266	18,767	0.829	B+	112
St Pierre & Miquelon 	5,725	242	23.7	4,288	39,030	0.788	NR	66
Easter Island 	7,750	163.6	47.4	3,750	~5,000	NR	A+	169
St Helena & Ascension Island 	5,420	394	13.76	7,517	10,700	0.756	BBB-	141

Case study one: Niue



Country overview

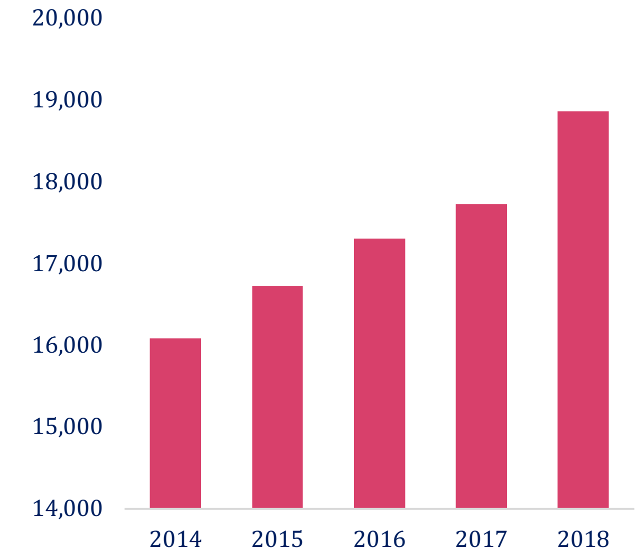
Niue is a self-governing small island Pacific state of ~1,750 people which is in a free association with New Zealand, a member of the Commonwealth, and with King Charles III as the head of state. It has a legislative assembly of 20 members albeit New Zealand is responsible for its foreign affairs and defence matters as well as economic and administrative assistance (when requested).[51] Wellington, the central 'metropolis', is 2,862km away.

Economic overview

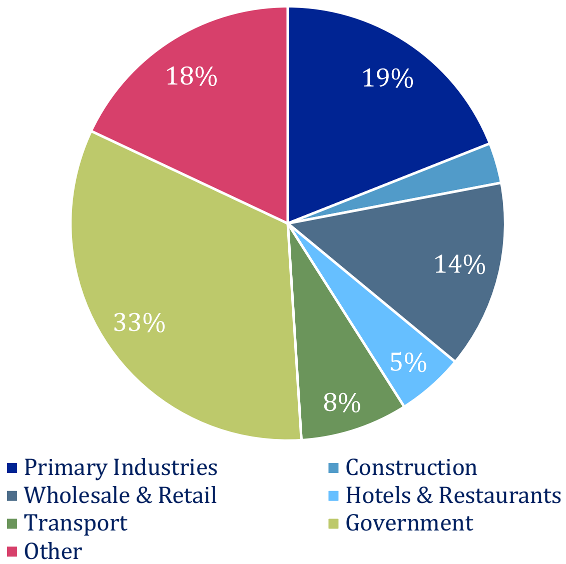
The population of Niue had an 18% decline through the decade from 1997 to 2007 but has since stabilised. This decline can be explained by economic migration, indeed there is now over 30,000 ethnic Niueans residing in New Zealand.[52] Niuean's are also New Zealand citizens, and they share the same currency – the New Zealand Dollar ("**NZD**").

The population decline has been a challenge to Niue's macroeconomic performance notwithstanding the recent challenges presented by the Covid-19 pandemic. Tourism represents the main driver of its economy with ~12,000 visitors in 2019 (six visitors per resident).

GDP per capita (US$ - 2023 prices)



Economic Composition



Source: Statistics Niue[53]

Primary industries also make up a sizeable portion of its economic composition (19%), but it can suffer from significant fluctuations year to year. Foreign aid particularly from New Zealand and the Asian Development Bank help to supplement government revenues.

Communications infrastructure on the island has recently been improved through the arrival of an interconnector communications line from New Zealand. Previously, Niue was dependent on satellite internet services.

[51] New Zealand Legislation, "Niue Constitution Act 1974," https://www.legislation.govt.nz/act/public/1974/0042/latest/DLM412793.html.
[52] Ministry of Foreign Affairs and Trade New Zealand, "About Niue," 2022, https://www.mfat.govt.nz/en/countries-and-regions/australia-and-pacific/niue/new-zealand-high-commission-to-niue/about-niue/.
[53] Statistics Niue, "Home," December 2022, https://niuestatistics.nu.

Overview of the banking sector

Westpac, the Australian bank, previously operated in the Island however they sold their operations to the Bank of the South Pacific in 2004, who in turn exited the island in 2013. Commercial banks would seem to find it difficult to operate profitably in this small, relatively impoverished market. It should also be noted that there are no insurance companies on the island due to the high risk of cyclones and small population making it commercially unviable.

Niue Commercial Entities Limited (NCE)

Two entities are in operation under this State-Owned Enterprise ("**SOE**"), a Kiwibank agency and Niue Development Bank:

Kiwibank Agency

The Niuean government, through NCE, partnered with Kiwibank to provide an agency offering of selected Kiwibank products to individuals and businesses. The products include transaction bank accounts, call accounts and internet/mobile banking access with EFTPOS card access and full payment functionality. New Zealand legislation and regulation applies, thus all services relating to AML and KYC comply with New Zealand law. There are no ATMs provided but rather cash can be drawn out from the local Kiwibank teller, or via cashback at retailers. There is a general confidence in the Kiwibank service stemming from it being an SOE of New Zealand and linked to the governments strong commitment to the territory.[54]s

Niue Development Bank (NDB)

Kiwibank does not provide any credit products – these are provided by the Niue Development Bank, which has a total asset book of ~NZ$12 million (approximately one-third of Niue's total GDP). They are the only official lender on the island. There is a significant client base made up of both individuals and businesses. Commercial and lending products range from micro-loans, car loans and mortgages to working capital and loan facilities. Work is underway to ensure NDB is able to offer online services where customers will be able to access and administer their lending products remotely. In 2020 their loan advances totalled almost 4.25 million NZD.[55]

Australia and New Zealand Banking Group Ltd. (ANZ)

Merchant services are provided by ANZ bank and there are ~65 businesses on the island accepting EFTPOS / Credit Cards. Visa and Mastercard are thus options which enables ease-of-travel for tourists. In 2022 ANZ announced its commitment and renewed investment towards the Pacific region stating they are "committed to the economic, social and environmental development of the Pacific" even when the past years have not seen any profit.[56] This may have a flow on effect for Niue as well.

Internet infrastructure

Sufficient internet connectivity has been available on the island since 2000, with Telecom Niue providing mobile, fixed-line and internet telecommunication services. Since 2020, Niue has been connected to the Manatua fibre cable (an extension of the cable which runs from Hawaii) which has resulted in significant improvements in services. There is a high level of use of internet service, but with the major challenges being

[54] Ministry of Foreign Affairs New Zealand, "New Zealand – Niue statement of partnership," December 2022, https://www.mfat.govt.nz/assets/Countries-and-Regions/Pacific/Niue/Aotearoa-New-Zealand-Niue-Statement-of-Partnership-2022-2025.pdf.
[55] Government of Niue Department of Finance and Planning, "Financial snapshot: 1 July 2020 – 31 January 2021," 2021, https://www.gov.nu/wb/media/2021/GON%20Snapshot%20Report%20of%20the%20Niue%20National%20Economy-%2031Jan21.pdf.
[56] ANZ, "ANZ to strengthen focus on core Pacific markets," 2022, https://news.anz.com/new-zealand/posts/2022/03/ANZ-strengthen-focus-Pacific-markets.

affordability for the public, reliable power, and return on investment due to the small population. Despite such challenges, Kiwibank offers a full internet banking service, even before the cable was completed.

Overview of available banking services

Personal Banking

	Kiwi bank.		
Money Transmission Accounts			
Savings Accounts			
Online/Digital/Mobile Banking			
Share dealing & Investments			
Lending			
Mortgages			
Credit & Charge Cards			
Insurance			
Foreign Exchange Services			
Asset Finance			

Commercial Banking

	Kiwi bank.		
Money Transmission Accounts			
Savings Accounts			
Online/Digital/Mobile Banking			
Markets			
Lending			
Commercial Mortgages			
Real Estate Finance			

Asset Finance			
Credit & Charge Cards			
Trade Finance			
Business Insurance			
Card Merchant Acquiring			
Support Services			
Relationship Manager Service			

Climate change resilience

Niue is particularly concerned about the impact of climate change upon its residents, owing to its geographic vulnerability, and has therefore prioritised the promotion of sustainable infrastructure projects as well a number of conservation projects. In their National Strategic Plan 2016-2026, the government deems climate resilience as the primary consideration and hence only prioritises investments in its economy that are economically sustainable and climate friendly.[57]

Of primary importance is improving the Islands resilience to sea level rises, and extreme weather patterns by building flood containment and weather resilient infrastructure. Australia, New Zealand, the UK and a number of development banks have committed resources towards projects to help build Niue's economy to be sustainable and climate resilient. Banks in Niue are not lending, so green financing is thus only adopted through development aid and government.

Summary

In the context of an economy that has a low relative income, a hostile and uninsurable environment, an uncompetitive market, and a dependence on foreign aid, the banking service portfolio seems to have found a sufficient resolution for residents. The relevant findings highlight access to required banking services albeit via Kiwibank in New Zealand. The arrangement that Niue Commercial Enterprises has with Kiwibank seems to enable all necessary banking products for clients, as well as meeting the needs of the diaspora in New Zealand, and Australia. This arrangement also resolves issues around regulation and legislation within the jurisdiction as it is able to rely on New Zealand's banking regulation which has the confidence of markets. This banking arrangement is an overt example of the relationship between New Zealand and Niue; although New Zealand doesn't deem itself as 'owning' the Island by any means, it does consider itself as having an important role in the upkeep in services and socio-economic wellbeing.

Two significant features are highlighted in this case. Firstly, there is comprehensive internet/digital banking which is maintained despite there being comparatively less need in Niue for electronic banking due to both smaller travel distance and population size. The second aspect is that there is a superior communications infrastructure to that of the Falkland Islands. It should be noted that this infrastructure was not an investment made only by Niue itself, but with the support of foreign aid programmes.

[57] Government of Niue Department of Environment, "Niue national strategic plan 2016-2026, https://niue-data.sprep.org/dataset/niue-national-strategic-plan-2016-2026-0.

Case study two: Cook Islands

Country overview

The Cook Islands is constituted as a self-governing Pacific state which is in a free association with New Zealand, a member of the Commonwealth with King Charles III the head of state. The Cook Islands administers its own affairs with an expectation of good governance, yet New Zealand holds responsibility for foreign affairs, defence and security.[58] Wellington, the central metropolis, is 3,266km away. The New Zealand government, with the consent of Cook Islanders, assists with the state's administration, providing vital expertise and was highly influential in ensuring it stepped away from becoming an international financial centre because of concerns about its international reputation.

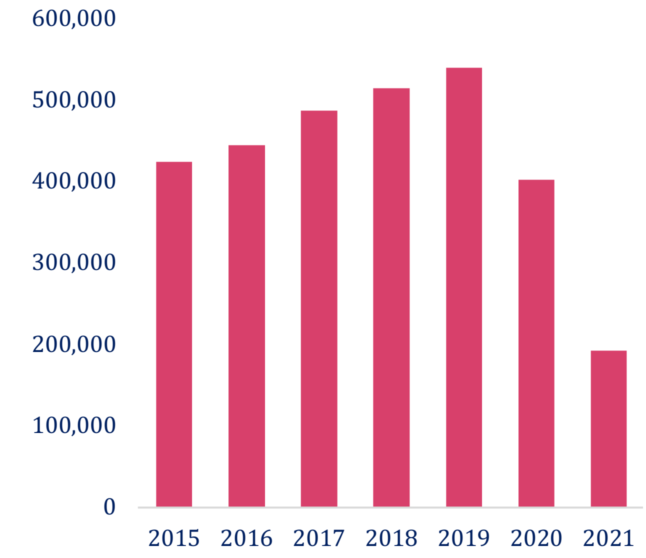
The population of the Cook Islands is larger relative to other jurisdictions in the cohort but still sits within the limits the framework prescribes. The population is roughly 17,500, with a diaspora of ~80,000 living and working in New Zealand. Cook Islanders are New Zealand citizens with full rights to live and work there. The currency used is the New Zealand Dollar. The Cook Islands consists of 15 small islands spread over 1.8 million km^2.

Economic overview

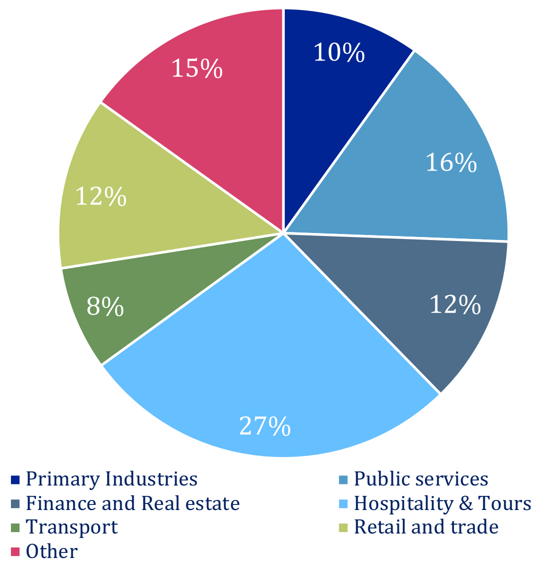
Tourism has been the main cause of economic growth over the past 2 decades of which 2018 saw the islands receive almost ten times the population in tourists. This culminated in a record total of 65% of the annual nominal GDP. The strong tourism sector has increased from ~40% to ~60% of GDP since 2012 but was profoundly affected by the Covid-19 pandemic in 2020.[59] This triggered significant demands from the residents to build up other areas of the economy to reduce its reliance on a single industry.

It is important to note that although real GDP has increased and decreased significantly over the past decade, per capita GDP has stayed relatively constant meaning that other factors need to be considered such as population changes, government intervention or foreign aid transfers. The Asian Development Bank and the New Zealand Government both supported through match funding.

GDP (NZ$ - 2016 prices)



Economic Composition



Source: Cook Islands Statistics[60]

[58] Ministry of Foreign Affairs New Zealand, "Joint centenary declaration of the principles of the relationship between the Cook Islands and New Zealand," 2001. Accessed at https://www.mfat.govt.nz/assets/Countries-and-Regions/Pacific/Cook-Islands/Cook-Islands-2001-Joint-Centenary-Declaration-signed.pdf.

[59] Ministry of Finance & Economic Management Cook Islands, "Economic development strategy," December 2022, https://www.mfem.gov.ck/economic-planning/economic-development-strategy.

[60] Ministry of Finance & Economic Management Cook Islands, "Statistics," https://www.mfem.gov.ck/statistics.

Main industries other than tourism are the public services and some primary industry materials exported mostly to New Zealand. It should be noted that there is an international financial centre operating out of the Cook Islands with Trust Business, insurance (including captives), and banking services but deemed small in comparison to other industries. This is largely a legacy of previous policy decisions when the Islands were attempting to become an international financial centre.

As with Niue, New Zealand remains committed to the territory. Especially with indigenous roots stemming from the Cook Islands, the mutual obligations and cultural identification remains strong between the two states.

Overview of the banking sector

The Cook Islands is serviced by 4 banks as expanded on below. Each bank operates under the Financial Supervisory Commission (FSC) which provides and administers a complete regulatory framework according to parliamentary legislation. The banking sector has NZ$1.11 billion of lending assets, of which ~30% is in real estate. Insurance is provided via one bank and a small number of insurance companies. The aggregate loan-to-deposit ratio is currently ~50%.[61]

Bank of the South Pacific

BSP began operations in the Cook Islands after it acquired Westpac's branches in 2015. Full services are offered (personal and commercial) including multiple transaction and savings accounts, investment options, personal and home loan availability, with access services through ATMs, full online services, Visa Debit cards, and EFTPOS. BSP was founded in Papua New Guinea and has recently become one of the most dominant banks in the South Pacific, offering its full services across borders throughout the region. The banks total Customer loan-to-deposit ratio was 56.95% in 2021.[62]

ANZ Banking group

ANZ's presence in the Cook Islands dates to 1988, and since then has become a well-established branch integrated into ANZ's Pacific division. Personal banking includes transaction accounts, saving and lending. Business banking, in addition to the former, includes international trade finance, asset finance and leasing, structural finance, and acquisitions. Customers access banking services through branches, online banking, ATMs, EFTPOS and credit cards. ANZ has recently announced intentions to expand its role in the Pacific region, seeing it as core to its customer proposition.

Bank of the Cook Islands

BCI is the only locally owned bank on the islands. It was founded in 2001 after the local savings bank and development bank merged. It boasts the largest branch network in the Islands supporting even the outer islands. The business operates as a State Owned Enterprise at arms distance from the government. As with both ANZ and BSP, BCI offers a wide range of products and services to both the personal and commercial sectors. Beyond this, they also offer what they term "community accounts" towards charities, clubs and organisations in the community for ease of access. They also offer currency exchange and are an intermediary for insurances.

[61] IMF, "Cook Islands: technical assistance report." August 2020, https://www.elibrary.imf.org/view/journals/002/2020/269/article-A001-en.xml.
[62] Bank of the South Pacific, "Annual Reports," https://www.bsp.com.pg/investor-relations/investor-resources/annual-reports/.

Capital Security Bank

CSB has been in operation for 25 years as a private bank in the Cook Islands. Its operations are largely a legacy of the Islands' move towards becoming a financial centre. It now operates with licensing and administering from the FSC for regulatory purposes. It caters to both domestic and international customers. It largely offers investment services, and does not do traditional banking.

Internet infrastructure

Residents of the Cook Islands benefit from internet banking and mobile apps from all four banks. All telecommunications on the islands are provided by Vodafone with 4G access on the two main islands, 3G on the smaller ones, and over 300 WIFI hotspots spread across the Islands. Access to such effective internet is due to the establishment of the Manatua fibre cable (2020). Spreading throughout the pacific region, the Cook Island's financial involvement stems from New Zealand aid programmes and a development loan from the Asian Development Bank. Vodafone has the sole multi-year use of the cable to provide the Islands with fibre internet.

Despite only the recent development in cable, each bank already had a fully operational internet service in the Cook Islands. This was dependent on satellite services which sometimes came from provisions based out of Hawaii.

Overview of available banking services

Personal Banking

	BSP		BCI	CAPITAL SECURITY BANK LIMITED
Money Transmission Accounts				
Savings Accounts				
Online/Digital/Mobile Banking				
Share dealing & Investments				
Lending				
Mortgages				
Credit & Charge Cards				
Insurance				
Foreign Exchange Services				
Asset Finance				

Commercial Banking

	BSP		BCI	CSB CAPITAL SECURITY BANK LIMITED
Money Transmission Accounts				
Savings Accounts				
Online/Digital/Mobile Banking				
Markets				
Lending				
Commercial Mortgages				
Real Estate Finance				
Asset Finance				
Credit & Charge Cards				
Trade Finance				
Business Insurance				
Card Merchant Acquiring				
Support Services				
Relationship Manager Service				

Climate change resilience

The government of the Cook Islands is susceptible to the effects of climate change and has therefore adopted policy that will support their resilience against rising sea levels and extreme weather events. To this end, the government has established a specific climate change fund that has the intention of prioritising investment in 11 different sectors including; energy generation, coastal protection and restoration, water security, disaster and risk management, waste management, infrastructure, agriculture and ecosystems.[63] The Cook Islands have a positive reputation with a number of banks, including the Asian Development Bank, which has contributed to the favourable lending criteria allocated to green investment projects on the Islands. BCI, as the Delivery Partner for the Green Climate Fund, have access to further funding to support green investment ventures from both private and public entities.

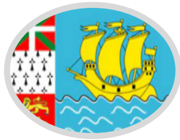
[63] Green Climate Fund, "Country programme: Cook Islands," 2019, https://policy.asiapacificenergy.org/sites/default/files/Cook%20Islands%20Climate%20Change%20Country%20Programme%202018-2030.pdf.

Summary

The Cook Islands has a larger population than the Falkland Islands, yet as an economy it is not as productive (diverse but more reliant on tourism). It is neither as wealthy as shown by the lower per capita GDP. As a whole, the Cook Islands remains dependent on development aid from New Zealand and the Asian Development Bank. The legacy of being an International Financial Centre cannot be ignored, but may also be part of the reason for the first key observation of this case; that it (i) has an independent regulatory system in place through the Financial Supervisory Commission. This in part likely stems from its plan to become an international finance centre, nevertheless it is reputable with required accountability and upkeep coming from New Zealand. The second observation and possibly a flow-on effect from the first point, is that (ii) the Cook Islands is not only well serviced by several banks, but these banks are competitive with one another. With three banks in full operation, and another in private banking, the Island has the range of services one would expect to see in a developed nation-state. It does however have comparatively higher lending interest rates (sometimes up to double) than that found in New Zealand. This is the main limitation to the availability of financing options within the Cook Islands and generates a significant level of dissatisfaction from local residents – something that recently New Zealand has also expressed discontent with.[64]

[64] Newsroom, "NZ extends hand to Pacific as foreign banks pull anchor," July 1, 2021, https://www.newsroom.co.nz/nz-extends-hand-to-pacific-as-banks-exit.

Case study three: St Pierre and Miquelon



Country overview

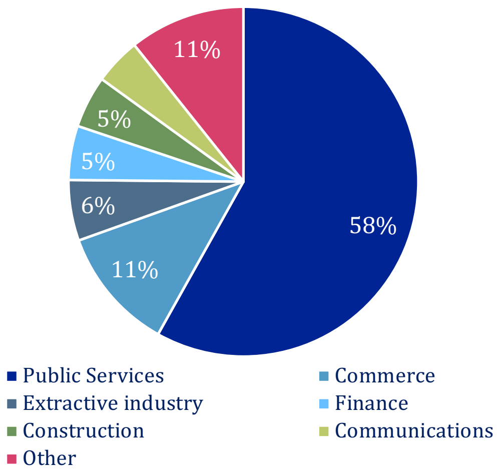
St Pierre and Miquelon is a self-governing state that consists of two main islands with an area totalling 242km². It is a parliamentary dependency of France, and has been officially titled a "Territorial Collectivity" since 1985. Located off the coast of the Burin Peninsula in Canada, Paris the central metropolis, is 4,288km away. All French Territorial Collectivities are represented in the French parliament. Reflecting this, the relationship of the territory and France is well integrated in governance, administration, defence, foreign affairs, law enforcement and even legislation. It does however have a degree of autonomy in its implementation of taxes, customs and council responsibilities (i.e. budgeting and project implementation). It is not part of the EU unlike some of the other French island territories

The census in 2016 recorded a population of 6,008 residents with a dominant ethnic composition representing immigration from the Francophone world. This, along with its proximity to a second nation (Canada), is similar to the Falkland Islands (Argentina). Official currency is the Euro, but Canadian Dollars (CAD) are also widely accepted.

Economic overview

St Pierre and Miquelon's economy has traditionally centred around the fishing industry however since quotas and economic zone reductions were enacted in 1992 this industry has been through major adjustments and is currently in a restructuring process the aim of which to diversify the market. Over 80% of its fishing exports are to Canada yet with the economy largely dependent on imports, it is running significant trade deficits each year. The dominant sector is found in tertiary industries such as education, health and other public services. Tourism is deemed as having significant potential for growth on the islands with large investments from both the public and private sectors. Per capita GDP is currently ~ 40,000 Euros.[66]

Economic Composition



Source: IEDOM[65]

Overview of the banking sector

Delegated Central Bank for the French Overseas Departments and Territories (IEDOM)

IEDOM acts as the central bank for the French Collectivities "on behalf of and under the authority of the Banque de France."[67] Their operations and services are the same in all jurisdictions: Issuance and maintenance of fiduciary money, and production of information for financial stability and regulation. IEDOM carries out some functions which would not ordinarily be associated with its role as a central bank. These include: listing of companies, small business support and technical analysis, public sector national strategy reports, mediation, over-indebtedness prevention (private and corporate), research, expertise and advice etc. IEDOM enables each jurisdiction to set up its own agency of IEDOM, thus providing even small overseas jurisdictions with access to regulatory oversight, registration procedures and the rights to all banking provisions as mainland France would. Throughout the Covid-19 pandemic, IEDOM was able to oversee support

[65] IEDOM, "Évaluation de PIB de Saint Pierre et Miquelon en 2015," 2015, https://www.iedom.fr/IMG/pdf/evaluation_du_pib_spm_22032018.pdf.
[66] Public Expenditure and Financial Accountability program, "Collectivité Territoriale de Saint Pierre et Miquelon: Evaluation de la performance du systeme de gestion des finances publiques," 2022, https://www.pefa.org/sites/pefa/files/2022-04/PM-Apr22-PFMPR-Public%20with%20PEFA%20Check.pdf.
[67] IEDOM, "Institut d'émission des départments d'outre-mer," 2015, https://www.iedom.fr/IMG/pdf/plaquette_iedom_2015_version_anglaise.pdf.

for the economy in St Pierre and Miquelon, such that their economy had a similar intervention to France.

Caisse d'Epargne

The French cooperative Caisse d'Epargne bank has two divisions in operation in the territory: Provence Alpes Corse (CEPAC), and Ile de France (CEIDF). The former has a focus and commitment towards the French territories and offers its full service in all regions, the latter is one of the regions' bank and thus also identifies with them. In effect, it is two separate banks that operates the majority of services on the Islands, including a large percentage of the Islands' annual lending. Both are fully authorised to offer full operations. The cooperative ownership structure of the bank may be the reason for such identification with the overseas territories.

In 2016, CEPAC merged with Bank of St Pierre and Miquelon which enabled it to have a branch on each island, even though Miquelon represents only 10% of the population. CEPAC expanded their role by opening 4 ATMs on the island in 2018, all with international bank card availabilities.

Banque Postale (LBP)

LBP is the only commercial bank on the island, operating out of the post offices located on both St Pierre Island and Miquelon Island. It is however, a limited service with less than 1% of residents being clients. Founded in 2006, the bank aims to serve all French citizens in which St Pierre and Miquelon is considered an integral part. All general management services of current accounts are offered on the islands, presuming the exclusion of lending services.

Real Estate Cooperative of the St Pierre and Miquelon Islands (CISPM)

CISPM is a cooperative lending company that supports individual investments. It was set up in 1950 with the intention of enabling access to ownership for residents of the Islands. It acts as an intermediary by borrowing from the AFD in order to offer scaled loans out to individuals who may not be able to obtain from banks directly. It currently offers around 30 loans per year at competitive rates with over 1,600 households having obtained ownership. As of 2019, there are 703 members in the cooperative – just over 10% of the population. CISPM also participates in the deposit guarantee scheme of France.[68]

French Development Agency (AFD)

AFD is a French finance company that seeks to fund sustainable development projects around the world – primarily within French jurisdictions. Where CISPM funds individuals, AFD primarily lends to companies and other entities. 2017 saw an agency of AFD established in St Pierre and Miquelon. Since then, €19 million have financed projects ranging from aviation, to medical services, tourism and housing. Their services in the territory focus on financing of loans for social development projects with an aim to go beyond what a commercial bank may be able to offer.[69]

Internet infrastructure

Both islands in the territory have access to a communications cable via the St Pierre and Miquelon cable line which connects to the nearby Canadian links in Fortune and Lamaline. This has been in place since 2018 and is fully owned by the local government. SPM Telecom provides internet access well above the minimum required bandwidth threshold, leaving the islands well serviced with internet infrastructure.

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[68] The Banks EU, "Coopérative immobilière des îles Saint-Pierre-et-Miquelon: Deposit Guarantee," https://thebanks.eu/banks/13746/deposit_guarantee.
[69] AFD, "Saint Pierre and Miquelon," https://www.afd.fr/en/page-region-pays/saint-pierre-and-miquelon.

Overview of Available services

Personal Banking	CAISSE D'EPARGNE	CAISSE D'EPARGNE	LA BANQUE POSTALE	CISPM	AFD AGENCE FRANÇAISE DE DÉVELOPPEMENT
Money Transmission Accounts					
Savings Accounts					
Online/Digital/Mobile Banking					
Share dealing & Investments					
Lending					
Mortgages					
Credit & Charge Cards					
Insurance					
Foreign Exchange Services					
Asset Finance					

Commercial Banking	CAISSE D'EPARGNE	CAISSE D'EPARGNE	LA BANQUE POSTALE	CISPM	AFD AGENCE FRANÇAISE DE DÉVELOPPEMENT
Money Transmission Accounts					
Savings Accounts					
Online/Digital/Mobile Banking					
Markets					
Lending					
Commercial Mortgages					
Real Estate Finance					
Asset Finance					
Credit & Charge Cards					
Trade Finance					

Business Insurance					
Card Merchant Acquiring					
Support Services					
Relationship Manager Service					

Climate change resilience

Green investments in the Collectivity once again highlight the level of integration that it has with 'the metropolis.' Since 2016, the French Environment and Energy Management Agency (ADEME) has been present in St Pierre and Miquelon with the aim of supporting companies and communities in taking steps towards a green transition. It is prioritising projects on waste management and energy consumption.[70] Beyond this agency, AFD also invests in projects that are climate friendly and promote the protection of the biodiversity in the region.

Summary

St Pierre and Miquelon has a per capita GDP similar to that found in other continental European states, marking it as the wealthiest of the peer cohort (excl. Falkland Islands), this is driven mostly by the public service at the time being as it faces transitions in the economy. This drastic shift in the economy due to challenges in the fishing industry has not caused poverty on the island presumably due to a support base from France; The level of public services within French territories is very high, and in general there is a significantly greater integration into France that the UK would have with its BOTs. It must also be noted that it is far from its metropolis but close to Canada, which must be considered when analysing its relative remoteness as it has a large French language market (Quebec) relatively close in proximity.

Within this context, and through the research and verification processes, the main observations are that (i) the banks are fully operational and take a greater proportion of the total lending than the development corporations. Indeed, 85.7% of lending on the Islands comes from the banks even when there are two development agencies, one of which, being state-supported, has access to significant funds. The second significant observation is (ii) banking service provisions are on par to that of France. In fact, French territories are enabled to be able to provide a full banking service through the operations of IEDOM which acts like a central bank, regulatory service, and a support for all the territories.

[70] ADEME, "L'ADEME Saint Pierre et Miquelon," https://www.ademe.fr/direction-regionale/saint-pierre-et-miquelon/.

Case study four: Easter Island (Rapa Nui)

Country overview

Easter Island is often regarded as being the most isolated inhabited island in the world. This in itself is an explicit factor when considering any particular challenges the Island may face to its banking and telecommunications – its closest continental point is 3,510km away. The Island comes under the governance of Chile where in 2007 it was titled with the status of "Territorio Especial." It is in this sense non-sovereign and administered as a region of Chile, albeit distinct from the continental state. The land cannot be alienated from its indigenous people and much of the Island is a designated national park. It also has its own distinct language. The distance to its central metropolis, Santiago, is 3,750km. Easter Island uses the Chilean Peso, yet interestingly is exempt from taxes (resulting in a highly informal economy).

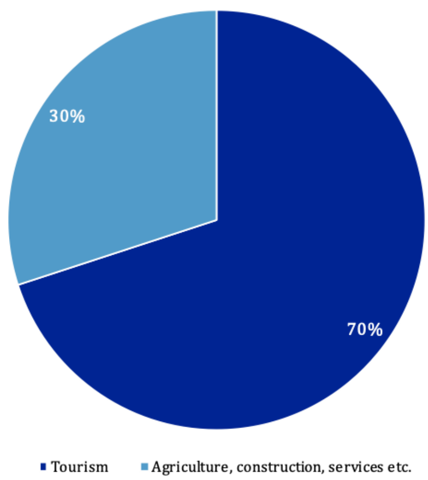
The population sits at ~7,750 (pre-pandemic) with almost 50% being the Rapa Nui indigenous people. This demographic is a noticeable difference to the other jurisdictions within the cohort, here state/indigenous interests both need to be navigated more carefully. Previous energy analyses have highlighted the complexities of needing to adhere to two sets of laws (territorial law, and the indigenous law), resulting in longer processes in decision-making and implementation.[71] In 2014/2015 significant protests occurred over land use and ownership contestations.[72] This has had a flow on effect on the local economy, which has relied on tourism, yet does not have the necessary infrastructure to sustain it.[73] Something which protests exacerbated by stalling local investment.

Economic overview

Easter Island in the past practically had no working economy outside of its own borders. The residents there grew their own food and lived off the sea. Since Chile's direct involvement from the 1960's, the population has increased by almost 400%. The internationally connected economy is due to the attraction of tourism. The 2020 pandemic has thus seen a sharp challenge arise for the economy. The awareness of such a dependence on tourism is present, and an increase in other productive activities is now being fostered. It is estimated that around 70% of the island's economy is composed of the tourism industry.

It is apparent that Easter Island's economy faces stark challenges and has only been able to sustain growth due to tourism. Whether the government will introduce any measures to reduce the Islands reliance on tourism is currently unknown. The most important factor to consider in relation to the level of development in the Easter Island's financial sector is the involvement of the Chilean government.

Economic Composition



Source: *Economia Y Negcios*[74]

[71] SD Strategies, "Energy and transport profile: Easter Island, Chile," 2019, https://sd-strategies.com/wp-content/uploads/2020/06/Profile_Easter_Island.pdf.
[72] Christina Newport et al, "Polynesia in Review: Issues and Events, 1 July 2014 to 30 June 2015." *The Contemporary Pacific (2016): 28(1), 204-244.*
[73] Elena S. Rotarou et al, "Sustainable development or Eco-collapse: Lessons for tourism and development from Easter Island." *Economic and Business Aspects of sustainability* MDPI (2016), https://www.mdpi.com/2071-1050/8/11/1093#B90-sustainability-08-01093.
[74] Economía y Negocios, "Rapa Nui in figures: no taxes, only two banks and 4,000 islanders with declared economic activity," 2018, http://www.economiaynegocios.cl/noticias/noticias.asp?id=503237.

Overview of the banking sector

Easter Island makes an interesting comparative case study owing to its stark economic, geographic and demographic challenges. The nature of the economy both causes risk for the banks but also opportunity with support from the Chilean government. Despite the challenges, two banks service the Island, with a total of ~6,000 clients. The informal economy of the Islands creates significant challenges from a banking perspective as asset ownership as well as business and personal cash flows are less transparent than banks would be used to. Insurance and support services are offered under a different institution, Caja Los Andes.

Banco Estado

Banco Estado is a banking group owned by the Chilean government. It is the only publicly owned bank in Chile, beginning operations in 1953. Chile has a large number of isolated communities, and the bank prides itself in having the ability to reach these communities with key services and products.[75] This includes Easter Island where they have ~5,000 current accounts and the ability to service the complete tourism industry, currency exchange, online banking and 24hr ATMs. They also hold current accounts available in Pesos and USD. Financing, when sought, is also available albeit in an unknown quantity. As an SOE, the Banco Estado has a mandate from its shareholder to promote financial inclusion among the people of Chile, thus not all its operational decisions are made on a purely commercial basis.

Banco Santander

Banco Santander is a publicly traded, multinational Spanish banking group. It has a smaller number of clients on the Island, but also helps to cater to the numerous tourists the Island receives. Its lending tends to be more competitive and unrestricted compared to that which is offered by the state-owned bank. It offers ATMs, customer and executive advice to clients, as well as the full provision of internet banking, investment services, and lending. The bank's financing ventures on the islands largely revolve around construction such as a recent debt financing for a hotel project.

Internet infrastructure

The Island, since 2016 has been connected to satellite broadband. It can only access 3G mobile data, yet most hotels are able to offer WIFI (albeit warning that it can be patchy at times). It is a limited service, and its speed is the subject of widespread discontent.

Overview of available services

Personal Banking

Money Transmission Accounts		
Savings Accounts		
Online/Digital/Mobile Banking		
Share dealing & Investments		
Lending		

[75] Banco Estado, "Integrated annual report 2020," 2021, https://investor.bancoestado.cl/sites/default/files/content/documents/BE%20Or%20Libro%20Memoria%20BE%20Ingles%2026_04_2021.pdf.

Mortgages		
Credit & Charge Cards		
Insurance		
Foreign Exchange Services		
Asset Finance		

Commercial Banking

Money Transmission Accounts		
Savings Accounts		
Online/Digital/Mobile Banking		
Markets		
Lending		
Commercial Mortgages		
Real Estate Finance		
Asset Finance		
Credit & Charge Cards		
Trade Finance		
Business Insurance		
Card Merchant Acquiring		
Support Services		
Relationship Manager Service		

Climate change resilience

Easter Island struggles with its investment in climate projects. There is potential for a high level of renewable energy to be implemented on the Island however due to a number of political and economic complications this has not been taken any further. It is currently 100% dependent on diesel generation. The influx in tourism over the past 20 years has not been met with the adequate infrastructure which would be required to minimise its environmental impact. There are four energy projects in the planning and development stages, which will aim to improve efficiency and reduce reliance on fossil fuels.[76] It is unclear as to whether these have advanced in light of capital allocation changes which have occurred as a result of the Covid-19 pandemic.

Chile has a commitment to reduce its carbon emissions through green investment which Easter Island will likely benefit from. Nevertheless, any development of green infrastructure will still need to navigate the more complex legislative processes on the Island.

Summary

The context of Easter Island, in comparison to the other jurisdictions within the cohort, may be the most challenging from a market perspective. Its remoteness makes the transporting of raw materials for physical infrastructure challenging; it also makes it difficult to attract human capital. As a market, the Island poses significant risks environmentally, politically, and geographically. Beyond this, its high reliance on tourism leaves it largely exposed to global economic cycles. All of this has made economic development a challenge from a public policy perspective.

The key observation in the Easter Island case is that despite the above context, (i) two banks are present on the Island with offerings of a wide range of services. Although communications infrastructure is slow and patchy (arguably far worse than the Falkland Islands), internet banking is still provided to personal customers. This cannot be noted, however, without also considering (ii) the level of integration that the Island has with Santiago as its metropolis. It seems that there is a trade-off between; support, development and provision of services on the one hand; and integration into the 'mother country' on the other.

[76] SD Strategies, "Energy and transport profile: Easter Island, Chile."

Case study five: Saint Helena & Ascension

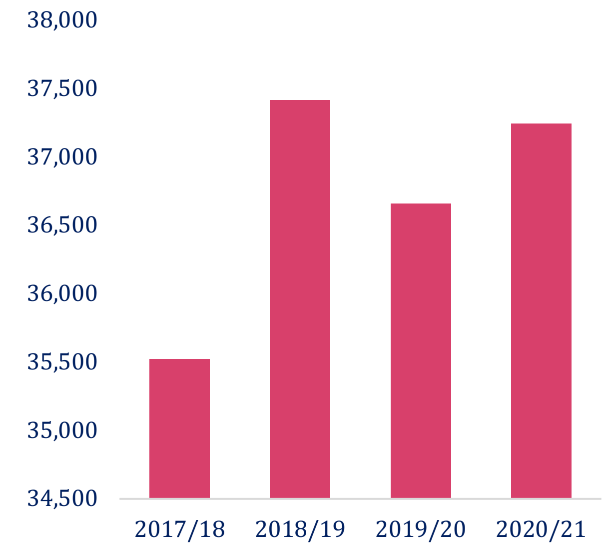
Country overview

Saint Helena, Ascension and Tristan da Cunha is a British Overseas Territory located in the South Atlantic with its closest landmass being continental Africa at ~2,000km away. It is one of the most remote Islands in the world. London, the central metropolis, is ~7,500km away and is responsible for the territory's foreign affairs and defence. A significant expression of the UK's relationship with St Helena is found in the completion of the UK-funded airport in 2016, enabling a few commercial flights per week and greater ease of access for the RAF. It is one of the few BOTs still dependent on the UK's foreign aid.

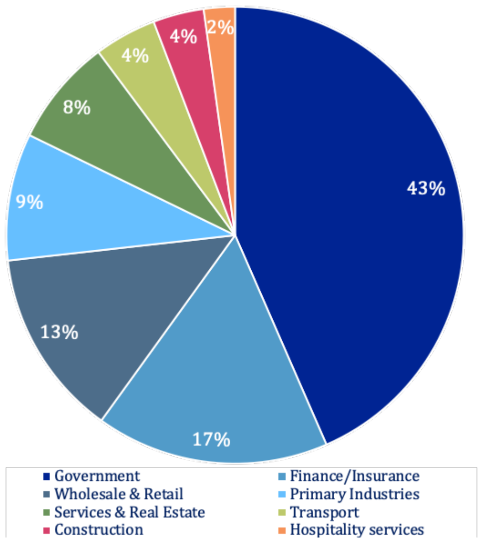
Economic overview

The population of St Helena is ~4,255 with Ascension and Tristan Da Cunha adding another ~1,000. The early 2000's saw a third of the Island's residents move elsewhere for work as the UK confirmed full citizenship status for residents of the Islands. This event was preceded by two decades of economic growth owing to the UK's revamped support for the territories after the Falkland Islands war. This period of growth increased GDP per capita, and reduced instances of poverty throughout the Islands.[77] Despite this early period of growth, the most recent decade has seen GDP per capita become stagnant, if not decline.

GDP (SH£ - 2020/21 basic prices)



Economic Composition



Source: Government of St Helena and Ascension

In further reference to the economy, the Island's largest sector is public administration. As of 2020, 43.5% of GDP was produced by government and public services. This reflects the dependence that it has on aid from the metropolis. The information sector (finance, insurance, communication) is the second largest, generating 16.5% of GDP.[78] The composition shows a strong leaning towards a service-based economy, something that, owing to their location and size, is not deemed sustainable. In this light, St Helena has adopted a 10-year-economic-plan with the overall intention of minimising the risk of decreasing national wealth due to large net imports. The intentions set out to diversify the economy even further in the primary markets and exports by better utilising their comparative advantages, and by overcoming the obstacles such as a lack of skilled workers, logistical issues, small scale and remoteness.[79]

[77] BBC, "St Helena, Ascension, Tristan da Cunha profiles," 2022, https://www.bbc.com/news/world-africa-14123532.
[78] St Helena Government, "Statistical bulletin no. 8," September 2021, https://www.sainthelena.gov.sh/wp-content/uploads/2021/09/Stats-Bulletin-8-2021-GDP.pdf.
[79] St Helena Government, "St Helena's sustainable economic development plan 2018-2028," https://www.sainthelena.gov.sh/wp-content/uploads/2022/03/Sustainable-Economic-Plan.pdf.

Overview of the banking sector

The Islands of St Helena and Ascension each have one branch of St Helena Bank, who provide the majority of banking services on the Islands. Gibraltar International Bank provide some additional financial services which may facilitate better international payment flows. The currency is the St Helena Pound which is pegged 1:1 with Sterling.

Bank of St Helena (BOSH)

BOSH was founded in 2004 when it took over the operations of two banks; St Helena Government Savings Bank, and Ascension Island Savings Bank. It is an SOE of the Island's government, yet the bank has been operationally independent from the government for a while now. Products and services have improved over time with present capabilities being current and savings accounts, personal and commercial lending, online banking, local debit cards, foreign exchange, and cash-back services in retail shops around the island.

There are of course, improvements to be made to these services in comparison to what is offered in continental banks. The advantage of the locally owned bank is that the unique and niche challenges can be addressed through unique and innovative solutions such as "St Helena Pay." This is a service that mediates between the credit card restrictions and international payment challenges they have, where ease-of-access is made for tourists to the island by uploading money to a "tour card" using a QR code. Perhaps because of its position as an SOE, the bank has made great strides in terms of financial inclusion, even winning an award recognising this.

There are, however, unique challenges that the bank faces. Wider infrastructural challenges have an impact on the ability for the bank to operate efficiently. Without cable internet, online access is very expensive and although internet banking is offered, a significant majority of the public seems to prefer (or be limited to) in branch services. It is anticipated that as internet connectivity improves, the banks e-banking platform will become increasingly popular. There have been some reputational challenges due to the status and risk categorising of the island. This has made it difficult to adopt new banking services that are available internationally as the bank is often categorised by other financial institutions as representing a greater risk than its country profile would suggest. The bank strives to meet international standards in order to continue existing correspondent banking relationships, but this still has its challenges. In regards to lending, the cost is comparably higher than what mainstream banks can offer and the bank has not reflected the global trend of decreasing interest rates over the past decade. On this point it is necessary to note St Helena's Government agreed with the UK not to raise government borrowing.

Gibraltar International Bank (GIB)

GIB is domiciled in Gibraltar but offers retail and commercial clearing services in St Helena. It is an added provision of business flow for international banking services. St Helenian customers can obtain an account in Gibraltar and a debit card with access to online banking and purchasing, along with of the ability to conduct money transfers whilst abroad.[80] In a sense, it provides the locals in St Helena with greater ease of access to international banking services which BOSH cannot provide owing to issues relating to its perceived risk profile. Albeit a valuable service, the engagement of local St Helenians has been less than 1% of the population and may be due to costs, convenience and underdeveloped international industry issues.

Internet infrastructure

The present reality for St Helena is that its internet services are via satellite; making it both patchy and expensive. A spur of a large cross-Atlantic cable has been acquired with connection scheduled to take place

[80] St Helena Government, "Gibraltar International Bank supports St Helena," 2020, https://www.sainthelena.gov.sh/2020/news/gibraltar-international-bank-supports-st-helena/.

in early 2024. This will increase communications capabilities significantly. It is expected that this will have a positive impact on the ability to upskill and modernise public and private sector services.

Overview of Available services

Personal Banking

Money Transmission Accounts		
Savings Accounts		
Online/Digital/Mobile Banking		
Share dealing & Investments		
Lending		
Mortgages		
Credit & Charge Cards		
Insurance		
Foreign Exchange Services		
Asset Finance		

Commercial Banking

Money Transmission Accounts		
Savings Accounts		
Online/Digital/Mobile Banking		
Markets		
Lending		
Commercial Mortgages		
Real Estate Finance		
Asset Finance		
Credit & Charge Cards		
Trade Finance		

Business Insurance		
Card Merchant Acquiring		
Support Services		
Relationship Manager Service		

Climate change resilience

St Helena has already made a significant contribution towards adopting its energy strategy of being 100% self-sufficient on renewable energy.[81] The original goal was to have this complete by 2022, however in 2021 only 25% of energy consumption came from renewable sources.[82] It is an ambitious project but it is deemed achievable and may make a large difference on the income for the Island if they are able to implement it. It has however not been able to meet its ambitious goal of completion by 2022. In addition to energy sources, in accordance with the governments “Altogether Greener” vision, a waste management plan has been implemented as well as a fund to protect the environment from invasive plants. Future projects include reducing sea pollution due to sewerage, new incentives to encourage green practises, and a more resilient water resource management plan.[83]

Summary

St Helena and its banking services are a case that should be considered for further in-depth discovery and research due to the many similarities it has with the Falkland Islands, most notably in the political status and relationship each has with Great Britain. In terms of remoteness and sovereignty status, St Helena is the most comparable jurisdiction in the cohort. The unique and key observation is that the banking system in St Helena is quite different from the Falkland Islands, following the path of opening a state-owned bank having been unsuccessful in attracting an international banking group.

The most relevant consequence of this approach is the ability of St Helenians to access electronic banking, despite less resilient internet and a smaller economy. More than this it shows that access to internet banking is possible in a jurisdiction as remote and isolated as the Falkland Islands. Indeed, looking at the profitability of BOSH’s annual reports, it shows that there is a business case for implementing an e-banking platform.

Saint Helena does face many of the same problems as the Falklands in terms of being unable to access card payments using existing bank infrastructure. However, where the Falklands were able to secure coverage using Square and GIB, no such solution has been possible for St Helena.

Without speaking with a similar swathe of businesses it is impossible to dimension its commercial lending appetite. At first glance they had total commercial lending facilities extended of ~£5 million in the 2021/2022 financial year. This is significantly higher than SCB, who have a larger deposit base, and a more active business sector in which to lend. The services offered by the bank in St Helena, in an economy comparatively not as wealthy, equally remote, with poorer internet infrastructure, and with a similar jurisdictional status, are arguably superior to the services available in the Falkland Islands in areas of electronic banking systems and commercial lending.

[81] St Helena Government, “St Helena energy strategy,” 2019, https://www.sainthelena.gov.sh/wp-content/uploads/2019/11/161025_St-Helena-Government-Energy-Strategy-FINAL-October-2016.pdf.
[82] St Helena Government Statistics, “Utilities.” 2021, https://www.sainthelena.gov.sh/st-helena/statistics/the-economy/.
[83] St Helena Government, “St Helena 10 year plan 2017-2027,” https://www.sainthelena.gov.sh/wp-content/uploads/2012/08/10-Year-Plan-20-January-2017.pdf.

Section 4: Benchmarking of the Falkland Islands

This section of the report benchmarks the provision of banking products and services in the Falkland Islands against the cohort of peer jurisdictions reviewed in the earlier section. To achieve this, the current offering and functionality in the Falklands has been benchmarked against the findings in the peer countries. Given businesses typically require a broader and more sophisticated range of products compared to individuals the benchmarking has been undertaken separately for each. The results of the benchmarking exercise are summarised in the schematics below. These give a clear view of how the Falkland Islands compares together with some high-level commentary where appropriate as to what is driving the particular rating. The 1-4 rating scale has been devised on the following basis:

- 1 No in-country access to this product
- 2 Access but limited functionality
- 3 Sufficient functionality from a single service provider
- 4 Sufficient functionality from multiple providers

Personal banking products & services benchmarked against cohort peers

Product/Service	1	2	3	4	Comments
Money Transmission Accounts		FK, SH	N	CK, SP, EI	Falklands have a limited range of bank accounts. Niue has a broader range through its Kiwibank agency access. Other territories have a fuller range.
Savings & Deposit Accounts		FK, SH	N	CK, SP, EI	Falklands have a limited range of savings accounts. Possible to refer to SCB - Jersey for a wider range of regulated investment products.
Online, Digital, Mobile Banking	FK	SH	N	CK, SP, EI	Falklands clear outlier with lack of any online, digital or mobile banking. St Helena has ability to view / make payments but limited functionality.
Share dealing & Investments	FK, SH, N			CK, SP, EI	Demand for these products is considered relatively low. Referrals can be made to SCB, Jersey for certain investment products.
Personal lending (overdrafts and personal loans)			FK, SH, N	CK, SP, EI	Single bank provider in Falklands for overdrafts/personal loans. Car finance also available from dealerships and credit accounts from certain retailers.
Mortgages (owner occupied and buy-to-rent)			FK, SH, N	CK, SP, EI	Majority of SCB mortgages underwritten using Joint Mortgage Scheme. Single provider in St Helena and Niue.
Credit & Charge Card Payments	FK, SH, N		EI	CK, SP	No ability to access credit and charge card payments in the Falkland Islands. Some may retain cards linked to UK addresses or legacy arrangements.
Insurance (Home, Car, Travel, Pet, Life)		FK, SH, N, EI, SP	CK		Insurance services are provided through agents of insurers based overseas with the exception of Cook Islands.
Credit & Charge Cards Payments	FK, SH, N		EI	CK, SP	No credit or charge card payment capability in Falklands, St Helena or Niue. A single service provider only in Easter Island.
Automated Teller Machines	SH, N	FK		CK, SP, EI	Falklands have a limited ATM capability provided through Stanley Services. Only dispenses cash and no other banking services e.g. paying-in.
Asset Finance (excluding HP, car finance)	FK, SH, N			CK, SP, EI	No asset finance capability in the Falklands for private aviation or marine assets. Considered to be relatively low demand for this product.

Commercial banking products & services benchmarked against cohort peers

Product/Service	1	2	3	4	Comments
Money Transmission Accounts		FK, SH	N	CK, SP, EI	Falklands have a limited range of bank accounts. Niue has broader range through its Kiwibank agency access. Other territories have a fuller range.
Savings & Deposit Accounts		FK, SH	N	CK, SP, EI	Falklands have a limited range of savings accounts. Possible to refer to SCB - Jersey for a wider range of regulated investment products.
Online, Digital, Mobile Banking	FK	SH	N	CK, SP, EI	Falklands clear outlier with lack of any online, digital or mobile banking. St Helena has ability to view / make payments but limited functionality.
Markets – Debt Capital Markets / Equity Capital Markets	SH, N	FK, SP, EI	CK		Demand for products of this nature very low – ability for SCB to refer to wider SCB network. Similar situation in St Pierre and Easter Island.
Commercial Lending (working capital loans & overdrafts)		FK, SH, N		CK, SP, EI	Single banking provider for working capital loans and overdrafts in Falklands, St Helena and Niue. Multiple providers in other countries.
Commercial Mortgages (owner occupied)		FK, SH, N		CK, SP, EI	Single banking provider for commercial mortgages in Falklands, St Helena and Niue. Multiple providers in other countries.
Real Estate Finance (Investment & Development)	FK, SH, N			CK, SP, EI	No access to real estate finance in the Falklands, St Helena or Niue. In Easter Island highly restricted in terms of zone permitting real estate activity.
Asset Finance (Plant, machinery, business equipment)	FK, SH	N	EI	CK, SP	No asset finance offering in Falklands or St Helena. Niue Development Bank will fund smaller ticket plant and machinery assets for businesses.
Credit & Charge Cards Payments	FK, SH, N		EI	CK, SP	No credit or charge card payment capability in Falklands, St Helena or Niue. There is only a single service provider only in Easter Island.
Trade Finance (Letters of Credit, Bonds & Guarantees)		FK, N, EI	SP	CK	No native capability but referrals to wider SBC network available. Similar situation in Niue and Easter Island. St Pierre access also available via France.
Business Insurance		FK, SH, N, EI, SP	CK		Cook Islands has access to a native insurance company. Other countries have agencies who broker cover through insurers based overseas.
Accepting Card Payments		SH	FK	CK, N, SP, EI	Falklands have capability through Square. St Helena cannot accept tourist cards. Remaining countries have multiple banks providing service.
Business Support Services	FK, SH	SP, N, EI		CK	Falklands and St Helena do not offer ability to integrate support services (invoicing, accounting software) to bank accounts.
Relationship Manager Service	FK, SH, N, EI			CK, SP	Only the Cook Islands and St Pierre offer relationship management support/advice to commercial banking customers.

Section 5: Banking sector outlook

Overview

Global banks have had a remarkably dull decade or so. Revenues were growing albeit lagging GDP growth. New competitors, in the form of well-funded fintechs, and ultra-low interest rates meant their margins were being gently squeezed. Asset prices, fuelled by quantitative easing, kept surging spawning the rise of volatile new asset classes such as cryptocurrencies. These animal spirits were barely checked by the economic shutdown caused by the pandemic.

But, now the landscape has changed inexorably. Suddenly, firms large and small have to consider the geopolitical context and what it means for their energy costs or supply chains following Russia's hostile incursion into Ukraine and rising tension over the fate of Taiwan. Interest rates, hiked in response to surging inflation, meant that banks could start to widen spreads which has cheered long-suffering stockholders who have endured below par returns since the financial crisis. Fintechs, the darlings of finance for the last decade, found the tide of easy money going out exposing business models and, valuations underpinned by hubris and what some might consider outright fraud in crypto-markets. One thing that has not changed is that a great many banks are still valued at a significant discount to their book value.

The geopolitical landscape and economy will remain in a fractious and brittle state for some time to come

The ongoing war between Russia and Ukraine combined with further Western decoupling from China will mean that energy costs will remain volatile and supply chains under pressure for an extended period of time. Stubborn inflation and tightening monetary policy will be felt unevenly across different economies and across the banking industry. Meanwhile the world is facing the reality of a potential new economic order driven by an increasingly multipolar world and the unwinding of globalisation.

In the near-term higher interest rates will benefit banks as interest rate spreads widen which will provide a boost to profitability. Revenues derived from trading activity should benefit from the prolonged volatility although fee income more susceptible to an economic recession could come under pressure. Households and businesses will find the environment tough and the longer these conditions persist the more likely it is that there will be some distress seen in loan portfolios.

Banks are well positioned to weather these headwinds. Unlike during the global financial crisis, capital levels are strong and there is ample liquidity which means banks can continue supporting their customers. Should a prolonged recession emerge or loan portfolios deteriorate more quickly than anticipated banks will inevitably start to focus on their expenses. In this scenario, banks are likely to focus heavily on cost controls with discretionary projects being deferred, rationalising branch footprints and deploying greater use of advanced technologies to drive efficiencies.

Banks, including SCB, may choose to pare back on discretionary spending projects and instead focus on investing in those markets and geographies where the investment spend has the biggest impact in terms of scale. In this scenario there is a risk that the funding to introduce the eagerly anticipated upgrade to introduce digital and mobile banking for customers in the Falklands might be deferred, again.

A discernible trend in 2022 which will continue to feature over the next 18 months is the level of out-reach being undertaken by the UK high street banks to both households and smaller businesses. Nearly all of the major banks are proactively contacting these customers to offer them financial health checks and to explore how they might be able to save money or reschedule their borrowing to avoid loans falling into default. It is expected banks will offer a number of options to customers who are struggling to make their debt repayments including providing capital repayment holidays.

The housing market in the Falklands remains buoyant notwithstanding the cost of living pressures being experienced. Historically, it is understood that there has never been a default on the SCB mortgage portfolio albeit it should be anticipated there will be some borrowers, both individuals and businesses who might benefit from proactive support from SCB and the FIDC along the lines being seen in the UK.

Banks will turn the dial up on product innovation as they are no longer distracted, under-capitalised and remediating sins of the past

Executives at many banks have spent much of the last decade focused on restructuring their balance sheets, exiting unprofitable markets where they lack scale. These clean-ups have been particularly expensive not just in financial terms but it has also sapped banks in terms of having the bandwidth and financial resources to launch new products and harness the true potential of the technological innovation which is underway.

Individuals are demanding more from their banks. A revealing survey completed in 2022 by J.D. Power revealed that "hands on guidance during challenging times" is the thing that retail customers wanted most from their banks and is more important than convenience or efficiency.[84] With many households facing a cost of living squeeze for the foreseeable future there is no better time for banks to provide this support.

Banks will in future organise more around the customer experience and not just narrow product lines. Customers want to use multiple channels when completing a task with the bank – when seeking a mortgage, they might start researching rates on their phone, want to come to a branch to talk with a mortgage advisor during the application process and review the mortgage offer on their laptop. Banks will need to ensure they can complete the various stages of obtaining a mortgage through the full range of channels. Banks will increasingly deploy robotic automation and machine learning to improve the overall customer experience.

There will also be increasing use of embedded finance – where financial services products are offered on third-party technology platforms. At present this takes the form of payments or lending options such as Buy Now Pay Later. But, expect to see additional financial services being woven into retail platforms. For example, supplementing shopping experiences with financial management tools.[85]

Financial innovation also brings novel risks which banks will need to contend with. An increasing number of people are venturing into new asset classes such as cryptocurrencies and digital assets. Banks have been building new capabilities to support digital wallets and regulators will be keen to understand how banks intend to protect consumers from these new risks. The advent of technology will help as AI and machine learning can allow banks to shift away from a point in time risk assessment to a more dynamic situation where these automated tools constantly scan for unusual changes in customer behaviour using live transactions.[86]

In the commercial and corporate banking space banks will increasingly seek to augment the relationship manager proposition with new digital tools noting that a significant amount of time is still devoted to manual processing of activities e.g. arranging and monitoring of loans. The role of the relationship manager will remain important as they serve as brand ambassadors but also being an advocate for their customers. Deploying technology will require a culture shift from many of the relationship managers who will be instinctively wary of their role being marginalised.

Work to bring international payments more into line with domestic payments in terms of efficacy and cost will gather pace. The Financial Stability Board in 2020 recognised that international payments had fallen well behind the innovations being seen in domestic payments with the SWIFT system still lying at the heart of cross-border payments. A roadmap has been delivered which will explore how new technology can be exploited to speed up payments, reduce routing errors and lower the costs. However, this will be a long-term project as it will require extensive work to re-plumb central market infrastructure.[87]

As one regulatory chapter closes, another one opens

Most of the heavy-lifting to ensure banks are more resilient to financial shocks is now largely complete. The sector is well capitalised, better funded and with strong liquidity buffers as demonstrated by how it has come through the pandemic and the advent of a war in Europe. There are further changes – dubbed Basel 3.5 which

[84] J.D. Power, "US retail banks struggle to differentiate, deliver meaningful customer experience as economy sours," press release, 7 April 2022.
[85] Deloitte, "2023 banking and capital markets outlook," November 2022.
[86] Ibid.
[87] Financial Stability Board, "G20 cross-border payments roadmap," November 2022, https://www.fsb.org/work-of-the-fsb/financial-innovation-and-structural-change/cross-border-payments/

will change the way banks calculate capital in certain asset classes but represents nothing like the step change between the second Basel Accord and the third.

There will be a continuing focus on the conduct of business and in particular around how firms interact with consumers (individuals and smaller businesses). In the UK, the Financial Conduct Authority has launched what it terms a 'paradigm shift' in its expectations of firms. They have introduced a new regime which requires firms to "act to deliver good outcomes for retail customers." It will force firms to deliver a higher standard of customer care and protection - all products and services will need to be designed and delivered in a way that puts the customer first. Banks in the UK will need to review their product range, how they communicate with customers and the end-to-end customer journey. This new Consumer Duty will also impact how new products are approved and monitored, as well as the pricing and ongoing servicing and staff training. The FCA has made it clear to industry that they will be taking an 'assertive' approach to the implementation of the new regime with a particular focus on tracking how firms monitor customer outcomes. This new regime will go live in July 2023.[88]

Policymakers in Europe and the UK are also setting out their plans to regulate digital assets, decentralised finance and cryptocurrencies. They are taking very different approaches. The EU is creating a dedicated regulatory regime under the Markets in Crypto-Assets regulation which will set out harmonised discrete rules for digital assets. The UK instead has set out a detailed consultation paper to bring digital assets including cryptocurrencies within the envelope of existing financial services regulation. Some in the industry are nervous about lending credibility and legitimacy to crypto – they would prefer to let 'let it burn' outside of the formal financial system citing its lack of a clear use and the propensity for investors to lose their money. The reality is that with up to 10% of retail bank customer having some form of crypto exposure it has grown to a size where it could start to exhibit systemic risks for the financial system and wider economy.

So long Fintech 1.0, hullo Fintech 2.0!

With lower levels of funding available and valuations falling there is a significant change taking place in the Fintech sector. Banks will play a much bigger role owing to a more positive landscape for them moving forwards.

Higher margins mean banks can shift from just surviving to starting to think more about how they will thrive. Following nearly a decade of ultra-low interest rates the earnings outlook for banks is more constructive – they are in a better position to access capital whereas it was virtually on 'free-vend' for fintechs over the past 10 years.

The health of banks is much improved – they hold sufficient capital and are increasingly capital generative. They can also look forward as they are not having to worry about their back books so much. This means they will be able to play a more influential role in shaping the fintech sector through either building their own offerings, pursuing joint-ventures or taking stakes in promising fintech firms. Higher interest rates have also raised the cost of capital for fintech firms which means a growth strategy underpinned on burning through cash no longer works. Fintech and technology firms are for the first time having to address their bloated cost bases and set out a path to achieving profitability.[89]

Many banks have also overhauled their technology estates which will enable a more rapid rollout of new products and boost innovation. There is a growing ability to take new technology on a 'plug and play' basis' which is giving banks the ability to roll out and scale new products much more quickly. There is also growing competition in the Banking as a Service industry which is also fomenting innovation and bringing down costs.

Banks across Europe are also building their own Neobanks – these operate without a branch network and being lumbered with legacy technology. Goldman Sachs estimates the return on equity for these new digital banking platforms is ~20% vs. ~10% for traditional branch banking. In 2022, Societe Generale's digital bank Boursorama added over 700,000 customers in the first half of the year whilst Credit Suisse owned CSX had grown its customer base to 150,000 by the year end from just 25,000 in the first quarter. Intesa Sanpaolo

[88] PWC, "The FCA's new consumer duty: Raising the bar on consumer outcomes," August 2022, https://www.pwc.co.uk/industries/financial-services/understanding-regulatory-developments/fca-proposes-new-consumer-duty-in-paradigm-shift-for-firms.html
[89] Chris Hallam et al, "European Banks – Adjusting to Fintech 2.0," *Goldman Sachs*, September 2022.

followed in the footsteps of Lloyds and Mox, who both worked with Thought Machine, to launch its own Neobank. Whereas UBS, launched their *key*4 digital banking app which will provide current and savings accounts together with global foreign exchange payments. There is also innovation on the lending front with Credit Agricole investing €450 million in BforBank which aims to become a digital lender with a focus initially on France before rolling out across Europe.[90]

In addition to building out capability, banks are also engaging in partnerships and joint ventures to expand their product ranges. BBVA launched BBVA Spark which is in effect a corporate banking product dedicated to high-growth technology start-up firms. Standard Chartered entered into an agreement with SBI Holdings to gain blockchain and digital assets capability which builds on their *Zodia* crypto asset custody platform.

Finally, regulatory focus is also starting to shift from banks to the fintech sector with a focus on conduct and corporate governance. There is a shift from being concerned about the banks to scrutinising more closely new market entrants, new business models, and greater vetting of owners and the corporate governance arrangements in place to provide effective oversight and challenge.

[90] Ibid.

Section 6: Setting up a domestically owned bank

This section of the report provides advice and guidance on the key considerations involved in establishing a domestically owned and operated bank. Establishing such a locally owned bank might bring a number of potential benefits – not least it could be designed with the needs of Falkland Islanders in mind in terms of its range of products, services and credit appetite.

Equally, setting up a domestically owned bank is not only a considerable undertaking but will also bring other challenges which might impact on the customer proposition which would need to be addressed. This section draws on insights gained from interviews with senior management of government-owned banks established in other British Overseas Territories including some of the lessons learned based on their experience of setting up and operating a domestically owned bank.

A core assumption, given the small size of the Falklands market, is that the setting up of any domestically owned bank is not in competition with the existing SCB operation. Therefore, the business currently undertaken by SCB would transfer to the new bank with SCB through an ordinance having opted to exit the market. It is envisaged that some of the existing SCB team would also migrate to the new bank.

Shareholders and senior management must be ready, willing and able

- **Ready and thinking ahead** – the shareholders and senior management will need to make sure they have a comprehensive and well researched proposition. The proposition needs to include consideration of the full range of risks and mitigating measures needs to be reflected in the business plan. Whilst, input from external advisors might be useful the senior management intending to run the firm should lead on the development of the firm's business plan.
- **Willing** – Senior management will need to demonstrate they have undertaken comprehensive research – showing an understanding not only of what activity they will be undertaking and with whom but also how they will deliver their products and services in terms of premises, technology and financing their operations. They will also need to clearly articulate the rules and regulations which will apply to them.
- **Able** – the firm will need to ensure they are operationally ready to start their regulated activity at the time they are granted their licence. Securing an appropriately experienced technology provider will be key and a significant cost commitment. Therefore, having an early and iterative dialogue with the authorities who will consider the licence application is considered essential.

A credible business plan is an important component of the mobilisation and start-up process which will guide the setting up of the new bank

- The business plan is the key artefact that articulates the proposed proposition and will also act as a guiding document throughout the build-out of any new bank. It must set out what products and services the bank intends to offer, to which customers, and how the bank will be set up in terms of its governance and its business model. This business model needs to clearly articulate how it will achieve short term viability and become sustainable through the medium-term economic cycle.
- The business plan should also set out the risks the proposed business model brings and how these will be identified, monitored and prudently managed. The business plan will also be an important tool in communicating to broader stakeholders including the Governor, acting in Council, who is ultimately responsible for granting the licence to commence operations.
- It is recommended that any business plan be developed on an iterative basis and include independent review as it is developed. This could take the form of sessions with a number of stakeholders including the proposed shareholders of the new bank and the proposed board of directors of the firm.
- Consideration should also be given to arranging review and challenge sessions with a group of people from outside of the Falkland Islands, who have significant banking experience, in order to test the viability of the proposed proposition and business plan. The feedback from these sessions will tend to lead to a

more robust and resilient business plan and ensure senior management are going into the endeavour with their eyes fully open as to the challenges they will encounter.

Ownership and shareholder considerations

The shareholding and ownership structure of any Falklands owned bank should be given careful and thoughtful consideration. Whilst banking as a business lends itself well to private ownership, there are potentially a number of challenges associated with establishing a bank owned by a small group of private individuals. Policymakers and regulatory authorities have become increasingly wary about a small group of individuals exerting a high degree of influence over the affairs of financial institutions – particularly if they are considered to be systemically important to the local economy.

Research undertaken to understand the impact that ownership structures had on banks based in the Eurozone during the 2007/08 financial crisis shows that listed banks were more transparent as a result of the need to comply with greater disclosure requirements compared to their unlisted counterparts. This boosted **transparency** relative to those controlled by a single or small group of shareholders.[91]

Another consideration for banks owned by a sole or smaller group of shareholders is the **ability to raise fresh capital**. In the event of unforeseen losses, raising much needed equity can be difficult as controlling or influential shareholders don't wish to see their stakes diluted. The ability to raise capital in a timely fashion can be critical in order to preserve and/or restore the confidence of depositors that the bank can absorb losses and that their deposits are safe.

Ownership by a small group of private individuals' also runs the risk of '**politicisation' of management** which might influence the operation of a bank. In some circumstances it can lead management teams to move away from commercially motivated business decisions e.g. lending to preferred borrowers or not pricing risk appropriately. This could lead to unacceptable trade-offs in relation to risk taking and profitability.

It's only fair to note that government-owned banks in smaller jurisdictions also run the risk of politicisation with political pressure applied to management to lend to certain sectors, or perhaps the government itself or during economic downturns. Equally, poor risk assessment can be found across many banks no matter their ownership structure – with listed banks losing significant amounts of money in multiple financial crises.

The ability to **secure and retain correspondent banking relationships** is another key factor when considering the ownership structure of a bank. Access to correspondent banking is a critical enabler as they clear payments on behalf of banks, particularly smaller institutions who do not meet the eligibility criteria for direct access to payment schemes on an economically viable basis.

Larger financial institutions have, in response to increased scrutiny from regulatory agencies and enforcement action, undertaken a significant level of de-risking in relation to correspondent banking. This has resulted in many larger banks terminating or limiting their correspondent banking services to certain regions, jurisdictions, or categories of clients.

This de-risking is creating challenges for small banks notwithstanding their shareholding structure. However, there is evidence that institutionally and government owned banks are able to maintain or secure new correspondent relationships whereas privately owned banks are finding it more challenging in meeting the new level of requirements around due diligence.

Finally, in a Falkland Islands context, it is also worth reflecting **on whether customers would feel comfortable in placing their deposits with and giving visibility of their financial affairs to a bank owned by single private shareholder or small group of shareholders**. Concerns of this nature could be allayed in part by ensuring the operational management of any new bank is independent of the shareholders and clearly seen to be so.

With all these considerations in mind and with institutional investment being improbable it is likely that government ownership, in part or full, would have to feature in any domestically owned Falkland Islands bank. A significant level of taxpayers' funds would be required to cover the initial set-up costs and capitalise

[91] Nicolas Veron, "The governance and ownership of significant euro-area banks," *Bruegel Policy Contribution* 14 (May 2017): 9-10.

a new bank (further analysis below) at a time when there is also a need to invest in renewing the wider Falkland Islands infrastructure e.g. Stanley's port, a new airport terminal, power generation, or aged care facilities.

Operational management and oversight should be independent

The senior management of a bank must operate within the risk appetite and mandate established by its owner(s) whether they be private individuals, institutional or government. However, oversight by the shareholders should be exercised through appropriate corporate governance mechanisms and reporting as opposed to being involved in the day-to-day operational running of the bank.

Whilst, it is not uncommon to have a shareholder representative appointed to the Board of Directors of a bank they should avoid taking the role of Chair - nor should they be able to dominate the Board. Ideally, and as a matter of good corporate governance practice, the Board of Directors should have a majority of independent non-executive members led by an independent Chair together with a small number of executive directors.

Ensuring that experienced senior management are able to take the day-to-day operational decisions will ensure that the risk to reward ratio remains acceptable. It will also constrain the propensity for poor decision making which could lead to reputational issues or financial impairments at a later stage. This is vital given that confidence in the sound running of a bank is an important consideration for depositors particularly when there is not any depositor compensation scheme in place within the Falkland Islands.

Estimated financial resources required of ~£20m to establish a new bank

In order to assess the estimated financial resources required to establish a new bank in the Falkland Islands a high-level financial profile has been worked up premised on the following assumptions:

- The SCB business transfers to the new banking entity which presently consists of up to £180 million of deposits and £21 million of customer lending.
- At the end of year 5 the new bank will have prudently grown the business to have £240 million of customer deposits and £80 million of customer lending. The customer lending will be comprised of £30 million of residential mortgage lending and £50 million of commercial lending.
- The surplus deposits will be placed with a range of financial institutions outside of the Falkland Islands on a range of maturities with a significant proportion also invested in a portfolio of high-quality liquid assets such as UK Gilts or Bonds. Ideally, FIG would also provide a quasi-central bank role noting that a Falkland Islands bank would not be eligible to have a bank account with the Bank of England under the current Sterling Monetary Framework rules. FIG would place these deposits with their own bankers or seek to open an account with the Bank of England (noting some other BOTs have similar arrangements).
- The new bank will adopt the standardised approach to calculating both credit risk and operational risk weighted assets ("**RWAs**"). The following credit risk weightings have been applied in this high-level analysis: Residential mortgage lending @ 35% risk weighting, commercial lending @ 100% risk weighting, placements with banks @ 20% risk weighting (assumes minimum credit rating of A-) and placements with sovereign counterparties including government bonds @ 20% risk weighting. Any exposure to FIG could be zero-weighted should FIG choose to exercise their national discretion.
- Given the start-up situation, operational risk RWAs have been calculated at 20% of anticipated annual revenues in the interests of prudence.
- The business will achieve a blended net interest margin of 2.5 percent which generates net interest revenues of ~£6 million per year with fees and commissions generating a further ~£1 million per year.
- The business will operate with a 75 percent cost : income ratio which is broadly in keeping with peers in other British Overseas Territories and reflecting the 'digital first' strategy of the bank.

Balance sheet (after 5 years)

Assets	
Loans to banks (at amortised cost)	£60,000,000
Loans to customers (at amortised cost)	£80,000,000
Liquidity portfolio / placements with FIG	£100,000,000
Other assets	£15,000,000
Total Assets	**£255,000,000**
Liabilities	
Customer deposits	£240,000,000
Owners' equity	
Shareholder funds	£15,000,000
Total liabilities & equity	**£255,000,000**
Risk weighted assets	
Credit risk RWAs	£92,500,000
Operational risk RWAs	£1,400,000
Total risk weighted assets	**£93,900,000**

Income statement (after 5 years)

Revenue	
Net interest margin	£6,000,000
Fees & commissions	£1,000,000
Total revenues	**£7,000,000**
Expenditure	
Operating expenses and impairment reserves	£5,250,000
Total expenditure	**£5,250,000**
Profit before Tax	**£1,750,000**

Key performance metrics and ratios (after 5 years)

Assumed regulatory minimum CET1 capital (@14% RAR)	£13,146,000
Regulatory trigger CET1 capital (@15% RAR)	£14,085,000
Management target CET1 capital (@16% RAR)	**£15,024,000**
Cost : income ratio	75%
Return on equity	**11.6%**
Leverage ratio (target minimum 5%)	6.25%

Based on this high-level analysis a new bank would require £15 million of capital. It is estimated that start-up costs will be ~ £5 million which would lead to a total investment commitment of ~ £20 million.

It should be noted this is a high level analysis based on a range of assumptions which require further validation. It should however dimension the level of capital and shareholders' funds which would be required to set up a domestically owned bank.

Significant level of non-financial resources also required

In addition to the financial resources required to establish a sustainable new bank there would also be a requirement for a significant level of non-financial resources.

Specifically, there would need to be: (i) An experienced senior leadership team hired in order to mobilise the new bank and lead the wider team; (ii) A Board of Directors including non-executive, independent members to provide oversight of the senior management team; (iii) A technology platform to be procured which is connected to the Swift payments network and ideally the UK banking system; (iv) securing and fitting out of suitable premises to reflect the needs of Falkland Islands customers today; and (iv) Experienced legal and risk resources to develop the initial customer contracts and the control framework. Further detail of the likely requirements is expanded on below.

- **Hiring of an experienced senior leadership team:** Whilst a number of the existing SCB team would transfer to the new bank – not all roles would be required given the new bank would be established on the basis of offering a "digital first" approach i.e. the majority of customers would interact primarily through online or mobile channels with in person contact primarily for vulnerable customers who require a more traditional service or those customers who are relationship managed.
- There is also a need to hire a senior leadership team from outside of the Falkland Islands who have suitable track record of running a fully-fledged bank as opposed to a branch. The senior leadership team would need to be experienced in managing the balance sheet of the new firm including its liquidity position. The new firm would also be solely responsible for underwriting and managing its credit positions together with managing the full range of risks that a banking entity is exposed to including cyber security risk. It is likely that in addition to a Managing Director there would also be a need for a Finance Director, Head of Risk and a Head of Operations.
- A key objective for the senior leadership team would be to upskill the wider team with a view to equipping Falkland Islanders with the skills required to undertake the senior leadership roles. However, at the outset, talent will need to be hired into the Islands at remuneration levels pitched so as to be sufficiently attractive to bring them to the Falklands. An annual remuneration budget for these roles in the range of £400,000 - £500,000 would likely to be required to achieve this.
- **Board of Directors:** Best practice requires that a Board of Directors should comprise a majority of independent, non-executive directors with a smaller number of executive directors (perhaps just the Managing Director and Finance Director) as members. It might also be prudent to establish one or two sub-committees to support the Board of Directors – by way of example this might include a Board Risk Committee and / or Audit Committee. These would typically be chaired by one of the independent, non-executive directors with the other independent directors as members.
- The majority of the Board of Directors should be drawn from the Falkland Islands community itself and encompass a sufficiently broad range of skills / experience. This might include a track record of successful running a sophisticated business with multiple business lines but more important is the ability to provide effective challenge and oversight to the executive management team. Remuneration of independent, non-executive directors would need to be in the range of £25,000 - £50,000 each with the Chair role being at the upper end of that range.
- **Technology and correspondent banking/payment systems access**: A new bank would need to procure a technology platform which would provide both the 'back office' platform for accounting and data management but also support the channels through which customers would be served including digital / mobile banking. Doing this is less of a challenge for small, start-up banks now given the advent of dedicated technology companies who provide a 'Bank in a Box' service (more on this below).
- Another important enabler of any new bank will be gaining access to international payment systems including SWIFT for international payments and ideally the UK banking network through a sponsoring agency bank in the UK. In addition, to this access the new bank would need to establish correspondent banking relationships with banks who will 'clear' payments in the major international currencies. As a

minimum, correspondent relationships will need to be established in the United States for USD, in the United Kingdom for GBP, and in the Eurozone for EUR.

- Securing correspondent banking relationships as a new bank can be an arduous and time-consuming task particularly given many correspondent banking providers have raised both the level of due diligence undertaken and the minimum price to recognise the high-risk nature of providing correspondent banking. It also should be noted that correspondent banks might potentially be uneasy about having high levels of concentration risk /reliance on them i.e. all payments for a particular country being cleared through them.
- The experience of domestically owned banks in other British Overseas Territories is that once correspondent banking relationships have been secured they need pro-active relationship management in order to sustain them. Regular review meetings and ensuring a good two-way flow of information about the performance of the bank, the business being undertaken and demonstrating a robust risk and control environment will be key. In a Falklands context it will be important to ensure they are briefed on geo-political issues and it would be prudent to consider including FIG and perhaps the FCDO in doing this.
- **Securing and fitting out of premises**: A new bank will need premises to operate from. One option given the core assumption outlined earlier would be to inherit the existing SCB premises which are situated in a good location in Stanley. However, this building is currently configured in a way that reflects how SCB operates today. Any new bank will be operating on a 'digital first' basis and therefore will require much less by way of space for traditional banking activities that involve a teller. Taking on the existing bank premises and then reconfiguring them would be both costly and disruptive to the operations of the new bank. It might therefore make better sense to acquire and set up new premises - configured to reflect the new banks customer proposition and staffing arrangements from the outset. In a practical sense this might also be required to give SCB time to wind down their operations as they exit the country.
- **Setting up the legal, risk and control framework**: As part of mobilising the new bank there will be a need to stand up a team of legal and risk professionals. Legal advisors would need to lead on drafting a range of customer and supplier documents. These would include albeit this is not an exhaustive list - terms and conditions for all products being provided, product application forms, borrowing and security documentation to reflect the unique legal characteristics of the Falkland Islands.
- In addition, arrangements would need to be made to secure an auditor likely from the UK given that there is not a firm of sufficient size or with experience of auditing a bank resident in the Islands. Arrangements would also need to be put in place with surveyors and solicitors in the Islands in order for them to act on the bank's behalf when conducting secured lending.
- There would also need to be a significant up-front investment in developing an appropriate risk and control framework. This would include developing a comprehensive risk management framework for the firm which would include exercises to identify all of the risks the firm is exposed to and how they will be managed effectively. Detailed policies and procedures will also need to be put in place and maintained to cover the end-to-end operations of the bank.
- Specialist treasury expertise will also be required to manage the capital and liquidity position of the new bank including undertaking the annual capital and liquidity adequacy assessment processes. The treasurer would also be responsible for developing a recovery plan for the firm which would provide senior management with a range of options should the bank experience either idiosyncratic or market stress events.
- In the start-up phase it might make sense to bring in contingent resources or a consulting firm with access to significant and experienced resources to achieve these tasks and to implement the target operating model of the new firm. After standing up the target operating model a smaller team within the bank would be responsible for monitoring, managing and reporting on its risks whilst ensuring the control framework remains apposite for the ongoing operations of the bank.

The 'Bank in a Box' concept is significantly reducing technology costs and time to reach the market for start-up banks

A significant evolution over the past ten years is the way that new banks can access scalable technology solutions both relatively cheaply and easily. Historically, most banks operated on natively developed technology systems which were expensive to maintain and cumbersome to change. These legacy technology systems have also made it difficult for larger financial institutions to be agile in how they respond to changing customer needs in the digital age.

As far as procuring technology and payment capabilities go, an IT firm like Temenos or Fiserve can provide a new start-up bank with a standardised 'bank in a box', hosted in the cloud on equipment rented from a leasing partner. The operating costs of the platform are set to flex with the number of customers and employees of a new bank which means that costs therefore scale more in line with revenues, reducing the upfront costs of setting up a new bank. Gibraltar International Bank and the Bank of St Helena both operate in this fashion.

Both Temenos and Fiserve focus only on providing banking and finance software. Each typically invests 20 percent of their revenue in research and development. Firms running their platforms – provided they do not extensively customise them – receive regular software updates. These updates allow banks to stay up to date in a cost-effective way with regulatory and market needs whilst avoiding the need for extensive technology expertise and teams of their own.

A criticism that could be levelled at this approach is that product design and delivery ceases to be a differentiating factor between banks which leaves them only being able to compete on service and price. In a Falklands context this is not an issue – customers require a relatively straight forward set of products albeit delivered through contemporary digital channels.

UBS believe that increased regulation and technology combined are, perversely, increasing the scale requirement for larger, international banks while driving it down for simpler newer banks which are backed by new technology.[92] Indeed, new banks might find handling a significant cyber-attack very challenging whereas established banks have survived significant technology outages (think TSB in the UK) – nevertheless new banks with simpler technology architecture are easier to control and defend than larger, complex firms.

OakNorth Bank in the UK provides a good case study of this changing landscape in terms of scale for new banks. OakNorth was set up by two London based entrepreneurs and received its authorisation from the UK regulators in March 2015. They started trading in September of that year and within a year reached breakeven, spending just £5 million in set up costs whilst going on to achieve a profit before tax of £33.9 million and a return on capital of 19% in just their third year of operations with a loan book of £1.3 billion.

A domestically owned bank would require additional regulatory infrastructure to be established by FIG to meet international standards

The current Falkland Islands banking legislative and regulatory framework can be fairly characterised as rudimentary. It exclusively comprises the current banking ordinance which was enacted in 1987 and monitoring of compliance with its requirements is undertaken by the FIG due to the absence of a separate regulatory authority.

It could be argued that this is an acceptable arrangement bearing in mind that there is a single bank operating in the Islands which is a branch of a UK firm regulated by the Prudential Regulation Authority ("**PRA**"). Therefore, the PRA is responsible for the prudential oversight of SCB and monitoring that it holds an appropriate level of capital and liquidity reserves to reflect its risks and ongoing programme of operations.

The current Ordinance and lack of a regulator would not be considered sustainable in the event that a domestically owned bank was to come into existence. The Ordinance would need to be significantly overhauled to reflect contemporary international expectations – it was framed the year before the first Basel

[92] Jason Napier et al, "Big banks and the bigtech, fintech & digibank incursion. What is at stake?" *UBS Q-Series* (June 2019): 32-34.

Capital Accord was introduced in 1988 which set minimum capital levels for banks. Since then the Basel framework has been expanded to include not just minimum capital expectations but granular standards on how banks should calculate risk weighted assets and minimum standards in relation to liquidity and stable funding ratios and maximum levels of leverage.

It is difficult to see how it would be considered acceptable to continue having just FIG being responsible for overseeing a domestically owned bank. This becomes even more acute given the earlier observations about the likelihood of FIG being on the shareholder register either in part or full. There would need to be a regulatory authority created whose senior management and board would be appointed by FIG and/or the Governor but operating independently of it.

The principal role of a new regulatory agency would be to provide oversight of any bank established in the Islands to ensure they are operating in a safe and sound fashion so that depositors are adequately protected. A secondary objective of ensuring consumers are protected in terms of the conduct of business would also be desirable particularly around providing guardrails around acceptable lending practice not just by banks but also firms offering consumer finance.

A new independent regulatory agency would also be important for two additional reasons. Firstly, it would be required to demonstrate the Falkland Islands' commitment to meeting international standards in relation to the management of its finance sector. These standards relate to observing the Basel Core Principles in respect of the prudential oversight of domestic banks but also the expectations of FATF in demonstrating that there is an effective anti-money laundering and terrorist financing framework in the country.

Secondly, it is highly likely that correspondent banks would expect there to be a more sophisticated regulatory architecture in the Falkland Islands overseeing the operation of a domestically owned bank. The absence of an independent regulator might constrain the ability to secure and maintain a network of correspondent banks which would adversely impede the ability of a new bank to meet its customers' needs.

Setting up a new regulator would be a significant endeavour for FIG and would require investment in hiring appropriately skilled personnel to stand up and run such an agency. In addition, there would also need to be a significant level of additional drafting of primary and secondary legislation to enable the new regulatory authority and its various functions. It is noted that there is already an ambitious legislative programme envisaged for the next four years with FIG in the process of hiring an additional legal drafter.

A final important consideration relates to dimensioning whether a Depositor Compensation Scheme would need to be established. During the global financial crisis of 2008, the levels of deposit insurance cover was increased in order to re-assure depositors that there funds were safe. In the UK and across Europe the industry is responsible for meeting any shortfall of retail deposits up to a maximum of €100,000 in the event of a bank failure. However, designing Depositor Compensation Schemes is much tougher in small jurisdictions particularly when you have a small number of banks or even just one bank.

At present, there is no such cover in the Falklands for deposits placed with SCB locally – depositors instead can draw comfort that their deposits are being placed with a large, systemically important financial institution which is supervised by the UK regulators and with extensive financial resources. Depositors might have different expectations in the event they were placing deposits with a much smaller and locally incorporated bank with a far more concentrated business model.

Section 7: Key observations

This section sets out the key observations based on the review of the current banking provision in the Falkland Islands and the benchmarking of services available across the cohort countries. It also draws on the information gathered during the various meetings and interviews undertaken whilst visiting the Islands. The analysis of products and services across the cohort countries has been conducted on a desktop basis albeit interviews and meeting have been undertaken where possible in order to validate the desktop research.

1. **The idiosyncratic constitutional arrangements of each country studied appears to heavily influence the banking provision available. As a rule of thumb the more integrated a territory is to its 'metropolis country' the greater breadth and plurality of banking services there is.**

In terms of banking in small island jurisdictions the study reveals there is an apparent trade-off between the levels of integration and autonomy a country enjoys. There is academic research available, reviewed as part this work, which highlights that small, non-sovereign territories tend to fare better than their small, sovereign counterparts. In large part, this is because they are able to leverage the resources and political influence of their metropolis country.

There is, based on the cohort studied, a correlation between the level of integration and the breadth of banking services provided. Easter Island is the most constitutionally integrated out of the cohort with it, in effect, being a province of Chile albeit having its own additional local law. Chilean banks have established themselves on the Island notwithstanding the politically charged and economically under developed environment.

Likewise, St Pierre and Miquelon also benefits from a high level of integration with France. Although not part of the EU, it is represented within the French parliament. It is also noteworthy that the French central bank has a division which is focused entirely on the economic wellbeing of the French territories and ensuring they have access to an appropriate range of financial services.

Easter Island and St Pierre and Miquelon have the greatest breadth and plurality of banking provision considering their remoteness and population. A clear factor in these two jurisdictions is the constitutional arrangement that links them closely together with their 'metropolis country'. Some however, particularly in Easter Island may ponder at what cost given concerns about the pace of change to their way of life and heritage.

Niue and the Cook Islands are more unique. The formal constitutional arrangement is first and foremost with the United Kingdom given King Charles III is the Head of State albeit they are in a free association with New Zealand. Both countries have a higher level of devolved decision-making compared to Easter Island and St Pierre however there are also important normative factors (cultural and political) to consider in terms of their relationship with New Zealand. A significant proportion of New Zealand Māori identify strongly with their Pacific Island neighbours given their strong heritage links. In addition, there are more Niueans and Cook Islanders living in New Zealand than in their home of origin. As a small democracy with a proportional electoral system and with concentrations of these groups in just a handful of electorates this tends to lead to them having a significant influence in New Zealand government policy. Indeed, the Deputy Prime Minister and Central Bank Governor both celebrate their Cook Islands heritage. Consequently, the New Zealand government and private sector firms exhibit a strong sense of obligation to support the development of their Pacific Island neighbours. Finally, there is also a unique geopolitical context in the Pacific region. Both Australia and New Zealand are cognisant of the rising influence of China, as Xi Jinping pursues a more muscular foreign policy. Supporting their Pacific Island neighbours is critical to their national interests as a way to underpin their influence in the region.

St Helena and the Falkland Islands enjoy a long-standing relationship with the British Crown as British Overseas Territories. St Helena continues to be reliant on aid from the UK government whereas the Falkland Islands is financially independent owing largely to the success of the fisheries industry. Both countries have small markets and have only a single bank providing a limited range of services. The British have tended to adopt a less interventionist approach in terms of the provision of certain infrastructure compared to, say, France. This includes the banking sector. More broadly, as part of the evolving post-Brexit relationship between the British Overseas Territories and the UK, consideration should be given as to the future role the UK government might play in ensuring each Territory has access to the core infrastructure, including banking, required to support further economic development.

2. **Standard Chartered Bank took a risk in 1983, when their clearing bank cousins would not, in opening a branch in the Falkland Islands to support the Islands development. Their presence has contributed to the remarkable success and prosperity of the Islands over the past forty years.**

The need for a commercial bank in the Islands had been originally identified in the first Shackleton report of 1976. Efforts were made to persuade one of the UK clearing banks to open a branch or to set up a subsidiary – these came to nothing as both Lloyds and Barclays did not believe it was economically viable to do so. As a result, in the years preceding the 1982 conflict, plans were being laid to set up a National Falklands Bank owned by the Government.

That SCB established their branch in Stanley is due principally in no small measure to the personal intervention of then Chairman Lord Anthony Barber. Politics and the right people being in the right roles were also factors. Margaret Thatcher, in the political ascendancy following the liberation of the Islands, was determined to see a commercial bank established there. It was fortuitous that at the helm of SCB was a former Conservative Chancellor of the Exchequer and member of the House of Lords. Barber put the wheels in motion against the advice of his executive team and a somewhat perplexed Bank of England.

Setting up a new branch in a new country always comes with challenges, but the mobilisation encountered problems which might have been foreseen with the benefit of greater planning. It is also fair to recognise it was not just the SCB executive team who lacked enthusiasm for this new endeavour. The arrival of SCB felt like an imposition in some quarters of the Falkland Islands owing to the terms attached to their entry which also scotched the plans to set up a National Falklands Bank.

Nevertheless, the branch opened and began to thrive as the rehabilitation of the Falkland Islands got underway in earnest. The archives reveal that there has always been a simmering tension in the relationship between the bank and the local community over the years - often stemming from a perception that they are not providing the full breadth of services expected of a UK high street bank. But, SCB never did hold themselves out as being a typical high-street bank. This tension continues to echo down the years and still frames the relationship today. Often, the frustrations of the day have been resolved either through changes in stance/policy by SCB over time or the case of more intractable problems through strategic partnerships with FIG such as the launch of the Joint General Mortgage Scheme.

If the original decision to open a branch was a patriotic and politically driven gamble in 1983, the fact SCB have remained in country for 40 years is even more remarkable. No doubt being the ‘only show in town’ and the political profile of the Falkland Islands has influenced their longevity. However, the fact they have remained committed to the Islands when most banks, including SCB, over extended periods of time were exiting larger and more profitable markets should be commended. It would have been easier to cut and run as any political fallout would have soon blown over. Their presence has contributed to the success and economic prosperity of the Islands over the past forty years.

3. **SCB’s operating model and lack of digital/mobile channels is incongruent with how systemically important financial institutions meet their customers’ needs in 2023. The outdated operating model creates a poor customer experience with a commensurate impact on the SCB brand, lacks resilience elevating operational risk and is a drag on productivity for the bank and businesses.**

The current SCB operating model leads the Falkland Islands to benchmark unfavourably in terms of breadth of banking products and services available relative to the peer group, particularly when considering its overall economic prosperity and wealth. The banking proposition is inferior to that found in Niue and St Helena – two countries which are far less developed and continue to require direct development aid from New Zealand and the UK respectively.

Every business, without exception, interviewed as part of this study expressed their dissatisfaction and frustration at the lack of online or mobile banking channels with SCB. The lack of ability to view their SCB bank accounts let alone originate payments creates a drag on productivity for all customers. For businesses with a higher level of payment volumes this necessitates team members spending extensive time manually reconciling payments and calling the bank during their opening hours to raise queries. There is also no ability to interact with the bank outside of their core opening hours. It was common to receive feedback during the interviews along the lines of "we do not want anything out of the ordinary – we just want them to be a normal bank doing what normal banks do." The lack of online / mobile capability also hampers businesses from linking their banking to accounting, invoice and payroll platforms which would bring efficiencies.

During the course of the interviews it was striking to note that the businesses struggled to identify many positive features in their relationship with SCB save for noting the friendliness and dedication of the people they interact with on a daily basis. There is a clear cognitive dissonance between what businesses feel about SCB and how the bank thinks its customers view them. It is noted the bank does not undertake any form of customer satisfaction or net promoter surveys.

When SCB first opened their branch in the Falklands the current channels and operating model would have been regarded as fit for purpose. But, online banking in some form has been available since the late 1990's in the UK. In fairness, the communications infrastructure in the Falklands was likely an historic impediment to upgrading the Stanley branch. The wider bank will have moved ahead with the Islands remaining on its legacy platforms owing to internet bandwidth constraints. Typically, in large international banks, business wide technology upgrades are often funded centrally. Smaller business units which then seek to catch up later have to demonstrate a clear benefits case to justify the cost of the upgrade and will likely be competing with other larger business units for funding allocations. That being said, the internet bandwidth in the Falklands has improved significantly over the past five years. Both St Helena and Niue have operated online or mobile banking for some time with an inferior internet capability. It is noted that the banks operating in St Helena and Niue are government owned and therefore may have different return on investment hurdles to banks operating exclusively in the private sector.

In addition to the poor customer experience the resilience of the current operating model appears fragile. A number of businesses interviewed report an increasing number of errors being made in terms of the processing of their payments. In the run up to the recent busy Christmas period the bank had a significant number of staff absent owing to Covid. As customers cannot self-serve it was necessary to reduce the opening hours of the branch in order for the days' work to be processed. However, a number of firms indicated they had payments made up to four days late including wages for their employees.

Nearly all of the businesses interviewed recognised that the SCB team they deal with on a day-to-day basis strive to provide the best service they can notwithstanding the operating model constraints. Within the current technology envelope, the team at SCB have also endeavoured to innovate to improve the customer experience. The bank introduced a number of initiatives during the pandemic to send payment instructions by email and to also streamline the forms required to initiate multiple payments. The bank have also introduced a number of other changes in an effort to improve the day-to-day customer experience including in-house debit card PIN number production, an online mortgage calculator and bulk upload of salary payment instructions. The recent migration to a new core banking platform is also an important enabler for the bank to introduce digital or mobile banking at some point in the future.

SCB in recent years introduced a debit card in an effort to reduce the number of manual payments and improve the customer proposition. This has seen some success, however businesses have reported that they cannot often use their debit cards for higher value items such as flights for international business trips. SCB have advised that one of the contributing factors for this relates to how a number of retailers in the Islands have set up their card acquiring system with a generic retailer coding. This means that higher value transactions might be flagged as suspicious and be automatically declined. It is not apparent whether this issue is widely understood and retailers in the Islands could potentially make amendments to reduce the incidences of these issues.

Another contributory factor relates to the way SCB have set up the debit card capability in the Falklands. Usually, debit card transactions automatically check that the account has sufficient funds in place at the point of sale. However, due to its current system configuration SCB is not able to do this in the Islands – instead they take a risk-based approach to setting payment thresholds for each card. This unusual arrangement means that SCB can offer the debit card product in the Islands but customers who attempt to undertake transactions above this threshold may experience declined payments which requires them to use alternative methods of payment.

Another feature of the current operating model is that SCB in Stanley has job roles which do not exist elsewhere in contemporary banking today. The manual nature of the branch's operations is also a drag on the efficiency and profitability of the bank. When online/mobile banking is introduced many of these operational roles will become obsolete. These changes may give SCB the opportunity to create a broader range of career paths for its team as part of a strategic workforce plan. Some of the team could be reskilled and deployed into new roles which would not only enrich the customer experience but also enhance the career prospects for its colleagues.

It should also be acknowledged that when digital/mobile banking is introduced it is unlikely that the majority of customers will be able to also use the current manual processes (e.g. funds transfer slips) as SCB will not wish to operate a hybrid model. This means a small number of businesses will need to embrace new payment methods such as accepting card payments. SCB have confirmed their intention is to continue to support vulnerable customers who may not be able to readily access digital/mobile channels.

Finally, the time and cost of remitting payments to and from the Falkland Islands and the UK was raised as a key challenge particularly for smaller businesses. This is largely a factor of the Stanley branch not forming part of the UK banking network and having to rely on the SWIFT international payments network. The Financial Stability Board in 2020 identified international payments as an area which has been neglected at the expense of speeding up domestic payments. Work is underway to explore how technology could be deployed to speed up settlement, reduce the incidence of misrouted payments and reduce the costs of payments. The introduction of the IBAN number for the Falklands will help with more efficient routing and it is understood this will be adopted by SCB within the next six months.

4. **Setting up a domestically owned bank to replace Standard Chartered is unlikely to be a panacea and solution to addressing the current challenges. The Islands have, and continue, to benefit from the presence of a large international bank.**

A domestically owned community bank would be able to tailor its product range and services to reflect the needs of its local community. The evolution of technology in banking means that 'out of the box' banks are easier and cheaper to set up than ever before. However, community banks work best when they are part of a wider eco-system of banks and should be considered complementary to larger financial institutions. As a country develops the needs of businesses become more sophisticated and they need to access expertise and capital which is often beyond the reach of community banks.

There is an extensive body of research which contends for the presence of international banks in developing markets because they bring a range of benefits including financial stability, knowledge and technology transfer, tried and tested risk management frameworks, robust corporate governance arrangements and high standards of consumer protection. Foreign banks can also be an important catalyst in stimulating exports in developing countries by providing links to larger and more developed markets.

The presence of international banks also enhances the reputation and credibility of a country as noted in the recent Standard & Poor's rating opinion for the Falkland Islands. Having a branch of a large international bank also means that depositors money benefits from the safe harbour of being placed with a large, well-capitalised institution with a diversified business mix and with recourse to a lender of last resort (central bank). During the global financial crisis, many smaller community banks encountered funding difficulties and were not able to access the support mechanisms from the large central banks.

Larger international firms are also able to leverage support and expertise from within their wider network, particularly in relation to specialist areas of credit underwriting, compliance and technology support. A domestically owned community bank will often struggle to compete for and to retain expertise, if indeed the requisite skill set is even locally available. Community banks can therefore struggle to stay abreast of contemporary banking developments which could ultimately impact the customer experience.

Community banks established in small island-based economies are also likely to find it more challenging to secure and sustain correspondent banking relationships. As already highlighted, the significant de-risking which has taken place means that correspondent banks are tightening their due diligence criteria or imposing higher minimum volume requirements. This can potentially impact the customer experience for island-based community banks. It should be noted that, of the adopted peer group in this review, St Helena and the Cook Islands are the two jurisdictions with a local bank. Even so, the Cook Islands' community bank is found in the context of having two other international banking groups with a full service offering. Most of the studied jurisdictions seem to have adopted the strategy of preferring the presence of an international bank within their territories.

It is also noted that St Helena has had its own community bank since 2004 which has delivered a number of innovations including the launching of internet banking and a local card merchant service. However, the Government of St Helena and Ascension are exploring how they might either attract an international bank or financial institution who can introduce greater international connectivity. It was remarked in interviews that St Helenians regard the Falkland Islands as more favourably placed because of the presence of an international bank in the form of SCB.

5. **The commercial lending market is not functioning as it ought to in the Falkland Islands – established and profitable businesses with acceptable collateral are struggling to secure the lending to enable them to grow and diversify.**

It is not appropriate within this report to comment on specific cases raised by businesses during the interviews. There will always be sound reasons why a commercial bank will not lend money to a specific business and its circumstances – they will understandably wish to avoid the reputational risk of having to enforce their security in a small community. SCB's commercial lending criteria are detailed in Appendix 3.

However, a pattern clearly emerged during the interviews conducted - established businesses across a variety of sectors with a profitable track record and acceptable collateral cannot secure loans with SCB. There is a perception in the market that SCB are not 'open for business' and the size of their commercial lending book, at just £600,000 or 0.4% of total deposits, lends credence to this perception. This does not appear to be an issue related to demand – the FIDC has a loan book of ~£2.5 million outstanding. Typically, it would be usual to expect a development agency to have a smaller share of the total lending market compared to the commercial banks but here they have a total book several times the size.

FIDC would be expected to focus their efforts on supporting start-up businesses or on those businesses that have high growth potential but cannot yet evidence a sufficient track record to secure senior debt from a bank. SCB require a business to be able to provide them with three years financial accounts in order to consider a lending proposal. However, it is clear from the interviews conducted that FIDC will also support more established businesses when SCB have declined facilities so as to make sure that viable businesses are getting the funding support they need.

A number of businesses noted that FIDC provide their lending on more favourable terms than SCB with interest rates being more keenly priced. In these circumstances there is little incentive for businesses to borrow from SCB on commercial terms which therefore makes transitioning from FIDC support to the bank challenging. Equally, it is clear that FIDC, given their mandate, strive to be as proactive and supportive as possible of businesses that have the potential to contribute to the economic development of the Islands.

Given the time constraints in conducting this work it has not been practicable to undertake a deeper dive into the underlying reasons for SCB's stance in relation to commercial lending. However, it is noted that SCB do not presently run a relationship manager service for their commercial banking customers and do not have experienced commercial lending managers on island. At other banks the commercial relationship manager plays a key role in ensuring that banks understand their customer's businesses, the key risk drivers and how they best structure lending proposals to meet their borrowing needs.

Finally, one other issue was raised on a number of occasions in terms of SCB supporting the fisheries sector with their upcoming fleet renewal programme. Many of the long-established fishing companies and their joint venture partners have or are in the process of placing orders for new vessels. These assets represent an attractive funding opportunity and at present the Spanish banks are cornering this market. It is understood that SCB have considered a number of loan proposals but it is not a sector in which they have experience of lending to. A lack of expertise and track record in a sector can lead to having to allocate higher levels of capital against such lending which can impact the profitability of facilities. A lack of expertise can also lead to poorly structured facilities and credit problems. However, given the growing scale of the fisheries business perhaps market-based or co-investment credit solutions might be explored with the support of SCBs corporate and investment bank.

6. **The size of the Falkland Islands market and lack of scale means Standard Chartered Bank cannot reasonably be expected to provide the breadth of products and services found in larger markets. The focus of all stakeholders should be on securing access to 'brilliant banking basics.**

The business model for large international banks hinges on operating at scale in order to drive operating efficiencies. The financial crisis of 2008 led to policymakers requiring banks to both boost the levels of capital and liquidity reserves in order to make them more resilient to shocks. This has served the sector well and has ensured they continue to support their customers and the economy during the Coronavirus pandemic and amidst the recent geopolitical turmoil.

However, the extraordinary policy responses of quantitative easing and a much longer than anticipated era of ultra-low interest rates have meant that banks have been forced to aggressively pursue greater operating efficiencies as they seek to deliver an acceptable return to their shareholders. Consequently, there is little scope for product customisation and banking products are becoming more commoditised as a result. Many large banks are also withdrawing from business lines and countries where they do not enjoy sufficient scale. In addition, there is a far greater regulatory scrutiny on the conduct of credit business on a cross border business with banks cognisant of the potential of regulatory and enforcement action should they inadvertently fall foul of local consumer protection rules and requirements.

In the Falklands context this inevitably means that not all banking products can be offered in a sustainable or cost-effective fashion. By way of example, the size of the market means it is just not feasible to set up and offer a credit Card or charge Card product to individuals or businesses in the Falkland Islands. It is also noteworthy that larger Island territories, including those with significant international finance centres, are finding that their residents can no longer access credit products on a cross-border basis.

SCB do offer these products in other markets and the question was raised in a number of our interviews as to why they cannot just extend them to also include the Falkland Islands? However, the unique nature of SCB's entry into the Falkland Islands is a factor which should be considered here. They are set up as a branch of the Standard Chartered Bank in London. The bank does not provide high-street banking services in the UK – it instead focuses on multi-national corporates and financial institutions. It would not be practicable nor cost effective for SCB to extend these products from another region which operates to a very different regulatory and legal framework.

7. **The regulatory framework and architecture needs updating to reflect the contemporary banking landscape. In addition, the Government needs to also play a key role in leading by example in the wider digitisation of the economy including in its delivery of public services.**

The banking ordinance in the Falklands dates back to the late 1980's – a situation not out of keeping with a number of the territories surveyed in this study. For the Falklands arguably, it has not been a priority because it does not need to concern itself with the prudential oversight of SCB given it is regulated primarily by the Prudential Regulation Authority and Financial Conduct Authority in the UK. The regulation of banks has changed markedly over the past three decades with the introduction of the Basel Capital Accords, depositor compensation schemes, recovery and resolution regimes for banks, and notable consumer protection measures. Clearly, not all of these are necessary for the Falkland Islands. However, it would be advisable for FIG to consider bringing forward a revised package of banking legislation. This will ensure that the Islands are keeping pace with international standards in this area and also should be considered a foundational element should another financial institution consider operating in the Islands.

It is anticipated that there will be greater digitisation in the Falkland Islands. The business community is keen to leverage the digital economy where it can – the advent of digital/mobile banking is eagerly anticipated and will build on the switch to card payments. SCB, as the Islands' only financial institution, and FIG lie at the heart of the Falkland Islands community. How they each progress on embracing the digital economy will inevitably set the tone for the wider business community. Both institutions should set out their strategic plans for delivering their services digitally. These plans will also need to include measures to ensure that vulnerable individuals remain able to access vital services and not fall victim to financial fraud. There might also be value in FIG and SCB running joint educational campaigns focused on anti-fraud measures to reduce the incidences and impact of digital fraud.

8. There are opportunities for collaboration with other British Overseas Territories to raise awareness of the British Overseas Territories, the shared challenges faced in relation to banking and to build new capabilities on a shared basis.

Awareness of the British Overseas Territories, what they are, their relationship with the United Kingdom and the challenges they are facing is lacking. In the banking fraternity the assumption might be that they are all international finance centres with a read across being made from the Caribbean territories. As a result, territories such as the Falkland Islands, St Helena and Ascension, and South Georgia may be regarded as higher risk territories which could be a factor in framing appetite for UK based banks to offer services on a 'remote' basis. We know that a number of firms operating in the Falklands do have legacy relationships with UK banks and whilst these banks have indicated they are content to maintain their existing arrangements they are not inclined to open new accounts for them.

For those territories which do not have an international finance centre it might be useful to work together to raise awareness with politicians in the UK, perhaps through relevant All-Party Parliamentary Groups and the UK Overseas Territories Association. This outreach might also usefully extend to include a number of the key trade bodies including UK Finance. By working collectively, there is a greater propensity to help educate key UK stakeholders about the unique character, identity and challenges facing the islands and the British diaspora who live there.

A number of the Territories need to update their banking legislation and regulatory architecture. A number have banking legislation which has not been updated for some considerable time and now needs to reflect the latest international standards in terms of Basel prudential accords, consumer protection, and recovery and resolution. The scale issue is not just a challenge that commercial banks face – operating regulatory architecture to cover relatively small populations inherently causes diseconomies of scale and accessing specialist expertise can be cost prohibitive.

Section 8: Structural options and proposed initiatives

This part of the report sets out the key recommendations and initiatives which stakeholders can consider exploring in order to boost the provision of banking services in the Falkland Islands. Three overarching structural options have been considered and analysed.

A series of proposed initiatives are then outlined. To help guide prioritisation, the initiatives have been assessed on a portfolio basis to determine their cost/ complexity to execute and their anticipated impact. Detailed below are a summary of the initiatives, the rationale for them and narrative on their potential impact. A number of these initiatives will benefit from working groups being formed comprised of the key stakeholders to explore the issues and a potential approach to implementation.

Analysis of structural options

Based on the work and benchmarking completed, there are three structural options / approaches open to the key stakeholders in order to improve the provision of banking services in the Islands:

(i) Work with SCB to facilitate improvements to their existing service provision – this might also entail considering whether there needs to be financial support/incentives for addressing certain issues;

(ii) Seek to bring in another financial institution either physically or virtually to compete with SCB; and

(iii) Establish a domestically owned and operated national bank to replace SCB.

Set out below is an analysis of each of these structural options in terms of their advantages and disadvantages.

Work with SCB to facilitate improvements to their existing service provision

Summary of option
▪ The key stakeholders work with SCB to make improvements to the overall service proposition including the launch of online/mobile banking and improving the availability of commercial finance. Consideration to be given to providing support and/or incentives to fund service improvements.
Advantages
▪ This option preserves the existing SCB presence and retains an internationally recognised and systemically important financial institution in the Falkland Islands. ▪ Leverages SCB's wider business in terms of capabilities and expertise including risk management, compliance and the safety of customer deposits. ▪ Significant heavy lifting has already been undertaken by SCB in terms of remediating their book of customers in terms of KYC / due diligence and also upgrading their back-office platform which is considered a key enabler of digital/mobile banking. ▪ There are a number of initiatives which do not require a significant technology spend and associated risk which would potentially improve the overall customer proposition and experience albeit they rely on SCB having the appetite and desire to explore them.
Disadvantages
▪ Limited scope to customise the products and services to reflect the unique needs of the Falkland Islands. ▪ Relies on SCB to allocate the funding and resources to progress a number of the initiative's including the introduction of the digital/mobile functionality required. ▪ Technology cost will be benchmarked against other investment priorities – efforts to improve the profile of the Falkland Islands with SCB senior stakeholders may improve prospects of success.

- Support / contribution from FIG may be required to incentivise SCB into addressing some of the service shortcomings. Other options to be considered include launching a commercial lending equivalent of the JGMS.

Seek to bring in another financial institution either physically or virtually (i.e. fully digital basis)

Summary of option

- Seek expressions of interest from other financial institutions in the UK and further afield to gauge appetite to serve the Islands market – either with a physical presence or on a virtual (fully digital neo-bank) basis.

Advantages

- Bringing in a new financial institution either physically or virtually would solve a number of the challenges in terms of service provision e.g. digital/mobile banking as a new entrant would seek to enter the market with a contemporary banking offering.
- The presence of another competitor in the market might add additional incentive to SCB to 'up their game' in terms of service provision.
- Opportunity to collaborate or partner with other BOTs e.g. St Helena and Ascension who are also seeking to attract another firm to sit alongside their existing domestic bank. Being able to serve multiple markets might stimulate additional interest.

Disadvantages

- Highly dubious that a market the size of the Falklands can realistically support two banks operating in direct competition with one another – might also prove to be a catalyst for SCB to exit the market as they are no longer the 'only show in town'.
- A neo-bank operating virtually in the Falklands is unlikely to have appetite to provide credit products given lenders typically need an on-ground presence to ensure a prudent approach to underwriting and monitoring their facilities. Provision of service to vulnerable customers would also need to be considered.
- Any bank operating virtually in the Islands would hold their deposits outside of the jurisdiction which would support further 'capital flight' and FIG would lose the tax revenues associated with this activity.

Establish a domestically owned and operated national bank to replace SCB

Summary of option

- Set up a domestically owned and operated national bank with the existing business of SCB transferring to the new bank

Advantages

- A new national bank's products and services could be customised to reflect the unique needs and character of the Falkland Islands community. It could be set-up on an omni-channel basis to provide up to date digital capabilities with a smaller traditional branch presence to ensure needs of vulnerable community members are met.
- The cost and complexity of setting up the technology platform of a new bank has reduced significantly following the advent of 'banks in a box'.
- Opportunity to explore collaboration with other territories e.g. Saint Helena and Ascension – reshaping of Bank of St Helen to also serve the Falklands.

Disadvantages

- The Falkland Islands would lose the presence of an internationally recognised banking brand. Notwithstanding, the current service challenges the presence of SCB has served them Islands well.

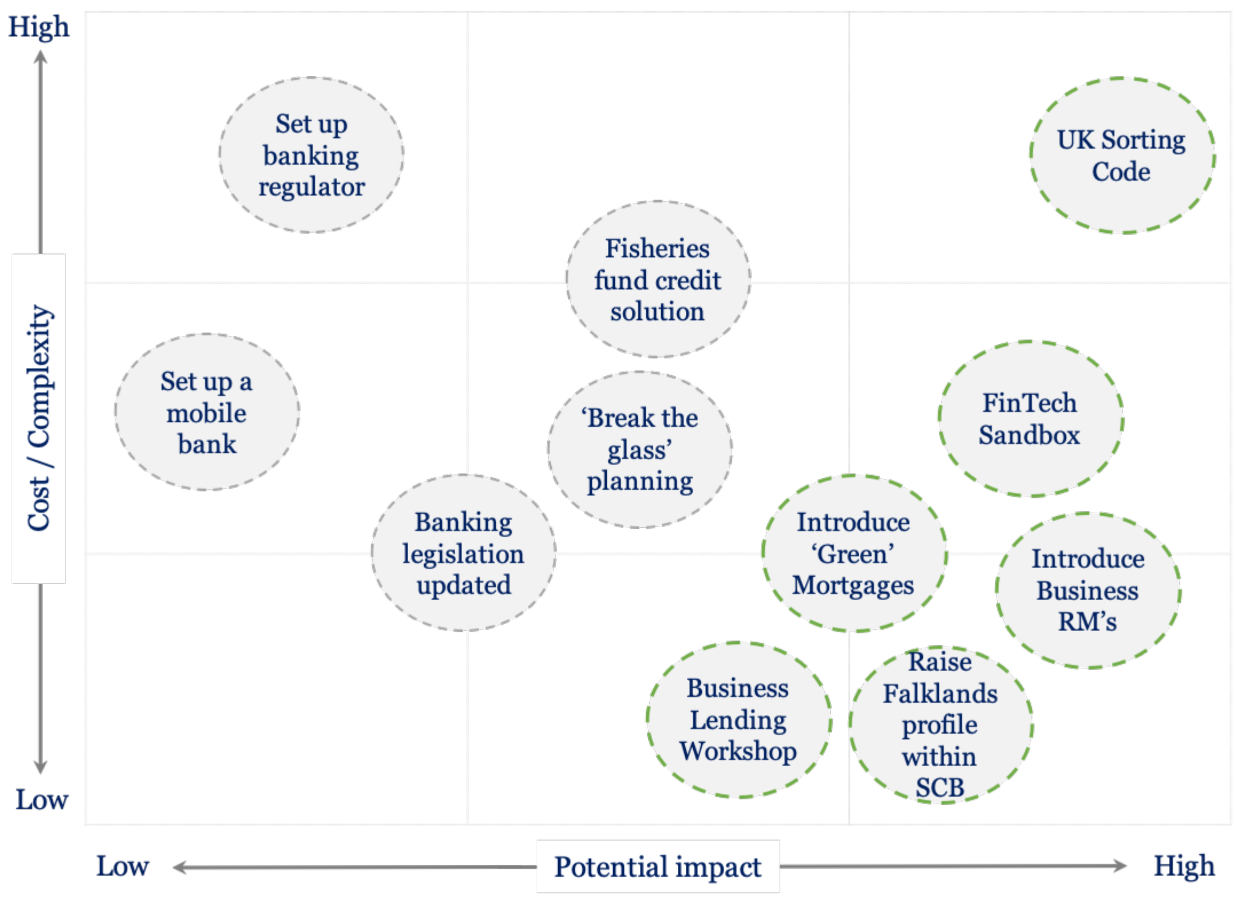
- Capital of ~£20 million would be required to set up a new national bank including ~£5 million of set-up costs. Sourcing private capital to support a venture of this nature likely to be a challenge necessitating partial government ownership.
- Securing new correspondent relationships for a new bank may prove difficult given the levels of de-risking seen and these underpin the customer proposition and ability to make payments.
- Lack of local expertise/skills required to operate a fully-fledged bank will necessitate senior management being hired outside of the Islands. Hiring of this nature is not without its challenges.
- FIG would need to overhaul the banking legislative framework and also put in place an independent regulator to oversee the bank including the prudential safety and soundness of the firm. The ability to rely on the PRA in the United Kingdom to undertake this would not be available. The new bank would not have access to a 'lender of last resort' and Bank of England support during market and idiosyncratic stress.

Recommendation

Based on the research undertaken, benchmarking completed and the current market landscape it is considered Option 1 represents the soundest way forward for the Islands. Retaining an international bank in the form of SCB but with an improved service proposition will bring the Falklands into line with the peer group jurisdictions. It is considered unlikely that sustaining two banks in the Islands is a realistic prospect given the small population. Establishing a domestically owned national bank will potentially solve some of the current service issues but runs the risk of creating other challenges which could be the detriment to the Falkland Islands community.

Portfolio of initiatives

In the context of option 1 being the favoured recommendation, a number of initiatives for consideration by the stakeholders are set out below. They have been assessed based on their cost/complexity to execute and their likely impact. A high-level summary of each initiative is then also detailed. It is recommended that the high impact initiatives are explored in further detail through a dedicated working group.



1. Explore migrating the SCB Branch onto a UK sorting code

Description of initiative					
▪ SCB to explore the feasibility of extending their existing agency banking arrangements with NatWest to enable the Stanley branch to become, in effect, part of the UK bank network. This would see the Stanley branch on par with the Jersey branch of SCB which already has a UK sorting code and would enable same day and lower cost payments to be made by Faster Payments, BACS and Direct Debit.					
Cost & Complexity	High	**Level of Impact**	High	**Suggested priority**	High
Rationale & further information					
▪ A common frustration voiced by all businesses was the cost and time it takes to transfer money to and from the UK. At present the branch operates only on the SWIFT payment platform which means that payments are expensive, prone to routing delays/errors and can take days to process. ▪ Having a branch operating with a UK sorting code gives a bank the option of enabling it for the following payment types: Direct Debits, Faster Payments, CHAPS transfers, Cheque & Credit Clearing, and BACS payments. ▪ Standard Chartered Bank are not a direct participant in the UK payment schemes reflecting their status as a non-clearing bank. Instead they use NatWest who act as their agent and sponsor them as an indirect participant. Standard Chartered London has a sorting code issued by NatWest and is enabled for all of these payment types.[93] ▪ It is noted that SCB Jersey branch has a UK sorting code issued by NatWest and it has been enabled for Direct Debits, Faster Payments and BACS payments. ▪ Discussions have been held on a 'no names' basis with PayUK and NatWest to understand whether there are any technical specifications/constraints which would prevent the Falkland Islands from being eligible – they have both confirmed there are no technical impediments. It is possible to enable sort codes for certain types of payment only as SCB have done for their Jersey branch. ▪ NatWest provide agency and correspondent banking to a range of financial institutions including Gibraltar International Bank and Starling. ▪ Should the Stanley branch be able to utilise a UK sorting code it would significantly reduce the cost and friction of sending payments to/from the UK. Square payments could be made directly to SCB bank accounts in Stanley. ▪ Payments in other currencies would continue to be routed via SWIFT albeit it is understood payments to and from the UK represent a significant component of current payment traffic.					
Key dependencies					
▪ NatWest would need to be comfortable with the risk profile of the Falkland Islands as a jurisdiction to enable them to extend their existing agency arrangements with SCB. They will also wish to assess the commercial aspects of the arrangements in terms of payment volumes. ▪ SCB would also need to secure funding and project resource to roll out this capability. Ideally, this would be achieved ahead of or alongside the roll out of digital/mobile banking. ▪ Customers might need to be issued with new bank account numbers and sorting codes to reflect the new arrangements.					

2. Commercial Lending Workshops

Description of initiative
▪ A series of workshops between SCB, FIDC and FIG to 'deep dive' the challenges related to the commercial lending marketplace and why it is not properly functioning at present.

[93] All information relating to Standard Chartered's agency arrangements has been derived from sources in the public domain including PayUK websites.

Cost & Complexity	Medium	Level of Impact	High	Suggested priority	High

Rationale & further information

- The commercial lending marketplace is not functioning properly at present with SCB's total commercial lending book standing at a negligible 0.4% of total deposits. FIDC are having to step in and provide lending facilities to established, profitable businesses which have solid collateral to pledge in support of their facilities.
- The series of workshops would explore: (i) Rationale and challenges for SCB in making commercial lending available - e.g. risk appetite, legal/security issues, lack of local experience/expertise; (ii) The role and mandate of FIDC and how does it work more effectively with SCB – e.g. alignment on loan underwriting approach/terms, how to transition borrowers from FIDC to SCB; and (iii) Ideas and solutions to boost supply – e.g. a commercial lending equivalent of JGMS, a Falklands equivalent of the UK's Enterprise Finance Guarantee Scheme, reforms to Companies Act / insolvency regime required.

Key dependencies

- Input and commitment required from SCB, FIDC and FIG. It is suggested that workshops are also supported with wider subject matter experts from SCB to help find and shape solutions.

3. Raise Falkland Islands profile within executive levels of SCB

Description of initiative

- It has been over 20 years since SCB Executive visited the Falkland Islands. The upcoming 40th anniversary of the branch represents an opportunity to hold a dinner in London with the bank's senior management, Governor and FIG to celebrate their commitment and ongoing support.

Cost & Complexity	Low	Level of Impact	High	Suggested priority	High

Rationale & further information

- The last SCB executive visit to the Islands was in 2001 (not including visits from the Jersey management team). Given the findings in this report and the current challenges being experienced by customers it is recommended that senior stakeholders from the Falkland Islands look to engage at executive level.
- The forthcoming 40th anniversary represents an ideal opportunity to re-engage with executive level management to celebrate their commitment to the Islands and to secure their buy-in/commitment to the investment and resources required to address some of the operating model challenges.
- It is proposed that an intimate dinner be held in London attended by the CEO of FIG, the Governor, the FCO (ideally political level) and invitations extended to the Chair and CEO of Standard Chartered. The Local CEO should also be invited to attend and to ensure appropriate briefings are prepared.
- The dinner would also represent an opportunity to understand more about the wider SCB strategy and how the Islands fit into those plans.

Key dependencies

- Buy-in from the relevant stakeholders required including Government House, FIG and SCB.

4. Introduce relationship managers for businesses

Description of initiative

- As digital/mobile banking is rolled out, reposition some of the existing team resources into new roles within the branch which support customers with financial health checks and roll-out a relationship manager service for businesses.

Cost & Complexity	Medium	Level of Impact	High	Suggested priority	High

Rationale & further information

- Businesses in the Falkland Islands are growing in sophistication as the Island's economy continues to flourish. Their financial needs are also growing more complex particularly those larger businesses who have international reach and are seeking to explore opportunities to diversify.
- Commercial banks, including SCB in Asia, have dedicated teams of relationship managers whose role is to meet customers at their businesses, get to know them and to explore how the bank can best support them with their growth plans. Relationship managers are there to deliver product solutions from the wider bank including financing, ESG advisory, cash management, trade finance and investments.
- Initial training would be required from an experienced commercial banker to upskill existing team members to take on these new roles. These new roles would also provide a greater level of career progression within the Falkland Islands for SCB colleagues. Having on the ground RMs would also help address the current challenges with commercial lending which are being experienced.
- Opportunities to retool colleagues in the branch to focus on brand accretive activities such as undertaking financial health checks with customers to explore how they can save money, improve their budgeting and meet their saving goals. These colleagues could also be engaged in community outreach in the form of financial literacy seminars and workshops.

Dependencies

- Dimension SCB appetite to explore creating these roles and supporting the redeployment of resources.
- An expatriate commercial banker would also be required in the initial stages for 12/18 months in order to provide training and to establish the RM proposition.

5. Explore setting up a Fintech 'Sandbox' network with other British Overseas Territories

Description of initiative

- Explore the feasibility of partnering with like-minded BOTs to establish a regulatory sandbox to attract fintech firms who want to test their products and services in a live but controlled environment. As an alternative option, explore joining an established network such as the Pacific Regional Regulatory Sandbox.

Cost & Complexity	Medium	Level of Impact	High	Suggested priority	High

Rationale & further information

- Small island economies struggle to attract innovators because of the higher costs related to geographical and infrastructure challenges. Fintech firms will want to road-test their products and services in a 'live' environment before scaling up. Having access to a number of small test populations might be attractive for early stage trials.
- There would need to be suitable guard rails in place to screen fintech applicants and to ensure that products are suitable for the participating territories. However, this initiative might attract financial innovation which otherwise would not be available. It also provides a controlled and safe environment for policymakers to undertake evidence-based research which is a useful tool in understanding the risks associated with new financial products.
- The new sandbox could target products and services focused on a broad spectrum of areas including financial inclusion, improving digital and financial literacy, new tools for small and medium enterprises, and products with a social or environmental impact. The sandbox could also seek to engage with UK based fintechs who are looking to conduct live trials of new products and services into a 'British' market.

Key dependencies

- A feasibility study is recommended to understand whether demand exists amongst fellow BOTs and to develop a proposal for consideration. The study could also review case studies from the existing networks and projects to understand the lessons learned.

6. SCB & FIDC to introduce Green Mortgages

Description of initiative					
▪ SCB and FIDC to introduce 'Green Mortgages' which reward customers with discounted mortgage rates for purchasing homes with an Energy Efficiency rating of A or B. Customers taking out home improvement loans would also be eligible.					
Cost & Complexity	Low	**Level of Impact**	High	**Suggested priority**	High
Rationale & further information					
▪ Banks across all regions are introducing 'green products' which encourage/incentivise customers to change their behaviours and carbon footprint. It is noted that SCB already do this in regions of Asia. ▪ Customers are able to obtain a significant discount on standard mortgage interest rates (up to 1% discount is not uncommon) should their homes meet either an A or B rating for energy efficiency. Existing mortgage customers can also access these discounts should they undertake home improvements. ▪ Valuations would need to include an opinion on the energy performance of a property and whether it meets a defined set of criteria to meet an A or B rating.					
Key dependencies					
▪ Work to be undertaken by [FIDC] to understand whether this capability exists within the surveyor community within the Falkland Islands and whether it can be sourced. An enabling framework will likely be required.					

7. 'Break the glass' contingency planning

Description of initiative					
▪ FIG to undertake contingency planning in relation to setting up a domestically owned and operated bank. This would ensure that a level of planning has been undertaken should SCB ever signal their intention to exit the jurisdiction.					
Cost & Complexity	Medium	**Level of Impact**	Low	**Suggested priority**	Medium
Rationale & further information					
▪ Given SCB continues to trade at a significant discount to book value there continues to be media and market speculation that they remain vulnerable to a bid from a larger bank who sees value in their Asian and African network. This poses a potential risk for SCB's operations in the Falklands. ▪ Ultimately, a bid may not emerge or might be successfully defended by SCB Senior Management. However, as has happened previously in SCB a defence strategy might require divestments of businesses/units which are not deemed to be core. Likewise, a new owner might choose to exit sub-scale markets including the Falklands. ▪ Given the experience in Gibraltar of Barclays exiting after more than 150 years in country it is recommended that FIG undertake a level of planning to dimension what would be required to take on SCB's operations in the Falklands by creating a national bank. The Gibraltar government are known to have started planning for the set-up of Gibraltar International Bank well before Barclays exit was announced to the market. ▪ Scope of this work might also be extended to consider wider coverage across the British Overseas Territories and may benefit from support from FCDO.					
Key dependencies					
▪ FIG resources to support the scoping and execution of the work. Securing expertise could be challenging. ▪ Support may also be desirable from FCDO should a wider scenario planning exercise be considered desirable.					

8. Update the banking legislation and regime

Description of initiative					
▪ FIG to introduce an updated set of banking legislation which would consider introducing consumer protection measures – regulation of consumer lending and the principle of all firms engaged in financial services having to act in the best interests of their customers at all times.					
Cost & Complexity	Medium	**Level of Impact**	Medium	**Suggested priority**	Medium
Rationale & further information					
▪ The banking legislation is outdated having been last updated in 1987. It lacks references to the Basel Capital Accords and the requirements regarding bank solvency, capital and liquidity requirements, funding and leverage requirements, recovery and resolution standards. This should be updated to reflect international standards albeit in a way that is proportionate to the Falkland Islands context. ▪ Consideration should also be given to introducing consumer protection features which have been longstanding in the UK but are now also being introduced in the Crown Dependencies e.g. regulating the provision of consumer finance. ▪ With a de-facto monopoly situation in the Falkland Islands in terms of banking provision, consideration should be given to introducing a formal requirement for the bank to undertake customer satisfaction surveys which should be published. There might also be a case for examining whether a general 'consumer duty' should be introduced which would require all firms engaged in financial services to ensure that their products are designed and delivered in a way that puts the consumer's interests first.					
Key dependencies					
▪ FIG resources to develop an updated policy approach in this area. It is anticipated that a revised policy approach and proposals would be put out to public consultation.					

9. Fisheries credit fund solution

Description of initiative					
▪ Explore with SCB, FIG and the Fisheries Association the feasibility of developing a co-investment fund which would provide asset finance for the fishing industry as they undertake their programme of fleet upgrades.					
Cost & Complexity	Medium	**Level of Impact**	Medium	**Suggested priority**	Medium
Rationale & further information					
▪ The Falkland Islands fishing companies as part of their joint-venture arrangements are undertaking a significant programme of fleet renewal. This lending is largely financed by Spanish banks who have a long-standing provenance in this market. ▪ Explore, with the support of SCB's investment bank, the feasibility of establishing a Falkland Islands based co-investment / credit fund which would provide asset finance to the joint-venture companies against a suitable package of security and loan covenants. ▪ The loans would be originated by SCB who would continue to retain a participation (say 20%) in order to ensure interests are aligned. Remaining investors would be comprised of credit investors (pensions, insurance companies) and could also include FIG and/or other Falkland Islands investors. ▪ A structure of this nature might reduce the amount of 'capital flight' and ensure that the Falkland Islands benefits from this financing activity.					
Key dependencies					
▪ Further exploratory work would be required by all stakeholders to dimension the level of demand and SCB appetite to support with structuring and origination.					

- Other considerations would include reviewing Falkland Islands legislative regime to understand whether there are any technical impediments to setting up a structure of this nature and perfecting suitable security over the assets.
- Work would need to be undertaken to determine investor appetite for the notes and whether alternative structures might be a better fit e.g. credit linked notes.

10. Set up an independent regulator

Description of initiative

- FIG to lead on setting up an independent financial services regulator who would be responsible for the oversight/management of the financial sector including financial/economic crime matters.

Cost & Complexity	High	Level of Impact	Low	Suggested priority	Low

Rationale & further information

- It is recognised that establishing a financial services regulator would yield no tangible improvement in the proposition for banking customers in the Falkland Islands. Instead it should be considered as an enabler for maintaining the reputation of the Islands and a commitment to meeting international standards.
- Having the appropriate regulatory architecture in place might become vital in the event that another bank wanted to operate in the Islands or if it was necessary to set up a domestically owned and operated bank in the future.
- Setting up the architecture would be a significant undertaking and carry a high level of costs. Hiring suitably experienced staff would also be challenging. It is recommended FIG explore partnering with other BOTs to share regulatory infrastructure, as seen in the Caribbean and Pacific regions.

Key dependencies

- FIG to consider extent of ambition and whether any early stage planning would be prudent to ascertain the need and associated timing.

11. SCB set up and operate a 'mobile bank'

Description of initiative

- SCB to set up a 'mobile bank' which would take the bank to customers outside of Stanley on a similar basis to the Scottish banks who serve the remote Scottish Highlands and Island communities (the Bank of Scotland van is pictured below).

Cost & Complexity	Low	Level of Impact	Low	Suggested priority	Low

Rationale & further information

- Customers who are not based in Stanley might benefit from being able to use a 'mobile bank' which would follow a set route at an agreed frequency.
- The mobile bank is in effect a van which is driven by a member of staff and then 'pitches up' at community centres or village halls.
- It is recognised this represents a low impact / low priority given the relatively small number of businesses and people living in Camp (outside of Stanley).
- The introduction of digital/mobile banking would improve the service provision for those in Camp and should be the primary focus.

Key dependencies

- A suitable vehicle would need to be fitted out by SCB to include appropriate security/tracking measures. A fixed route and timings would need to be devised which is communicated in advance for customers.

Appendix 1: Terms of reference

Overview

The Falkland Islands Chamber of Commerce (the "**Chamber**") is commissioning a project to review the current provision of banking services on the Falkland Islands. The project will benchmark the current banking proposition with comparable jurisdictions to gauge whether the current service provision is in line with the contemporary expectations of stakeholders, given recent technological and regulatory developments in the banking sector.

At the project's conclusion the Chamber will be able to understand: (i) how the current provision of banking benchmarks against a cohort of comparable jurisdictions; (ii) the challenges, constraints and opportunities faced by both the current service provider in the Falkland Islands and other service providers in other similar jurisdictions; (iii) what measures and initiatives (including investment required) can be undertaken to improve the service provision by the existing provider; (iv) the current banking landscape including regulatory and technological developments which may shape the banking provision for the islands; and (v) an outline of initiatives which may support the retention of a greater level of savings and investment within the Falkland Islands.

The project will deliver the Chamber and its key stakeholders a target blueprint which will enable them to develop the local banking system to better support local residents, businesses, NGO's and the government with their growth aspirations. The project will also give some preliminary guidance and advice in relation to the steps, investment required and key considerations/risks that would need to be considered in order to operate a domestically owned bank, in the event the existing service provider is unable to commit the investment required to boost the service provision.

Deliverables and strategy

	Key Deliverables	Proposed strategy to deliver
1.	To review the banking services available in the Falkland Islands to Government, businesses, NGOs, and individuals and to examine whether these are adequate for their needs.	▪ Understand the primary needs of customers and how these are currently met through a series of face to face interviews. ▪ Desktop review and interviews / mini-workshops with existing service providers (e.g. SCB and GIB).
2.	To advise what services might reasonably be expected in a community of this size and location, given the restrictions on available infrastructure.	▪ Develop a peer group of internationally comparable jurisdictions based on population, density, geography and economic profile. ▪ Research the banking proposition across this peer group, mapping how this compares to services in the Falkland Islands. ▪ Outline the regulatory and technology architecture in the peer group jurisdictions (telecoms, government policy) and how the Falkland Islands benchmarks.
3.	To advise how the Chamber might go about implementing improvements to the banking services available using the existing players and infrastructure.	▪ Articulate the constraints and challenges faced by the existing service provider and measures/steps which could be taken by key stakeholders to unlock further investment in the customer proposition. ▪ Provide a SWOT and risk analysis of these options for the key stakeholders.
4.	To advise on potential future global developments that may further change the landscape of "banking" and whether they may be appropriate for the Islands.	▪ Outline the changing nature of the banking system in light of digitisation and the advent of virtual "neo-banks". ▪ Provide an overview of the evolving regulatory expectations and international standards e.g. Basel III, recovery and resolution, depositor compensation and anti-money laundering/financial crime expectations for the industry and what this might mean for the Falkland Islands.

		▪ Other relevant developments including the advent of alternative providers.
5.	To suggest banking / finance models which may unlock additional investment and financing opportunities within the local economy including "green" investment opportunities.	▪ Provide an overview, based on the cohort of comparable jurisdictions, of initiatives which could be considered with a view to boosting savings and investments being invested locally in the Falkland Islands including "green" investment opportunities.
6.	High level overview of the key considerations and risks of operating a domestically owned bank.	▪ Provide a small number of case studies and advice based on the peer group jurisdictions to inform the Chamber and key stakeholders on what might be required in terms of investment, architecture and the key risks associated with developing a domestically owned bank.

Project summary

Key Dates

- Project commencement - 1 December 2022.
- Desktop research – 1 December 2022 – 1 January 2023.
- Interviews/workshops to begin - w/c 10 December 2022.
- Proposed field trip to the Falkland Islands – 7 January 2023 – 14 January 2023.
- Final report issued in draft for review - 31 January 2023.
- Review meeting with the Chamber - w/c 6 February 2023.
- Final report issued - 15 February 2023.

Key Assumptions/dependencies

- Access to and appropriate availability of key stakeholders to support the proposed project timelines including: (a) the existing service provider Standard Chartered; (b) a number of island-based businesses in order to understand their banking needs; and (c) relevant government officials (as appropriate). Reliable and timely access to relevant information from stakeholders.

About Queenstown Strategic Advisors

A boutique advisory firm specialising in financial services with 22 years' experience in the financial services industry having worked with one of the UK's largest banks. Over 15 years' experience operating in international finance centres and small island economies advising firms on their strategic and commercial development plans in light of evolving regulatory requirements.

Recent engagements include: (i) supporting a financial services firm engaged in a confidential M&A transaction by developing detailed profiles of the target acquirers and a framework to enable the shareholders of the business to select a preferred bidder based on achieving the optimum outcome for their existing clients, staff and shareholders; and (ii) advising on and leading a legal entity restructuring for an international bank to comply with new European regulatory requirements.

Extensive experience working constructively with the regulators and government in the Channel Islands, Isle of Man, Luxembourg, Gibraltar and the United Kingdom including negotiating a series of authorisations for new banking entities. Experienced chair of an industry technical working group focused on prudential regulation, recovery and resolution, and banking reform.

Experienced participant in government and industry working groups to support the development of the banking sector in small island economies. Comfortable operating at senior management and board level, with a proven ability to develop actionable solutions for institutions operating in small island economies to enable them to support their community's ambitions and thrive whilst meeting increasing regulatory expectations and requirements.

Appendix 2: Sources of information

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Appendix 3: Standard Chartered Bank lending criteria

Core commercial lending guidelines:

- Net profit after tax must have been positive in 2 of the last 3 years;
- Net Current Assets must have been positive in 2 of the last 3 years;
- Shareholder funds must be in surplus in the latest financial statements; and
- Net cash after operations must have been positive in 2 of the last 3 years.

There is flexibility to consider underwriting outwith of these guidelines on an exceptional basis depending on the circumstances of each borrower.