



ANNA'S ECONOMY

THE JAK MEMBERS BANK

SWEDEN

An Assessment of Sweden's No-Interest Bank

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Preamble

The purpose of this report is to provide North Americans with one of the first English assessments of Sweden's remarkable JAK Members Bank – a cooperative, no-interest, members-owned-bank. Sweden is already well known for its enviable standard of living under a mix of high-tech capitalism and extensive welfare benefits. Sweden is a highly egalitarian democracy and has produced industrial legends like IKEA, Volvo and Saab, not to mention individuals like Karl-Henrik Robert (The Natural Step), Bjorn Borg (Tennis) and ABBA (musicians). Sweden's 8.9 million people generate a GDP of US\$ 227 billion (PPP) or US \$25,400 per capita GDP.¹

My analysis examines why I believe the JAK Members Bank model might become the international benchmark for “sustainability banking” serving the interests of citizens, businesses and communities committed to sustainability and improved quality of life. I also examine the step-change opportunities for existing North American savings and credit unions, such as Van City Savings and Credit Union in Vancouver, British Columbia, to adopt (in whole or in part) the JAK model. The study contrasts the full benefits and costs of operating JAK versus Van City and assesses the tangible and intangible benefits of no-interest banking.

The JAK Members Bank is a remarkable enterprise that redefines the business of banking and lending of money. The most unique feature of the JAK Bank is that doesn't charge interest on loans nor pays interest on savings. It is thus similar, yet distinct, to Islamic banking. Ideologically, JAK is opposed to making money on money: namely, charging interest for the services of money (loans) – defined as usury.¹ JAK is also a model of a bank of reciprocity where members share their savings that makes no-interest loans available to other members and their families. In essence each member becomes a banker. This cooperative aspect of JAK is a remarkable feature that distinguishes it from all other banks. Moreover, the JAK Bank management takes on a more meaningful role in the community by maintaining a strong relationship with the members and a shared interest in the well-being of member households, businesses and the communities that benefit from no-interest loans. JAK's original aim was to counter the way in which established banks are channeling savings from rural regions to urban centers abroad. Now it appeals to a broader spectrum of Swedes across the country.

Some ask: how does JAK make money? In essence, it doesn't; at least it does not make money from money through interest. JAK simply covers its operating costs (25 employees) by charging minimal fees to its members. More importantly it empowers individuals to realize the power of money as a medium of exchange rather than a store of value or something to be hoarded. In JAK, all members and their communities are better off by pooling their financial wealth and sharing it with those members most in need. Instead of financial wealth, it is the “real” or “genuine wealth” of the household and community that is being built up. JAK is a viable enterprise; I will show in my analysis of their operating costs compared to Van City Savings and Credit Union (based in Vancouver, Canada).

JAK has several comparative advantages that make the model worth considering, particularly for savings and credit unions in North America. I believe that credit unions could achieve the benefits of the JAK, no-interest banking model with a rather small operational step change, yet, with a challenging educational step for bankers and citizens so conditioned to paying interest.

JAK, established in 1965, exists in part to educate its members against the negative effects on individual and community well-being of the prevailing interest-bearing monetary system. The bank is currently owned and managed by 25,000 members – as a truly cooperative bank with a one share, one vote system. Since 1997 (the year JAK was given official bank status) membership is growing at 1000 per year and deposits are growing at 10% per year.

I conducted my study out of interest that JAK might provide a model for sustainability banking in North America. Bob Williams, Chair of Van City Capital Corporation, shared that vision and supported me in this

¹ Usury is often defined as the civil or criminal wrong of charging interest that is beyond the legal limit set by a State. We use a stricter definition of usury as any form of making money by lending at interest or the receipt of any profit whatever for the use of money. In historical teachings of the Church, usury by this definition was considered a sin. JAK is fundamentally opposed to this latter definition of usury.

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discovery. My assessment is based on consultation with Oscar Kjellberg (past-CEO of JAK), Bengt Landegren (Active Member) and Börje Johansson (JAK Consultant), from JAK website materials, and from English materials prepared by Dana Hofford (JAK Board member) in 1998 describing the JAK Bank and an article on JAK by Irish economist Richard Douthwaite in YES! Magazine in the fall of 2002.

I would like to thank Oscar Kjellberg and his wife Anna for there hospitality during Bob Williams and my visit on July 27-August 2 to their beloved “Leo” the tugboat in Stockholm and to Skvöde (JAK’s headquarters). I believe JAK offers on of the best models for the future of what I call “genuine wealth banking” which is a value-based, sustainability-principled enterprise which sees money simply as a means of exchange with an economy rather than a store of value for hoarding and power.

Mark Anielski

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A. Introduction to JAK

Oscar Kjellberg, the CEO of the Swedish **JAK Members Bank** is no ordinary banker. But JAK is not our ordinary bank! It was founded on a revolutionary principle: no interest will be charged on loans.

Oscar explains the rationale:

“Interest causes unemployment, inflation and environmental destruction. Every hike in interest rates means that business has to pay more to service their loans. To counteract this financial strain they must either cut their labour costs, which worsens unemployment; or raise prices, causing inflation; or re-engineer their work to increase output, which leads to increased use of natural resources.”²

Irish economist Richard Douthwaite explains how the modern money system works:

“Most of us imagine money is created by government. In fact, over 95 percent of all money in circulation in a typical industrialized country is created by banks lending it into existence. Conventional banks lend out more money than they have received in deposits, confident that, as other banks are doing the same thing, each will get enough of the new money its rivals create to balance the outflow of funds resulting from its own excess loans – creating money through a kind of musical chairs game. JAK by contrast does not play this risky game. It never lends out more money than its members have saved with it. As a result it plays no part in the money creation process.”

The **JAK Members Bank** (www.jak.se) is **the first cooperative, interest-free bank in Sweden, perhaps the world** (with its beginnings in Denmark in the early 1930s) where members share the benefits of a viable, interest-free banking system that they themselves have responsibility for. When you open up an account at JAK you become a shareholder or “careholder”; everyone only has one share therefore one vote and equal influence in the annual vote for the board of directors.

JAK stands for Jord Arbete Kapital in Swedish or **Land Labour Capital**.

JAK serves over 25,000 members throughout Sweden providing the benefits of traditional banking services without charging interest on loans. JAK is a highly cost efficient enterprise operated by a small compliment of 26 professional staff based out of a single office located in Skvöde, Sweden, roughly 180 kilometers west of Stockholm. All business is done by telephone, internet or post through a state-of-the-art computer system. The enterprise is supported by 380 specially trained volunteers who support JAK’s 24 regional communities. These dedicated volunteers are represent the “marketing force” which spreads the good news about JAK’s benefits and services, without any labour cost. So great is the faith in the benefits of the JAK model.

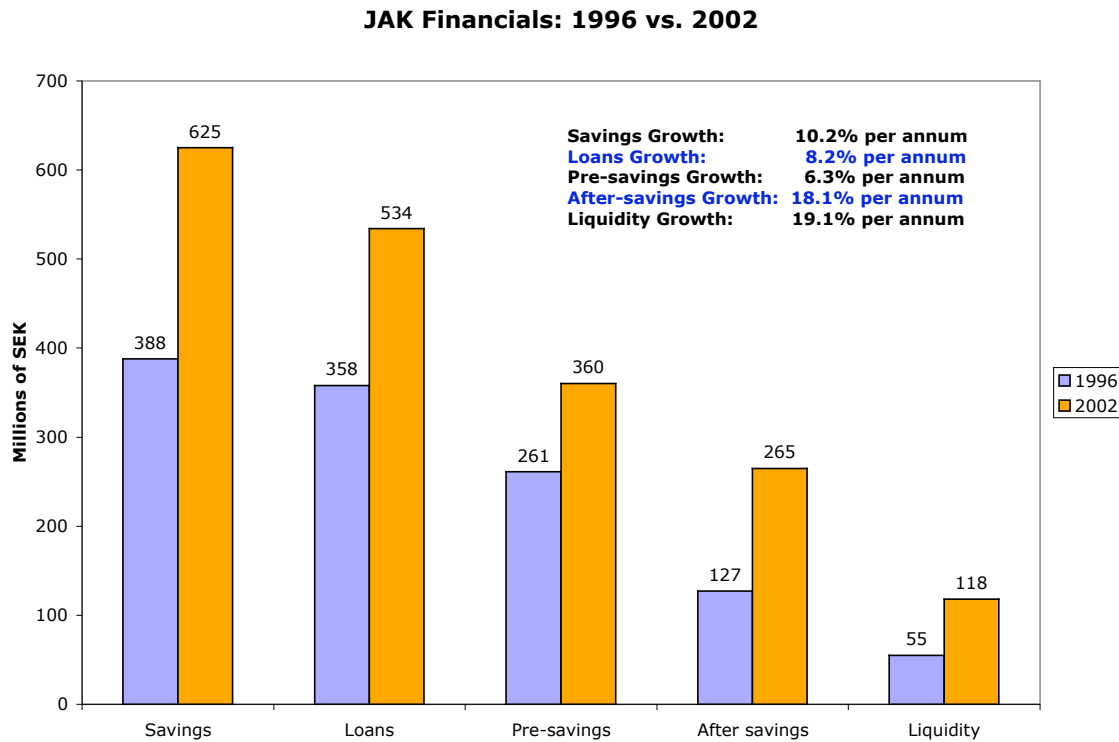
Bank deposits as of year-end December 2002 totaled about 625 million SEK (C\$101 million or US\$ 64 million) and outstanding loans about 534 million SEK (C\$86 million or US\$55 million). JAK also maintains a reserve of Treasury Bills totaling 97.8 million SEK (C\$15.8 million or US\$ 10 million). Operating income in 2002 was roughly 26.1 million SEK (C\$ 4.2 million or US\$ 2.7 million) while operating costs in 2002 were roughly 22.2 million SEK (C\$3.5 million or US\$ 2.2 million). Net profits for 2002 were 789 thousand SEK (\$C 136 thousand). Since 1996 JAK’s growth rate in all categories of its financial well-being has been significant (Figure 1).

A1. Impressive Growth!

Since JAK became an officially recognized bank, its growth rate has been impressive. Savings have increased an average of 10.2% per year between 1996 and 2002 composed of pre-savings (6.3% annual increase) and after-savings (18.1% annual increase). Loans have increased at an average annual rate of 8.2% per year. Overall liquidity has increased at 19.1% per annum between 1996 and 2002.

² From Richard Douthwaite’s article “Saving Together“ in *YES! A Journal for Positive Futures*, Positive Futures Network Fall 2002

Figure 1: JAK Financial Performance 1996 to 2002



**JAK Historical Figures
(million SEK)**

	1996	2002	% change	Annual Change
Savings	388	625	61%	10.2%
Loans	358	534	49%	8.2%
Pre-savings	241	360	49%	8.2%
After savings	127	265	109%	18.1%
Liquidity	55	118	115%	19.1%

Most banks make their profits from the margin between the interest rate they pay savers and the much higher interest rate they charge borrowers and service fees. JAK is not in the business of making a profit. JAK operates as close to break-even as possible charging just enough in loan fees and membership fees to cover its operating costs. In 2002 it covered over 90% of its 22.2 million SEK (C\$3.9 million) in operating costs (which includes 25 paid employees) through these fees. Those costs amount to an average per member operating cost of only C\$144 per each of its 25,000 members. All members pay an annual membership fee of 200 Swedish kronor (about US \$20 or \$25 Canadian) that helps support the costs of operating their account and for a magazine that informs them about banks activities and educational workshops it organizes. Other sources of revenue include interest earned on liquid assets, including Swedish Treasury Bills that are held as a safety reserve against member savings.

The following Table 1 provides some of the most recent Facts on JAK.

Table 1: JAK Facts for 2003

JAK FACTS (January 2003)	
•	JAK does not charge any interest on loans, nor is interest paid on savings; only a self-cost administration fee is taken for loans.
•	In 2002, operating costs (including depreciation costs) were 22.2 million SEK (\$C 3.9 million) or C\$144 per member; These costs were over 90% offset by 19.2 million SEK (C\$3.1 million) in loan fees and annual membership fees.
•	In December 1997, JAK was granted a banking license by the Swedish Financial Supervisory Authority.
•	Savings time can be zero (new rule from September)
•	Average savings time is 4 years
•	Smallest loan is 5 000 SEK (C\$ 863)
•	Largest loan is 7.5 million SEK (10 percent of the capital base) (C\$1,294,562)
•	Average loan is ~92 000 SEK (C\$15,880)
•	Shortest repayment time is 2 years
•	Longest repayment time is 30 years
•	Average repayment time is 10 years
•	Time between installments is 3 months
•	There is no lowest repayment size
•	Total loan fee is 3.5 % plus 1.0 % for each repayment year
•	Minimum loan fee is 600 SEK. (C\$104)
•	Annual Membership fee is 200 SEK (C\$ 35)
•	Comparable cost: a discount rate of 2.0 - 4.9 % produces a NPV equal to zero. The longer the repayment time the lower the discount rate.
•	Credit losses has typically been in the area of 100 000 (C\$17,260) to 200 000 (\$C 34,521) SEK per annum on a stock of loan to a value of 500 million SEK (\$C\$86.3 million).

A2. What Makes JAK Different from other Banks?

JAK Members Bank is different from conventional banks in several ways:

Key Attributes	JAK Members Bank	Conventional Banks
Clients	A members-based, cooperative enterprise; one share, one vote.	Conventional corporate model with major shareholders and client-based.
Bank System	100% reserve system. Loans are lent out on the basis of the total liquidity (savings) in the system, thus loans are 100% supported by member savings and liquid assets. All money is fully secured.	Fractional reserve system: Whenever a loan is issued, new money is created through two simple bookkeeping entries. The loan is largely unsupported by other member savings; only a small fraction of the loan needs to be secured by the private bank, under law, with the Central Bank. The reserve requirement of US private banks is currently a mere 0-3% on chequing accounts.
Loans	Loans are issued on the basis of bank liquidity and the member's income capacity to both save and repay the loan; loan repayment is	Loans are issued on the basis of credit worthiness (assets that support the loan); loan repayments include principle plus

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	ONLY the principal of the loan.	interest charges.
Interest on loans	Does not charge interest on loans but does recover operating costs through an administrative loan fee.	Charges interest on all loans and credit.
Interest on savings	Does not pay interest on savings but does provide a means of earning savings points which are like interest income.	Pays interest on savings, but at current low interest rates these are minimal.
Returns to investors	JAK operates like a not-for-profit bank enterprise , with it's members as "careholders" whose "returns" include interest cost savings on all loans.	Private banks have shareholders who receive returns in the form of share value and dividends that result from profits earned from interest rate spreads, user fees and other bank profits.

JAK operates the following fundamental principles:

- Taking of interest is inimical to a stable economy;
- Interest causes unemployment, inflation and environmental destruction - in some combination;
- Interest moves money in the long term from the poor to the rich, and;
- Interest favours projects, often large-scale, which yield high profits in the short-term.

JAK's ultimate **goal** is **the abolishment of interest as an economic instrument and to replace it with other, less harmful ones, that are in the best interest of supporting its members in building healthy and sustainable communities.**

To achieve this goal, JAK works on two fronts:

1. **Ideological:** - To disseminate information on the ill effects the taking of interest has on the economy, society at large and the environment and to inform of alternatives.
2. **Practical:** - To administer an interest-free savings-and-loan system to show that interest-free financing is not only feasible but also quite valuable in helping to liberate people weighed down with heavy interest loans.

JAK does have a positive effect on unemployment but it is an indirect effect. As JAK liberates more people from interest expenses that much money is freed up which can be used instead to buy goods and services. This will stimulate businesses so that they can employ more people.

JAK's interest-free savings and loan model have appealed almost exclusively to consumers - especially those purchasing homes (90% of the membership). There are only a relative few commercial enterprises using the system.

Because JAK is officially recognized as a bank, the savings of members are covered by the Swedish banking system's deposit guarantees. The official recognition also confirms that JAK has an approved structure and management and that it offers a viable, trustworthy and interesting alternative to other banks.

B. The Ideological History of JAK Bank

The JAK Bank does not believe in the need to charge interest on loans and credit. JAK ideology maintains that the taking of interest causes economic instability. Interest does serve a useful function for the circulation of unused funds. Charging money for the service of money is deemed regressive and has many negative and regrettable side-effects.

"The process by which banks create money is so simple the mind is repelled. Where something so important is involved, a deeper mystery seems only decent."

John Kenneth Galbraith
Money: Whence It Came, Where it Went (1975)

Interest moves money in the long term from the poor to the rich. The borrower gains a short-term benefit but in the final cut, he must pay back much more money to the lender than what was originally borrowed. German economist Margritt Kennedy has estimated that hidden interest expenses could make up between 30-50% of the prices of goods and services. This amounts to an indirect taxation of the population by the wealthy.

Current money systems – whether private banks or national banks – create money in parallel with debt and literally with no relationship to the actual life conditions or needs of a community. Modern currency is in fact called "fiat" which means "created out of nothing"

whenever a bank issues a loan or when a central bank prints currency. Loans are essentially book keeping entries. As such, the creation of money in this manner bears no relationship to the actual conditions of life or the genuine wealth needs and stewardship aspirations of a household, community or nation.

"I know only three people who understand money. A professor at another university; one of my students and; a rather junior clerk at the Bank of England."

John Maynard Keynes

Few people understand where money comes from or how it is created. Yet, money is the very life-blood of an economy and debt-money is what drives all world economies.

What is money? Bernard Lietaer (one of the chief architects of the Euro) describes money as "an agreement within a community, to use something as a means of payment."³ According to Bernard Lietaer⁴, it is important to realize that money is not a living thing; it is not life

capital. It is a human creation: i.e. "fiat." While economic textbooks invariably talk about money in terms of what it *does*, they never define it in terms of what it *is*.

The system of debt-money creates an "artificial scarcity" of money. Lietaer explains that "the device used to create the scarcity indispensable for a bank-debt system to function involves having people compete for the money that has not been created, and penalizes them with bankruptcy whenever they do not succeed."⁵ Money is thus like a treadmill that requires continuous economic output (growth) in order to sustain the demands for interest payments even if the real wealth of the community has been optimized and the real standard of living remains high for all in a community.

Interest favours short-sightedness. Only projects yielding a profit higher than the interest rate are worth investing in. This leads to an overemphasis on large-scale projects (i.e. shopping centres, new highways, nuclear plants etc.) and/or high yielding projects in the short-term (i.e. extracting finite natural resources) at the expense of long-term lower-yielding projects (i.e. alternative energy, ecological farming and many small-scale projects). The higher the real interest rate is, the higher the yield from the project must be for it to be worth investing in.

Interest encourages exponential economic growth. The compounding effect of interest costs throughout an economy actually fuels and necessitates more economic, measured in terms of Gross Domestic Product or GDP (or GNP-Gross National Product). More economic output is required by households and firms in an

³ Lietaer, Bernard. 2001. *The Future of Money*.

⁴ Lietaer, Bernard. "A World in Balance", November 2002.

⁵ Lietaer, Bernard. 2001. *The Future of Money*. p. 52

economy to both pay the imbedded interest costs plus the principal on the debt used to finance household management and business enterprises. There is a chronic scarcity of money (liquidity) in the entire system forcing all households and firms to compete amongst each other to help them service their debt costs, debts which were necessary to enter into production. Bankruptcy is the only way out for those who fail to compete. Economist Herman Daly has noted that because over 90% of money is created in the form of debt, the GDP must continue to grow simply to keep up servicing the interest costs on an exponentially growing mountain of total debt in an economy. In essence, a perpetual growth model is created which has no logical end short of eventual systemic collapse as the compounding mountain of debt becomes impossible to service out of current economic production.

Mort-gage

“A pledge unto death”

“A grip of death”

Consequently, even if a households, a firm or a nation has reached what might be considered a steady state or “sustainability” it is effectively compelled to over produce and over consume human, natural and social capital with deleterious effects to a community and the environment. Ironically, the growing mountain of debt, fueled by the power of compound interest, represents a permanent and non-repayable claim against life’s assets – human capital (time), natural capital (resources and the environment) and social capital (community and relationships). This is probably why the term mortgage is so appropriate – it means literally “a grip of death” from the French *mort* (death)-*gage* (pledge).

Interest causes unemployment, inflation and environmental destruction - in some combination. Every hike in interest rates means increased capital costs for all businesses with loans. To counteract the increased financial strain (other things being equal), the business must either: 1) cut labour costs (e.g. worsen unemployment) 2) raise prices (e.g. inflation) or 3) produce more goods/services at the same cost leading to an increased depletion of natural resources, adding more strain on the environment and degrading the condition of human and social capital (i.e. community well-being). Another aspect to be considered is that the higher the interest rate, the more productive people must be in their work in order for it to be economically viable. As not everyone is equally productive, high interest rates will tend to exclude more people from the productive employment. JAK’s ultimate goal is to show that charging of interest is an unnecessary and regrettable instrument for operating a financial service if the goal is serve the well-being interests of households, businesses and community.

Interest represents depletion of life’s energy (time). It is often said that time is money. When we work we trade our life energy (time) for money (a wage). Those wages are used to purchase goods and services to meet our needs and the needs of our households. Since interest costs represent a significant imbedded portion (30-50%) of the price of goods and services, it suggests that a large percentage of our life energy (time) is being dedicated to pay for the interest costs on a growing mountain of societal debt. Imagine a world with more time devoted to building genuine wealth and improving quality of life. In the JAK system, a significant amount of human energy (time) is freed up by members forgoing labour to pay for the interest cost portions of their loans.

JAK’s ultimate goal is to raise awareness of these harmful and regrettable “costs” of interest in a debt-money world and to re-establish a healthy relationship with money so that it is no longer a store of value (something to be hoarded) but a genuine medium of exchange amongst households and businesses to build real wealth and sustainable and flourishing communities.

C. The History of JAK

C1. J.A.K. Begins in Denmark

JAK had its beginnings in Denmark during the Great Depression of the 1930’s. Many farms were going bankrupt due to the shortage of money and the high real interest rates prevalent at the time. Several of them got together under the leadership of Kristian Kristiansen and in 1931 founded the co-operative society *Jord Arbejde Kapital* (Land Labour Capital - the three pillars of classical economics) abbreviated J.A.K.

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J.A.K. considered the taking of interest to be a chief cause of economic instability, with inflation and high unemployment as a consequence. J.A.K. started three interest-free projects to prove that the idea was not just a nice theory but was quite practical. Their first project was the issuance of an interest-free local currency in Sønderjylland. These notes were backed by real wealth (farm property) in contrast to the national currency and they were enthusiastically accepted by the cash-starved population. At the most, J.A.K. currency amounted to 1.5% of the total Danish note circulation! The Danish government saw its authority threatened, however, and prohibited the experiment in 1933.

A second experiment, started in 1934, was an interest-free savings-and-loan system (*andelskassen*). By saving together without taking interest, they were able to give interest-free loans in turns to all participants which were used to pay off expensive bank loans. This venture also became quite popular. Certain defects in the system together with strong opposition by the media and authorities forced the *andelskasse* to liquidate in 1938.

The third experiment was also started in 1934. It is what would now be called a LETS (Local Exchange and Trade System) - an interest-free checking account system / clearing house whereby members traded goods and services with each other without cash. The accounts were simply adjusted up or down as the case may be. Money lying unused in the system was loaned out at low cost to members. (This second experiment, by the way, served as the chief inspiration for the highly successful business barter exchange system WIR in Switzerland.) Even this experiment was quashed by the Danish authorities in 1935.

In 1944, J.A.K. started up a new interest-free savings-and-loan system with different rules and this time it grew steadily. In 1958, J.A.K. became licensed as a bank beginning a 10-year period of rapid growth. At its zenith, J.A.K. bank was among the 20 largest banks in Denmark.

The system promised loans at a level of 3.2 times one's savings. Example: If one deposited 1.000 DAK/month for 2 years, it resulted in a savings of 24,000 DAK. One could withdraw this savings and also borrow 77,800 DAK to be repaid over 2 years. This worked quite satisfactorily when the growth rate for funds entrusted was over 35% per year. In 1968, however, the growth rate began to fall, due possibly to the high inflation rate. No changes were made to the system, however, until it was too late. The loan demand became increasingly difficult to meet, reserves dwindled to fatal levels and the board saw no choice but to fuse with Bikuben Bank in 1973.

This was not the end, however! Shortly afterwards, many J.A.K. members started afresh but this time in the form of independent local savings-and-loan associations (*andelskasser*) rather than a centralised bank. As of 30/06/96 there were 20 with a total of 6,574 shareholders. There is one national organisation that deals exclusively with ideology that has a membership of 900.

C2. JAK in Sweden

During the 50's and early 60's, the ideas and success of J.A.K. in Denmark attracted quite a bit of attention in Sweden and there was great interest in starting up a J.A.K. system there. After several years of meetings and talking, *Jord Arbet Kapital - Riksförening för ekonomisk frigörelse* (National Association for Economic Emancipation) was registered in 1965 as a non-profit organisation. As in Denmark, the primary purpose was, and still is, to relieve people from the yoke of interest-debt through mutual co-operation and to spread information about the effects of and alternatives to interest.

The first deposits were accepted in 1967 and the first loans were paid out in 1970. The association grew quite slowly to begin with. Only towards the end of the 1980's did the system really take off.

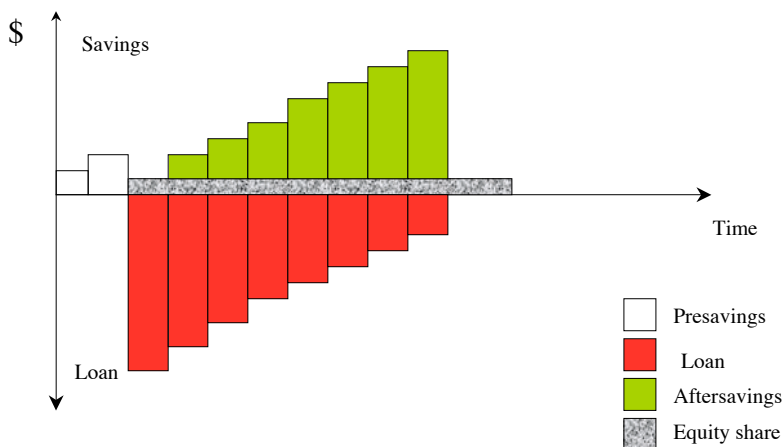
D. How Does the JAK Savings and Loan System Work?

Here is a brief explanation of how the JAK savings and loan scheme works.

JAK is essentially a cooperative organization where members agree to pool their savings from which interest-free loans can be extended to members. In effect, the benefit of having an interest-free mortgage, home-improvement loan, car loan, student loan or other loan, is equally available to any member and thus the benefits of no-interest loans are reciprocated from one member to the other. In JAK, there is a high degree of social cohesion and trust amongst members; so much so, that spreading the good news (i.e. marketing) is done by volunteers in their communities who have experienced the benefits to their quality of life.

In JAK all members are treated equally. The benefits of JAK, especially no-interest loans, are also available to all members. The savings of each individual member forms the larger financial capital pool from which loans can be offered to members who are in need of a loan. The amount of deposit savings ultimately determines the amount that may be borrowed by individual members. No other considerations are applied. JAK accepts deposits and issues loans in Swedish Crowns (SEC). Mortgage agreements or personal guarantees secure the loans

When one becomes a member of JAK, one may open an account and begin using the savings and loan system. Members save in a common pool but, instead of interest, the account accrues **savings points** (based on a formula determined by JAK management) which gives one the right to borrow without interest. The savings points formula depends on the whether a member is in pre-saving period (i.e. prior to receiving the loan) or in an after-saving period (i.e. repaying a loan). Savings points are “used up” or consumed during the loan period.



The diagram above is a portrait of the typical JAK loan showing a progression from pre-savings (prior to the loan), to receiving the loan, to repaying the loan and building up after-savings to replenish the liquidity pool for other members, to paying an equity share (membership fee). This process will be described in greater detail.

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When a member applies for a loan the decision by JAK management to issue a loan is based on many factors including: a) liquidity in the system (the balance between savings and other liquid assets (e.g. Treasury bills held as a reserve) vs. loans outstanding) and, b) members pre-savings prior to receiving a loan (pre-savings are the amount of money a member has saved in his/her account prior to requesting a loan).

When a member is granted a loan they are required to commit to regular (usually quarterly) repayments of only the principal amortized over the loan period. In addition, a member's right to a loan is conditional on continued regular saving during the repayment period till the total savings points are in balance with the points consumed by the loan. This means that ***when the loan has been fully repaid, not only has the debt been repaid but there has also been an additional saving equal to the Additional Loan.***

The loan is not free, but the cost (recovered through an annual **Loan Fee**) reflects a fair share of JAK's administration expenses. Each loan fee is unique for a particular loan and is based on a formula which considers the sum of the loan and the repayment period. The Loan Fee is now divided over the repayment period and paid together with repayment installments.

Loan Fee: A **Loan Fee** is used by the bank to cover the cost for development and administration of the savings and loan system. Some may equate the **Loan Fee** with an "interest" rate (i.e. the "**effective interest rate**"⁶) but it is technically equivalent to a charge for

Loan Fee Formula:

$$\text{Loan fee} = L * [(3,5 + (1.0 * A)/100)]$$

or

$$\text{Loan fee} = L * \ln(33,12 * 2,72^A)/100$$

(Logarithmic function)

where

L = loan amount

A = repayment time (years)

JAK's annual operating costs with respect to loan services. In Sweden the "effective interest rate" is a well-known concept established by the "National Board for Consumer Policies" in order to compare different credit offers in a fair and just way. The "annual effective interest" differs for *each* respective loan; a higher rate on short-term loans and lower rate on long-term loans. During JAK's 38-year history the annual effective rate of interest has ranged from 2.03% (30 year loan) to 4.91% (2 year loan). The effective rate of interest is thus highest for short-term loans and lowest for long-term loans.

In the year 1998, the annual effective rate of interest ranged from 1.47% (on a 20-year loan) to 4.19% (on a 2-year loan). In the fiscal year 2002 the effective rate of interest averaged 2.93% for all member loans (i.e. the ratio of the loan fees collected to the outstanding loan total). These rates have remained largely unchanged over JAK's history. As an example, the **effective rate of interest** (when calculated according to a procedure set by the Swedish Consumer Services Authority) on a 10-year JAK home ownership loan of 100,000 (roughly C \$ 17,000) would be about **two percent**. This compares favourably with, for example, the current rate on a 10-year mortgage with the Toronto Dominion Bank in Canada of 8.05% interest, not including service fees for related banking services). It is the interest costs saved on a JAK loan that give it a clear comparative advantage over conventional banks.

Equity Deposit: In addition to the Loan Fee a member is required to pay a refundable **Equity Deposit** of 6% of loan value. This provides JAK some security against potential loan default. Between 7 and 19 months after the last repayment on the loan the loan equity deposit is repaid to the borrower. It is booked as equity in the bank.

Membership Fees: Members of JAK pay an annual **Membership Fee** of between 0 and 200 SEC (maximum C\$ 35) which goes towards the bank's equity and is paid upon joining JAK and annually throughout the loan period. A membership fee can range from 0, 100 to 200 SEK depending on age and size of household: whether the member is an individual, a family, and or under 18 years of age, who do not

⁶ According to Oscar Kjellberg "The effective rate of interest is nothing more than the internal rate of interest [one can use the internal rate of return (IRR) function to estimate]. You should look for the discount rate that makes the present value of loan and aftersavings payments stream equal to zero."

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pay any fee. Many people are members join for other reasons than to take out a loan; they do so because JAK aligns with their own life ideology or some of them want to be active in an organisation that actively tries to reshape society. Therefore, the highest membership fee is not a requirement for securing a loan, per se.

Loan Repayment: The member is required to repay the loan on an amortized basis, that is a portion of the original loan divided equally over the months of the loan period. This is akin to paying only the “principal” on a conventional bank loan.

After-Savings: A regular saving that the borrower has to make during the repayment of the loan. During the life of the loan, the member is obliged to replenish the liquidity in JAK (providing balance in the system) that he or she has used to benefit from the loan through a regular monthly savings schedule. This is called **After Savings**. The amount of regular *after savings* required depends on whether the member pre-saved prior to the loan. If the member has no pre-savings going into the loan, they would have to save the same amount as the regular loan repayment schedule. If they have pre-savings, the *after savings* is reduced by a factor related to the pre-savings. The after savings deposit is released for withdrawal when the produced savings points (during the loan repayment period) equals the used savings points.

Savings Points: Savings points are a key instrument by which JAK manages member savings and loans, thus manages its liquidity. You get saving points for your saving efforts (e.g. One dollar saved for one

JAK Saving Point Formulae:

$$\text{Saving points} = (S + (S \cdot M)) / 2 \cdot M$$
$$\text{Saving points} = S \cdot M \cdot SF$$
$$\text{Loan} = (2P (F+1)) / (A+3)$$
$$\text{Basic loan} = 2P / (A+3)$$
$$\text{Additional loan} = G \cdot F$$
$$\text{After savings} = LF / (1+F)$$

S = Saving/deposit
M = saving period
SF = savings factor
A = repayment period (months)
F = allocation factor
G = basic loan
L = total loan
P = saving points
T = additional loan

month yields one saving point). And one dollar borrowed for one month consumes one savings point. Thus savings points are used to ensure the sustainability of the system. Savings points are earned by the member on savings that accumulate prior to exercising the loan option and on savings accumulated during the loan repayment period.

A formula is used to estimate the savings points using both a **Savings Factor** (determined by JAK management based on liquidity calculations) and the time of savings prior to the loan. Savings points are also earned during the loan repayment period. In essence, the monetary amount of the loan is equated with a stock of savings points which are consumed or used up during the loan repayment period. This helps JAK keep track of the production and consumption of saving points for every member making it possible for JAK to supervise the aggregate system and do the checks that are needed in order to avoid liquidity crisis. JAK keeps track of the total sum of points on all accounts in the system, pre-

saving accounts, after saving accounts and loan accounts. During the first years of the 90-ies the system accumulated a big saving points deficit but after the lowering of the savings factor to 0.7 on base accounts the deficit is now only 1.4 billion (10 percent of what it was then).

Allocation Factor (F): Historically (prior to 2003) the amount of money available to loan out was determined by JAK management using what is called the **Allocation Factor (F)**. The Allocation Factor (F) was set depending on the amount of reserves and the rate of deposits, withdrawals and loans. The JAK board fixed the **allocation factor (F)** monthly and this determines how large the loans can be. The more money in the pool and the quicker it comes in, the higher F will be. F can vary between 0 and 19, and has averaged 15 over the last few years. What F actually indicates is the relative size of the after-savings pool of all members. Historically, the maximum amount of any individual loan was proportional to the members accumulated savings points plus an amount that is determined by JAK management using what is called a **allocation factor** (essentially a formula for determining how much cash exists in the system from total member savings that can be distributed to a meet a member’s loan request). This system is undergoing changes that will be explained later on in this report. The distribution factor, historically, has been the key instrument for determining how large of a loan can be given to any member with a given amount of money pre-saved. For example, the distribution factor has been 15 for several years which meant that a member could receive 15 times the amount of a base loan they were entitled to with only pre-saving points. In order

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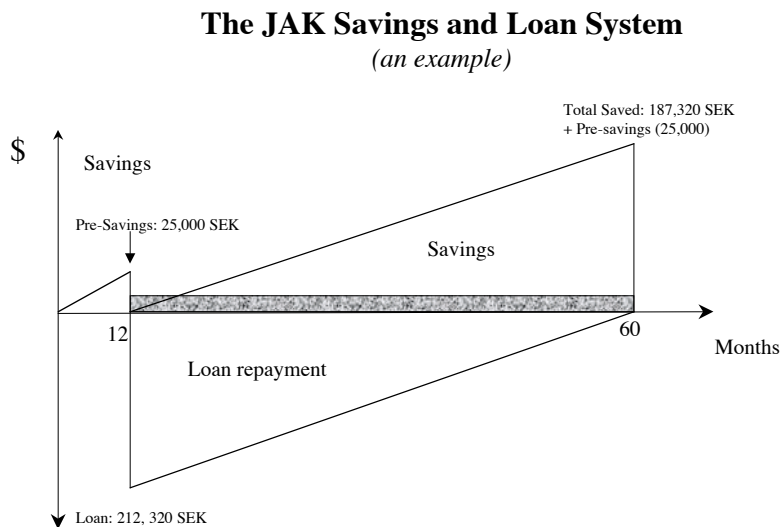
to get the benefit of the distribution factor (i.e. a larger loan) you have to agree to produce the savings points that your additional loan will consume, during the repayment period. As of November 2003, the Allocation Factor will no longer be used in favour of a new JAK savings-loans system which is described below.

End of the Loan: Roughly three months after the final repayment of the original loan is made, the JAK member is allowed to access the accumulated pool of savings. When the loan is repaid and the sum of savings points total is equal to the consumed savings points total, the deposited sum of after-savings is moved to the pre-savings account and the accumulation of savings points resumes. The member has the option of withdrawing the total amount of savings or keeping the money in JAK to benefit others or to be used as a basis of future lending. At this point all of the savings points have been used up in the process of repaying the loan and the member could begin a new loan cycle, again by earning savings points on new savings thus qualifying for the next loan. In the process of repaying an interest-free loan, the member has also accumulated a pool of savings equivalent to the original equity of the loan!

Insurance against liquidity crisis: In order to provide added security to JAK members and their savings, JAK adopts a policy of investing a minimum of 20% of the value of savings in Swedish **Treasury Bills**. This healthy reserve protects member savings in the event of a potential, unexpected run on the bank.

D1. A JAK Loan by Example

Figure 2: Example of a JAK Loan



Let's look at an example of a new member and a new JAK loan. The first step a new JAK member must take is to purchase a membership in the JAK for 200 SEK (C\$35): one share gives the member one equal vote in the annual general meetings in which the Board is elected. The membership is really an equity share in the bank and is paid annually.

The second step is the new member opens up a bank account with JAK making an initial deposit. At this stage a member is technical eligible to apply for a loan. Traditionally, members were required to save for a minimum of 6 months before being considered eligible to apply for a loan. However, under the new system, introduced in September 2003, this requirement will be relaxed (we will explain the new system further on in this report). As a member builds up his or her pre-savings account they are earning what is called **pre-savings points**. In our example, the member pre-saves a total of 25,000 SEK (C\$4,315) over 12 months (about 2,083 SEK per month or C\$ 360 per month).

The pre-savings points earned are based on a formula:

Pre-savings Points = Total amount saved * number of months of saving * Pre-savings Factor (PF) of 0.7

In our example:

Pre-savings Points = 25,000 SEK * 12 months * 0.7 = 420,000 points

The Pre-savings Factor is determined by JAK management in consultation with the Board of Directors. The Pre-savings Factor is adjusted according to liquidity risk and depends on the relationship between total savings (deposits), outstanding loans and current demand for new loans.

The member is now in a position to apply for a loan. The key factors which the member must consider in their decision is the amount of disposable income they anticipate over the life of the loan; enough to pay both the principal of the loan plus equivalent saving installments plus the annual loan fee. In addition they have to have enough income to pay the 6% deposit fee on the value of the loan. Committing to both loan principal repayment can be onerous depending on the households income profile. Generally, middle to

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higher income households are most likely to have the ability to make such a commitment while poorer households will be limited. Moreover, many of these households may already be indebted to other conventional banks in terms of mortgages, car loans, student loans or credit card debt.

JAK management must also assess the member's loan request in terms of how much available liquidity (savings) are in the whole JAK system that can be safely loaned to the member without risk of a liquidity crisis. The relationship between savings and liquid assets (e.g. Treasury Bills) are carefully managed and calibrated on a regular basis. Fortunately, a healthy reserve of Treasury bills (no less than 20% of the value of the total pre-savings amount) is maintained as insurance against potential run on the bank or liquidity crisis.

D2. How is the size of a JAK loan determined?

The ultimate decision on the size and duration of the loan are made by JAK's professional analysts and bankers based on a careful and regular assessment of the available total liquidity (savings) in the bank. JAK management continually assesses the liquidity in the system. They do not use a formula, per se (though historically formulas were used reflecting the influence of an engineering mentality amongst the early founders of JAK). Currently, JAK management act just like other bankers making daily judgments about the health of the banks liquidity and sensitive to the needs of individual members and the collective membership in making their assessments. Decisions are made based on past experience and a sense (feelings) for people and the financial figures.

As with other bankers, JAK is sensitized to the members capacity (i.e. individual and household income and socio-economic conditions) to commit to a repayment and savings routine during the loan repayment period are critical. Historically, member commitment has been high with very low levels of loan defaults.

Each loan is considered on an individual basis, negotiated between the member and JAK officials. Liquidity (the amount of money that can be lent out every month) is regularly assessed to determine what amount of lending can be sustained. Each loan can be customized according to the desired length of the loan, the desired principal repayment amount, and other issues such as the members income capacity to both repay the loan over time but also to save an amount that will rebuild the liquidity pool in the amount equivalent to the original amount of the loan.

JAK continually assesses and calibrates the relationship between the pool of savings and the outstanding stock of loans to determine what new loans can be made available to members or new members. JAK also carefully monitors the inflow of cash in the form of savings, loan payments and loan fees to ensure there is a sustainable stream of payments in and out of the bank. The amount of savings (both pre savings and post-loan-savings) and the flow of saving payments are all critical in determining the additions to the stock of loans. In principle it is simple and in practice the delicate balance between savings and loans are stable as long as circumstances are "normal".

D3. THE NEW JAK Savings and Loan System

In 2003 the JAK Board approved a new JAK savings and loan system (see *Rational for New Savings and Loan System* by Oscar Kjellberg). While most of the features are the same as the old system, key difference is that pre-savings are no longer required (they are optional) to qualify for a loan, whether by new or current members of JAK (Figure 4).

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be abandoned in November 2003, and pre-savings will become optional. Without the complication of the pre-saving requirement, loans the JAK system will be easier to understand and easier to explain - which is important since the system is spread mainly by members talking to others.

3. Three criterion will help determine if loans can be granted: a) the members financial security (liquidity and loan deposit) b) the member's ability to repay the loan and c) the supply of liquid assets in the bank.
4. Members who choose to pre-save can earn pre savings points during the pre loan saving period to reduce the need to save during the loan repayment period. The bigger the accumulation of savings points before the loan the lower the monthly payments will be during the repayment period.
5. The members have the entire disposal of their pre-savings points. They can therefore decide if their savings points shall be used for reduction of the payments during the repayment period, be given away to another member or be saved for future use.
6. The new rule does not change the workings of the Support-the-Local Accounts. The supporters use the accounts to support local projects financially but without taking the risk as a lender of money. The saving points produced by their support savings are given to the local project that gets a loan from the bank. This eliminates the need for the project to save during the repayment period and thereby reduces the monthly payments to the bank.
7. The bank also has two saving point funds that are used to back up particularly important purposes. A "**general fund**" and a "**women's fund**" -- designed to encourage women who have given up asking commercial banks for loans for their small businesses. In both cases the loans are given only to projects that supports the local community's ecological, social or economic well-being objectives.

Period of amortization

The average period of repayment of a JAK loan is approximately 11 years. It has increased from 9 to 11 years during the last 5 years. The amortizations times are generally speaking relatively short considering that a majority of JAK loans are for housing purposes (home purchases, building and home improvement).

There may be several causes for the short period of amortization but it is likely that the following is part of the explanation:

- The accumulated savings points restricts both loan and period of amortization
- The longer the period of amortization the longer one has to wait for the after savings to be available for withdrawal
- You want to become debt free as soon as possible

In other words, there is an incentive to repay the JAK loan as quickly as possible.

A major part of the new rule is that a high rate of turnover shall be maintained in the system. Longer periods of amortization shall be discouraged and even restricted by JAK management. The goal is to keep the average period of amortization between ten and eleven years for all members.

Another way of controlling the period of amortization is to let it be guided by the purpose of the loan. A loan to finance a car should not be longer than five years while a home ownership loan might be 10 years.

The examination of the purpose of each members' loan by JAK employees (loans managers) will be critical in ensuring a healthy degree of liquidity in the whole system. In situations where this is insufficient to ensure a healthy liquidity, more stringent control measures may need to be employed. The pool of money (liquidity) that can be lent out shall be determined one member at a time based on demand. Loans could, for example, be stratified according to both the amount of the loan requested and the amortization period and

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the maturity profile of the stock of all loans by directing more of the liquidity flow to periods with higher liquidity risks. If there is a period with a higher liquidity risk a few years is expected more loans with shorter periods of amortizations would be encouraged and granted so that more liquidity is transferred to the weaker liquidity period.

The supply of loanable funds (accessible liquidity)

All loans are internally financed by the deposits of the members and the equity of the bank.

Loanable funds are increased by pre-savings, loan repayments, after-savings, interest income on treasury bills and loan fees. They are decreased by withdrawals of ordinary deposits and loan equity deposits. The loanable funds are restricted by the minimum level of liquidity that is set a minimum of 20 percent of the total sum of pre-savings.

The new JAK rule for savings and loans is directed towards a simpler system and better control of the liquidity. It is accomplished by having the allocation of loans be guided directly by the projected liquidity and by a greater control over the future loan amortization period.

In the old system, liquidity was controlled by using the Allocation Factor for all loans that would limit the maximum saving points consumption for every loan applicant. In the new system the JAK member has more flexibility in defining the terms of one's loan by adjusting the loan amount and the period of amortization to suit one's need and capacity to repay the loan.

Under the old rule, the maximum loan was determined by the formula:

$$2 * \text{the Saving Points} * (\text{Allocation Factor} + 1) / (\text{Period of Amortization} + 3)$$

The board of managers stipulated the Allocation Factor (F). Within this frame of limitation the member could vary the loan and the period of amortization according to his needs and capacity to pay.

The new rule has increased the need for more sensitive liquidity planning tools.

Possible liquidity effects of the new system

The following section projects the potential impacts of the new system, based on historical trends.

Pre-savings

The growth of pre-savings has been steadily rising growing at almost 14% in 2002. Monthly variations from 1996 and onwards have been between 3 and 5 million SEK. The historical year-end balance of pre-savings is shown in the following table.

Year (December year-end)	(million SEK)	Annual growth rate (%)
1996	241 .000	
1997	239.000	-0.8%
1998	251.224	5.1%
1999	261.030	3.9%
2000	268.467	2.8%
2001	315.883	17.7%
2002	359.851	13.9%

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Period of amortizations

Estimating the amount of liquidity generated by pre-savings for the period 2003-2004 is shown in the following table.

Quarter	2003:1	2003:2	2003:3	2003:4	2004:1	2004:2	2004:3	2004.4	Sum
Amount (million SEK) per amortization period.	13.8	24.3	20.3	19.9	18.9	18.4	17.7	17.1	150.4

This amounts to a system that generates SEK 150,4 million in loanable funds during this period. Additional liquidity will come from after-savings during the amortization period of new loans granted during the period.

After savings

Projecting anticipated after-savings, the following table shows the flow of after-savings into the pool resulting from new loans and after-savings withdrawn from the system after members have repaid their loans.

Quarter/Million SEK	2003:1	2003:2	2003:3	2003:4	2004:1	2004:2	2004:3	2004.4	Sum
After-savings in	10.2	16.3	16.1	15.9	15.2	14.9	14.4	14.0	117.0
After-savings out	3.5	6.8	11.7	10.8	11.5	10.6	11.7	10.1	76.7

This example estimates 117.0 million SEK is supplied as payments on after savings and 76.7 million SEK is withdrawn from the system by the release of after-savings and withdrawal by members. The net effect is an addition of 40.3 million SEK to the total liquidity pool. On top of this comes the payment of after-savings for new loans granted during the period.

Loan equity deposits

In addition, during 2003 loan equity deposits are projected at 4.5 million SEK with counteracting refunds of 3.5 million SEK the year after. All new loans generate loan equity deposits equal to 6 percent of the granted loans.

Income from treasury bills

Interest income from JAK's stock of Treasury Bills has generated the following flow of income between 1999 and 2002 as the following table shows:

Year	(million SEK)
1999	2.800
2000	3.200
2001	4.300
2002	4.800

One of several purposes of the simplified JAK system was to decrease the over liquidity required and thereby the income from treasury bills in favor of increased loan fee income.

Loan fees

The normal variation in revenues from loan fees does not change under the new system and only has a marginal effect on liquidity.

Forecast for the liquidity

Liquidity can be projected or forecast based on the payment streams in the savings-loan contracts. While pre-savings are not contracted a projection can be made based on historical experience and anticipating new member response to the new system. The following estimates the liquidity stream for the period ending December 2004, with the following assumptions.

Assumptions:

- Every years new lending increases by 160 million SEK in new loans.
- Average period of amortization is 10 years.
- Pre-savings increase by 1 million SEK per month (historically it has been increasing at 2 million SEK per month).

Based on these assumptions JAK projects the following liquidity budget for 2003-2004

Figure 4:Liquidity projections for 2003 - 2004

Liquidity Table
(million SEK)

Liquidity Brought Forward March 6, 2003	128.5										
	Wk. 11-03	Wk.12-03	Wk. 13-03	Q 2-03	Q 3-03	Q 4-03	Q 1-04	Q 2-04	Q 3-04	Q 4-04	Sum Total
After-Savings In	1.0	1.0	1.0	19.9	19.7	19.5	18.8	22.1	21.6	21.2	145.8
After-Savings Out	-1.2	-1.2	-1.2	-6.8	-11.7	-10.8	-11.5	-10.6	-11.7	-10.1	-76.8
Amortizations (Repayments)	1.5	1.5	1.5	28.3	24.3	23.9	22.9	26.4	25.7	25.1	181.1
The System Generates	1.3	1.3	1.3	41.4	32.3	32.6	30.2	37.9	35.6	36.2	250.1
Loan Equity Deposits Out				-4.3					-3.5		-7.8
Pre-Savings Changes	0.5	0.5	0.5	3.0	3.0	3.0	3.0	3.0	3.0	3.0	22.5
New Loans	-3.0	-3.0	-3.0	-41.0	-41.0	-42.0	-40.0	-40.0	-40.0	-40.0	-293.0
Loan Equity Deposits In	0.2	0.2	0.2	2.5	2.5	2.5	2.5	2.5	2.5	2.5	18.1
Liquidity 1	126.2	125.2	124.2	130.1	122.6	118.7	114.4	117.8	115.4	117.1	
Member Fees				3.0	0.5			3.5	0.5		7.5
Interest Income				1.3	1.3	1.4	1.0	1.0	1.0	1.0	8.0
"Own Payments" (Bank Expenses)	-1.0	-1.0	-1.0	-5.5	-5.5	-5.5	-6.0	-6.0	-6.0	-6.0	-43.5
Loan Fees	0.2	0.2	0.2	0.5	0.5	0.5	0.5	0.5	0.5	0.5	4.1
Miscellaneous											
Liquidity 2	125.4	124.4	123.4	129.4	119.4	115.1	109.9	116.8	111.4	112.6	
Granted yet not paid Loans											
Payment Reserve	-74.0	-74.0	-74.0	-75.0	-75.0	-75.0	-76.0	-76.0	-77.0	-78.0	
Liquidity Surplus ("Lending Capacity Beyond Surplus")	51.4	50.4	49.4	54.4	44.4	40.1	33.9	40.8	34.4	34.6	

According to the budget JAK projects a surplus of liquidity of 41.1 million SEK by the end of 2004 assuming 160 million SEK in new loans is granted during 2003 and 2004 (i.e. 320 million SEK (the budget predicts 293 million SEK since 27 million SEK already has been granted). This means that JAK should be able to grant an additional 41.1 million SEK in new loans.

You can also say that based on these projections that JAK could potentially lend 334.1 million SEK to the end of 2004 (293.0 million + 41.1 million SEK). This is the amount available to allocate to the members as members parts and savings parts.

Supply of loanable funds

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One of the most important tasks in the simplified system is to estimate the supply of loanable funds during the manageable future period. Based on this estimation it will be possible to decide the size of the member-part of the loan and how much there is left to be used for the savings-part. It is important to stabilize these concepts so that the members feel that they can trust the bank and the savings and loan system.

The available amount for lending can be calculated based on the liquidity projection that is updated every morning in order to present the actual liquidity every day and its likely development.

The main uncertainty in the projections is tied to the anticipated amount of pre-savings. The assessment has to be based on the history of the pre-savings and influenced by expectations concerning the savings behaviour (boom or recession, rate of employment, rate of inflation, deflation, war and peace) of new and current members.

Members-part of the loan

The member's part is the part of the loan that each member can get whether he/she has been pre-saving or not. It is a condition that the loan can be repaid and that a guarantee can be made for the loan.

The purpose of the member's part is to increase the possibility of the members that find it difficult to accumulate the pre-savings points that up to 2003 has been required for a loan. The amount of the member's part should therefore be decided with this taken into consideration.

There are, however, other effects in the system that also need to be considered. The bigger the member's part, the smaller the incentive to pre-save since the members part is granted irrespective of any pre-savings. And as the pre-savings is essential for the growth of the system there has to be an obvious and strong stimulus.

Frequent or large changes in the member's part will probably create apprehensions but somehow we do need to find the appropriate level where there is a trade off between the supports for those that find it difficult to pre-save and the incentive to pre-save.

Two different criterions can be used as a point of departure for the assessment of the suitable initial size of the member's part:

1. The average initial loan is currently SEK 100,000
2. Approximately 80 percent of the current loan applications are for less than SEK 200,000

JAK therefore recommends that the member's part initially is SEK 150,000 partly because we will then meet the need of a large group of members and partly because we thereby will save time because of a fewer number of loan applications that also covers the savings part. In the beginning JAK will need time to gather experience, develop routines and get into the way of the things.

Savings part

The savings part is granted because pre-savings have been performed. Several factors can be used to influence the allowance for instance the applicant's number of years as a member. However we recommend that the savings part be allocated in relation to the savings points accumulated during pre-saving.

Control columns

There are now two control columns: allocation number and savings factors for the pre- and after-savings.

According to the simplification proposition the allocation number will be dropped as control column. Three new controls will be used instead:

1. Guidance and rules for the period of repayment of a loan

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2. The monthly liquidity pool, if required divided into different pools for different periods of repayment
3. The member's part
4. The savings factors for pre- and after-savings

Currently the JAK Board decides upon the savings factors and allocation number at every board meeting. The decisions are based on information the use (demands) of the system and the liquidity position of the bank.

When the allocation number is dropped the board has to decide about the amount required for the member's part based on the liquidity assessment and desired returns to the bank. When appropriate the board will issue instructions about the liquidity risk and call a board meeting in case of drastic liquidity changes.

Sensitivity analysis

These simplified rules differ little from the previous system. JAK would immediately lower the Distribution (allocation) Factor (F) to zero if JAK, for some reason, should find that the total sum of pre-savings dropped to SEK 100 million in a few days.

If, instead, the rules were simplified by the scrapping of the Distribution Factor (F) JAK would react by decreasing the member's part to zero or close to zero. All lending would then be in form of savings parts and within the frame of a smaller monthly liquidity pool.

D3.2 The Rational for a New JAK New Savings and Loans System?

(The following description is presented by Oscar Kjellberg, past-CEO of JAK Members Bank, with editorializing by Mark Anielski)

At several AGMs the JAK board had been lobbied by several members to simplify the savings-loan rules to make the interest-free concept more accessible to new prospective members who otherwise found the old system too complicated to understand and to explain. The new, simplified system is called **Scrap F** because it means that the **Factor of Distribution** (distribution factor) between pre-saving and after-saving is scrapped and replaced by more effective system controls.

Part of the reason for this change was that a growing part of the deposits could not be lent out and at the same time there were prospective new members who wanted to take out loans but were prevented by the existing rules; primarily the need to pre-save.

The Board also wished to acknowledge the concerns of some members that had a longstanding request to make it easier to borrow for those who find it difficult to pre-save. There are many members with lower incomes that makes pre-saving difficult along with a commitment to payment and savings. Some of them have been caught in the interest trap of other credit situations (loans, mortgages, credit card debt) that restricts their capacity to pre-save for a JAK loan even though such a loan would be cheaper for them.

Hence, the JAK Board proposed a simplification of the savings and loans rules in September 2002. The proposition was scrutinised in a long and lively debate preparing the way for a final Board decision in August 2003.

“Scrap F”

The following summarizes the proposed changes, which are called “**Scrap F**”:

- All new and existing members can be granted loans to the extent there is sufficient liquidity (savings reserves) in the bank. The monthly liquidity would be assessed on an ongoing basis and reviewed monthly. **Control lever: the amount of money that can be lent out each month (the monthly pot).**

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- New and existing members now have the option to pre-save prior to requesting a loan. It is no longer a pre-requisite.
- Every member shall continue to produce at least as many savings points as he or she consumes by loans. All borrowers must therefore undertake to save, during the repayment of the loan, in order to create this balance between produced and consumed savings points.
- A global system balance shall be upheld within the system between the sum total of members accumulated savings points and the savings points that they will consume by borrowing. The banks rationing of savings points and members borrowings regulate this balance. The rationing of savings points is controlled by the use of a **Savings Factor**. This factor should be the same for all savings (and -1.0 for loans). **Control lever: the savings factor.**
- The bank shall lend money only after a careful analysis of the liquidity risk of the bank. **Control lever: payment periods depending on the purpose of the loan and the future expected supply of liquidity in the bank.**
- The loan consists of two parts. One part is because you are a member (the memberships part) and the other because you have been saving in the system (the savings part). **Control lever: the membership part (can be decreased to zero whereby the system will operate as today).**
- The savings part of the loan is proportional to the amount of savings points that the member has accumulated. Every applicant gets a share of the monthly pot that represent the share of his sum of savings points in relation to the sum of all applicants' savings points.

The scrapping of F will not end the importance of pre-saving

The pre-saving, while no longer a condition of receiving a JAK loan, will remain an important part of the savings and loan system since it provides an advantage to loan recipients by reducing their repayment and after-saving requirement. The proposed simplification of the system by scrapping F does not mean the eradication of the pre-saving as some critics has feared. The aim is only to make the system easier to understand and explain and especially to give members increased opportunities to borrow money. Pre-saving will not be mandatory anymore but we expect them to continue as before since the advantages of pre-saving are unaltered.

Usually the borrowers have been pre-saving but seldom as much as it takes to balance the loan. Therefore one has to undertake to save also during the repayment period. If the rules are simplified so that pre-saving is no longer mandatory and we thereby avoid the concept of F (factor of distribution), we will get a group of borrowers that has not been pre-saving at all, fulfilling their whole savings performance during the repayment period. This group will be supplementary to the pre-saving group. Apart from the current situation with borrowers who are either with or without after-saving (100 % pre-saving) we will also attract a group without pre-saving (100 % after-saving).

Member's motives for pre-saving are well known:

- You save in order to get a loan.
- You pre-save because you know that the bigger the pre-saving performance the less saving it takes during the repayment period.
- You pre-save in order to improve your possibilities to handle an unexpected payment where you can use both savings and loan.
- You pre-save in order to transfer savings points to someone who needs a loan now or in the future.

One of the criticisms of the Scrap F proposal is that a liquidity risk could present itself should all new and existing members decide not to pre-save. That would signify a situation where the members will reduce their pre-saving dramatically and, at the same time, begin to apply for loans on a big scale. However the motives and benefits of pre-saving are not affected by the Scrap F proposal as a control lever and hence there is no reason to expect a drastic decrease in pre-saving by new or existing members.

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Today, the key challenge JAK faces is not a flood of new loan applications, rather the fear is that the current situation, of saving outgrowing the demand for loans, will continue. In fact, if JAK does not improve the possibilities of lending it will eventually be forced to do resort to other measures (e.g. decrease the savings factor).

It is also important to remember that all loan applications have to be granted. The opportunity to borrow without pre-saving should be regarded as a special offer to help certain members in specific economic situations but there are no reasons to believe that more than a small number will actually take advantage of it.

Most members need to pre-save quite a lot to get a reasonable loan that they can handle. There is also the tendency of many members to have savings, which are idle or targeted to no specific goal other than a kind of reserve in case of life emergencies. Therefore JAK expects that pre-savings behaviour will not be negatively affected if they implement the Scrap-F policy. Pedagogically JAK will gain a lot by simplifying an otherwise complicated education process to explain, for example, F: the factor of distribution.

A typical Scenario under the new Scrap F Policy

JAK anticipates the following potential scenario and response by the bank:

A new member asks:

- How much can I borrow?
- When can I borrow?
- For what can I borrow?
- How much do I have to save?
- When do I have to save?

JAK responds:

- Our condition this month is that we have this amount of money available for lending and that many members asking for loans with various amounts and repayment periods.
- The available amount of money is almost enough to give everybody what he or she wants.
- Let all members have a loan where one part is because they are members (the memberships part) and another part because they have been saving (the savings part) and thereby helped others to get a loan in our system.
- The bank shall lend money in such a way that an even flow of payments in and out of the bank is created and the level of liquidity does not sink below the level where we are forced to let members line up and wait for their loans.
- Let the memberships part be x krona (this is an important control lever for the system and will be altered when it is necessary to keep the system in good balance).
- Let the members also have a savings part that is proportional to his or hers savings performance – the more savings points the bigger savings part.
- We can begin by reviewing the demands together with the applicants in order to see how we can best align their requirements with the opportunities of the bank. We cannot grant all demands for long and big loans because of the risk for long queues.
- Some members will realise that they will gain by asking for several shorter and smaller loans instead of one big and long loan.
- Others will understand that they will not be able to have the large and longer-term loan that they had planned either because they have too little savings points or because their household liquidity (disposable income) is too small for the monthly instalments.
- We also need to approve the security that they are offering for the loan.

D4. The Old Loan System

I have provided a description of the OLD JAK savings-loans system, simply to show what progress has been made in JAK's almost 50-year history. It is useful to describe the old savings and loan system, even though it may lead to some confusion and questions.

In the old system (prior to 2003) the pre-saving points determined how big a basic loan you can get. Members had to pre-save for at least 6 months before applying for a loan. When members were ready to borrow from JAK, the Savings Points gained through pre-savings gave them the right to two kinds of loan: A **Basic Loan** and an **Additional Loan**.

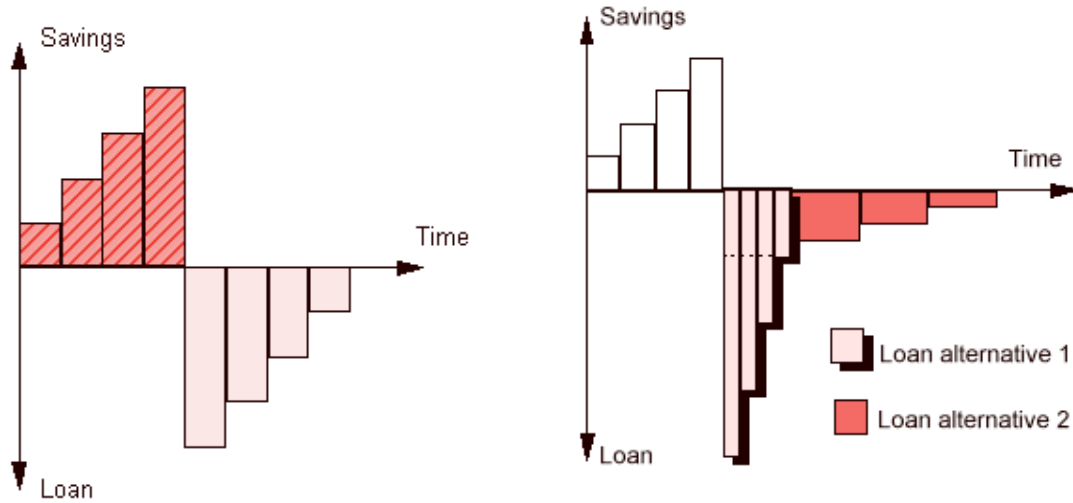


Figure 5 The Basic loan.

The filled-in bars denote savings performance (savings points). One borrows an amount corresponding to one's accumulated savings points

Figure 6. Two basic loans with different repayment times.

Larger repayment installments allow for a larger loan.

The **basic loan** corresponded exactly to the number of savings points one has (See figure 2). The total area under the loan columns may not exceed the total area under the savings columns. It is this requirement that gives balance to the JAK system. The size of the basic loan depended on the members' decision on how quickly one was willing to repay the loan (see figure 3). The faster one can repay, that is, the larger monthly payments one can make, the larger the loan can be (loan alternative 1). Repaying in small amounts will entitle to a smaller loan and a longer repayment time (loan alternative 2).

The basic loan was usually a relatively small amount. It was however, also possible to take a loan which was larger than what one's savings points entitle to. This is called the **extra loan** and required a regular **after-saving** to maintain balance in the system. This means that together with one's quarterly repayments, one deposits a certain fixed amount in a blocked account. One could not withdraw from this after-savings account during the repayment period. But three months after the last installment, the entire amount is available for withdrawal. The **total after-savings are always at least equal to the size of the extra loan** (see figure 4).

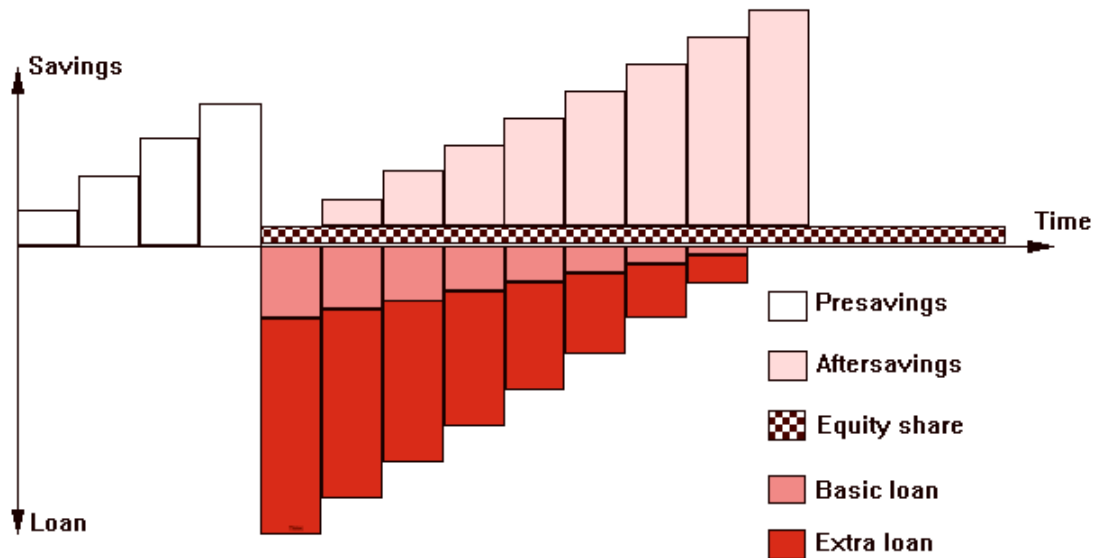


Figure 7: The basic loan + extra loan.

One can take the basic loan, an amount corresponding to the actual savings points one has collected, plus the extra loan, an additional amount determined by the distribution number (= 3 in the above diagram). The extra loan requires that one continue to save regularly during the repayment period. The equity share is explained below.

The amount of the Additional Loan was determined by what is called the Allocation Factor. The higher the cash liquidity of JAK, the higher the Allocation Factor allowed by the JAK Board of Directors. The currently operative Allocation Factor is Fifteen (15), which is high – a factor of Eight (8) or lower is likely to apply in the longer term as more loans are taken out.

A member's right to the Additional Loan was conditional on continued regular saving during the repayment period till the total savings points are in balance with the points consumed by the loan. This means that ***when the loan has been fully repaid, not only has the debt been repaid but there has also been an additional saving equal to the Additional Loan.***

Roughly 3 months after the loan has been repaid, the member is entitled to withdraw their accumulated savings or consider retaining the money within JAK, earning again pre-savings points that would qualify for a future loan.

In the above example of a Basic Loan of 9,555 SEC, if the Allocation Factor is Eight, an Additional Loan of 76,445 SEC (C\$13,146) is made possible, to give a total of 86,000 SEC (C\$ 14,789), for amortization over five years – i.e. $9,555 \times (1+8) = 86,000$.

D5. Other JAK Bank Attributes

D5.1 Accounts in JAK

Idle liquidity in the system is non-productive and should not therefore generate savings points. For this reason and to stimulate long-term savings and give the managers better control over liquidity, a **Savings factor (S)** is set each month by the board and applied to that month's savings points. S reflects the quotient of loans divided by deposits. When lending is large or small relative to deposits, the savings factor will be

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high or low, respectively, varying normally between 0.8 and 0.9. A higher S is applied to funds deposited in JAK's long-term accounts of which there are two types:

- The **Goal Account** is for regular savings. The maturity period is at least two years and deposits are made by automatic transfer of a certain amount each month. Withdrawals are allowed with six months notice.
- The **M-24 Account** is for one-time deposits. The maturity period is at least two years. Withdrawals are allowed with two years notice.

Under normal circumstances, there are no restrictions on deposits or withdrawals in the **Open Account**, but the S applied is lower.

Deposits are made by means of Post Giro, Bank Giro or Auto Giro and withdrawals can be made only to a predetermined bank account or by means of a payment slip.

It is possible to earmark one's savings so that they are only loaned out to environment-friendly projects, the financing of studies, projects that promote mental or physical health or similar ends. The same requirements apply to one's own loan, however.

D5.2 Transfer of Borrowing Rights

Savings points can be freely transferred without exception. In this way, members can support each other by giving away or loaning out their borrowing rights. The buying and selling of savings points goes against JAK's principles, however, and is strictly discouraged.

Another way to support a fellow member with savings points is by means of the so-called **C-loan** whereby one can sponsor a project financially without risking one's money or dealing with the bothers of administration - JAK takes care of it. One (and perhaps others) deposits a certain amount in a blocked account and the C-loan recipient may then borrow that amount. The blocked account is opened for withdrawal after at least one-half of the repayment time has passed.

In contrast to other forms of savings and loan systems, borrowing rights are retained even if one removes all one's money for a time or even for good (provided one remains a member). Before a loan is granted, however, there must be at least 6% of the loan amount in one's account.

D5.3 Liquidity Placement

Twenty percent of all deposited pre-savings are kept liquid to assure payment readiness. This money is kept in a bank account and in short-term government bonds (Treasury Bills). The interest income that comes in is used to cover operating expenses and keep loan fees down.

D5.4 Deposit Protection

JAK has been granted a banking license under the new law for Member Banks. Upon registration, the bank deposit insurance program will cover all pre-savings. A large part of the equity consists of shares at 6% of total outstanding loans that all borrowers must set aside upon receiving their loan. This sum does not generate savings points during the repayment period and is paid out 7 - 19 months after the loan is repaid. By means of the equity shares, the borrower covers possible losses in proportion to the size of his own loan, which reflects the risk he himself presents to the system.

JAK also maintains a healthy reserve of Treasury Bills and other liquid asset investments to the targeted amount of 20% of the total pool of member savings. This provides considerable security against a potential bank run or liquidity crisis.

D5.5 Security

JAK requires 100% security in Sweden for all loans. Acceptable collateral is mortgage deeds in real estate (100% of assessed value or 70% of market value), personal guarantees from at least two guarantors, bank guarantees, and bond depots. A guarantor can go surety for at most one third of his gross yearly income. With assessed property, the guarantee can be increased.

D5.6 Borrowing Procedures

Historically, any member who fulfilled his savings obligations and has satisfactory collateral is entitled to borrow (unless the member has bad payment marks within the last 3 years). This will change with the new "Scrap F" system as new members will be entitled to apply for a JAK loan, conditional on the determination of JAK management as to the available liquidity (distribution factor) available for lending. New members can still make pre-savings in advance of a loan, but this will no longer be a firm obligation. However, new members will have to commit to after-savings, just as in the old system.

The borrowing procedure goes as follows: An "Application for Loan" form is sent in whereupon one receives a loan offer with information on savings points. With this as a basis, a number of loan alternatives with differing loan amounts, repayment times and distribution numbers are listed one of which is chosen.

When the loan is granted, one signs a promissory note and provides collateral for the loan. The money is then paid out. One's savings may also be withdrawn at this time - minus the 6% equity share.

Handling time can be around one month before the loan is paid out. When the loan is repaid, one gets back the promissory note and the papers that comprised the collateral. The after-savings are available three months after repayment and the equity share is paid out 7 - 19 months afterwards.

JAK does not offer financial counseling, skills training, networking, legal counseling or follow-up.

D5.7 Local Enterprise Banks

JAK is branching out to establish subsidiary Local Enterprise Banks (bygdebanks). The aim is to counter the way in which established banks are channeling savings from rural regions to the urban centers and abroad.

Behind the growing disinvestment in the rural regions is the global deregulation of banking in the 1980s, by which mergers have been forced on the major banks, with consequent staff reductions and branch office closures.

Sweden has a long history of local savings banks that have been of genuine service to the local community. However, under the now dominant globalization imperative the small savings banks have not been able to hold their own, and local enterprises are finding it increasingly difficult to raise finance.

The globalization crisis is seen by JAK as an opportunity to fill the gap left by the more traditional savings banks that have gone out of business or been swallowed up. JAK is able to provide the people of the countryside with a renewed means of self-finance because of the way it has matched its decentralized, voluntary membership network and its highly centralized, state of the art banking system.

This is how the Local Enterprise Banks scheme works: Where a local group wanting to support a local enterprise has not been able to raise the money through an established bank, they now have the alternative option of opening a Local Enterprise Bank (LEB) account with the JAK MEMBERS BANK. Their savings will then go into the LEB account and JAK will use those savings as the base for financing the local project. See Savings and loans for a more detailed description of how the interest-free system works. All savings are protected by the national bank deposit guarantee – see Background – and JAK naturally carries the credit risk.

D5.8 The First Local Enterprise Banks

Two Local Enterprise Bank (LEB) accounts were opened in 2000 and three more were in the pipeline for 2001-2002. The JAK membership is enthusiastic about this development.

The first LEB account is for a small ecological slaughterhouse called Ekokött, which has applied ethical standards to the transport and treatment of animals – see www.ekokottbohuslan.se The Ekokött slaughterhouse serves the small farmers of the coastal region and islands of Bohus Province, north of

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Goteborg. Support for Ekokött has come from local environmental groups and the Swedish Society for the Prevention of Cruelty to Animals, amongst others. A number of small farmers in the region have also switched their savings to the Ekokött LEB account, because the slaughterhouse has made it possible for them to raise their cattle in the traditional, ecological sound way in enclosed common grazing grounds.

The second Local Enterprise Bank was started by Hornbore village www.hornboreby.o.se to financially support a replica that has been built of a Viking village from the year 1000. This combined cultural, youth, and Eco-tourist project is important for local community building. When the local savings bank refused to lend the money needed for the project, the JAK Members Bank stepped in. An interest-free loan is being financed through savings that have been switched from other banks to the Hornbore LEB account.

D5.9 Staying in Touch

The JAK MEMBERS BANK has been built up on the strength of its 25,000 and more members, who are one and all for a just and fair economy.

Membership contact is maintained through 350 voluntary representatives working through 24 regional offices. The local representatives help other members make up their savings and loan plans. They also organize study groups, action groups and exhibitions. The branch offices are not involved in banking as such, which is centralized at the Skövde head office.

There is a quarterly magazine for members called Grus & Guld (Gravel & Gold), which reports on the activities of the local branches, serves as a forum for open and lively discussion between JAK members and management, and offers in-depth articles about issues related to personal finance and JAK's vision of a just and fair, sustainable economy for all.

Through its savings and loan program and its efforts to spread information about the ill effects of interest on money, JAK is working actively to promote a sustainable economy that does not exploit people or nature.

The contact address to get in touch, and stay in touch, with JAK is: JAK MEMBERS BANK Vasagatan 14, 541 50 Skövde SWEDEN Telephone: 0500-46 45 00 Fax: 0500-46 45 61 E-mail: jak@jak.se

D5.10 International Connections

There is growing international interest in the JAK system of interest-free banking, and JAK is giving more attention to participating in international discussions on local enterprise initiatives, alternative currencies and other aspects of monetary reform. JAK members are also taking an interest in making their savings available for interest-free loans and risk-sharing projects in the Third World.

JAK is not seeking partners for an international expansion, however. If you and others are interested in starting a similar banking system to JAK in your own country, the JAK management team will be as supportive as it can be with its limited resources.

E. What is JAK's Comparative Advantage Over Conventional Banks?

JAK's key comparative advantage over other banks is that it saves its members interest charges on loans which conventional banks charge. JAK also offers the benefits of being a cooperative enterprise where members have one vote in decisions of board governance.

How does the cost of a JAK loan compare to conventional bank loans? Using the JAK loan calculator (Figure 7), developed by Börje Johansson and modified by Bengt Landegren, it is possible to compare the full costs of a JAK loan with a conventional bank loan. It also compares a JAK loan with a conventional bank loan to reveal the actual net savings in interest costs realized by a JAK member.

Figure 8: The JAK Loan Calculator: Example: \$20,000 loan (JAK vs. Conventional Bank Loan)

JAK MEDLEMSBANK		Loan calculator	
Calculate your saving points		Scroll to get the loan	
One single deposit	0 kr	you wish	\$20,000.00
Monthly deposits	0 kr	Loan equity deposit	\$1,200.00
Time of deposit (months)	0	Loan fee	\$2,701.29
Sum of saving points	0	Loan fee per month	\$22.51
Add existing saving points	0	Repayment of loan per month	\$166.67
Scroll for repayment period	10	After savings per month	\$166.67
		Payment per month	\$355.84
		Payment per Q	\$1,067.53
		Sum total of after savings	\$20,000.00
Comparison between a conventional loan and a JAK loan			
Borrowers annual service fee	\$40.00	Size of bank loan	\$20,000.00
Estimated interest payment	8.05%	Cost (interest) of bank loan (annuity loan)	\$9,708.75
		Cost per month	\$80.91
		Payment per month	\$247.57
		Cost of bank loan (straight loan)	\$8,651.25
Net Savings of a JAK Loan versus Conventional Bank Loan			
		Cost (loan fee) of JAK Loan	\$2,701.29
		JAK Annual Membership Fee	\$339.27
		Subtotal JAKLoan Costs	\$3,040.56
		Cost (interest) of conventional bank loan (annuity loan)	\$9,708.75
		Annual service fees	\$400.00
		Subtotal Conventional Loan Costs	\$10,108.75
		Net Cost Savings with JAK Loan	\$7,068.18
		Estimated Life Energy (days working) saved	80

In my example, I compare the costs of a \$20,000, 10-year JAK loan with the cost of a conventional mortgage bank loan of \$20,000, 10-year amortization period at the current 8.05% rate of interest.

In the case of the JAK loan, a Loan Equity Deposit of \$1,200.00 is paid upfront, refundable 3 months after the last loan repayment is made. The sum of Loan Fees paid over the 10-year period total \$2,025.97 spread over the life of the loan (61 months or 5 years); that is, a monthly loan fee payment of \$22.51. The monthly loan repayment is \$166.67. The member also saves the same \$166.67 per month (assuming the member has no pre-savings in his or her account prior to receiving the loan; if they did, the savings requirement would be lower by the amount of pre-savings). The member also pays an annual membership fee over the life of the loan which totals \$339.27. The total cost of this JAK loan is thus \$2,365.24. Without any pre-savings in advance of the loan, the member is also obligated to make monthly savings of \$125.00 (the same amount as the loan repayment). These savings accumulate over time but are not accessible by the member until 3 months after the last loan repayment has been made. At the end of the loan period (10 years and 3 months) the member would have a total of \$15,000 in savings available for withdrawal or maintaining a JAK savings account for financing a future JAK loan.

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I then compare the total costs of a JAK loan with the interest and other costs of a conventional 10-year mortgage bank loan (e.g. a 10-year, Toronto Dominion Bank mortgage at 8.05%: current market rate). The cost of interest alone is \$7,381.56 plus an estimated total annual banking service fee (associated with the loan) of \$400.00 would total \$7,781.56.

Compared with the cost of a JAK loan (\$2,365.24) the JAK member would have saved themselves \$5,416.32 in interest costs alone! We have estimated that this dollar value would amount to the equivalent of 62 days of working at an estimated Canadian hourly “living” wage of \$11.00/hour. That means roughly three months of time that would otherwise be available for other life-giving activities.

Figure 9: JAK Loan Costs vs. Conventional Loan Costs

JAK Loan vs Conventional Bank Loan comparison at different rates of interest but constant monthly payment

A loan of \$ 65 000

Interest-rate	Monthly payment. ~\$ 500	Total cost of loan
5,75 %	Repayment period 17 months	\$ 38 580
7,75 %	Repayment period 24 months	\$ 80 080
9,75 %	Repayment period 30 months	\$ 137 550
JAK-loan	Repayment 24 months	\$ 17 875

Note: The accumulated after savings deposit of \$ 59 080 is released for withdrawal 3 months after the end of the repayment period.

A loan of \$ 15 000

Interest-rate	Monthly payment ~\$ 200	Total cost of loan
7,75 %	Repayment period 9 months	\$ 6 380
9,75 %	Repayment 10 months	\$ 91 500
11,75 %	Repayment period 12 months	\$ 12 720
JAK-loan	Repayment 13 months	\$ 2 475

Note: The accumulated after savings deposit of \$ 13 630 is released for withdrawal 3 months after the end of the repayment period.

F. Comparing JAK's Operations with a Conventional Bank: VanCity Savings Credit Union (Canada)

The JAK Bank by comparison with Canada's cooperative bank, VanCity Savings Credit Union, is a very efficient operation. Even though JAK is not in the business of "making money" or at least not earning a healthy profit.

VanCity is the largest credit union in British Columbia, Canada and Canada's premier cooperative savings and credit union with over 286,000 members. VanCity is one of the most progressive businesses in Canada and has some of the most progressive corporate social responsibility policies in Canada.

VanCity Savings Credit Union's mission is "To be a democratic, ethical and innovative provider of financial services to our members. Through strong financial performance, we serve as a catalyst for the self-reliance and economic well-being of our membership and community." Its core purpose is "working with people and communities to help them thrive and prosper." And its core values include: integrity, innovation and responsibility.

VanCity is committed to important values including:

- Corporate social responsibility (CSR) which is about living VanCity's values in how they do business.
- Use of social audits to measure how well they are doing at living up to their commitments, and helps in a continuous improvement of performance.
- Commitment to the Co-operative Principles of the International Co-operative Alliance (ICA).
- Doing business in a more responsible way and in ways that that supports social justice, environmental sustainability and economic self-reliance.

VanCity actively participates in the communities it serves through generous donation and sponsorship programmes. It supports the VanCity Community Foundation and subsidiary VanCity Enterprises who work to develop innovative grants and affordable housing respectively. In 2001 it launched the VanCity \$1 Million Award – a grant given annually for a community project. It has also seeded a subordinated debt arm called VanCity Capital Corp. to promote job-creating enterprise in Vancouver and B.C. The membership and community have shown their reciprocal support to VanCity by supporting the credit union's network that exceeds 40 branches and assets of close to \$8 billion under administration.

VanCity and JAK share similar ideals and values. Both are cooperative enterprises and are member-well-being focused. Yet, VanCity, like conventional banks, charging interest on loans and paying interest on deposits and providing a full range of financial services. VanCity does provide alternative, progressive banking services such as discounted (prime +0%) loans towards the purchase of fuel-efficient, hybrid vehicles. They recently introduced the "living by water loans" (with funding from VanCity's Community Investment Deposit program) that offers members who live near water access to a low-fee site assessment and a loan interest rebate for shoreline improvements. VanCity can provide a Living By Water term loan of up to \$10,000 over 1 to 5 years to help you implement these actions. Loans of up to \$20,000 are considered if the environmental value is particularly high. In addition, VanCity offers members an option of investing their money in a special account which pays 0-2% interest (the amount is the discretion of the member) that goes towards building a liquidity pool for low interest loans to less fortunate members of the community [need to confirm the name of this program with Chris Dobrzanski, VanCity].

Table 2 compares the operating income, costs, retained earnings, assets, liabilities and equity of JAK and VanCity for the year 2002. My analysis also compares these figures on a "per member" basis as a means of examining operating efficiencies.

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My analysis reveals that JAK has significantly lower per member operating costs (\$146 per member) compared with Van City's \$1,494 per member. It is difficult to assess whether or not JAK's operations are more efficient for the same level of services compared with VanCity. JAK's services are more limited than the full financial services offered by VanCity. VanCity has much higher revenues with a per member income of \$1,738 compared with JAK's \$168 per member. JAK's net retained earnings were a mere \$22 per member compared to Van City's cooperative model of \$244 per member. Notwithstanding the differences in the scope of financial services offered by both organizations, the cost efficiencies of JAK are impressive and are worth exploring. If JAK were to expand its financial services to include cheque-clearing, ATM and other financial services, similar to VanCity and other banks its operating costs would undoubtedly rise accordingly. However, even so JAK's current ideology of not charging interest would not change nor would their commitment to operating as close to not-for-profit though service fees to cover additional operating costs would likely rise for all members.. Indeed, JAK is currently expanding its services beyond the current savings-loans system by providing cheque-clearing services for its members.

Table 2: Comparison of Operations of the JAK Bank vs. Van City Savings and Credit Union

Financial Performance Comparisons: JAK Bank vs. VanCity Savings Credit Union,
based on 2002 Financial Statements

	C\$ 000	C\$ 000	C\$ per member	C\$ per member
	VanCity Savings Credit Union	JAK	VanCity Savings Credit Union	JAK
Income				
Interest (mortgages, commercial mortgages, other loans)	\$439,257	\$0	\$1,536	\$0
Service Fees	\$57,788		\$202	N.A.
Loan Fees	?	\$2,527		\$101
Membership Fees	?	\$572		\$23
Income from liquid assets (T-bills)		\$769		\$31
Other operating income		\$338		\$14
Subtotal Income	\$439,257	\$4,205	\$1,738	\$168
Expenses				
Interest on savings	-\$208,379	\$0	\$729	\$0
Loan default/credit losses	-\$32,220	-\$48	\$59	\$2
Operating costs (* JAK figure includes amortization and depreciation)	-\$188,282	-\$3,869	\$658	\$144
Distribution to members and community	-\$11,922		\$48	\$0
Subtotal Expenses	-\$440,803	-\$3,917	\$1,494	\$146
Net Retained Earnings by Van City	\$39,571	\$789	\$244	\$22
Assets	\$8,202,820	\$119,123	\$28,681	\$4,765
Liabilities	\$7,864,178	\$106,798	\$27,497	\$4,272
Equity	\$338,642	\$12,064	\$1,184	\$483
Statistics				
Average loan per member			\$ 24,727	\$3,453
Average loan				\$15,880
Average deposit per member			\$ 26,544	\$130
Average interest paid on deposits			2.96%	0
Average interest on loans			6.02%	0
Spread			3.06%	0
Effective rate of interest (loan fee only)				2.93%
Members			286,000	25,000

Source: VanCity 2002Annual Report; JAK 2002
Financial Statements

There are other differences between JAK and VanCity. VanCity's contribution to the broader community of Vancouver and British Columbia is significant. VanCity's annual \$1 Million Award represents a significant gift of net revenues from all of the members to the broader community. JAK has no equivalent since all of the benefits of paying no interest on loans are immediately realized by all members. JAK does, however, encourage members to work together, pooling their savings, to support and finance community development initiatives that share similar environmental and social justice goals as VanCity.

The JAK Members Bank

Because JAK loans require a healthy level of personal income liquidity to both make regular principal payments, plus a regular savings deposit (plus loan fee and membership fee payments), this might limit the clientele to middle class income households who could afford such a commitment. VanCity, on the other hand, might attract a broader socio-economic spectrum of clients.

One of the key strengths of a JAK loan versus conventional bank loans is the certainty which is afforded the JAK loan recipient. A JAK loan is a straight loan where the cost (loan fee and loan repayment schedule) is agreed for the whole repayment period and which does not change throughout the loan repayment period. This is usually not the case with conventional bank loans, which are usually renegotiated on a regular basis (e.g. mortgages). While JAK members do forgo interest on their savings, they also forgo the uncertainty that is typical for conventional loans which becomes an opportunity cost that has to be taken into account when comparing a JAK and conventional bank loan.

The following tables provide more detailed financial statements for both VanCity and JAK for the 2002-operating year.

The JAK Members Bank

Table 3: Van City 2002 Financial Statements (selected items)

Van City Savings and Credit Union 2002 Financial Statement							
\$ 000	\$ 000	\$ 000		\$/VanCity Member	\$/VanCity Member		
Income Statement	Income	Expenses		Income	Expenses		
Interest Income							
Mortgages	\$ 259,314			\$906.69			
Commercial mortgages	\$ 55,939			\$195.59			
Other loans	\$ 105,693			\$369.56			
Cash and securities	\$ 19,819			\$69.30			
Other interest	\$ (1,508)			-\$5.27			
Subtotal	\$ 439,257			\$1,535.86			
Interest expense		\$ 208,379			\$728.60		
Net Interest Income			\$ 230,878			\$807.27	
Other Income							
Service fees, credit cards, wealth management fees	\$ 57,788			\$202.06			
Impairment of Loan							
Loan default and fraud		\$ 32,220			\$112.66		
Operating Expenses							
Salaries	\$ 104,285			\$364.63			
Occupancy	\$ 27,273			\$95.36			
General operating	\$ 56,724			\$198.34			
Distributions to Community and Members							
Community and Van City Community Foundation		\$ 3,745			\$13.09		
Van City Award		\$ 1,000			\$3.50		
Membership share dividends		\$ 2,350			\$8.22		
Patronage rebates		\$ 4,827			\$16.88		
Subtotal		\$ 11,922			\$41.69		
Earnings before income taxes				\$ 54,040			\$188.95
Provision for income taxes			\$ 14,469			\$50.59	
Net Earnings (to Retained Earnings)				\$ 39,571			\$138.36
Statistics							
Members	286,000						
Employees	1706						
Average deposit account payment	2.96%						
Average loan interest cost	6.02%						
Balance Sheet							
\$000							
Assets							
Cash	\$ 943,270						
Loans	\$ 7,071,926						
Other assets	\$ 187,624						
	\$ 8,202,820						
Liabilities							
Deposits and shares	\$ 7,591,664						
Risks							
Derivative exposure	\$ 974,344						
Calculations							
\$ per Van City member							
Income		Normal conditions					
Interest	\$ 1,536						
Service Fees	\$ 202						
	\$ 1,738						
Expenses							
Interest on savings	\$ 729						
Loan default	\$ 113	\$ 59	Average rate of loan default				
Operating costs	\$ 658						
Distribution to members and community	\$ 48						
	\$ 1,547	\$ 1,494					
Net Retained Earnings by Van City	\$ 191	\$ 244					
Average loan per member	\$ 24,727						
Average deposit per member	\$ 26,544						
Average interest paid on deposits	2.96%						
Average interest on loans	6.02%						
Spread	3.06%						

The JAK Members Bank

Table 4: JAK Bank 2002 Financial Statements

JAK Mendelsbank Financial Statements	Suppl			C\$	C\$	\$C/JAK Member	\$C/JAK Member
Balance sheet	discl	12/31/02	12/31/01		2002	2001	
Assets							
Cash and bank balances		20,183,227	16,571,763	3,479,867	2,857,201	139.19	114.29
Treasury bills	8	97,767,659	102,332,686	16,856,493	17,643,567	674.26	705.74
Loans to members (and others)	9	534,278,742	472,716,272	92,117,024	81,502,806	3,684.68	3,260.11
Receivable loan fees	10	<u>74,903,904</u>	<u>56,238,305</u>	12,914,466	9,696,259	516.58	387.85
		727,133,532	647,859,026	125,367,850	111,699,832	5,014.71	4,467.99
		-	-	-	-	-	-
Intangible assets	11						
EDP system		<u>898,713</u>	<u>1,782,563</u>	154,951	307,338	6.20	12.29
		898,713	1,782,563	154,951	307,338	6.20	12.29
		-	-	-	-	-	-
Tangible assets	12						
Equipment		1,659,639	1,448,852	286,145	249,802	11.45	9.99
Land and buildings		<u>5,581,548</u>	<u>5,689,648</u>	962,336	980,974	38.49	39.24
		7,241,187	7,138,500	1,248,481	1,230,776	49.94	49.23
		-	-	-	-	-	-
Other assets	14	514,478	711,675	88,703	122,703	3.55	4.91
Advance payments and accr. income	15	<u>1,472,472</u>	<u>1,276,990</u>	253,874	220,171	10.15	8.81
		1,986,950	1,988,665	342,578	342,873	13.70	13.71
		-	-	-	-	-	-
Sum of assets		<u>737,260,382</u>	<u>658,768,754</u>	127,113,859	113,580,820	5,084.55	4,543.23
Balance sheet, continued							
	Suppl						
	discl	12/31/02	12/31/01				
Liabilities							
Members and others deposits	16	624,644,246	560,211,677	107,697,284	96,588,220	4,307.89	3,863.53
Pre paid loan fees	17	32,980,430	23,512,454	5,686,281	4,053,871	227.45	162.15
Other liabilities	18	1,389,350	4,561,663	239,543	786,494	9.58	31.46
Accrued expenses	19	<u>1,964,605</u>	<u>1,696,911</u>	338,725	292,571	13.55	11.70
		660,978,631	589,982,705	113,961,833	101,721,156	4,558.47	4,068.85
		-	-	-	-	-	-
Untaxed reserves	20	1,615,000	1,115,000	278,448	192,241	11.14	7.69
		-	-	-	-	-	-
Equity	21						
<i>Restricted equity</i>							
Capital contributed by all members		4,196,870	4,431,115	723,598	763,985	28.94	30.56
Capital contributed by all borrowing members		56,012,739	50,757,594	9,657,369	8,751,309	386.29	350.05
Statutory reserve		<u>12,498,609</u>	<u>10,232,298</u>	2,154,933	1,764,189	86.20	70.57
		72,708,218	65,421,007	12,535,900	11,279,484	501.44	451.18
<i>Non-restricted equity</i>							
Profit brought forward		1,169,065	510,866	201,563	88,080	8.06	3.52
Profit for the year		<u>789,468</u>	<u>1,739,176</u>	136,115	299,858	5.44	11.99
		1,958,533	2,250,042	337,678	387,938	13.51	15.52
Sum of equity		74,666,751	67,671,049	12,873,578	11,667,422	514.94	466.70
		-	-	-	-	-	-
Sum of equity and liabilities		<u>737,260,382</u>	<u>658,768,754</u>	127,113,859	113,580,820	5,084.55	4,543.23

The JAK Members Bank

JAK Mendelsbank Financial Statements

Income statement	Suppl disc	SEK (Swedish Crowns)	SEK (Swedish Crowns)	C\$		\$C/JAK Member	
		2002	2001	2002	2001	2002	2001
<i>Operating income</i>							
Return on liquid assets	1	4,757,458	4,335,616	820,251	747,520	32.81	29.90
Interest expense		<u>-5,575</u>	<u>-5,337</u>	- 961	- 920	- 0.04	- 0.04
		4,751,883	4,330,279	819,290	746,600	32.77	29.86
Loan fees	1	15,638,158	15,754,999	2,696,234	2,716,379	107.85	108.66
Member fees	1	3,539,992	3,500,449	610,343	603,526	24.41	24.14
Other operating income	3	<u>2,092,272</u>	<u>1,434,282</u>	360,737	247,290	14.43	9.89
		26,022,305	25,020,009	4,486,604	4,313,795	179.46	172.55
Administrative expenses	4	-9,721,489	-9,132,616	- 1,676,119	- 1,574,589	- 67.04	- 62.98
Other operating expenses	5	-12,560,277	-10,330,038	- 2,165,565	- 1,781,041	- 86.62	- 71.24
Amortization and depreciation	11.12	<u>-1,664,634</u>	<u>-1,908,264</u>	- 287,006	- 329,011	- 11.48	- 13.16
				-	-	-	-
Profit before credit losses		2,075,905	3,649,091	357,915	629,154	14.32	25.17
Credit losses	6	<u>-298,706</u>	<u>-327,000</u>	- 51,501	- 56,379	- 2.06	- 2.26
				-	-	-	-
Profit before transfers and taxes		1,777,199	3,322,091	306,414	572,774	12.26	22.91
Transfers to/from untaxed reserves	7	<u>-500,000</u>	<u>-860,000</u>	- 86,207	- 148,276	- 3.45	- 5.93
				-	-	-	-
Profit for the year		1,277,199	2,462,091	220,207	424,498	8.81	16.98
Tax on profit for the year		<u>-487,731</u>	<u>-722,915</u>	- 84,092	- 124,641	- 3.36	- 4.99
				-	-	-	-
Net profit for the year		<u>789,468</u>	<u>1,739,176</u>	136,115	299,858	5.44	11.99

G. Could VanCity Savings Credit Union Adopt the JAK Model?

Could VanCity or a similar cooperative, credit union in Canada operate on the JAK model? That is, “can a bank or credit union operate without charging interest on loans or credit?” My analysis of the JAK Bank suggests that the answer is yes! And moreover why not?

The JAK banking model demonstrates that charging of interest is not a necessary requirement of running efficient and effective and indeed profitable financial services of a members-owned cooperative enterprise. Indeed, if money is simply viewed as a means of financing the well-being of individual households and the community as a whole (rather than a store of value), then JAK proves that a loans association committed to the ideology of no-interest banking is viable. JAK promotes the sharing of savings of a community of households (and potentially businesses) thus spreading the risk and making a larger pool of liquidity or financial capital available for the common good. JAK promotes the sharing of savings amongst those households who have significant savings or cash reserves and who may not require credit with those households or individuals who (for reasons of age or socio-economic position in life) have less financial capacity.

While, introducing a JAK, no-interest loan program within an existing cooperative credit union banking institution like VanCity might be easier than conventional private, shareholder-owned banks, the shift would nevertheless be a difficult one. I am under no illusion that a banking culture, even as progressive as VanCity, would consider adopting the JAK model for its entire operations. Educating both management and members as to how the benefits of the JAK system and showing how saving interest cost on loans while forgoing interest income on their savings could be a significant challenge. Though introducing the concept through a phased-in approach might work.

For example, VanCity might consider offering a JAK-style no-interest savings-loans account or a separate banking unit that could develop within VanCity like an incubator. VanCity members could open up a “JAK account” with the same benefits and obligations of Swedes in the JAK Bank. The VanCity “JAK Bank” would operate on the same basis as its sister bank in Sweden. To provide a sufficient liquidity pool to make loans viable, VanCity might “gift” the enterprise with \$1 million in seed capital.

Such a JAK-option within VanCity would provide members with another option for banking services. The positive experience of VanCity members to the new JAK-banking-option would be spread organically, through word-of-mouth.

I personally believe that the key selling feature of the JAK Bank option is that members realize a net savings in the form of life “time” saved in not having to work for the cost of interest on loans. If shown that despite not receiving interest on their savings (which currently are meager for most standard saving accounts) they are in fact still better off (on a net basis) than with any type of conventional bank loan, I believe that most people would quickly embrace the JAK banking alternative.

Another tremendous opportunity for introducing the JAK bank option within VanCity is to provide a slightly modified version which would attract a greater diversity of low income households, students (requiring student loans), seniors and middle to upper-middle class households to share the collective bounty of financial assets for the benefit of a community of needs. For example, a JAK style bank would provide an opportunity for a wealthier, retired, debt-free couple to make available some of their excess liquidity to a younger, university-enrolled, indebted couple.

Yet, educating people that paying interest on loans is not necessary, except for recovering the actual operation costs of bank, will be a challenge. Let’s face it, most of us are habituated and comfortable with paying interest on loans, pre-approved mortgages, credit card balances and other forms of credit. To suggest a system that does not require interest payments is somewhat of a revolution in our understanding of banking and the role they play.

H. How Would You Start a JAK Bank in North America?

There are several ways to start a JAK-style bank in North America, whether in Canada or the US.

To our knowledge there are no barriers to starting a JAK style bank in North America. Unless Canadian or US Bank Acts prohibit banks from not charging interest on loans!

The easiest way to start a JAK bank is to form an association of individuals, households and businesses under a legal trust with a charter similar to Sweden's JAK Bank and with similar operating principles and guidelines. Such an association can be started at any scale from a group of friends, cluster of neighbours in a neighbourhood, or a community. Rural communities in North America, are perhaps the ideal place to consider a JAK banking opportunity (indeed it was in rural Sweden where JAK had it's greatest appeal and support).

The association would start with an initial deposit by each member (e.g. \$1000) to form the initial liquidity pool. The pool would then grow over time as new members join or existing members add to the liquidity pool with additional savings. The creation of a sufficient liquidity pool to offer sizable loans might take time, as it did in Sweden. Or members might commit more or a greater majority of their savings to the JAK community bank. They may also wish to attract some wealthy members of their community who are willing to share their excess financial liquidity for the benefit of the broader community. All lending and operating policies could be modeled after Sweden's JAK Bank with a local board of directors making policy decisions.

Another option, already suggested for VanCity, is to introduce a JAK-option within an existing credit union or bank in North America. There are many small credit unions in Canada which operate on principles not unlike VanCity who might find the JAK model attractive for retaining and growing it's membership. Again, as with VanCity, these credit unions might provide an initial seed capital to provide a sufficient economy of scale for a JAK option within their institution. This may lead to an eventual shift to a complete JAK-style operating model. Credit unions are the more likely candidate since they are member-focused and member "owned" as opposed to shareholder owned private banks.

As with JAK Sweden, any startup JAK bank or JAK option in North America would require time, patience and education. In a world too used to instant and easy credit, educating and convincing people of an alternative, slow yet cost efficient and prudent approach to financing household operations will be a challenge.

I. The Future?: The Genuine Wealth Bank

The JAK Members Bank of Sweden points to a new possible era for banking. JAK's as a model suggests that a bank can play an important role in any community, not only as a financial steward and coach but by being more engaged in the stewards of the total wealth or "genuine wealth" (the values-based conditions of well-being).

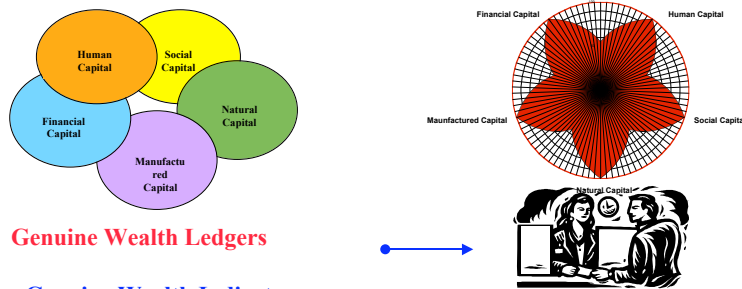
I have been exploring what I call the **Genuine Wealth Accounting (GWA)** and assessment model: a value-based, real asset measurement and reporting system that allows people to get in touch with their core values and then assess and manage their real **wealth** (by definition: the conditions of well-being) that aligns with their values. Genuine wealth "accounts" provides measures of the actual life conditions of a community, including the health of the environment and the economy, and the social cohesion of the community. Genuine wealth accounting would provide a "new balance sheet" for communities to track and measure the conditions of their human, social, environmental/natural, and economic assets in a new, holistic and comprehensive way. These "genuine wealth indicators" would be used in a kind of "community well-being checkup" to determine whether a community's quality of life is making genuine progress.

I envision a "Genuine Wealth Bank" which would use the **GWA**, in part, to help guide its lending policies

The JAK Members Bank

The Genuine Wealth accounting system could provide the management tool for operating these Genuine Wealth Banks at the local, regional/provincial and national banking and monetary policy decision-making. Private local banks could operate like JAK-style banks with households and businesses as the “careholders” sharing a common stewardship objective of genuine, common wealth of the community. These banks might operate on a “social contract” with the community to ensure loans are tied to building and sustaining genuine wealth. Like JAK they would operate on a 100% reserve system and be guided by “genuine wealth” accounts maintained at community level (e.g. by local governments or a non-partisan keeper of the genuine wealth accounts). The genuine wealth accounts would provide the well-being inventory to allow for monitoring the real needs and aspirations of the community. These Genuine Wealth Accounts would guide bankers, like other decision makers in the community,, in part.

Genuine Wealth Bank



Genuine Wealth Ledgers

- Genuine Wealth Indicators
- Genuine Progress Indicators

Indicator	Short-term	Medium-term	Long-term	Intrinsic
Human Capital				
Social Capital				
Natural Capital				
Financial Capital				
Manufactured Capital				

Liabilities

- short-term
- medium-term
- long-term
- expectations



ANIELSKI

Equity

Using the Genuine Wealth Accounts for each community of interests, Genuine Wealth Banks would operate providing credit/loans (creating money) that are directly linked to the “genuine wealth” needs and desires of the community. Genuine Wealth Banks would operate with a social charter or licence given by each community.

Each community would define its own unique set of needs and wants, using the Genuine Wealth inventory and assessment tools developed by Mark Anielski of Anielski Management Inc.. Each local “genuine wealth bank” would be unique, reflecting the unique local values, operating principles and goals for well-being. In essence, each community would self-diagnose their “conditions of their well-being” (genuine wealth) and maintain such an accounting system against which the creation of money (a medium of exchange that represents the real wealth and dreams of the community). Accountability for “returns to genuine wealth” would be clearly defined and readily measured.

Because the Genuine Wealth Accounts represent an comprehensive inventory of the economic, social, health and environmental conditions of well-being of a community, they can be used to diagnose the current state of wealth or well-being of a community, point to future “community wealth development” and then be used to assess the “real” returns to investment of time and resources to improving or sustaining well-being.

J. Commonly Asked JAK Questions

The following are a common set of questions that Mark Anielski raised in conversation with Oscar Kjellberg, past-CEO of JAK.

ANIELSKI: *Don't members forgo interest income on their savings? If so, doesn't this detract from prospective members from joining?*

JAK (Kjellberg): JAK does not pay interest on savings but nor do we charge interest on loans. The net benefit (interest costs saved less interest income forgone) is still greater than in a conventional bank. JAK loans also provide a greater degree of certainty to the members since the payment schedule and costs do not change over the term of the loan.

ANIELSKI: *How does JAK assess the risk of each loan and what is the average "risk premium" attached per loan? Does the risk premium vary according to the type of loan? Can this risk premium be expressed as a "cost" or % interest premium on each loan? How so?*

JAK (Kjellberg): We do not use risk premiums for the assessed risk of the individual loans. The same loan fee formula is used for all loans. Our credit losses are in the area of less than 0.5 percent.

ANIELSKI: *How does JAK make money? My answer has been that "it doesn't" since all operating costs are fully recovered in terms of salaries and other operating expenses. The goal is to provide liquidity/credit as a common good to the community yet in a viable and efficient business enterprise?*

JAK (Kjellberg): You are right. We recover our operating costs through loan fees and membership fees as well as try to make one million SEK per annum to add to our equity, that's all.

ANIELSKI: *Who makes the credit/lending policy decisions? The board? Members as free voting participants? Who decides who qualifies for a loan or not?*

JAK (Kjellberg): Yes, the policy is the decision of the board but the loans are decided by the boards credit committee; loan delegation decisions are made by a manager and two employees.

ANIELSKI: *Can loans be issued to non-JAK members from a JAK-member who deems their friend/neighbour a worthy credit risk?*

JAK (Kjellberg): No. Loans are only issued to members.

ANIELSKI: *What is the average number of hours worked per week by JAK employees, including yourself? How many days do you work on average per week? Do you have other employment?*

JAK (Kjellberg): Our employees work 38,5 hours per week and some of them do overtime now and then. The management does more hours.

ANIELSKI: *What infrastructure is required? I understand only a computer, a website and internet services, plus your desk and physical office.*

JAK (Kjellberg): We have a computer for every employee and a couple of servers for the systems. We are developing Internet services and we may have activated the first services in the autumn.

ANIELSKI: *Does JAK provide only personal/household loans or does it lend to small business enterprise?*

JAK (Kjellberg): About 15 percent of our lending goes to small business enterprises and organisations.

ⁱ CIA World Factbook found online <http://www.cia.gov/cia/publications/factbook/index.html>