

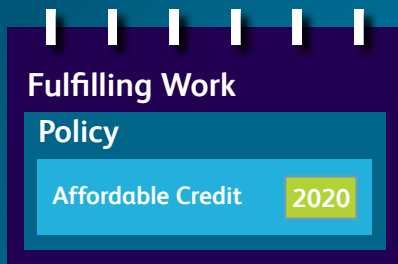


# The 10% solution

**How to make affordable credit more available to those who need it most**

Full Report

Alistair Grimes, Nick Hopkins and Jos Henson



## Acknowledgements

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# Section 1: Introduction

The Carnegie UK Trust's 2016 report 'Gateway to Affordable Credit' described the current credit landscape in which low income groups both:

- Have a significant need for access to small sums of affordable credit and
- Were finding that access increasingly difficult.

Too often, low income households have little option but to turn to high cost credit, putting further pressure on already strained finances.

The Gateway report suggested that support for, and investment in, not for profit community lenders, like credit unions and Community Development Finance Initiatives (CDFIs), would be key to the policy response in Scotland.

This stimulated a positive response from some Scottish local authorities, the Scottish Government and the Carnegie UK Trust itself.

The Carnegie UK Trust invested £1m to establish the Affordable Credit Loan Fund, subsequently matched by the Scottish Government. Fife, Falkirk and West Lothian Councils undertook a collaborative procurement which resulted in the establishment and support for a new CDFI across the local authorities, Conduit Scotland.

In the same period, other local areas including Edinburgh and Inverclyde have welcomed new affordable credit offerings, with the expansion of Scotcash into both of these areas, and Fair for You, an online affordable credit operator targeting customers in the rent to own market, has grown its engagement with the Scottish market significantly.

The Carnegie UK Trust commissioned this report to look at the potential for expansion of affordable credit supply in seven local authority areas of Scotland between them covering 22.5% of Scotland's population:

- Aberdeen,
- Aberdeenshire,
- Clackmannanshire,
- Moray,
- North Lanarkshire,
- Perth & Kinross and
- Stirling.

Our analysis was carried out before the onset of the COVID-19 crisis. This report presents evidence on:

1. Levels of high cost credit usage in each of these areas;
2. The context in which high cost lending was happening prior to the onset of COVID-19;
3. The extent to which local community lenders were serving low income customers who might otherwise go to high cost lenders;
4. The provision gap between high cost and community finance.

The report makes recommendations for:

- The local authorities involved;
- The Scottish Government;
- The Carnegie UK Trust;
- Community lenders.



The report concludes that taking action on the provision of affordable credit will offer an alternative for the c.49,000 annual customers of high cost credit in the seven local authorities that are the focus of this report.

Local and national leadership and commitment to achieving a realistic level of market impact could see low income consumers in those authorities save up to £4.1m, making a real difference to the disposable incomes of low income households, reducing poverty, including child poverty, and with further spin off benefits in terms of health, council tax payment, rent payment and housing stability also likely.

This report does not reflect the entirety of our delivery of the brief, some aspects of it are contained within more local reports.

In terms of the structure of the report:

- **Section 2** sets out the tasks that we undertook.
- **Section 3** sets out some of the income, labour market and financial pressures impacting on low income consumers using high cost credit prior to COVID-19, and the context in which high cost borrowing happens in each of the seven local authorities that are the focus of this research.
- **Section 4** sets out our understanding of issues surrounding high cost credit, and focuses on four key parts of the high cost credit market; high cost short term credit (HCSTC), home credit, rent to own and pawnbroking. It concludes with a discussion of trends in the high cost credit market.
- **Section 5** focuses on estimating the size of the high cost credit market in each of the seven local authorities in terms of customer numbers, annual originations and value of those originations. It concludes with an estimate of the potential customer base for any organisations looking to attract customers away from high cost provision.
- **Section 6** focuses on the extent to which existing affordable and mid cost credit providers are meeting the needs of low income customers, concluding by setting those market penetration figures against the size of the high cost credit market.
- **Section 7** looks at the extent to which investment in a mid cost credit provider (Conduit Scotland) delivering to a partnership of three local authorities (Fife, Falkirk and West Lothian) has enabled that provider to penetrate the high cost credit market in those areas.
- **Section 8** sets out our conclusions.
- **Section 9** sets out recommendations for Carnegie UK Trust, the seven local authorities, the Scottish Government and others.

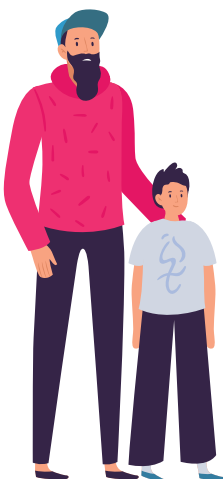


## Section 2: What we did

After an initial meeting with The Carnegie UK Trust (CUKT) we carried out the following tasks:

- Meetings with local authority staff in each of the seven areas to identify sources of data and available information;
- Two seminars (one with Moray, Perth & Kinross, Aberdeenshire, CUKT and the Improvement Service, one with Aberdeen, North Lanarkshire, Stirling, Clackmannanshire, CUKT and the Scottish Government) to present our initial findings;
- Data collection from:
  - Scotcash CIC and Five Lamps Trading (trading as Conduit Scotland) and Fair for You;
  - Individual credit unions operating in the seven areas;
  - The Financial Conduct Authority (FCA);
- Telephone interviews with Provident Financial Group and the Consumer Finance Association (CFA) to understand the perspectives of commercial lenders;
- Interviews with representatives from ABCUL and the Scottish League of Credit Unions to understand the Credit Union perspective;
- Telephone discussions with Scotcash and Five Lamps (Conduit Scotland) to understand the perspective of CDFIs in this area and, from Five Lamps (Conduit Scotland) the practical lessons from establishing their operations in Falkirk, Fife and West Lothian;
- Telephone discussions with a number of credit unions working in the seven areas;
- A presentation to the CUKT Affordable Credit Action Group.

We also revisited the initial feasibility study on setting up a CDFI in Falkirk, Fife and West Lothian.



# Section 3: National and Local Context: Income, Poverty, Financial Pressure

This section sets out some of the income, labour market and financial pressures on low income consumers using high cost credit prior to COVID-19, and the context in which high cost borrowing happens in each of the seven local authorities that are the focus of this research.

It does so to:

- Make clear the extent of the financial pressures on people on low incomes who may need affordable credit, and patterns in those pressures since the 2008/9 recession.
- Explore how economic trends might affect and have affected people's need for credit to make more significant purchases and to meet everyday needs.

It does not take into account the disproportionate effect of COVID-19 on lower income households.

## National Context

### Income Trends

The broad pattern of UK household income for those on lower incomes over the last two decades has been as follows<sup>1</sup>:

- Stagnation in the early to mid-2000s;
- Decline during the recession of the late 2000s extending into the early 2010s, with median income falling 0.7% per year on average;
- Growth since the early 2010s, with an average rise of 2.2% per annum in median income;
- Slight decline since the Brexit referendum, with an average decline in incomes of 0.3%.

The last two years have seen the lowest growth in median income outside any period apart from the four recessions since the early 1970s. The current period may end up being worse for incomes than the recession of the 1990s – a prediction made before the global pandemic created an economic crisis.

There is a slightly different pattern in Scotland<sup>2 3</sup>:

- Median incomes fell between 2007-13, only recovering enough to pass the pre-recession peak in 2013-16.
- Median incomes stand at £499 before housing costs and £448 after housing costs, and continued to increase slightly in the most recent period prior to COVID-19.

Particular pressures have been felt by:

- Families with young children, with income growth for those with children under 3 being only 5% since just before the recession;
- Working single parents, where incomes are lower than they were in 2003/04<sup>4</sup>.
- Younger groups, who form a significant proportion of those likely to use high cost short term credit:
- Typical incomes for 25-31 year olds have fallen since the mid 2000s, compared to 30% growth in the preceding 9 years.
- Real non housing spending for 18-29 year olds was lower in 2017/18 than it was in 2001/02<sup>5</sup>.

1 Corlett, A et al, *The Living Standards Audit 2019*, The Resolution Foundation: London, 2019.

2 Scottish Government [accessed online at gov.scot] *Poverty and Income Inequality in Scotland: 2015-2018*, 2019.

3 Median incomes here worked out on three year rolling average.

4 Corlett, A et al, *The Living Standards Audit 2019*, The Resolution Foundation: London, 2019.

5 Corlett, A et al, *The Living Standards Audit 2019*, The Resolution Foundation: London, 2019.

There are also particular pressures on:

- Private renters, with an average ratio of housing costs to disposable income of 35% in 2018/19, up from 32% in 2000;
- Social renters, with an average ratio of housing costs to disposable income of around 31%, up from 27% pre-recession.

For comparison the same ratio for those with a mortgage is 11%, down from 20% in 2007/08<sup>6</sup>.

### Impact of Welfare Reform, Benefit and Taxation Changes

The last decade has seen extensive changes to the benefits and tax credit system on which many of those accessing high cost credit rely for at least part of their income, and the taxation regime facing people on lower incomes. The change process is not yet concluded, with the introduction of Universal Credit not due to be complete until 2023, and the Scottish Government beginning the gradual assumption of powers over certain benefits, alongside their ability to make their own payments and establish variations on UK wide rules. The impact of COVID-19 will see many more people relying on the social security system, many of whom have not had to do so before. It is not yet clear what the implications of the crisis will be for the future design of the system.

There are four main strands to welfare reform affecting working age people:

- The creation of and transition to new benefits
  - From Incapacity Benefit to Employment and Support Allowance,
  - From Disability Living Allowance to Personal Independence Payment, and
  - From six legacy benefits / tax credits to Universal Credit;
- ‘Salami slicing’ through small but often significant changes to rules, for example:
  - the Bedroom Tax,
  - The tightening of criteria,
  - Calculating rates on different bases, and

6 Corlett, A et al, *The Living Standards Audit 2019*, The Resolution Foundation: London, 2019.

- The use of sanctions;
- The ‘benefit freeze’,
  - Eroding the year on year value of a number of key income related benefits;
- The devolution of powers under the Scotland Act,
  - Alongside the use of existing powers to mitigate some of the above changes by the Scottish Government, and the previous devolution of the DWP’s Social Fund, the forerunner of the Scottish Welfare Fund.

The consequences of these changes can be seen in Equality and Human Rights Commission (EHRC) research on the cumulative impact of welfare reforms and tax changes.<sup>7</sup>

The EHRC found that since 2010, the bottom two income deciles had lost 10% of their net income. The impact of the changes have not been even, being more significant for households with more disabled members and more seriously disabled members; households with children; black and minority ethnic communities and women, and people reliant on means tested income changes.

The EHRC predicted that in Scotland the income of the lowest two deciles would fall by 8% between 2012 and 2022 (by £900 and £1600 respectively) with the above groups experiencing the most severe cuts, and with 66% of the lowest two deciles losing income. This prediction will not take into account the impact of COVID-19, which could further decrease the income of the lowest two deciles.

The UK figures make clear that some of those losses for households with children would be very large:

- Lone parents in the bottom quintile of household will lose 25% of their net income, on average, £5,250 per year;
- A disabled lone parent with one disabled child, loses 30% of net income, £10,000 per year in cash terms;
- Couples with children would lose £3,000 per year.

7 Portes, J., Reed, H., *The Cumulative Impact of Tax and Welfare Reforms*, Equality and Human Rights Commission, 2018.



The age group experiencing the highest losses will be the 35-44 group, with women aged 35-44 losing over £2,200 on average.

## Changes in the labour market

Though rates of employment were very high before the COVID-19 pandemic, there were two trends with relevance for people's potential demand for credit, and their ability to access and repay credit.

**Underemployment** is defined by the ONS as people who; are willing to work more hours, are available to work more hours and have worked less than a specified threshold of hours<sup>8</sup>.

People who are seeking more hours may be looking to alleviate financial pressure, or to afford increased consumer spending. In the absence of being able to increase their income through employment, they may look to borrow.

In the period April to June 2019, an estimated 3.251m people wanted to work more hours, of whom the ONS estimates that 2.479m are underemployed (7.7% of the UK workforce).

The Resolution Foundation reports that from 2008, two thirds of jobs growth was in **atypical employment**; self employment, part time work, temporary work, agency work or zero hours contracts. The growth of such employment slowed, then stopped and in some areas reversed a little over the last few years, but 40.8% of those working prior to COVID-19 were in atypical employment.

Atypical employment is concentrated amongst some groups who may be more likely to use high cost credit:

- 58% of mothers are in atypical employment;
- 56% of single parents;
- 49% of women;
- 48% of disabled people.

8 ONS [accessed online at ons.gov.uk] *Dataset EMP16: Underemployment and overemployment*, 2019.

At the least secure end of the labour market, in 2018 there were 800,000 people in the UK working as agency workers, and just under 800,000 working on zero hours contracts. Together these types of employment make up 5% of the UK workforce.

Wages are lower for people in atypical work; £9.20 median wages per hour for people in part time work versus £12.80 per hour for those in full time work. There also appears to be a pay penalty, calculated by the Resolution Foundation as 6% for temporary workers, and 5% for people on zero hours contracts<sup>9</sup>. It is too early to quantify the impact of COVID-19 on the labour market, but it is likely to be significant. Over 628,000 jobs were furloughed in Scotland<sup>10</sup>, with this government support likely to be suppressing unemployment while it is in place.

## Poverty Levels

Levels of poverty have risen slightly since the recession<sup>11</sup>, and remain high, for both adults and children.

Figures published in 2019 show that in the UK:

- 22% of people live in relative poverty after housing costs.
- 17% of people live in relative poverty before housing costs.

Children are more at risk of living in poverty than adults:

- 30% of children live in relative poverty after housing costs;
- 26% of children live in absolute poverty after housing costs;
- 12% of children live in households that are both low income and materially deprived.

9 Clark, S., Cominetti, N., *Setting the Record Straight- How Record Employment Changed the UK* The Resolution Foundation: London, 2019.

10 UK Government [accessed online at gov.uk] *Figures show UK Government supporting incomes across all nations during coronavirus*, 2020

11 Department of Work and Pensions [accessed online at gov.uk] *Households Below Average Income: An Analysis of the UK Income Distribution 1994/95- 2017/18* 2019.

Table 3.1

Group	Numbers in Poverty 2012	Numbers in Poverty 2022	Percentage in Poverty 2012	Percentage in Poverty 2022
Households	390K	410K	15.4%	16.8%
Children	240K	320K	25.1%	33.1%
Adults	670K	700K	16.1%	16.9%

Table 3.2

	2007/08	2009/10	2011	2012	2013	2014	2015	2016	2017	2018
Managing well (%)	52	49	47	47	48	52	55	56	56	55
Getting by alright (%)	37	39	40	40	40	37	36	36	35	35
Don't manage well (%)	9	11	11	12	11	10	9	8	8	8
Deep financial trouble (%)	1	1	1	2	1	1	1	1	1	1

Figures from the same period show that Scotland's situation is slightly better than that of the rest of the UK<sup>12</sup>:

- 20% of people live in relative poverty after housing costs;
- 17% live in relative poverty before housing costs;

Scottish children are more at risk of living in poverty than adults:

- 24% of children in Scotland live in relative poverty after housing costs;
- 22% of children live in absolute poverty after housing costs.

In terms of working age adults and households with someone employed in Scotland:

- 20% of adults of working age are in poverty after housing costs;
- 60% of those adults are in a working household;
- 65% of children living in a poverty are in a working household;
- 39% of lone mothers are in poverty;
- 24% of people with a disabled person in the household are in poverty.

12 Scottish Government [accessed online at gov.scot] *Poverty and Income Inequality in Scotland: 2015-2018*, 2019.

For some people poverty is persistent. Although rates in Scotland are lower than in the rest of the UK, the proportion of people in persistent poverty after housing costs is rising. In 2017:

- 11% of the Scottish population were in persistent poverty (10%, 2012-2016);
- 17% of children were in persistent poverty, (14%, 2012-2016);
- 10% of working age adults are in persistent poverty, (9%, 2012-2016)<sup>13</sup>.

**Table 3.1** sets out EHRC projections for the impact of taxation and benefit changes on poverty in Scotland by 2022<sup>14</sup>. These projections do not take into account the economic impact of COVID-19.

### Financial pressure on households

Both the Scottish Household Survey and the FCA's Financial Lives Survey capture the extent to which Scottish households have felt financial pressure over the last decade.

13 Scottish Government [accessed online at gov.scot] *Persistent Poverty in Scotland: 2010-2017*, 2019.

14 Portes, J., Reed, H., *The Cumulative Impact of Tax and Welfare Reforms*, Equality and Human Rights Commission, 2018.

**Table 3.2** sets out data from The Scottish Household Survey's annual question about how respondents feel they are faring financially<sup>15</sup>.

The impact of the fall out from the recession, and possibly from aspects of welfare reform, are clear.

The Financial Lives Survey sets out a number of measures relating to financial pressure, finding that:

- 8% of respondents in Scotland are in financial difficulty;
- 11% have no savings or investments;
- Of those in debt, average debts are £8,530;
- 13% are overindebted<sup>16</sup>, defined as considering keeping up with domestic bills and credit commitments to be a heavy burden, or having missed any credit commitments and/or any domestic bills in any three or more of the last six months.

<sup>15</sup> Scottish Government [accessed online at gov.scot], *Scottish Household Survey 2018*, 2019.

<sup>16</sup> Financial Conduct Agency [accessed online at fca.org.uk], *Financial Lives Survey*, 2017.

## Context for Seven Local Authorities

This final part of this section sets out some key aspects of the data in the seven local authority areas, focusing on:

- The labour market.
- Poverty and income.
- Experience of financial pressure.
- Housing tenure.

### Labour Market Issues/ Income and Poverty

**Table 3.3** sets out key labour market and income/poverty indicators for each of the areas<sup>17</sup>. These figures do not take into account any effect of the COVID-19 pandemic on labour market and income indicators.

<sup>17</sup> Nomis [accessed online at nomisweb.co.uk] *Official Labour Market Statistics*

**Table 3.3**

	Aberdeen	Aberdeenshire	Clackmannanshire	Moray	North Lanarkshire	Perth and Kinross	Stirling	Scotland
Economic Activity	81.9%	84%	75.2%	78.6%	78.2%	84.3%	77.6%	77.9%
Employment Rate	78.2%	81.4%	74%	74.9%	75.6%	81.6%	74.7%	74.7%
Economic Inactivity	18.1%	16%	24.8%	21.4%	21.8%	15.7%	22.4%	22.1%
Long Term Sick Rate	5.5%	3.8%	6.6%	6.7%	7.1%	3.9%	7.3%	6.3%
Median Full Time Earnings	£578.3	£594.5	£480.2	£527.2	£548.9	£569.7	£592.8	£562.7
Full Time Earnings at 20th Percentile	£407.7	£418.8	£358.6	£346.4	£393.1	£370.8	£381.1	£388.5
Child Poverty*	18%	14%	27%	20%	26%	20%	20%	

\* End Child Poverty [accessed online at endchildpoverty.org.uk] *Poverty in your area*, 2019

Chart 3.1

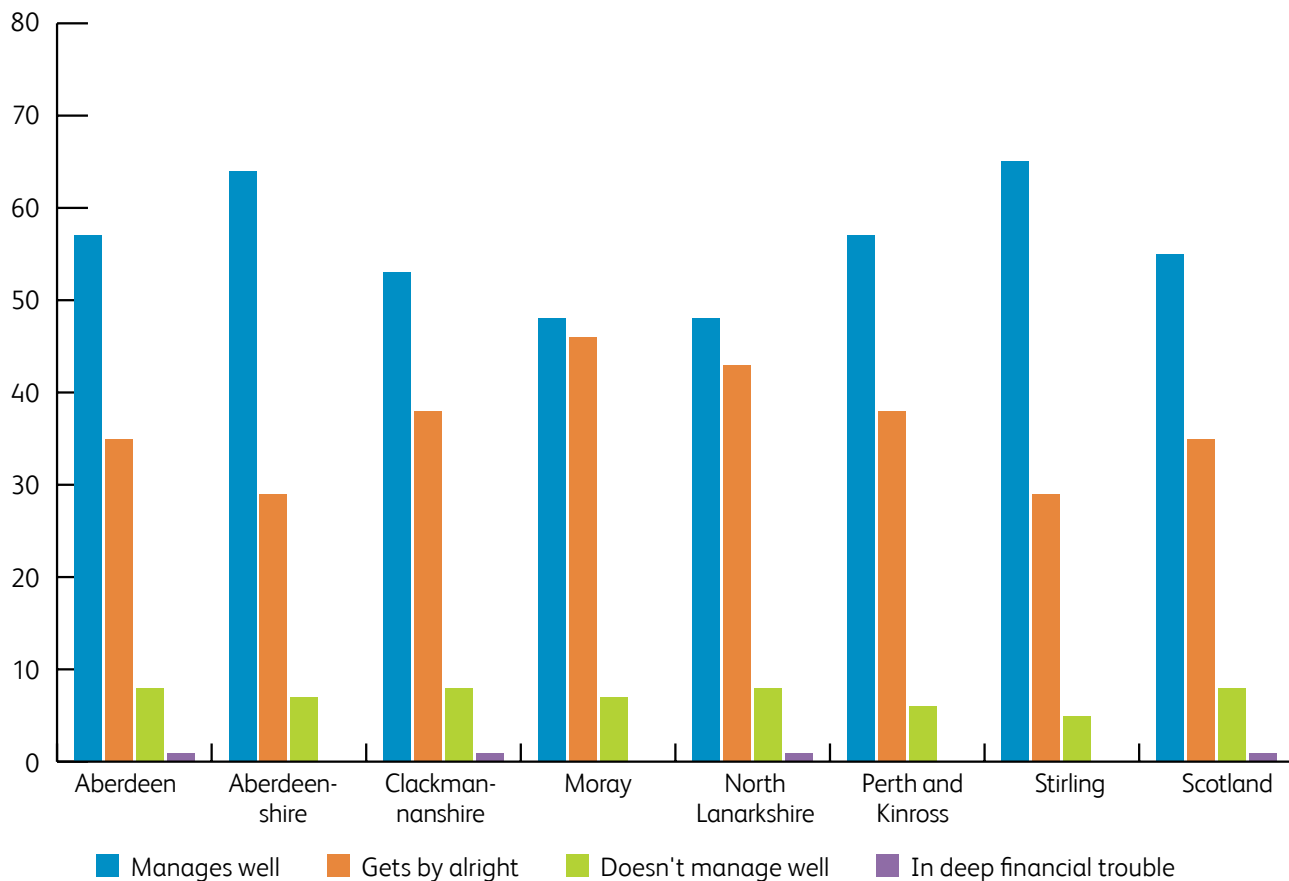
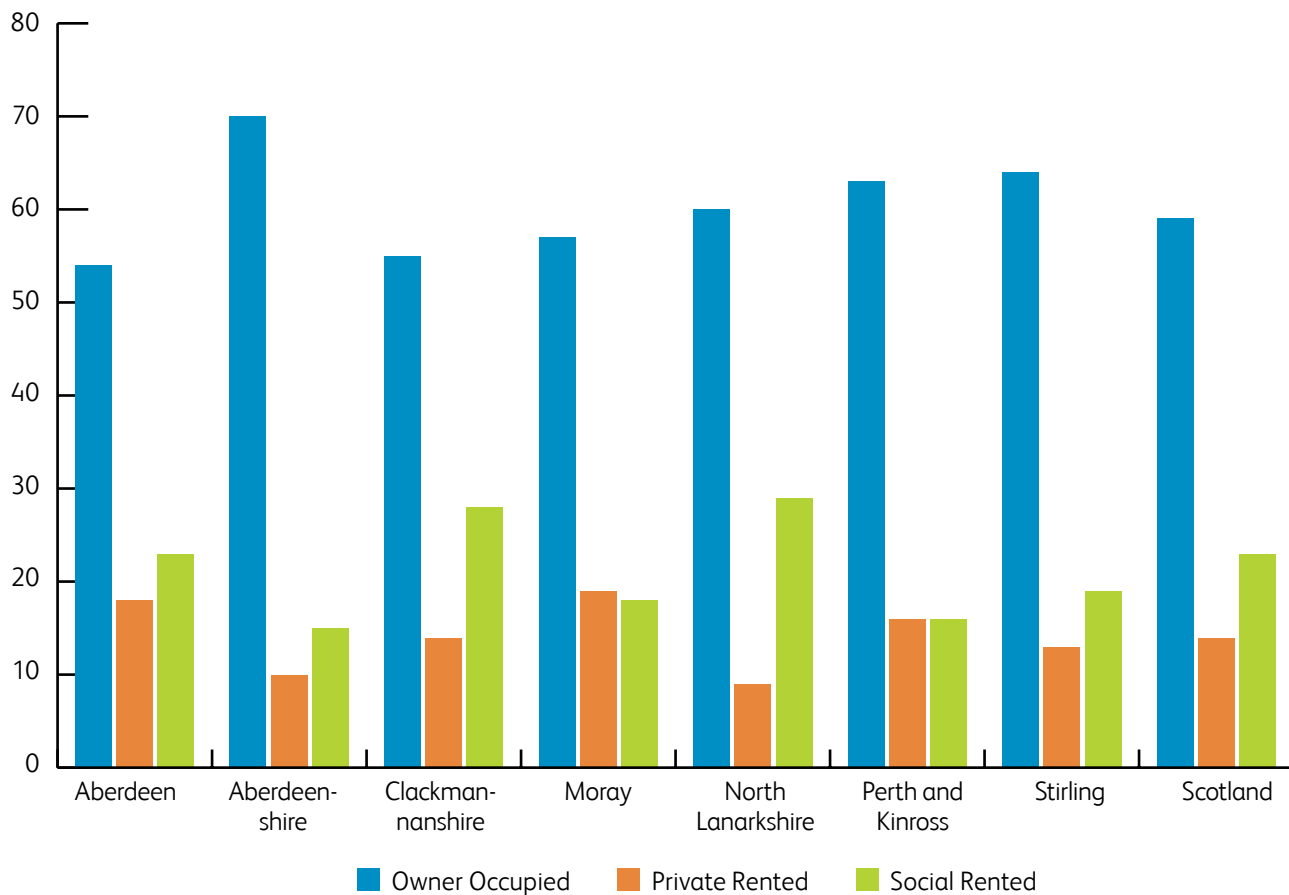


Chart 3.2



These figures suggest that we can characterise the local authorities as follows:

- Aberdeen: high employment, high wage economy.
- Aberdeenshire: very high employment, very high wage economy.
- Clackmannanshire: relatively low employment, low wage economy.
- Moray: average employment, low wage economy.
- North Lanarkshire: relatively high employment, with some issues around levels of pay.
- Perth: very high employment, with some issues around low pay for those at the lower end of the labour market.
- Stirling: average employment, with some issues around low pay for those at the lower end of the labour market.

### Managing financially

**Chart 3.1** sets out figures from the Scottish Household Survey on how well respondents were managing financially prior to the COVID-19 crisis<sup>18</sup>.

This graph shows that:

- There were few significant differences between the percentages of people in each local authority who report not managing well or being in deep financial trouble.
- There were significant differences between the balance between those ‘managing well’ and those ‘getting by alright’ across the seven LAs.
- In each local authority more respondents indicated that they were managing well than getting by alright. That gap is very much smaller in Moray and North Lanarkshire.

<sup>18</sup> Scottish Government [accessed online at gov.scot] *Scottish Household Survey 2018: Local Authority Tables* Scottish Government 2019.

### Housing Tenure

**Chart 3.2** sets out figures on housing tenure in each of the seven local authorities<sup>19</sup>:

This graph shows that:

- Levels of owner occupation are significantly higher in Aberdeenshire than across Scotland as a whole, and higher in Perth and Kinross and Stirling. They are at similar levels to the Scottish average in North Lanarkshire and Moray, and lower in Aberdeen and Clackmannanshire.
- Levels of living in social rented housing are significantly higher in Clackmannanshire and North Lanarkshire than the Scottish average, the same in Aberdeen, lower in Stirling and Moray and significantly lower in Perth and Kinross and particularly Aberdeenshire. Even in Aberdeenshire, 3 out of every 20 people live in social rented housing.

### Note on the relative affluence of some of the areas.

It is essential to understand that although Aberdeenshire in particular is a relatively affluent local authority compared to the rest of Scotland, there is still a significant population of people living in the more affluent areas covered by this report who are living in poverty.

Even prior to the COVID-19 crisis an estimated 6,900 children under the age of 16 lived in poverty in Aberdeenshire, more than the number of children in all of the target local authorities apart from Aberdeen and North Lanarkshire.

Those children, and the adults also living in poverty in Aberdeenshire should still be a priority for the local authority, and for national partners looking to impact on poverty across Scotland.

<sup>19</sup> Scottish Government [accessed online at gov.scot] *Housing Statistics: Stock by tenure* 2018.

# Section 4: Affordability and Credit

This section sets out our understanding of issues surrounding high cost credit, and focuses on four key parts of the non mainstream credit market; high cost short term credit (HCSTC), home credit, rent to own and pawnbroking. It concludes with a discussion of trends in these parts of the non-mainstream credit market.

## High Cost Credit: A Symptom of Poverty

There is a clear association between usage of high cost / non-mainstream credit and poverty and low income. Mainstream credit providers are less likely to be interested in lending to people on lower incomes due to the association between higher risk to repayment and lower incomes, and the cost of administration for the (typically) smaller amounts sought. An assessment of bank lending for example, will typically see unsecured loans beginning over £1000.

## High Cost Credit Reduces Disposable Income and Deepens Poverty

The poverty premium is defined as:

**‘the extra cost that households on low incomes incur when purchasing the same essential goods and services as households on higher incomes.’<sup>20</sup>**

The channels through which the poverty premium is generated may include:

- The cost of credit;
- The cost of accessing money; for example charging ATMs and the lack of a transactional bank account;
- Insurance premiums; reflecting the risk of the neighbourhood in which they live and payment method;

20 Keohane N and Corfe S [Measuring the Poverty Premium](#), Social Market Foundation, 2018.

- Energy related; because of payment method, such as fuel key / prepayment meters, and not being on the best tariff;
- Telecommunications, for example using Pay-As-You-Go rather than contract;
- Food and groceries costs, being unable to bulk buy, lacking transport for larger supermarkets and therefore using local shops.

Work has also been done to identify long-term poverty premiums around housing, and explore the concept of a transport related poverty premium.

Save the Children produced what might be understood as a reasonable worst-case scenario estimate of the annual poverty premium that someone would face if they were affected across all its potential dimensions, producing a figure of £1,289 (at 2010 prices)<sup>21</sup>.

University of Bristol’s Personal Finance Research Centre research produced an estimate of the average impact of the poverty premium on low income households based on the actual prevalence of different dimensions on low income households. This produced an estimate of £490, with £233 reflecting people not accessing the cheapest energy tariff and £84 reflecting insurance related issues. The estimate for the impact of the use of high cost credit was £55. It is critical to understand that this reflects the fact that not everyone on low incomes uses high cost credit. For those who do, the premium they pay will be much higher<sup>22</sup>.

More recently, the poverty premium related solely to the lack of a transactional bank account was estimated to be £485 per year.<sup>23</sup> The inflated cost of credit paid by financially excluded customers was the largest single component – estimated at £222 per year, based on the average cost of a cash-based loan offered by firms like Provident.

21 Westlake A, [The UK Poverty Rip Off: The Poverty Premium 2010](#), Save the Children, 2010. [Amount updated with inflation].

22 Davies S, Finney A, Hartfree Y, [The Poverty Premium – When Low-income Households Pay More for Essential Goods and Services](#), University of Bristol, 2016.

23 Pockit [available online at pockit.com] [The Banking Poverty Premium 2019](#).

Table 4.1

	People with Outstanding Debt (#)	Annual Numbers of Customers (#)	Annual Originations (#)	Annual Value of Originations (£)	Value of Outstanding Debt (£)
Catalogue Credit	7.6	1.9	2.5	0.8	4.0
Retail Finance	5.3	2.3	2.6	4.4	6.0
Storecards	1.9	0.4	0.4	0.2	0.7
HCSTC	1.6	0.8	3.6	1.1	1.1
Home Credit	1.6	0.7	1.7	1.3	1.1
Rent to Own	0.4	0.2	0.6	0.6	0.5
Guarantor	0.1	0.1	0.1	0.2	0.3

## What is High Cost Credit?

### Non-Mainstream Credit

The FCA's 2017 Technical Annex Report<sup>24</sup> focused on nine forms of what it identified as non-mainstream credit:

- **Catalogue Credit** – often called mail order / home shopping credit, enabling people to borrow from one or more retailer up to an agreed limit;
- **Retail finance** – where credit is provided by a single retailer and repaid in instalments;
- **Store cards** – which function like credit cards but are used with a single retailer;
- **High cost short term credit** – where loans are made at more than 100% APR and repaid in instalments over a term under 12 months;
- **Home credit** – where loans are collected from the borrower's home;
- **Rent to own** – hire purchase agreements whereby the borrower takes out credit to purchase a good, but does not gain ownership of the good until the last payment has been made;
- **Guarantor credit** – when a borrower takes out a credit agreement as part of which another individual has guaranteed payment if the borrower does not make payment;
- **Other running accounts;**
- **Logbook loans.**

24 Financial Conduct Authority [accessed online at [fca.org.uk](http://fca.org.uk)], *High-Cost Credit Review Technical Annex 1: Credit Reference Agency (CRA) Data Analysis of UK Personal Debt*, 2017.

This section of the report summarises the FCA's findings on the first seven of those types of credit, and identifies three that are the focus of the rest of the report.

**Table 4.1** sets out the size of the market for those seven non-mainstream forms of credit.

There is a difference between more recent patterns of borrowing and the rates at which borrowers experience problems for each of these types of debt:

- Use of catalogue credit declined from 2.8m consumers (2013) to 1.9m (2016);
- Retail finance grew from 1.9m consumers (2014) to 2.3m (2016). Only around 3% of accounts go into arrears;
- Numbers of customers using store cards showed a slight decline across the period from 500,000 to 400,000. Around 20% of accounts go into arrears;
- Use of high cost short term credit fell very significantly after regulation hit in 2014, from 1.7m in 2013 to 700,000 in 2015. Around 16% of accounts go into arrears;
- Home credit saw a slow decline in usage 2012-2015, from 900,000 in 2012 to 600,000 in 2015 followed by a small rise. Around 30% of loans ended up in arrears, though the figure peaked at as high as 50% in 2012;
- Rent to own credit saw a fall in customers from 250k to 200k across the period, with under 10% going into arrears<sup>25</sup>.

25 Financial Conduct Authority [accessed online at [fca.org.uk](http://fca.org.uk)], *High-Cost Credit Review Technical Annex 1: Credit Reference Agency (CRA) Data Analysis of UK Personal Debt*, 2017.

Table 4.2

	Median Age	Estimated Median Income	Outstanding Personal Debt	Median Credit Score*
Catalogue Credit	45	17.7K	1.3K	63
Retail Finance	41	24.7K	4.3K	69
Storecards	36	17.5K	1.1K	65
HCSTC	32	20K	3.6K	42
Home Credit	42	15.5K	2.8K	41
Rent to Own	36	16.1K	4.3K	38
Guarantor Credit	33	20.8K	7.4K	40

\* The credit score numbers in this table are rebased by the FCA, as individual credit agencies operate different scales. A lower value indicates increased credit risk, i.e. lower likelihood of repaying debt. Typically, 'sub prime' scores will be those below 45; as the FCA note, 'sub prime' consumers occupy the long tail of the bottom of the credit score distribution.

**Table 4.2** sets out the FCA's findings on the social characteristics of customers of each of these types of credit and their borrowing behaviour<sup>26</sup>.

It can be seen from this that:

- The market for high cost short term credit, guarantor loans, store cards and rent to own is significantly younger than that for catalogue credit, home credit and retail finance.
- Those using retail finance are significantly better off than those using the other forms of non-mainstream credit, with those using guarantor loans or high cost short term credit also somewhat better off.
- Levels of outstanding personal debt are much lower for catalogue credit and store cards, and particularly high for guarantor credit, and high for retail finance and rent to own.
- Credit scores are much lower for rent to own customers, users of guarantor credit home credit and high cost short term credit, indicating that they are much more likely to be excluded from credit by providers.

Based on the relative credit scores of each form of credit, on levels of income of borrowers and on levels of outstanding personal debt, this report will focus on three of the above types of credit which we will define collectively as 'high cost credit', plus pawnbroking. These are high cost short term credit,

home credit and rent to own; whose customers affordable / medium cost credit providers might seek to target with a better offer.

Guarantor credit is too recently developed as a market, with too little known about customers, to be the focus of this report, although it is now worth over £1 billion in the UK.

## Pawnbroking

This report also focuses on the extent of usage of pawnbroking in each of the local authorities. Pawnbroking involves the offer of loans to individuals with personal items used as collateral, which are then sold if the person does not repay the loan.

The FCA's report in 2017 did not look at pawnbroking, but in 2018 it carried out a survey of pawnbroking activity in the UK, to which 79% of UK firms in the market responded<sup>27</sup>. From this response the FCA estimate that:

- 350,000 people in the UK borrow from a pawnbroker each year.
- Pawnbrokers make one million loans a year, worth £300m, the average size of loan therefore being about £300.
- There are 290 firms in the market, working out of 1,056 stores.
- Seven of those firms serve 80% of the market.

26 Financial Conduct Authority [accessed online at [fca.org.uk](http://fca.org.uk)], *High-Cost Credit Review Technical Annex 1: Credit Reference Agency (CRA) Data Analysis of UK Personal Debt*, 2017

27 Financial Conduct Authority [accessed online at [fca.org.uk](http://fca.org.uk)], *Pawnbroking sector review*, 2018.

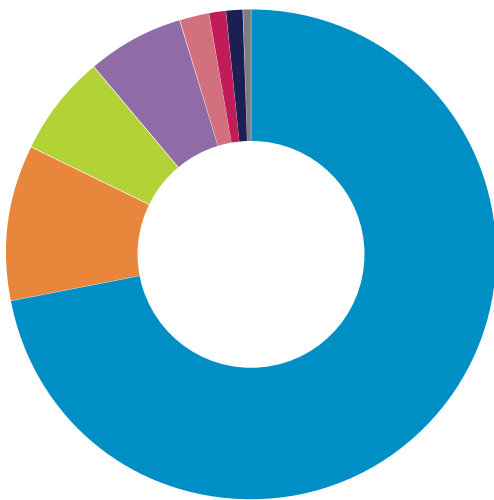


## Use of More than One Source High Cost Credit

The FCA looked at the numbers of people who took out more than one form of four types of non-mainstream Credit; Catalogue Credit, High Cost Short Term Credit (HCSTC), Home Credit and Rent to Own (RTO) in a year.

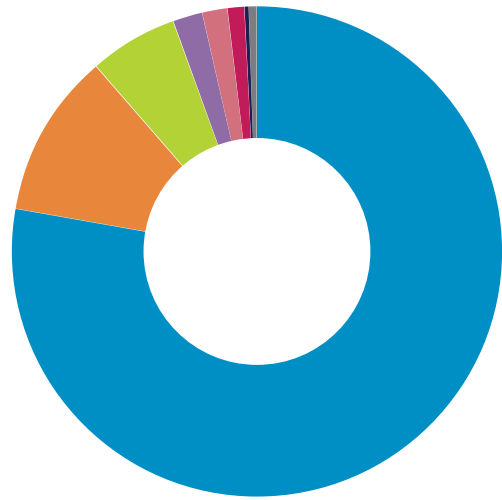
The figures from 2016 show a high degree of separation between markets, although there is a small amount of crossover<sup>28</sup>:

- **Chart 4.1** shows numbers of customers with Home Credit products only, and Home Credit products alongside other High Cost Credit products.



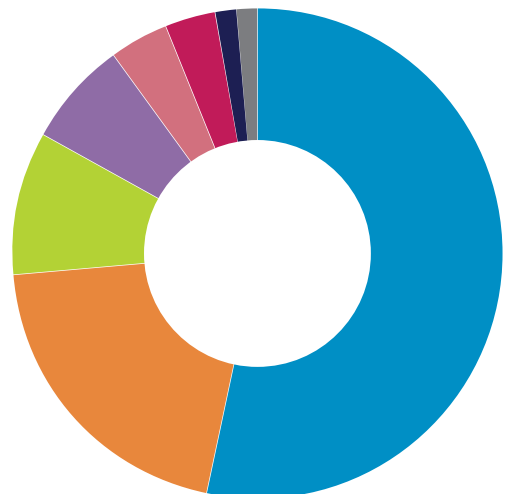
- Home credit only
- Home Credit & Catalogue
- Home Credit & HCSTC
- Home Credit & RTO
- Home Credit, Catalogue & HCSTC
- Home Credit, Catalogue & RTO
- Home Credit, HCSTC & RTO
- Home Credit, Catalogue, HCSTC & RTO

- **Chart 4.2** shows numbers of customers with High Cost Short Term Credit products only, and HCSTC products alongside other High Cost Credit products.



- HCSTC loans
- HCSTC & Catalogue
- HCSTC & Home Credit
- HCSTC & RTO
- HCSTC, Home Credit & Catalogue
- HCSTC, Home Credit & RTO
- HCSTC, Catalogue & RTO
- Home Credit, Catalogue, HCSTC & RTO

- **Chart 4.3** shows numbers of customers with Rent to Own products only, and RTO products alongside other High Cost Credit products.



- RTO
- RTO & Home Credit
- RTO & Catalogue
- RTO & HCSTC
- RTO, Home Credit & Catalogue
- RTO, Home Credit & HCSTC
- RTO, Catalogue & HCSTC
- Home Credit, Catalogue, HCSTC & RTO

28 Financial Conduct Authority [accessed online at [fca.org.uk](http://fca.org.uk)], *High-Cost Credit Review Technical Annex 1: Credit Reference Agency (CRA) Data Analysis of UK Personal Debt*, 2017.

## Keys to understanding use of high cost credit

It is important to understand why people on low incomes use high cost credit.

**People lack alternatives.** Banks and other credit providers generally do not offer loans as small (usually under £1,000) as those that low income consumers are looking for. Low income consumers may not have an overdraft or a large enough overdraft available to them, because they have thin credit files or poor credit ratings, or they may simply be at their existing overdraft limit.

**High cost credit providers offer quick access to cash, and target potential consumers very effectively.** Online HCSTC providers may put money into customers' accounts within minutes of approval. Home credit providers can provide cash there and then on the doorstep.

Companies have finely honed marketing strategies, backed by significant budgets, aimed at getting the offer of credit to customers. Home credit companies have an effective face to face marketing and customer engagement model, often involving women working directly with other women.

**High cost credit providers may be flexible about repayment.** Customers of some forms of high cost credit are able to miss some payments. However, Home Credit companies price their loans in part to reflect their expectation that their customers will frequently miss payments without further penalty.

**Borrowing behaviour is often habitual.** There may be family traditions of using home credit, or family or friends may be involved in work as agents.

**Access to credit is reassuring.** Knowing a line of credit is most likely available to you removes stress, even though the cost of the credit may be high.

**The cost of money is not the same as the price of money:** The **cost** of money is the weekly or monthly payment for a given loan – e.g. £101.48 per month for 6 months on a £500 loan from Conduit.

The **price** of money is the APR generated by this – ranging from 2.68% for your mortgage, 18.9% for your credit card, 42.6% as the maximum charge from a credit union, 99.8% for a Conduit loan, or 1,293% for a Sunny loan.

The price of money is heavily influenced by the length of a loan, not just the amount, and though the APR is a good way of assessing your 25-year mortgage, it is a poor and misleading way of assessing a six-month loan for a small amount of money as the example below illustrates.

**This can be understood in this worked through example.** A woman walks into a wine bar on a Friday to meet a friend and asks if she can borrow £30 until next week. The friend hands over the cash. They meet the following Friday and the first woman returns the £30. She asks "What do I owe you?" The friend replies "Just buy me a small glass of house white and we're even". If the glass costs £3, what is the APR on that transaction (£3 on £30 over 7 days)? The surprising answer is 14,100%. If she had asked for a bigger glass costing £3.75, the APR increases to 45,600%.<sup>29</sup>

The **cost** of the loan is still a reasonable £3. The **price** of the loan is anything between 14,100% and 45,600%, a simply staggering figure which no-one would accept if put to them in that way. APR is not a good way of assessing value for money here.

<sup>29</sup> Provident Financial Group [accessed online at [providentfinancial.com](http://providentfinancial.com)] 2009 Corporate responsibility report 2009, pg 24.

## Changes in the high cost credit market

There have been significant changes across the high cost credit market over the last decade:

- The rise of high cost short term credit, followed by its fall in response to legislation (and partial recovery) and contraction of lenders;
- The contraction and complete market exit of rent to own providers in response to legislation looking to regulate their activities;
- The contraction of home credit providers, resulting from and accelerated by regulation, market changes and commercial mistakes.

### Payday and Rent to Own Lending

Payday lending became a new feature of the non-mainstream credit market in the second half of the 2000s, rapidly expanding to a peak in 2013 of 1.7m customers, taking out 10.3m loans worth £2.5bn<sup>30</sup>.

In 2014 legislation came into force to curb what were perceived as excesses in the market, the key changes being:

- The introduction of a price cap which means that customers cannot be charged more than 100% of the original loan value in fees and interest.
- The introduction of a £15 cap on default fees, and the capping of interest at 0.8% per day.
- Restricting the use of continued payment authority (CPA) to two.
- Limiting the number of times a loan could be rolled over.
- The placing of risk warnings on financial promotions.

The impact of these was immediate; the number of high cost short term credit customers in 2015 falling to 700,000, the number of loans to 3.3m and the value of loans to £800 million<sup>31</sup>.

As a result, over the last five years some of the main providers of payday lending, in particular The Money Shop, have gone from the high street, and online providers such as Wonga and Quick Quid have entered administration.

The market has not disappeared, however, as the 2019 figures for high cost short term credit show. There has been a shift to short term instalment loans, with the loan typically repaid across a three-month period.

The market is not wholly dominated by a small number of providers, although 10 firms account for 85% of lending. There has been a degree of fragmentation;

- The FCA reports 90 providers operating in this section of the market<sup>32</sup>.
- Analysis of creditor information provided by Stirling and Moray Councils counted around 20 and 27 providers respectively clearly operating in the high cost short term credit market.

Across this period, rent to own continued to be a small part of the high cost credit market. However, in response to concerns about aspects of the practice of rent to own retailers, the FCA introduced regulations in 2019, which required high cost credit providers to:

- Cap the total cost of credit at 100%
- Benchmark the base prices of goods against a median of three retail prices.
- Implement a 48 hour moratorium in cross selling warranty products;
- Refrain from raising the prices of other goods and services sold to rent to own consumers with the credit agreement<sup>33</sup>.

30 Financial Conduct Authority [accessed online at [fca.org.uk](http://fca.org.uk)], *High-Cost Credit Review Technical Annex 1: Credit Reference Agency (CRA) Data Analysis of UK Personal Debt*, 2017

31 Financial Conduct Authority [accessed online at [fca.org.uk](http://fca.org.uk)], *High-Cost Credit Review Technical Annex 1: Credit Reference Agency (CRA) Data Analysis of UK Personal Debt*, 2017

32 Financial Conduct Authority [accessed online at [fca.org.uk](http://fca.org.uk)], *Consumer Credit — High-cost Short-Term Credit Lending Data*, 2019.

33 Financial Conduct Authority, *FCA Confirms Introduction of Rent-to-Own Price Cap* 2019.

The response has been the partial withdrawal of the two key firms from the market;

- Perfect Home who have retracted to an online only offering.
- Brighthouse entered administration in March 2020.

Brighthouse found itself under significant pressure, with pre tax losses in the six months to September 2018 totalling £22.1m, as against losses in of £19.1m in the previous comparable six months. Brighthouse has also had to repay a significant amount of money to customers under an agreement with the FCA, which responded to concerns about aspects of its practice. This scheme was worth £14.8m<sup>34</sup>.

### Home Credit

The trend in the home credit market appears consciously to move from targeting 'sub-prime' to 'near prime' customers. Companies are moving away from poorer people (not the other way around). In 2009 Provident Financial, the main provider of home credit, had 1.8 million such customers. A typical customer would be a female aged 35-45, with children, living in social housing, in social class C2 or D with an income of £15,000. Their 2018 figure for home collected credit was around 400,000<sup>35</sup>. Though other companies have increased their presence (Morses, Non-Standard Finance) the overall figures in this part of the market are still much lower than when the market was at its peak.

## Customer responses to credit market changes

It is possible to explore what happens when people on low incomes face restricted access to credit.

One of the concerns about the introduction of legislation on high cost short term credit was where people would turn to meet their need for credit if the legislation reduced the availability of pay day loans. The FCA explored the experience of those rejected by pay day lenders and former pay day lender customers.

34 Financial Conduct Authority, *Rent-to-own provider BrightHouse to provide over £14.8 million in redress to around 249,000 customers* <https://www.fca.org.uk/news/press-releases/rent-to-own-provider-brighthouse-14-8-million-redress-249000-customers>, 2017.

35 A further 117,000 use an on-line product, Satsuma; Provident Financial Group [accessed online], *Annual Report 2018*, 2018.

**Table 4.3** sets out their findings<sup>36</sup>.

The three most common responses from both categories of respondent are to approach families, or to go without credit, whether deciding to go elsewhere, or not knowing where else to go.

This suggests that where credit is restricted there remains a demand for credit that is not met in the formal credit market, but also acts as a reminder that a recourse to borrowing is not an automatic response to financial difficulties.

### Accessing financial support from families

Research has been carried out into the experiences of people accessing financial support from families<sup>37</sup>. This identified families as significant sources of financial support for younger generations:

- 27% of people with adult offspring reported providing them with regular financial assistance, including 32% of those in the lowest skilled occupations.
- 28% of those providing such help report running down their savings / pensions in order to do so.
- Nearly half of those providing support to family members had done so to help cover their general cost of living, pay bills, pay rent, or to help because family members had run out of money at the end of the month.
- 'Top ups' are still being given to adult offspring in their 30s, 40s and 50s.
- 38% of recipients say they would not have coped without the 'family bank'.
- 39% say the first turn to their family when they need financial help, 63% of those who turn to any source, say they turn to their family first.

The importance of families as a source of financial support raises two issues with the potential to impact on the demand for credit:

- For how long will such support be available in the context of pressures on incomes, and the long term impact of current generational

36 Critical Research [accessed online at fca.gov.uk], *Price Cap Research Main Report*, 2017.

37 Keohane N, Gicheva N, Barlow A, *Britain's Family Bank; An Examination of Family Financial Support Across the Generations and Its Impact*, 2018.

Table 4.3

Action Taken/ Considered	Declined Payday Lender Applicants	Former Payday Lender Users
Approached/ borrowed from family	20%	16%
New payday lender/ company or doorstep loan (Home Credit)	10%	3%
Approached/ borrowed from friends	7%	5%
Other sources of borrowing	3%	2%
Got in more debt/ struggled/ been in trouble	2%	5%
Had to wait until wages/ benefits paid	3%	1%
Cut back generally	2%	–
Used savings I already had	1%	5%
Sold something	1%	–
Bank loan/ overdraft	1%	3%
Requested more time to repay/ had an arrangement	2%	4%
Unable to buy food/ cutback on food use/ used foodbank	1%	3%
Late/ unable to pay bills	1%	5%
Nothing- nowhere else to borrow from	18%	10%
Nothing- went without/ gave up/ managed	17%	12%
Nothing- emotional/ cried/ panicked stressed	1%	2%
Nothing- everything was/ would have been fine	1%	1%
Don't know/ can't remember	3%	20%

inequity which may leave the older adults of the future struggling financially?

- Where can those without access to family support access money?
- The COVID-19 crisis may also lead to a greater need for borrowing from other sources, with alternatives such as turning to family ceasing to be an option.

### Borrowing from illegal moneylenders?

The FCA research did not find much evidence of turning to illegal / unregulated sources of credit amongst respondents to its research, although this was perhaps not unexpected given the higher incomes of those using payday lenders compared with groups traditionally at risk of using moneylenders.

Research for Trading Standards Scotland focused on the experiences of people using illegal moneylenders and those working with them. Whilst it was not

focused on calculating the number of people in Scotland using illegal moneylenders, it found little evidence suggesting an increase in usage, with anecdotal evidence actually pointing other way<sup>38</sup>.

The research proposed a number of reasons for this lack of growth; the existence of the Scottish Welfare Fund and foodbanks as a buffer for those facing destitution, a preference for retrenchment and for turning to families, household and broader family situations not having quite reached the tipping point at which people are pushed to a last resort lender.

It also identified reasons for underreporting of usage to advice and other workers; fear of reprisal, shame, fear of loss of credit lines and a belief that advice workers would not be able to assist.

<sup>38</sup> Hopkins, N, with Craigforth, *Illegal Moneylending in Scotland*, Trading Standards Scotland, 2018.

# Section 5: High Cost Credit

## Current Local Market Size and Customer Base

The focus in this section is on determining the size of the market in the seven local authority areas for the four types of non mainstream credit identified in section 4; high cost short term credit, home credit, pawnbroking and rent to own.

### Estimates for Individual Types of High Cost Credit

#### High Cost Short Term Credit

The FCA has released data on the number of loans and value of loans in each postcode district in the UK. This data underpins the FCA's report on the use of high cost credit in the UK from January 2019<sup>39</sup>.

This data enables a very accurate estimate of the number and value of loans in each local authority. It is an estimate because postcode districts are sometimes split between different local authorities.

Using FCA data also enables the calculation of the number of HCSTC loans taken out per person borrowing in the market. This enables an estimate of the number of people in each local authority using HCSTC credit annually<sup>40</sup>.

**Table 5.1** sets out that data.

**Table 5.1**

	Aberdeen	Aberdeen-shire	Clackman-nanshire	Moray	North Lanarkshire	Perth and Kinross	Stirling
Estimated Customers	6,706	3,503	1,330	1,857	10,143	2,982	1,593
Estimated Originations	21,459	11,210	4,255	5,942	32,457	9,541	5,099
Average HCSTC Loan Size	£259	£265	£247	£251	£244	£228	£232
Estimated Value of HCSTC Originations (m)	£5.55	£2.975	£1.05	£1.49	£7.92	£2.18	£1.18

39 Financial Conduct Agency [available online at [fca.gov](https://www.fca.gov)] [FCA response to freedom of information request from WageStream](#) [FCA response FOI request](#)

40 Financial Conduct Authority [accessed online at [fca.org.uk](https://www.fca.org.uk)], [Consumer Credit — High-cost Short-Term Credit Lending Data](#), 2019.

## Home Credit and Pawnbroking

Similar data on actual borrowing is not available from the FCA at a postcode district or local authority level in relation to borrowing from home credit companies and pawnbrokers.

We have therefore generated a set of estimates for the number of customers borrowing in both markets using:

- FCA figures for the UK as a whole on the size of those markets in terms of customer numbers, originations, and average value of originations<sup>41</sup>.
- Information relevant to local borrowing behaviour and the prevalence of low income consumers in each local authority.

We have used the local borrowing/ demographic information in the generation of three sets of estimates:

- Estimates of the likelihood relative to the UK as a whole of an adult in the local authority using high cost short term credit. Although the demographics of HCSTC users are different to those of other forms of high cost credit, areas with high numbers of people from groups likely to use HCSTC are also likely to have high numbers of people from groups likely to use home credit and rent to own, and this estimate has the virtue of being based on actual customer behaviour in each of the local authorities.
- Levels of Employment and Support Allowance (formerly known as Incapacity Benefit) and Housing Benefit claimants, as proxy measures of low income prevalence in the respective local authorities<sup>42</sup>, acknowledging that significant numbers of customers in these markets will be claiming benefits/ tax credits, and there is an association between use of home credit and being long term unemployed/ being unable to work due to long term conditions<sup>43</sup>.

**Table 5.2** sets out estimates of the size of the home credit market in each of the 7 local authorities based on the prevalence of HCSTC usage locally.

**Table 5.2**

	Aberdeen	Aberdeen-shire	Clackman-nanshire	Moray	North Lanarkshire	Perth and Kinross	Stirling
Estimated Customers	2,754	1,438	546	762	4,165	1,225	654
Estimated Originations	6,692	3,495	1,327	1,853	10,121	2,976	1,589
Estimated Total Value of Loans (£m)	£5.15	£2.69	£1.02	£1.43	£7.79	£2.29	£1.22

41 Financial Conduct Authority [accessed online at [fca.org.uk](http://fca.org.uk)], *High-Cost Credit Review Technical Annex 1: Credit Reference Agency (CRA) Data Analysis of UK Personal Debt*, 2017.

42 Department of Work and Pensions [accessed online at [dwp.gov.uk](http://dwp.gov.uk)] *Stat-xplore*

43 Worton, S. et al, *Usage and experiences of High Cost Credit: Consumer Research Report* 2018.

**Table 5.3** sets out estimates of the size of the home credit market in each of the 7 local authorities based on levels of ESA claims in each area.

**Table 5.3**

	Aberdeen	Aberdeen-shire	Clackman-nanshire	Moray	North Lanarkshire	Perth and Kinross	Stirling
Estimated Customers	2,212	1,804	822	880	5,766	1,420	971
Estimated Originations	5,376	4,384	1,999	2,139	14,011	3,451	2,360
Estimated Loans Taken Out (£m)	£4.14	£3.38	£1.54	£1.65	£10.79	£2.66	£1.82

**Table 5.4** sets out estimates of the size of the home credit market in each of the 7 local authorities based on levels of HB claims in each area.

**Table 5.4**

	Aberdeen	Aberdeen-shire	Clackman-nanshire	Moray	North Lanarkshire	Perth and Kinross	Stirling
Estimated Customers	1,984	1,391	723	751	4,649	1,201	764
Estimated Originations	4,822	3,381	1,757	1,825	11,297	2,918	1,857
Estimated Loans Taken Out (£m)	£3.71	£2.60	£1.35	£1.41	£8.70	£2.25	£1.43

**Table 5.5** sets out estimates of the size of the pawnbroking market in each of the 7 local authorities based on the prevalence of HCSTC usage locally.

**Table 5.5**

	Aberdeen	Aberdeen-shire	Clackman-nanshire	Moray	North Lanarkshire	Perth and Kinross	Stirling
Estimated Customers	1,381	721	274	382	2,089	614	328
Estimated Originations	4,005	2,092	794	1,109	6,057	1,781	951
Estimated Total Value of Loans (£000s)	£1,201	£628	£238	£333	£1,817	£534	£285



**Table 5.6** sets out estimates of the size of the pawnbroking market in each of the 7 local authorities based on levels of ESA claims in each area

**Table 5.6**

	Aberdeen	Aberdeenshire	Clackmannanshire	Moray	North Lanarkshire	Perth and Kinross	Stirling
Estimated Customers	1109	905	412	441	2891	712	487
Estimated Originations	3217	2623	1196	1280	8384	2065	1412
Average Loan Size (£)	£300	£300	£300	£300	£300	£300	£300
Estimated Loans Taken Out (£000)	£965	£787	£359	£384	£2,515	£620	£423

**Table 5.7** sets out estimates of the size of the pawnbroking market in each of the 7 local authorities based on levels of HB claims in each area.

**Table 5.7**

	Aberdeen	Aberdeenshire	Clackmannanshire	Moray	North Lanarkshire	Perth and Kinross	Stirling
Estimated Customers	995	698	362	377	2,331	602	383
Estimated Originations	2,886	2,023	1,051	1,092	6,760	1,746	1,111
Estimated Loans Taken Out (£000s)	£866	£607	£315	£328	£2,028	£524	£333

## Rent to Own

The FCA's 2017 Technical Annex Report set out statistics relating to the number of customers using rent to own credit.

However, these national figures do not provide the best base for estimating local market size for this form of credit. Whereas access to high cost short term credit, home credit and pawnbroking provision is reasonably well distributed geographically, access to rent to own credit will vary given the smaller number of retail outlets and retailers involved. The significant closure of stores announced by Brighthouse in February 2019 will have increased local variation in use, and will have affected two of the local authorities that are the focus of this report (Perth and Stirling).

Brighthouse, the main rent to own retailer, provides an alternative way of calculating the customer based in each local authority, based on the figures contained within the annual report prior to the latest round of closures<sup>44,45</sup>. This stated that in the year to March 2018 the company had 281 stores, and 202,900 customers, an average of 722 customers per store, and average revenue per customer of £1,532.

44 BrightHouse Group Limited [accessed online at [brighthousegroup.co.uk](http://brighthousegroup.co.uk)], *Annual Report for the year ended March 31st 2018*, 2018.

45 This used to capture a snapshot of the demand now potentially unmet in the areas focused on in this report.

**Table 5.8** and **Table 5.9** set out estimates for the market size for rent to own credit in each of those areas, with account taken of the likely use of the Aberdeen store by some Aberdeenshire residents, and the likely larger size of that store and smaller size of stores in the smaller centres of Alloa (Clackmannanshire) and Elgin (Moray).

**Table 5.8**

	Aberdeen	Aberdeenshire	Clackmannanshire	Moray	North Lanarkshire	Perth and Kinross	Stirling
No. of Brighthouse Stores	1		1	1	5	1	1
Estimated No. of Customers	750	250	500	500	3,610	722	722
No. of Contracts Per Customer	2.6	2.6	2.6	2.6	2.6	2.6	2.6
Estimated Contracts Held by Customers	1,950	650	1,300	1,300	9,386	1,877	1,877
Average Annual Revenue Per Customer	£1,532	£1,532	£1,532	£1,532	£1,532	£1,532	£1,532
Estimated Annual Revenue (£m)	£1.149	£0.383	£0.766	£0.766	£5.531	£1.106	£1.106

**Table 5.9**

	Aberdeen	Aberdeenshire	Clackmannanshire	Moray	North Lanarkshire	Perth and Kinross	Stirling
Estimated Number of Customers	750	250	500	500	3,610	722	722
Estimated Number of Originations	818	273	545	545	3,935	787	787
Estimated Value of Originations	572,250	190,750	381,500	381,500	2,754,430	550,886	550,886

## Estimates of Total Market Size

Tables 5.10-5.12 sets out the range of estimates of the total market size for people using high cost credit, the number of annual originations, and the total value of annual originations in each of the seven local authorities.

Table 5.10: Market Size: Number of Customers<sup>46</sup>

	Aberdeen	Aberdeenshire	Clackmannanshire	Moray	North Lanarkshire	Perth and Kinross	Stirling
Estimated Number of Customers Using High Cost Short Term Credit	6,706	3,503	1,330	1,857	10,143	2,982	1,593
Estimate Range: Number of Customers Using Home Credit	1,984-2,754	1,391-1,804	546-822	751-880	4,164-5,766	1,201-1,420	654-971
Estimate Range: Number of Customers Using Pawnbrokers	995-1,381	698-905	274-412	377-441	2,089-2,891	602-712	328-487
Estimate Range: Number of Customers Using Rent to Own	750	250	500	500	3,610	722	722
Estimate Range: Total Number of Customers Using High Cost Credit	<b>9,486-10,537</b>	<b>5,311-5,875</b>	<b>2,409-2,785</b>	<b>3,168-3,344</b>	<b>18,188-20,373</b>	<b>5,006-5,305</b>	<b>2,997-3,430</b>

Table 5.11: Market Size: Originations

	Aberdeen	Aberdeenshire	Clackmannanshire	Moray	North Lanarkshire	Perth and Kinross	Stirling
Estimated Number HCSTC Originations	21,459	11,210	4,255	5,942	32,457	9,541	5,099
Estimate Range: Number of Home Credit Originations	4,821-6,692	3,380-4,384	1,327-1,997	1,825-2,138	10,121-14,011	2,918-3,451	1,589-2,360
Estimate Range: Number of Pawnbroking Originations	2,886-4,005	2,024-2,625	795-1,195	1,093-1,279	6,058-8,384	1,746-2,065	951-1,412
Estimated Number of Rent to Own Originations	818	273	545	545	3935	787	787
Estimate Range: Total Number of High Cost Credit Originations	<b>29,984-32,974</b>	<b>16,887-18,491</b>	<b>6,921-7,992</b>	<b>9,405-9,904</b>	<b>52,571-58,787</b>	<b>14,992-15,843</b>	<b>8,426-9,658</b>

<sup>46</sup> This is based on the sum of the estimates of people using HCSTC, home credit, rent to own credit and pawnbrokers, and the ratio at national level between the addition of those first three numbers and the total number of individuals borrowing in those parts of the high cost credit market, which stands at 1.1: 1.

**Table 5.12: Market Size: Value of Originations**

	Aberdeen	Aberdeenshire	Clackmannanshire	Moray	North Lanarkshire	Perth and Kinross	Stirling
Estimated Value HCSTC Originations (£m)	£5.550	£2.975	£1.050	£1.492	£7.919	£2.175	£1.183
Estimate Range: Value of Home Credit Originations (£m)	£3.713-5.153	£2.603-3.375	£1.022-£1.539	£1.405-1.647	£7.793-10.788	£2.247-2.657	£1.224-£1.187
Estimate Range: Value of Pawnbroking Originations (£000s)	£866-1,201	£607-787	£238-359	£328-384	£1,817-2,515	£524-620	£285-423
Estimated Value of Rent to Own Originations (£000s)	572	191	382	382	2,754	551	551
Estimate Range: Value of High Cost Credit Originations (£m)	<b>£10.701-12.476</b>	<b>£6.376-7.328</b>	<b>£2.692-3.33</b>	<b>£3.607-3.905</b>	<b>£20.283-23.976</b>	<b>£5.497-£6.003</b>	<b>£3.243-£3.974</b>

## Potential Customer Base

The potential new customer base for affordable credit providers looking to tackle the poverty premium consists of:

- People currently using high cost credit.
- People who have used high cost credit in the recent past.
- People on low incomes who haven't used high cost credit recently, but might be interested in an affordable/medium cost credit offer.
- People falling from near prime credit scores with other choices to sub prime (estimated by PFG to be c.2m per year who flit in and out)

The report has attempted to quantify the first group of people in the tables above. We do not believe it is methodologically possible to robustly estimate the size of the third group of people.

The final part of this section focuses on the second group of people, people who have used high cost credit in the recent past, using information from the FCA about people with outstanding high cost debt, then using that to generate a conservative estimate of the potential market size for affordable/ mid cost credit in each area.

## Calculating the Potential Customer Base

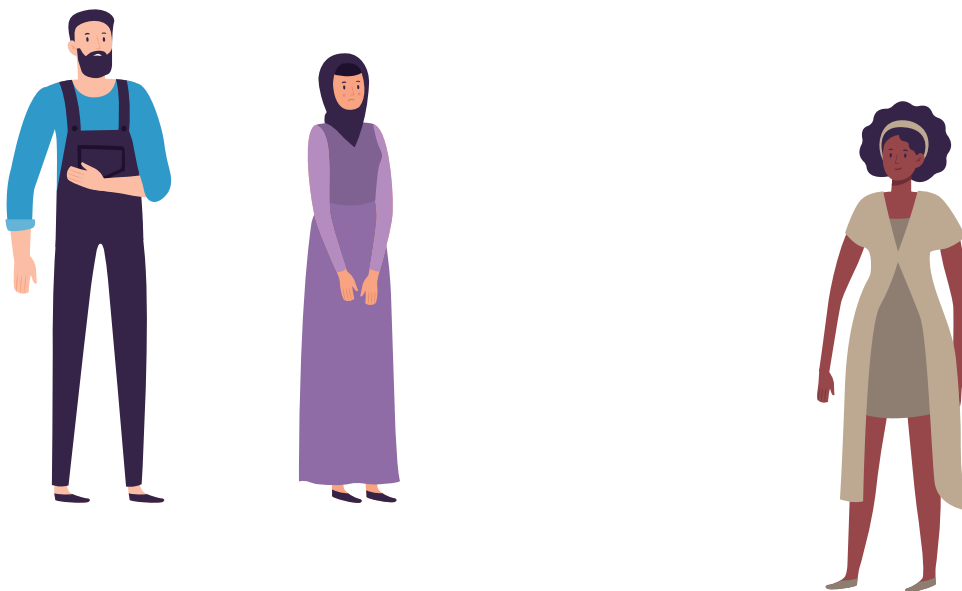
The FCA has set out information on the number of people who have outstanding debt on at least one high cost credit loan. Using this enables the generation of (conservative) estimates of the number of customers in each high cost loan market, based on the ratios calculated the FCA data between the annual number of customers and the number of customers with outstanding debt; 2:1 in the case of high cost short term credit and rent to own credit, and 2.3:1 in the case of home credit. We have applied a ratio of 2:1 for pawnbroking.

The **total** number of recent customers in the high cost credit market is calculated by the addition of the numbers in each individual market, divided by the ratio between that sum and total number of individuals recently in the high cost credit market, 1.2:1<sup>47</sup>.

**Table 5.13: Potential Customer Base in Each Local Authority**

	Aberdeen	Aberdeen-shire	Clackman-nanshire	Moray	North Lanarkshire	Perth and Kinross	Stirling
<b>Estimate Range: Total Potential Number of Customers Using High Cost Credit</b>	18,509-22,503	10,397-12,582	4,706-5,961	6,193-7,142	35,532-43,568	9,787-11,335	5,851-7,335

47 Financial Conduct Authority [accessed online at [fca.org.uk](http://fca.org.uk)], *High-Cost Credit Review Technical Annex 1: Credit Reference Agency (CRA) Data Analysis of UK Personal Debt*, 2017



# Section 6: Current low-income credit market penetration by affordable cost providers

This section provides an analysis of the extent to which credit unions and CDFIs, the two main socially driven providers of affordable credit to people on low incomes, are already meeting the demand for credit amongst low-income consumers in the seven local authority areas.

## Understanding the Providers

### Credit unions in Scotland

The development of credit unions in the UK as a distinct legal entity was enabled by the Credit Union Act 1979, but the growth of the sector was limited until 1999 when it became a primary objective of the government's financial inclusion strategy.<sup>48</sup>

The credit union sector in Scotland is more developed relative to the GB as a whole (Northern Ireland has significantly higher penetration and membership numbers and still operates a different interest rate level to GB); Scottish credit unions represent 20% of the sector, while the Scottish population makes up just 9% of the UK.

In 2018, there were 89 Scottish Credit unions, out of the 433 in the UK, with:

- 414,493 adult members (20.5% of the UK total) of whom 118,000 have loans;
- £350 million being lent (23.2% of the UK total), and an average loan of £2,920.

### Credit Union Provision in the seven local authorities

At the time of the research fieldwork, each of the seven local authorities had at least one credit union operational in their area;

- Aberdeen and Aberdeenshire are served by two credit unions.

- Clackmannanshire, Moray and Perth and Kinross are primarily served by a local community based credit union.
- North Lanarkshire is served by 17 credit unions.
- Stirling is served by three credit unions.

### Credit Unions and lending to people on low incomes

Research by Ipsos MORI for the Carnegie UK Trust highlighted the demographic / socio economic profile of credit union members, drawing on the Scottish Household Survey. It found that members broadly reflected the profile of the Scottish population<sup>49</sup>; rather than membership being concentrated amongst people on low income. Where there was variation from the Scottish average it tended to be in the direction of greater affluence, or characteristics associated with greater affluence.

The research found that in terms of:

- **Housing Tenure:** Credit Union account users broadly match the overall population in Scotland in terms of:
  - Tenure – 62% compared to 61% owning their home, and
  - 27% compared to 27% renting from a social landlord, whilst they were
  - Slightly less likely to be private renters, 11% compared to 15%.
- **Working status:** Credit Union account users were more likely to be working, 73% compared to 57%, and less likely to be retired, 16% compared to 28%.
- **Income:** Credit Union account users were more likely than the overall population to have a net annual household income above £20,000, 65% compared to 53%, and less likely to have an income less than £10,000, 7% compared to 13%.

48 HM Treasury, *Access to Financial Services*, Report of PAT 14, 1999.

49 Ipsos MORI Scotland, *Use of Credit and Financial Resilience: Analysis of the Scottish Household Survey*, 2018.

- **Financial Management:** Credit Union account users were broadly similar to the overall population; 44% were managing well, compared to 50% overall, 46% getting by, compared to 38% overall, and 10% were experiencing difficulties, compared to 12% overall.

## CDFIs in the UK

The development of the CDFI sector began much more recently than the credit union movement. Most CDFIs lend to businesses and social enterprises, but around ten lend to individuals. Many personal lending CDFIs are members of the trade body formerly the Community Development Finance Association now branded as Responsible Finance.

In 2018 personal lending CDFIs across the UK lent:

- £26 million in 45,900 loans to individuals (average loan size of £566);
- 23,230 of those taking out loans from a Responsible Finance personal lender had previously borrowed from a high cost lender.
- £5 million to 430 homeowners for home improvements.

## CDFIs in Scotland

Three CDFIs provide loans in Scotland; Fair for You, Five Lamps (Conduit) and Scotcash.

Fair for You was established in 2015 and offers an online product only. It made around 7,500 loans in Scotland last year, worth £2.48 million (average loan of £331), which represents very significant progress in a relatively short timeframe. They have successfully harnessed relationship style lending with transactional IT systems, thereby keeping the cost of loans down without the need for a local bricks and mortar presence. They have managed to build a loyal customer base via social media, and have a highly impressive rating of 4.9 out of 5 on Trustpilot, based on 6,000 reviews.

It is effective in targeting a low-income family customer base:

- 75% of its customers have children under 19 within the home.
- 60% of its customers are female lone parents.

- 50% are in employment, with over half of these in part time employment, 10% of these in low paid self-employment, and 3% on zero hours contracts.
- 33% have long-term health conditions, and 28% are caring for someone with a health problem or disability.
- The largest age group of customers is between 25 and 34<sup>50</sup>.

In July 2017, Five Lamps (Conduit) began operation in Fife, Falkirk and West Lothian under an agreement with those local authorities to deliver mid cost loans. At the start of September 2019, they had delivered over 2,700 loans to the value of £1.45m (average £537) to low income consumers and helped a number access other financial and debt services from local authorities and third sector organisations.

The aggregated statistics for CDFIs show that lenders like Scotcash and Conduit cater mainly for women (61%), those on benefits (66%), single parents (42%), those in social rented housing (53%) and those with an income under £15,000 (48%).<sup>51</sup>

Scotcash was established in 2007 with support from Glasgow City Council, Glasgow Housing Association, Communities Scotland and RBS. In 2018/19 it delivered around £2m million in 5,057 small loans a year to its customers (average loan size of £406) and has recently opened up operations in Inverclyde and Edinburgh.

Scotcash is effective in targeting low income consumers;

- 42% are single parents, and 40% are single adults,
- Five in six rent from a social landlord, the vast majority of the remainder from a private landlord.
- 45% have a long term condition impacting on their life.
- About the same proportion can't work, or can only work limited hours because of caring responsibilities.

Scotcash has also sought to move increasingly to online lending. In 2015 Scotcash had 70% of customers coming into a branch and 30% online. By 2018/19 the figures were 30% in branch and 70% online. This swing to online has continued and accelerated in 2020.

50 Gibbons, D. *The Social Impact of Fair for You* Centre for Responsible Credit: 2016.

51 Dayson, K et al, *Scaling up the UK personal lending CDFI sector*, 2020.

## Estimating Current Affordable/ Mid Cost Credit Provision in the Seven Areas

There is a dearth of publicly available statistics on lending by individual affordable/ medium cost credit providers. We have had to directly approach individual providers for information, and the return of information remained incomplete at conclusion.

This means that in each of the seven local authority areas we have had to take a different approach to calculating the extent of current provision.

For each local authority we have either the actual numbers and value, or a very accurate estimate of the numbers and value of loans taken out by customers of each of the CDFI.

For Aberdeen and Aberdeenshire, Clackmannanshire, Moray, Perth and Kinross and Stirling we have information from the credit unions which provide the vast majority of credit union loans in that local authority.

This information usually includes:

- The number of adult members;
- The number of loans taken out;
- The value of loans taken out.

For some credit unions we also have information on the number and value of loans targeted specifically at people on low incomes who may previously have been using high cost credit, usually in the form of loans guaranteed by benefit payments. Where we do not have this information we used the Carnegie research on credit union demographics<sup>52</sup> to estimate the number and value of loans made to customers on low incomes, or make the assumption that loans made under £1000 are made to people on low incomes with few other credit choices.

For North Lanarkshire we have information from two of the largest community based credit unions, and a large regional credit union. In this area we have therefore made use of data from the Scottish Household Survey to estimate the number of credit union members in the area.

<sup>52</sup> Ipsos MORI Scotland, *Use of Credit and Financial Resilience: Analysis of the Scottish Household Survey, 2018*





## Aberdeen and Aberdeenshire

### CDFI Provision

Each of the CDFIs has made some loans in Aberdeen and Aberdeenshire.

In Aberdeen:

- Fair for You has made 187 loans to a value of £62,965 since January 2016, an estimated 73 loans to a value of £26,707 in the year ending October 2019.
- Five Lamps/ Conduit has made 20 loans to the value of £11,350 in the year ending August 2019, with no lending made before that.
- Scotcash has made 8 loans to an estimated value of £3,520 over the last 18 months, an estimated 7 loans to the value of £3,080 over the year ending July 2019.

This suggests a market penetration of 215 loans to the value of £77,835, 100 loans to the value of £41,137 in the year ending October 2019.

In Aberdeenshire:

- Fair for You has made 159 loans to a value of £55,516 since January 2016, an estimated 62 loans to a value of £23,547 in the year ending October 2019.
- Five Lamps/ Conduit has made 4 loans to the value of £2,700 in the year ending August 2019, with no lending made before that.
- Scotcash has made 4 loans to an estimated value of £1,760 over the last 18 months, an estimated 3 loans to the value of £1,320 over the year ending July 2019.

This suggests a market penetration of 167 loans to the value of £59,976, 69 loans to the value of £27,567 in the year ending October 2019.

### Credit Union Provision

There are two credit unions operating in Aberdeen / Aberdeenshire, both of which have provided extensive information about their lending and the savings held with them:

- Grampian Credit Union serves the whole of both local authority areas.
- St Machar Credit Union has a common bond covering part of the Aberdeen City Council area.

In 2017/18 Grampian Credit Union:

- Had 4,206 adult members, holding £4.232m in savings, with 868 loans worth £2.174m being repaid.
- Of those 868 loans; 318 loans were of £500 or less, 322 between £500 and £1,000, 150 between £2,000 and £5,000 and 68 were for £5,000 plus.
- 44% of loans were made at between 26.8% and 42.5% APR.
- Issued 325 loans during the year; 137 loans worth £76,075 were made to people solely repaying through benefits.

St Machar Credit Union:

- Has 3,425 adult members, and 1,398 juvenile members who hold £1.942m in savings.
- Made 1,578 loans between April and September 2019 to the value of £779,372.
- 55% of those loans were of a value less than £1,000, 45% were of a value between £1 and £5k.

### Market Penetration

We estimate that 1,856 loans per year are made to people on low incomes by credit unions in Aberdeen, and 120 in Aberdeenshire, alongside 100 and 69 respectively by CDFIs, making a total of 1,956 loans in Aberdeen and 189 in Aberdeenshire.

## Clackmannanshire

### CDFI Provision

In Clackmannanshire:

- Fair for You has made 119 loans to a value of £34,584 since January 2016, an estimated 46 loans to a value of £14,669 in the year ending October 2019.
- Five Lamps/ Conduit made 12 loans to the value of £5,200 in the last 2 years, 9 loans and £4,300 in the year ending August 2019.
- Scotcash has made an estimated 15 loans to an estimated value of £6,600 over the last 18 months, an estimated 9 loans to the value of £3,960 over the year ending July 2019.

This suggests a market penetration of 142 loans to the value of £46,384, 64 loans to the value of £22,929 in the year ending October 2019.

### Credit Union Provision:

Clackmannanshire is served by Clackmannanshire Credit Union, which provided extensive information on its lending and membership.

Clackmannanshire CU is a volunteer led operation. In the year to 31<sup>st</sup> August 2019, it:

- Had 566 adult members, with £454,000 of savings and £229,000 of loans being repaid.
- Issued 139 loans, with *those still being repaid* value banded as follows; 28 less than £500, 22 between £500 and £1000, 28 between £1,000 and £2,000, 23 between £2,000 and £5,000 and 9 of more than £5,000.

### Market Penetration

We estimate that 63 loans per year are made to people on low incomes by credit unions in Clackmannanshire, alongside 64 by CDFIs, making a total of 127 loans.

## Moray

### CDFI Provision

In Moray:

- Fair for You has made 57 loans to a value of £19,920 since January 2016, an estimated 22 loans to a value of £8,400 in the year ending October 2019.
- Five Lamps/ Conduit made 2 loans to the value of £900 in the year ending August 2019, with no lending before.
- Scotcash has made 1 loan to an estimated value of £440 in the year ending July 2019.

This suggests a market penetration of 60 loans to the value of £21,260, 25 loans to the value of £9,740 in the last year.

### Credit Union Provision

Moray is served by Forres Area Credit Union which provided extensive information about its membership and lending. Forres Credit Union has one full time member of staff and three others working a small number of hours per week.

It has:

- 2,170 adult members, although fewer than 1,000 are active, 655 young members.
- The value of savings it holds is £1.24m, with lending at around 400 loans worth £400,000 per year.
- Over half the loans it makes are at 12.8-27.6% APR, about one fifth at 42.6% APR, very few at 12.68% APR.
- 85% of the loans it makes are unsecured.

### Market Penetration

We estimate that 140 loans per year are made to people on low incomes by credit unions in Moray, alongside 25 by CDFIs, making a total of 165.



## North Lanarkshire

### CDFI Provision

In North Lanarkshire:

- Fair for You has made 731 loans to a value of £242,974 since January 2016, an estimated 284 loans to a value of £103,058 in the year ending October 2019.
- Five Lamps/ Conduit made 69 loans to the value of £37,550 in the year ending August 2019, with no lending before.
- Scotcash has made an estimated 351 loans to the value of £154,440 over the last 18 months, an estimated 227 loans to the value of £99,800 over the year ending July 2019.

This suggests a market penetration of 1,151 loans to the value of £464,964, 580 loans to the value of £240,408 in the year ending October 2019.

### Credit Union Provision:

North Lanarkshire is served by 17 credit unions.

- Abronhill Credit Union
- Chryston and District Credit Union
- Croy and Kilsyth Credit Union
- Cumbernauld Central Credit Union
- Kilsyth and Villages Credit Union
- Kirklands Credit Union
- Lanarkshire Credit Union
- Mosshill Credit Union
- Motherwell and District Credit Union
- Newarthill Credit Union
- Newmains Credit Union
- North Airdrie Credit Union
- North Coatbridge Credit Union
- Scotwest Credit Union
- South Coatbridge Credit Union
- Thornliewood Credit Union
- Wishaw Credit Union

Only three of those credit unions provided extensive information about their membership and borrowing; Motherwell Credit Union, Newarthill Credit Union and Scotwest Credit Union.

Motherwell Credit Union has a single office in Motherwell town centre and is in the process of developing an online offer for its members. Last year it:

- Had 2,195 adult members, 256 younger members.
- Issued 1,174 loans to the value of £1.288m.
  - 255 under £500 in value.
  - 286 between £500 and £1,000 in value.
  - 363 between £1,000 and £2,000 in value.
  - 214 between £2,000 and £5,000 in value.
  - 55 of more than £5,000 in value.

Newarthill Credit Union has a permanent office in Newarthill, just outside Motherwell, and seven staff. Last year it:

- Had 5,204 adult members, 875 younger members, who hold £13.415m of savings.
- Made 2,175 current loans issued to the value of £5.388m, in the following size bands:
  - 377 under £500 in value.
  - 380 between £500 and £1,000 in value.
  - 497 between £1,000 and £2,000 in value.
  - 648 between £2,000 and £5,000 in value.
  - 273 of more than £5,000 in value.

Scotwest Credit Union lends across the West of Scotland. In North Lanarkshire

- It currently has 7,353 members, holding £18.036m in savings.
- Members are currently repaying 3,146 loans, of which 22 are mortgages.
- The total value of those loans is £15.119m, £13.195 without including the mortgages.
- Of those loans
  - 566 of the loans are for up to £500, a total value of £271K.
  - 1,514 are for between £500 and £4,999, a total value of £3.198m.
  - 664 are for between £5000 and £9999, a total value of £4.287m.
  - 380 are for between £10000 and £30000, a total value of £5.439m.

## North Lanarkshire

continued

### Market Penetration

The information received from credit unions serving North Lanarkshire is so incomplete that it is difficult to extrapolate from the above.

However, the Scottish Household Survey in 2015 asked respondents to indicate whether they had a credit union account. 12% of respondents in North Lanarkshire indicated that they did as against 4% of respondents in Scotland. This fits with the high number of credit unions operating on the ground in the area.

This would suggest that around there are around 33,000 adults who are members of credit unions in North Lanarkshire.

If the relationship across its 17 credit unions between loans and members reflects that which holds for Newarthill CU members, this suggests 14,900 loans per year being made by credit unions in North Lanarkshire.

We therefore estimate that 5,200 loans per year are made to people on low incomes by credit unions in North Lanarkshire, alongside 580 by CDFIs, making a total of 5,780.



## Perth and Kinross

### CDFI provision

In Perth and Kinross:

- Fair for You has made 133 loans to a value of £43,210 since January 2016, an estimated 52 loans to a value of £18,327 in the year ending October 2019.
- Five Lamps/ Conduit has made 19 loans to the value of £11,300 in the year ending August 2019, with no lending before.
- Scotcash has made 20 loans to the value of £8,800 over the last 18 months, an estimated 14 loans to the value of £6,160 in the year ending July 2019.

This suggests a market penetration of 165 loans to the value of £59,510, 85 loans to the value of £35,787 in the year ending October 2019.

### Credit Union Provision

Perth and Kinross is served by Perth and Kinross Credit Union.

Perth and Kinross Credit Union has 1,288 adult members, and 24 juvenile members. As at September 2019 there were 572 active loans.

The focus of its work with people on low incomes is through 'freedom' loans, of up to £300 which are accessible under the following conditions to people who are out of work, on benefits or earning a low wage, with an income not less than £90 a week and are prepared to become a member of the credit union. Interest on these loans is charged at 42.6% and borrowers must have at least one state benefit or tax credit paid into their account, and save alongside repayments. In the year to September 30<sup>th</sup> 2019, it made 933 freedom loans.

### Market Penetration

933 loans per year are made to people on low incomes by credit unions in Perth and Kinross, alongside 85 by CDFIs, making a total of 1,018.

## Stirling

### CDFI provision

In Stirling:

- Fair for You has made 100 loans to a value of £30,493 since January 2016, an estimated 39 loans to a value of £12,934 in the year ending October 2019.
- Five Lamps/ Conduit has made 13 loans to the value of £5,800 in the last 2 years months, 4 loans to the value of £1,800 in the year ending August 2019.
- Scotcash has made 19 loans to the value of £8,360 over the last 18 months, an estimated 14 loans to the value of £6,160 over the year ending July 2019.

This suggests a market penetration of 121 loans to the value of £44,653, 57 loans to the value of £20,894 in the year ending October 2019.

### Credit Union Provision

Stirling is served by:

- Cornton and District Credit Union.
- Cowie Credit Union.
- Stirling Credit Union.

Detailed information was received from Stirling Credit Union, but not from either of the other credit

unions. Some publicly available information was accessed in relation to Cornton and District Credit Union and Cowie Credit Union.

Stirling Credit Union operates from its base in Stirling, served by 4 part time staff. It was formerly Stirling Council Credit Union. It has:

- 995 adult members and 612 juniors holding £1.123m in savings.
- It has a loan book of £409,000, with 230 loans currently being repaid.

In 2016/ 17 Cornton and District Credit Union:

- Made loans worth £103,300 to members.
- Held members' deposits of £245,790.

In 2016/ 17 Cowie Credit Union reported:

- 140 members, holding just over £108,000 in savings.
- Making 15 loans worth a total of £17,750.

### Market Penetration

We estimate that 116 loans per year are made to people on low incomes by credit unions in Stirling, alongside 57 by CDFIs, making a total of 173.

## Reflections on this section

- Headline figures on credit union membership often hide a smaller impact in terms of affordable lending, particularly in terms of affordable lending to people on low incomes.
- Credit unions offering loans that are quasi-guaranteed by benefits make significant numbers of loans to people on low incomes.
- There is some 'leakage' from the areas in which Five Lamps and Scotcash operate with the support of a number of local authorities, but generally not to a significant extent.
- Fair for You has been successful in establishing a significant profile across Scotland, including the seven local authorities, through effective online marketing.

## Section 7: Size of the Provision Gap

The previous two sections have set out estimates of the size of the high cost credit market in each of the seven local authority areas, and of the amount of lending done by CDFIs and credit unions, in each area.

Table 7.1 sets out our estimate of the provision gap in each area, by expressing the number of loans made by community lenders as a percentage of the number of loans made by high cost providers.

It is clear that:

- The gap between the number of loans made by affordable / mid cost credit providers and the number of high cost credit originations in each local authority area is very large.

- The penetration made in that market by the organisations in whom hopes for providing an alternative to high cost lending are vested are currently small or very small, with the partial exceptions of Aberdeen, North Lanarkshire and Perth and Kinross.
- Closing this gap will require a significant effort from key partners, and is likely to prove a long term project, with many staging posts along the road to success.

Table 7.1

	Aberdeen	Aberdeen-shire	Clackman-nanshire	Moray	North Lanarkshire	Perth and Kinross	Stirling
Estimated Number of Loans Made by Community Lenders	1,956	189	127	165	5,780	1,018	173
Estimated Number of High Cost Credit Originations	29,984-32,974	16,887-18,491	6,921-7,992	9,405-9,904	52,571-58,787	14,992-15,843	8,426-9,658
Loans Made by Community Lenders as Percentage of High Cost Credit Originations	5.9%-6.5%	1.0%-1.1%	1.6%-1.8%	1.7%-1.8%	9.8%-11.0%	6.4%-6.8%	1.8%-2.1%

## Section 8: Future Possibilities

It is one thing to explore the potential size of a market, it is another to assess the level of penetration into that market that might realistically be achieved.

This section therefore focuses on the performance of Five Lamps, which provides mid cost credit in Falkirk, Fife and West Lothian. It sets the number of loans that it has made against the potential size of the high cost credit market in those areas, and suggests that its performance forms a benchmark for the level of penetration into that market that might be achieved by relatively modest investment.

### Five Lamps Market Penetration

Five Lamps was established in Stockton-upon-Tees in 1985. Its first focus was on unemployment and youth unemployment, but in 2007 it diversified into personal lending. Conduit (its trading subsidiary for loans) is now a separate entity within the Five Lamps family and won the Consumer Credit Association Award for 'Best Newcomer' in 2019. In 2017/18 Conduit made 7,000 loans worth £4.4 million across the UK. It has just received investment of c.£5 million from a consortium of social investors to make 100,000 loans over the next six years.

Conduit charges 99.9% APR. This means on a £500 loan over 52 weeks, the customer will pay £697.32, compared to £910 with Morses Club, £936 with Provident and £995 with Satsuma. This means that the annual savings range between £213 and £298.

**Table 8.1 sets out the estimated number of loans, market value and number of borrowers annual market for high cost credit in Falkirk, Fife and West Lothian.**

	Falkirk	Fife	West Lothian
Estimated Number of Customers	7,734-8,061	15,008-18,634	8,898-9,313
Estimated Number of Loans Per Year	23,226-24,155	42,544-47,168	26,958-28,156
Estimated Value of Loans Per Year	£8.039m-£8.726m	£15.115-£17.762m	£9.270m-£9.972m
Estimated Number of Potential Customers	15,116-17,211	29,346-35,589	17,396-19,890

**Table 8.2 sets out figures on lending by Five Lamps in Falkirk, Fife and West Lothian.**

	Falkirk	Fife	West Lothian
Number of Loans Made in Year Ending August 2019	261	555	325
Value of Loans Made in Year Ending August 2019	£135,986	£314,087	£191,555
Number of Loans Made Since Beginning of Operation	445	1148	684
Value of Loans Made Since Beginning of Operation	£225,679	£618,208	£373,762

**Table 8.3 sets out figures for market penetration by Conduit**

	Falkirk	Fife	West Lothian
Number of Loans Made by Five Lamps	261	555	325
Estimated Number of High Cost Credit Originations	23,226-24,155	42,544-47,168	26,958-28,156
Loans Made by Community Lenders as Percentage of High Cost Credit Originations	1.1%	1.2% - 1.3%	1.2%

## Section 9: Our conclusions

### There is a need and an opportunity

- Prior to COVID-19 there was a significant demand for small sums of credit from low income groups in all seven areas: a market of 49,000 people, potentially 100,000 people.
- COVID-19 could further increase the demand for credit from low income groups.
- Commercial supply is both changing and reducing as lenders move to less risky and more profitable groups.
- Affordable lenders are doing valuable work but so far at too small a scale to make a significant difference;
  - Combined CDFI/Credit Union lending across most of the seven areas is less than 2% of the current market and less than 2% of the potential customer base, except in Aberdeen, Perth and Kinross, and North Lanarkshire;
  - Credit unions and CDFIs have different customer bases. Credit unions do make a contribution to providing loans to people on low incomes, but their sustainability depends on balancing this with meeting the needs of higher income customers wanting larger and longer-term loans. CDFIs typically serve those wanting to borrow c£500 over a term less than 12 months.
- The benefits of supporting activity by credit unions and CDFIs to increase penetration in their respective market areas are considerable;
  - The potential saving on £500 borrowed over six months from a CDFI is £230 to £339 (compared with Provident and with Sunny);
  - If a market penetration of 7% could be achieved, it should be possible to be delivering 9,500 loans, worth £4.75 million a year, saving customers up to £2.8million.

- If a 10% share could be achieved, this would be 13,800 loans worth £6.9 million and saving up to £4.1 million. This would be a sound base for further growth.

- There is policy and financial support to build a bigger, sustainable, contribution from ethical lenders, but this needs to move from words to actions.

### The nature of the opportunity

We strongly argue that there is a significant opportunity for the seven local authority areas, with support from the CUKT and the Scottish Government to:

- Give a new focus to the provision of affordable credit as part of efforts to respond to and recover from the COVID-19;
- Use affordable credit as a **spearhead** to engage with low income consumers who need small scale loans and provide a **gateway** to;
- Link them to other services (savings, insurance);
- Link them to other types of support (including longer-term solutions to poverty);
- Have a direct impact on disposable income of people struggling, especially families with children;
- Provide an additional string to the bow in fight against poverty and child poverty.
- Generate wider benefits on financial capability, financial resilience and financial wellbeing through:
  - Reducing customers' stress and improving their mental health,
  - Helping customers change their financial behaviour, and sustain their tenancies, and
  - Improving council tax and rent payment
- Be a focus for joining up services in a better way.



## The challenges and how they might be overcome

We are clear that delivering successful and sustainable outcomes which have a lasting impact is achievable, but also difficult. There are a number of challenges:

- The range of many other urgent, important, competing priorities brought by the COVID-19 crisis and the capacity of services to respond to these demands.
- The need for affordable credit providers to develop new delivery models that meet the requirements of COVID-19 restrictions.
- The need for a small 'p' political will to see this as a priority and to bring about collaboration within local authority and third sector services;
- The need to focus individual organisations on what they can do well and effectively;
- The need for partners to be realistic about sustainability and the sort of investment required to make a difference;
- Recognising that affordable credit partnerships work best when a number of specialists collaborate, perhaps co-locate, and focus on their area of business expertise. Scotcash / Conduit / Fair for You sell money (and know their customers' needs) but refer people who shouldn't be borrowing money to a CAB or to other debt or money advice services;
- Recognising that finance is a volume business and that scale is important. It is likely that any work to expand CDFIs will have to work across council boundaries and not be constrained by them.
- Recognising that lending money is a trust-based service. Ambrose Bierce defined an acquaintance as "someone you know well enough to borrow from, but not well enough to lend to". Lenders need to trust customers (and vice versa) and that those supporting affordable lenders need to build trust. This takes time to develop. In our experience, it takes between two and three years for an effective local service and partnership to be in.

These challenges can be overcome because:

- There are existing and effective delivery mechanisms. The right expertise and track record is there; be that with existing CDFIs or credit unions, to tackle specific aspects of financial exclusion;
- There are potential partners. Non-financial organisations are present in sufficient scale and sufficient expertise in each of the local authority areas; be they housing associations, CABx, money advice services or welfare rights organisations;
- There has been successful collaboration to date;
- There are willing sources of funding and other support, such as CUKT (through the Affordable Credit Loan Fund), Fair4All Finance and potentially the End High Cost Credit Alliance;
- The policy framework being developed by the Scottish Government is a positive one.

## An effective local authority response

How local authorities and others respond to these opportunities and challenges depends on local factors. Our view, based on our findings, is that the responses can be 'layered'; in the following way:

- **Do nothing** – though the findings of this research may be interesting and informative, they are not a priority over the next three to five years because of other, more pressing local issues;
- **Do a little** – existing initiatives and powers can be used in a more effective way. For example, local authorities, housing associations and third sector organisations could use existing channels to promote affordable credit alternatives and to support credit unions to develop payroll savings schemes in their area.
- **Do more** – local authorities could take a decision to look at how best to create and deliver

affordable credit products (and complementary products) in their area, or in partnership with other areas (following the precedent set by Fife, West Lothian and Falkirk). As we have suggested earlier, this would involve:

- Identifying the specific roles for credit unions and CDFIs, and how these might develop over time;
- Identifying what they would want from affordable credit providers in terms of how many loans made and who to, and commissioning accordingly;
- Identifying non credit outcomes they want, for example referrals through affordable credit providers acting as a gateway to other services;
- Identifying internal services that could support affordable credit providers in kind, through referral, marketing and premises;
- Identifying key external partners, including housing associations, third sector organisations and banks.
- Identifying external sources of finance and other support.

## Our recommendations

### For local authorities

We recommend that each of the seven local authorities we have looked at considers the conclusions in the report at a strategic level and decides where it wants to be on the spectrum from ‘do a little’ to ‘do more’.

We recommend that every local authority develops an action plan aimed at increasing the availability of affordable credit in their area. Post COVID-19 there will be an increased demand for credit, and local authorities can support people to access to affordable credit rather than high cost alternatives.

Action plans should:

- Consider the contributions that both CDFIs and credit unions can make to promoting access to affordable credit, and involve them in development and delivery;
- Outline clearly the level of in kind and financial

investment local authorities and other partners will make in increasing affordable credit;

- Set realistic targets for increasing the availability of affordable credit in their area and monitor them;
- Involve those organisations engaging with low income residents around issues relating to money, including council tax payment teams, social landlords, and welfare rights and money advice organisations.

Those local authorities deciding to ‘do more’ should scope out a prospectus for commissioning an affordable credit provider. We provide a template for this at Appendix B.

### For Carnegie UK Trust

Carnegie is already playing a leading role in this area through the Affordable Credit Loan Fund, and its activities supporting the policy work within F4AF and the End High Cost Credit Alliance, along with its support for payroll savings and loans with credit unions.

We recommend that CUKT:

- Seeks a discussion with the Financial Conduct Authority about how the information it holds on high cost credit use might be made more accessible to local authorities as a way of encouraging them to take action as well as a planning tool. This will depend on the legal and regulatory powers of the FCA;
- Considers the value of further research into the experiences of low-income credit union customers using loans secured by benefit payments;
- Works with the Scottish Government, ABCUL, the Scottish League of Credit Unions and the CDFIs operating in Scotland to develop a common set of measures against which progress on tackling financial exclusion can be made, and financial indicators on which all affordable credit providers in receipt of public funding are expected to report;

- Considers how to deepen its existing offer by looking at other ways in which affordable credit can be delivered;
- Considers how to broaden its offer by promoting the conclusions in this report to other local authorities;
- Considers how best to use its unique ‘convening’ power in Scotland to bring together other actors who may want to supply finance or organisational support to affordable credit providers.

### For the Scottish Government

We note the Scottish Government’s commitment to promoting the agenda on affordable credit, including its financial support for the Affordable Credit Loan Fund and investment in credit unions. We recommend that it:

- Continues to invest in affordable credit providers and broadens this beyond credit unions to look at how all affordable credit providers can meet market needs.

### For Affordable Credit Providers

#### Credit Unions

Credit unions can have an important role to play in increasing the availability of affordable credit and savings to people on low incomes, though this may not be their main business. We think that they should concentrate on the market areas they are most effective in and can build a sustainable future from.

We recommend that Credit Unions in each of the seven local authorities:

- Consider how best to develop loan and savings schemes with employers;
- Consider their appetite for delivering and capacity to deliver loans backed by benefit payments. Where they are doing so already, think about their appetite and capacity to expand this provision.

- Consider how developing their offer to low income customers affects their long term financial sustainability, and how they can maintain balance in their customer base by attracting other customers;
- Look at how to improve their marketing to reach and attract the right customers;
- Look at significantly improving their IT and data systems;
- Look at how best to collaborate with CDFIs in their area.

#### CDFIs

CDFIs have a key role in delivering loans directly targeting people on low incomes struggling to access mainstream credit provision.

We recommend that the three personal lending CDFIs working in Scotland:

- Consider the five action areas contained within the Fair4All Finance “Transforming Affordable Credit in the UK” report<sup>53</sup> and the University of Salford “Scaling Up the UK personal lending CDFI sector” report<sup>54</sup>, both published in February 2020, particularly those in relation to marketing, IT and back office development, and opportunities for greater coordination among CDFIs.
- Prepare to engage with those of the seven local authorities who decide to proceed to develop an affordable credit strategy, and seek to consider how they might grow their business in those areas even in the absence of significant local funding.

53 Fair4AllFinance [available online at [fair4allfinance.org](http://fair4allfinance.org)] *Transforming Affordable Credit in the UK 2020*.

54 Dayson, K et al, *Scaling up the UK personal lending CDFI sector*, 2020

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# Appendix A: The cost and price of money

APR is a poor way to judge short term, small sum loans. The illustration below shows the impact of APR on short terms. Each is £100 borrowed with the total charge for credit (TCC) of £120, i.e. the borrower repays £120 in every case (principal and interest). It is the term that makes the difference from 9.6% APR over 48 months to 791.6% over 1 month.

Borrow	Repay	Interest	Term (months)	Instalment cost	APR
£100	£120	£20	48	£2.50	9.60%
£100	£120	£20	36	£3.33	13.0%
£100	£120	£20	24	£5.00	19.8%
£100	£120	£20	12	£10.00	41.3%
£100	£120	£20	6	£20.00	89.5%
£100	£120	£20	3	£40.00	203.7%
£100	£120	£20	1	£120.00	791.6%

***It is cost rather than price that matters to consumers***

# Appendix B: Commissioning an affordable credit service

We wish to commission an outside organisation to deliver the following services:

- Loans which will reflect the current home collected credit, rent to buy and HCSTC markets. We expect these loans to be largely between £250 and £500, but going up to £1,000 with repayment over a period of between 26 and 52 weeks;
- A savings account to those borrowing money;
- Opening a bank account for borrowers where this is appropriate;
- Access to financial advice and support, especially for individuals who are rejected for loans;
- A robust monitoring and evaluation process which will help us identify the savings being made compared with other alternatives, as well as the longer-term impacts on health and a range of other factors (such as rent arrears, family stability). This will enable us to assess the value for money of this type of intervention.

## Service specification

### Principles

We have two underlying principles in commissioning this service:

- Payment by results – we will clearly specify targets and the consequences of failing to meet them;
- A ‘black box’ approach – we will allow the organisation to describe what it sees as the best method of delivery and not specify a particular methodology (though we want you to tell us about your methodology and why you think it will be most effective).

In addition, we may be able to offer free office accommodation in parts of our area from which services can be delivered. This will depend upon the delivery model chosen and will be subject to negotiation at the next stage. Your proposal should clearly indicate the level and type of investment required to deliver the outputs we want.

### Details

Based on information from external consultants and evidence from similar types of operations, we are looking for (specify figures as required):

- A minimum of 000 loans in each year of operation;
- A minimum of 000 savings accounts in the first year of operation, increasing to 000 in subsequent years;
- A minimum of 000 bank accounts opened in the first year of operation and 000 in subsequent years;
- A minimum satisfaction rating of 80% from customers and 80% from advice agencies;
- An annual evaluation which can identify;
  - Level of savings made by customers compared with previous loans;
  - Other impacts to be agreed.

## Information we require

In order to assess the best value for money, we will expect you to produce a draft business plan which will describe in detail how you will achieve the targets outlined in the previous section, and any other areas in which you can add value. This must include:

- Your method of delivery and why it will be effective (for example, through shops, through a telephone or web site, through branch offices);
- The staff resources you will deploy for delivery;
- The products and services you will offer (e.g. level of loans/term, savings account interest rates);
- The price and cost of loans (APR and average weekly cost);
- Your arrangements (and partners) for opening savings accounts;
- Your arrangements (and partners) for opening bank accounts;
- How you will deal with arrears and bad debts;
- How you will market and promote your products and services (and what support you will need);
- Which advice agencies you will engage with and how you will liaise with them;
- How you will liaise with credit unions;
- How advice services will be funded and supported;
- Your plan and assumptions for sustainability within five years;
- Details of your senior management team and their relevant expertise;
- Who will lead this programme and their role in your organisation;
- Details of your board, their relevant expertise and your governance model;
- Your views on the risks associated with delivering these services and how you will mitigate them;
- Your investment requirements from us in both capital and revenue (amounts and term);
- How you will evaluate the impact and added value of your services;

- When you could start operations;
- Your track record in this area including:
  - Performance in lending/savings/opening bank accounts;
  - Developing partnerships with advice agencies/ housing associations;
  - Quality assurance standards.

The business plan covering these issues must be accompanied by evidence of performance in the areas indicated (loans/savings accounts/ bank accounts) over the last three years and your audited accounts for the last three years.

## How we will assess tenders

We wish to ensure that we achieve the best fit with any prospective provider. We will operate a two stage process.

In the first stage we will assess the contents of the business plan submitted to us and look at what constitutes best value in terms of:

- Outputs over 5 years (in terms of meeting or bettering our minimum requirements) – 50% of assessment;
- Financial investment required – 20% of assessment;
- Other support required – 10% of assessment;
- Speed setting up and of reaching sustainability – 10% of assessment;
- Evaluation of longer-term impacts including any added value identified by the tendering organisation – 10% of assessment.

We will select a preferred bidder for a competitive dialogue in which we will refine the areas described in your business plan and agree:

- Final targets;
- Investment;
- Reporting requirements;
- Break clauses;
- Timetable for implementation.





The Carnegie UK Trust works to improve the lives of people throughout the UK and Ireland, by changing minds through influencing policy, and by changing lives through innovative practice and partnership work. The Carnegie UK Trust was established by Scots-American philanthropist Andrew Carnegie in 1913.

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