

East Sussex Credit Union

Subordinated Loan Application to East Sussex County Council

Purpose of Application

To secure support from East Sussex County Council, in the form of a repayable subordinated loan for £150,000 for East Sussex Credit Union to enable the Credit Union to assist more residents in the County facing greatest hardship, to deal with immediate financial issues and build up savings to better manage future economic challenges.

How a subordinated loan will benefit ESCC

As local authority budgets are diminishing, yet need for support is increasing, this is a way of investing, to support people who are suffering financial hardship, without giving revenue grants. Investing in a subordinated loan to ESCU will allow it to expand its operations while retaining the investment as an asset on the council's balance sheet. It enables reserves that would usually be invested and earning minimal interest, to be invested ethically in the credit union whilst simultaneously contributing to ESCC's financial inclusion agenda. Investing in East Sussex Credit Union will contribute to ESCC achieving its four overarching priority outcomes by 2020: driving economic growth; keeping vulnerable people safe; helping people help themselves; and making best use of resources, as published in the Council Plan. In Economic terms, research by Salford University on behalf of Leeds City Council found that for every £1 the council invested in credit unions, there was a £9 benefit in retained income for the local economy.¹

Brighton & Hove City Council has invested in ESCU

In April 2016 ESCU received a subordinated loan of £250,000 from Brighton & Hove City Council for the benefit of residents in the city. Given that East Sussex Credit residents make up 32% of the total ESCU membership, with growth at 40% and potential membership in terms of population at 67%, ESCU is looking to ESCC to proportionately match fund this investment with a subordinated loan of £150,000. With this investment, the growth rate of new members from East Sussex will accelerate.

About East Sussex Credit Union

East Sussex Credit Union (ESCU) is a local savings and loans co-operative. It became East Sussex Credit Union in 2008. The Credit Union serves those who live and work in East Sussex, Brighton & Hove. ESCU aims to provide a high quality, sustainable and easy to access savings and loans co-operative, which is responsive to the needs of its members and actively combats the detrimental effects of poverty and financial exclusion.

ESCU has a current membership of over 6,300, savings of over £2.8 million (£730,000 from East Sussex members) and loan balances of £2 million, 35% of ESCU's lending in the last year is to people who are most in need.

When compared against interest rates offered by doorstep and payday lenders, it is estimated that ESCU has saved East Sussex residents £330,000 in interest in the past year. This means that the borrowers have more money available to spend in the local economy.

ESCU is regulated and authorized by the Financial Conduct Authority (FCA) and the Prudential Regulation Authority (PRA) and savings are 100% guaranteed by the Financial Services Compensation Scheme.

¹ Chris Evans (MP), 5/7/2013, quoting from Economic impact and regeneration in city economies: The case of Leeds, October 2009

What is a subordinated Loan?

A subordinated loan is lent for a minimum 5 years and 1 day. The loan debt is subordinated to the interest of the members i.e. in the event of liquidation; repayment of the debt would be made only after the repayment of members' shares. ESCU depreciates it over the 5 years so it can be paid back or rolled forward at the end of the period. Local authorities have invested in credit unions in this way because, although forgoing a low interest rate in a bank account, they invest for a social return, as set out below. Other local authorities that have given subordinated loans to support their local credit unions include Worthing and Adur, the London Borough of Islington and Brighton & Hove City Council. Recommendations from Fairness Commissions often include support for credit unions. This is an alternative to revenue/ grant funding as ESCC will have the option to have the loan returned or rolled forward at the end of the 5 year period.

Why now?

Nationally we are in a period of high debt, low levels of savings and increased stress on household incomes, 35% of households have no savings and 11% have less than £1,500² 'CPI inflation was 2.3% in February 2017 and is forecast to rise further. This is at a time when real earnings growth is projected to stagnate (OBR 2017), and the value of most working-age benefits is frozen (for both working and non-working households, for four years from April 2016). This will result in eroded purchasing power and people already struggling to cover the cost of essentials slipping further behind'.³

A Shelter/Yougov study found with high housing costs and many people having little or no personal savings to fall back on, three million working families could be just one paycheque away from losing their home.⁴

In times of households having minimal savings, increasing debt and squeezed incomes as well as rollout of Universal Credit, the services of a credit union are even more vital to offer safe savings, affordable loans and help on managing money. People, who are managing to save, borrow sensibly and manage their loan repayments are less likely to need advice and support from council and other public services to deal with their financial and other issues. ESCU offers a long term solution to help people get into a savings habit (even whilst borrowing, with our Saver Loans) build their credit history with affordable loans, and gain access to other services such as prepaid VISA cards, with a basic bank account that requires no credit check.

ESCU's offer aligns with ESCC Council Plan page 9 on strategic commissioning – 'Our strategic approach means investing in long-term and preventative solutions rather than short-term fixes that are more expensive overall. We will focus on early intervention to reduce demand and dependency on public services'. With local authority budgets (including the Discretionary East Sussex Support Scheme – DESSS) being cut, ESCU can help by working in partnership to deliver preventative measures that local authorities now have limited resource to do. This will reduce the burden on public services in the long term, by encouraging savings as buffer funds for 'Just about Managings' (working families and individuals on low incomes with high housing costs) so that they do not fall into high interest debt, rent arrears or homelessness. ESCU can also help people on low incomes build credit history by repaying small loans when they need them, and by offering the Engage prepaid card as a budgeting tool to help people put money aside for priority bills.

² themoneycharity.org.uk July 2017

³ Joseph Rowntree Foundation Universal Credit briefing Rising prices putting pressure on living standards

⁴ Family resources survey 2014/15, published in Households below average income Table 5.9db, DWP, June 2016.

The Local picture

There are currently 19 Lower Super Output Areas (LSOAs) in East Sussex (within the 10% most deprived areas in the nation) concentrated in Hastings, Rother and Eastbourne. This is followed up by a further 19 areas that fall within the second decile of the National Index of Multiple Deprivation, which are spread across the county and include rural areas.

'25% of people in Sussex (excluding Brighton & Hove) lives in rural areas, much higher than the England average (17.6%). People living on low incomes in rural areas continue to face significant disadvantage'⁵

East Sussex Credit Union in East Sussex

In 2014 to 2016 ESCU was awarded £90k from the East Sussex Business Innovation fund to establish an office, a volunteer network, new jobs and membership growth in East Sussex. This was largely achieved and its legacy, as well as an improved digital service, has resulted in 40% of all joiners now coming from East Sussex and 37% of all loans now being issued to residents of East Sussex. ESCU has continued to develop links with partners. ESCU works in partnership with SCDA, Citizens Advice, other voluntary sector organisations, housing associations church groups, transition town groups, advice networks, local employers, and with youth agencies - helping young people become financially included and banked. ESCU also provides accounts and prepaid card facilities to businesses and community groups in East Sussex now holding over £40,000 in savings.

An example of this is, our work with the Salvation Army in Eastbourne to set up prepaid cards for their clients - some of the most vulnerable in the town. This gives their clients an account to have benefits paid into. In 6 months 30 people have been signed up, this helps them get income, maintain housing, and improves their wellbeing. This work reduces demand on public services as they are becoming more financially capable. ESCU would like to build on partnership working like this to provide early intervention to help people maintain their independence. A subordinated loan will help ESCU take the risk to do more partnership working.

Roll out of Universal Credit across East Sussex

A key change for the most financially vulnerable and their ability to manage finances at this time, is the roll out of Universal Credit across East Sussex. This started in Hastings in December 2016 and has now been implemented in Bexhill and Rother. The results and impacts of this are now being reported by the DWP. The current planned roll out to further Jobcentres is Eastbourne in October and Lewes & Newhaven in June 2018.

For all new Universal Credit claims there is a 7-day waiting period where no money will be paid. There is also a standard 5 week wait for processing, based on the idea that newly unemployed claimants will have a month's final salary to tide them over. Many claimants are accustomed to being paid weekly or fortnightly. All claims must be submitted and managed on line. Some claimants, not used to applying on line, complete applications incorrectly and have their applications rejected. They have to re apply/appeal and wait a further 5 weeks.

In Hastings the Full System Roll-out started in December 2016:

- 6500+ people applied for Universal Credit in Hastings,
- 39% of UC claimants are in work (10% of all claimants are self employed so likely to have variable incomes which are reassessed on a monthly basis).
- Hastings & Rother Credit Union gained 200 new members in the first 12 months - these are people who did not have a named bank account to have their Universal Credit paid into (unbanked), as is now required. This unplanned increase in demand led to delays in Universal Credit recipients getting their money.

This is why ESCU has been working hard to prepare for the rollout across East Sussex. ESCU is currently talking to district and borough councils in East Sussex, the DWP and partners across the county about how it can work with them to minimise the impacts of the Universal Credit rollout across the county on household finances. ESCU has the benefit of learning from Hastings & Rother Credit Union about the importance of preparation for this change. Options being discussed are zero interest loans to bridge the standard 5 week wait for the first universal credit payment, a basic bank account via a prepaid card for the unbanked, financial support for initial account opening charges and rent payment processing for landlords of universal credit claimants.

What ESCU will deliver

By giving a subordinated loan to ESCU it will be better able to serve the residents of East Sussex in promoting financial inclusion, enabling ESCU to extend smaller loans to residents in East Sussex and improving access to credit union services across the county. See Appendix 1 for further details on this.

Hastings & Rother Credit Union (HRCU)

ESCU and HRCU have been sharing information and in particular learning from the rollout of universal credit. ESCU has benefitted by being able to plan and work with partners ahead of the rollout across the rest of East Sussex because of this shared learning. The two credit unions are in consultation about working more closely together with the potential outcome of shared resources/services/ merger. It is anticipated that out of this consultation process will come a coherent and robust credit union service to all residents of East Sussex including residents of Hastings & Rother.

Conclusion

East Sussex Credit Union has made significant progress over the past five years, more than doubling its membership, boosting savings, tripling the amount on loan to members, helping borrowers to manage their loans, and putting itself at the heart of tackling financial exclusion in the county. It is capable of much faster development and greater impact with the security of additional capital. The timing is now ideal. ESCU is well placed to tackle the challenges that universal credit poses to the most financially vulnerable. The investment will be used to enable ESCU to confidently increase the pace of development and take controlled risks; assessed and managed within its tried and tested risk framework. This will result in:

- A stronger, significant credit union confidently committed to a long-term role in East Sussex, with partners to develop the range of financial services, providing wider community access.
- A digital offer increasing accessibility and support for those in most need in East Sussex.
- A greater contribution to the East Sussex economy through support for businesses, particularly smaller and developing businesses that are a key feature of the local economy.
- Help for even more people within the County to develop their ability, confidence and independence in managing their finances by payment services, encouraging prudence, a savings habit and the wise use of loans, for the benefit of members and families.

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Appendix 1

How a subordinated loan will benefit ESCU and what it will deliver

A £125,000 subordinated loan invested in East Sussex Credit Union (ESCU) will make a significant difference to the organisation and to the county. ESCU's regulators FCA & PRA require that in order for credit unions to carry out additional activities which include loans over £15,000 which ESCU is already providing and / or have over 10,000 members or £10 million in shares it must have at least a 10% capital to assets ratio. When ESCU received the £250,000 subordinated loan from Brighton & Hove City Council its capital to asset ratio jumped from 9% to 16%. However, over five years this has to be written down in the accounts in preparation for repayment. A subordinated loan from ESCC would bolster this over a longer period, so that ESCU can move on to the next stage in its path of growth. This will allow ESCU to continue to expand financial inclusion activities across the county. Confidence of stronger reserves rather than relying on short term funding allows ESCU to contribute to longer-term partnership working and make a sustained impact on residents' lives. This money will benefit the county by enabling the delivery of a key strategic objective - the promotion of financial inclusion. This funding will give ESCU sufficient reserves to enable it to speed progress to sustainability by:

- Increasing its capital to assets ratio - this is one of the key ratios monitored by our regulators PRA and FCA
- Increasing its loan to assets ratios from 54% to 62% - the more money out on loan the more in dividends or interest rebates can be issued to our members.
- Increasing loan interest income by 33% in over the next 2 years by diversifying the loan book.
- Move ESCU's core business to becoming sustainable to within 2 years, thereby reducing its reliance on grants.

What ESCU will deliver in East Sussex

A subordinated loan will help underpin ESCU's work with district /borough councils to support some of the most financially vulnerable residents in the county, it will contribute to early prevention work in this area that local authorities have limited resources to undertake. ESCU will also:

- Build into its strategic plan increasing financial inclusion in East Sussex into the future, work to promote the value of savings to help local people
- Look to extend financial inclusion activities in the county, such as offering supported budget accounts to those affected by welfare reform, and develop the partnership network across the county for and innovating to create new joint projects such as the Eastbourne Salvation Army example.
- Take the risk to extend the offer of small loans by 60%, make them core business and engage members and potential members affected by high interest lenders, low income and welfare reform.
- Improve access to credit union services for the hardest to reach members including those in rural areas by increased use of partnership working supported by an accessible digital presence
- Target the 'in work poor' / 'just about managing' via extending our payroll deduction provision specifically healthcare, medical, facilities workers and, admin workers, drivers, engineers, cleaners and support workers.
- Work with local youth support agencies and services to develop the offer of prepaid cards including cards for 'young looked after' people – this gives vulnerable young people access to savings and debit card facilities

- Extend partnership working to pool resources and knowledge for greatest impact for residents including with local banks such as Lloyds and Halifax on loan signposting schemes.
- Work more closely with Hastings and Rother Credit Union to provide services across the county.
- Provide a stimulus to the local economy by increased services to local businesses