Community finance and the cost of living

13 September 2022

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12.00 **Niall Alexander**
Markets and Consumer Insights Manager, Fair4All Finance

12.15 **Dr Pål M. Vik,**
Senior Research Fellow, Community Finance Solutions, University of Salford

12.35 **Simon Gregory,**
Sales Director, Data on Demand

12.45 **Kate Pender**
Executive Director + Director of Growth and Development Programmes, Fair4All Finance

12.50 **Shiona Crichton**
CEO, Moneyline

Joanne Angus
CEO, NE First Credit Union

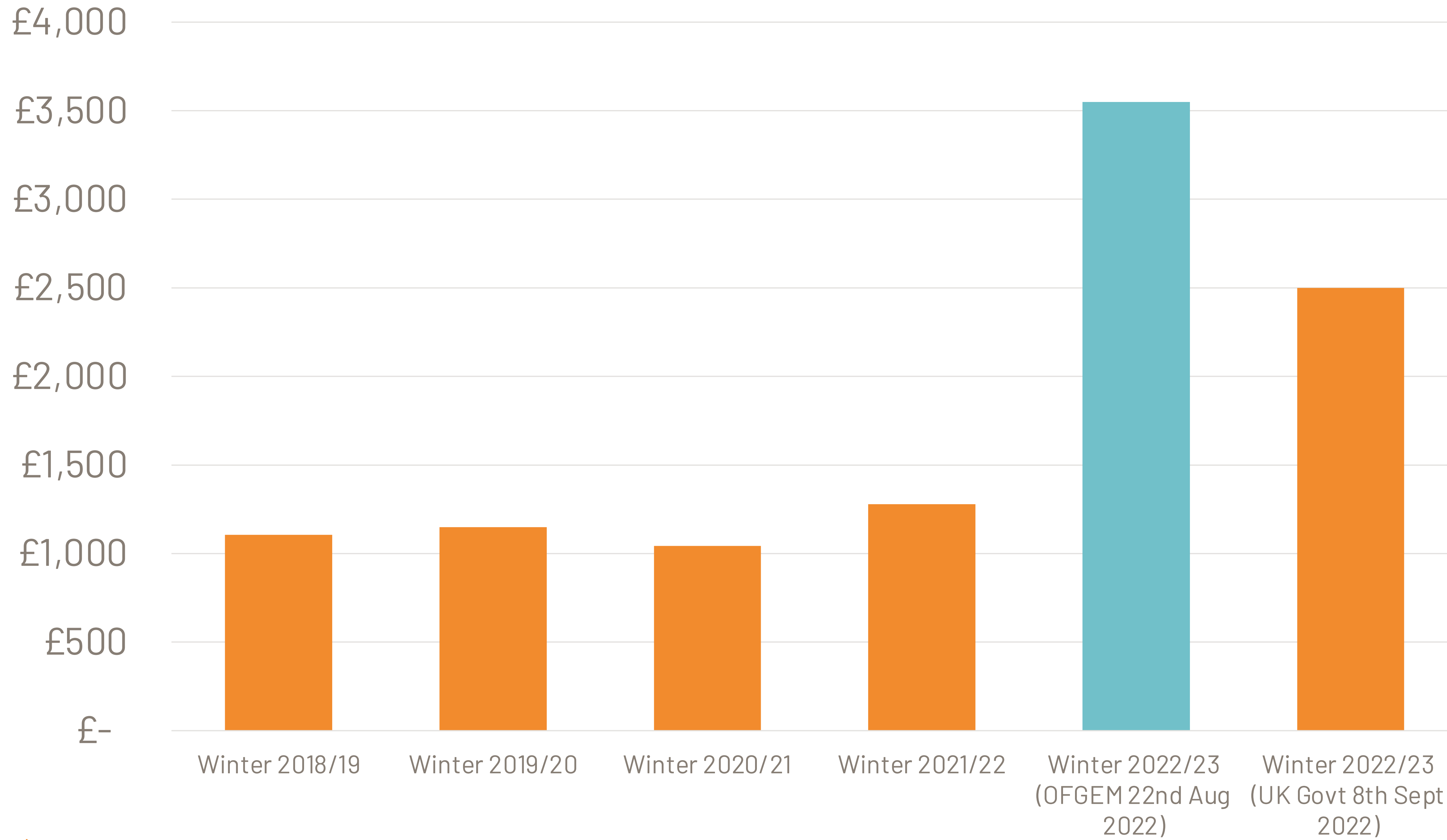
Paul Norgrove
CEO, Serve and Protect Credit Union

13.05 **Panel, Q&A**

13.15 **Close**

OFGEM Default tariff price cap (£ per annum) Winter 2018/19 to Winter 2022/23

(OFGEM, 26th Aug 2022, and UK Govt announcements 8th Sept 2022)



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There has always been a cost of living crisis for some households, the fact of the matter is there has always been more month than money

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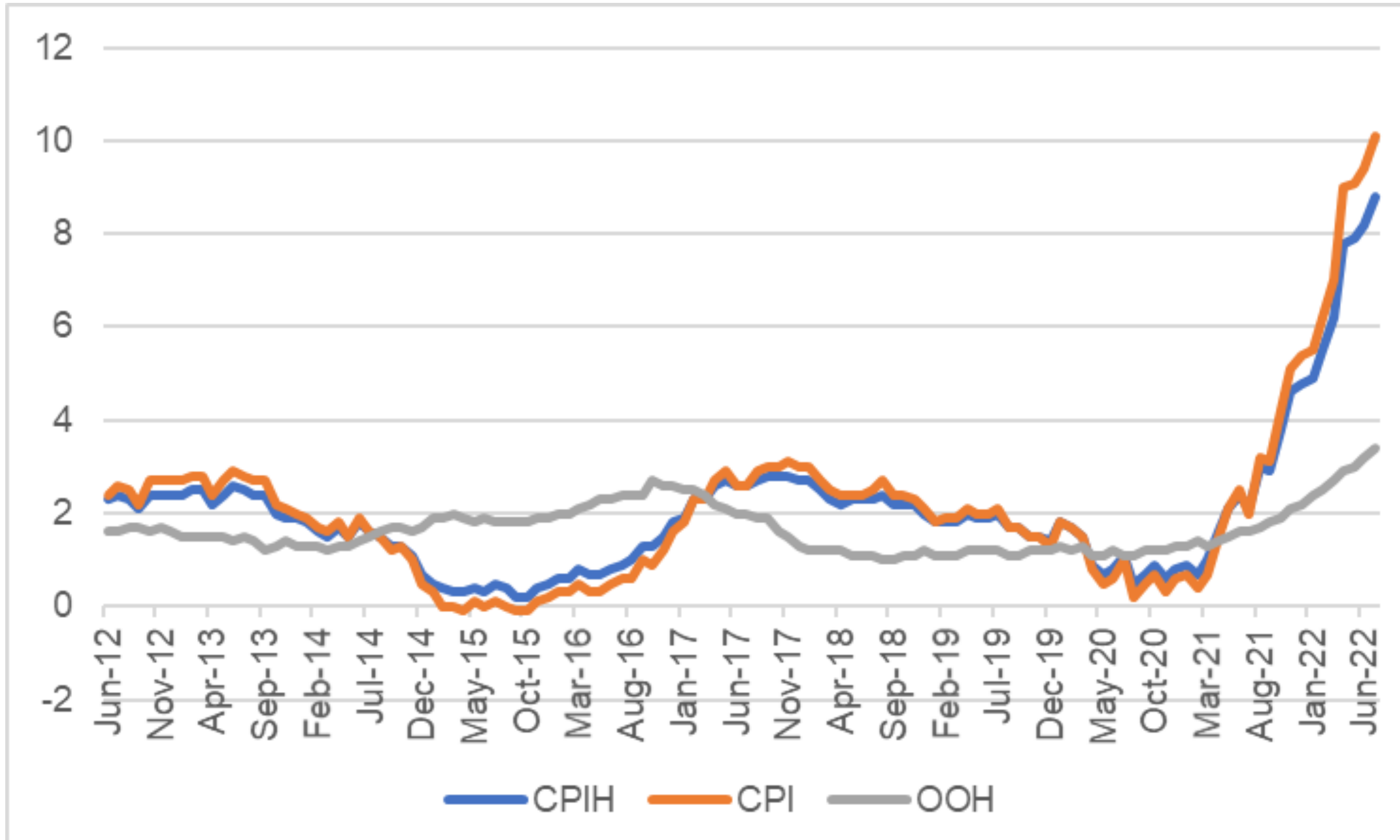
The impact of the cost-of-living crisis on British credit unions and CDFIs

Dr Pål Vik and Andrew Wallace
Community Finance Solutions, University of Salford

13th of September 2022

Significant increase in inflation



- CPI increased from 2% in 2021 to 10.1% in 2022 driven by energy (46%), fuel (32.8%) & food (8.7%)
- Analysis by IFS show inflation in April 2022 was higher for lowest income decile – 10.9% vs 9% avg

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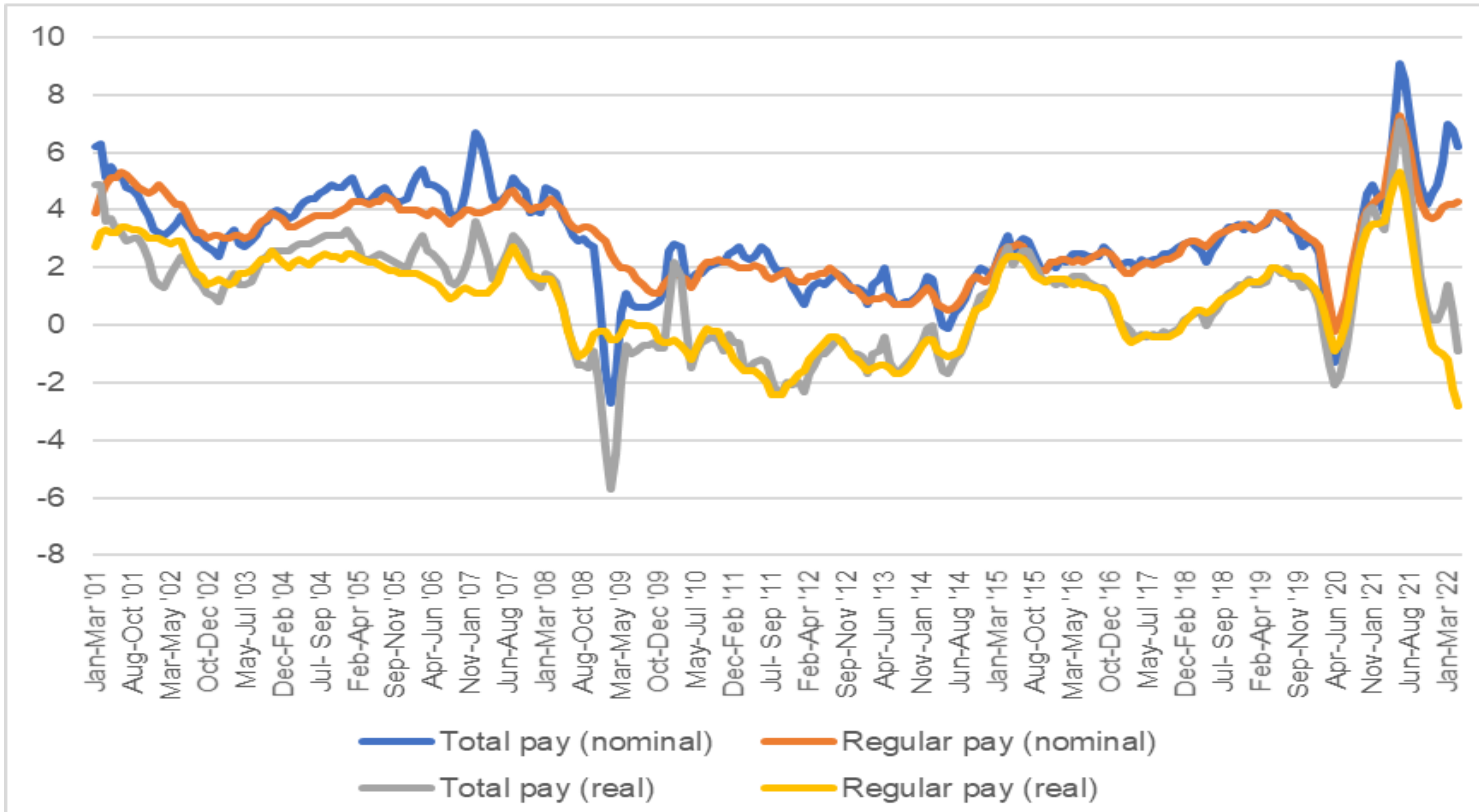
Wages not keeping up with inflation



- Regular pay fell by 2.8% in the year to March-May 2022, which is a record fall

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Methods and data

- **25 interviews** with credit union and CDFI (May-Aug.)
- **Focused on impact of COL crisis** on customers, lending activity & operational & financial effects
- **Online focus group** with four loan officers from one CDFI and two credit unions held 23rd of June

Sample overview

	Community credit unions	Employee credit unions	CDFIs	**Total**
Small	2	-	3	**5**
Medium	8	2	4	**14**
Large	3	2	1	**6**
Total	**13**	**4**	**8**	**25**

Definition of size based on outstanding loan portfolio: <£2m (small); £2m-£9.9m (medium); ≥£10m

- Findings reported widespread across range of different types of lenders and/or material within the organisations

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Headline findings

1. **Cost-of-living crisis is reducing access to affordable credit,** as lenders decline more loan applications
2. **Harder to assess loans**, as applicant's circumstances and behaviour more fluid and unpredictable
3. **Nature of demand and lending changing** with shift to smaller loans to cover living costs
4. **Savings growth falling or lower than projected**, as members withdraw more savings and deposit less
5. **Mixed picture on portfolio quality**, though mostly pointing to deterioration in quality
6. **Pressures on cost and income may be existential threat** for some lenders and manageable for others

1. COL crisis reduce access to credit as lenders decline more applications

- **14-15 lenders report declining more loan applications**, including from existing clients, and that the increase in declines is significant (7-15 percentage points)

  "[In] April…the cap was lifted, and the energy bills…went up for lots of people dramatically in some cases….in April, we saw our decline rate on loans reach 60%...whereas normally it's between…45 and 50%." (Interviewee 14, credit union)

- **Deterioration in applicants' financial circumstances**, some cases legacy of Covid-19
- **Increased value and volume of unsecured consumer debt**, especially BNPL, contributed to increased declines
- **Lenders have introduced tighter criteria** on lending and affordability (open banking, discretionary income)

2. Lenders are finding it harder to assess loan applications

- **Prices and customer behaviour dynamic is fast-moving**, especially for subprime, making it more difficult to rely on traditional underwriting and assessment methods
- **Concerning - if not widespread - applicant behaviours**, including becoming bankrupt on receipt of loan and taking out loans from other lenders whilst waiting for decision

"You…will get more and more customers who, if they go for more than one loan online, they might get offered two loans at the same time. Three loans. Do they take the one loan or do they take three loans and it's very difficult" (Interviewee 22, CDFI)

- **BNPL is problematic in many cases** as reports of many borrowers unaware of cumulative impact of multiple payments and many don't perceive it as credit

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3. Nature demand shifting to smaller loans to cover living costs

- **8 lenders are seeing an increase in demand and lending** (due to recent marketing campaigns or online lead generators), as they shift to better-off, lower risk clients
- **However, most lenders are experiencing a lower than projected growth** in the value of demand and lending
- **Many reporting lower average loan amounts**, as people cut down on or postpone large purchases and home improvements
- **People are applying for smaller loans** to cover living costs and to tie them over:

"Less of the, more, maybe aspirational purchases or aspirational loan applications. It's sort of shifted more towards [the] sort of lower value emergency loan, the 500 pound, £1000 which then drags that the average loan size down as well." (Interviewee 15, credit union)

4. Savings growth slowing or declining, as members withdraw more and deposit less

- **Fewer people (especially those on lower incomes) top up savings**, more requests for release of linked savings, share withdrawals increasing, and share intake falling:

"…we…build liquidity in the early part of the year up to the summer and …shed it up to Christmas…But…in March for the first time in the history of the credit union for the month of March was…an outflow [of] savings …across the whole book. We've never seen before for that time of year ever before. I think that's quite telling." (Interviewee 15, credit union)

- Part of savings reduction due to drawing down & spending additional savings accumulated during Covid-19
- However, lenders also reporting more people are taking out savings to pay for living costs:

"We have found in last few months that our member's ability to save has fallen. [The] growth per month in savings…is 20% lower. For many people, the rainy day has arrived…" (Interviewee 17, credit union)

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5. Mixed picture on portfolio quality, though mostly pointing to deterioration

- **Several lenders (8-10) are seeing an increase in missed payments**, lending written off and provisioning, whilst others are not seeing any deterioration in portfolio quality
- **Most are mitigating against increased delinquency** on current and future loans by imposing tighter lending criteria and restricting lending to lower-risk customers
- **Expectation that loan delinquency and provisioning will increase**, especially on loans made in run-up to COL crisis:

"I think the biggest concern [is] gonna be coming to October time. When the…cost of energy in particular rises again and it's when you start need to turn the lights on and the heating on. It's also the peak kind of Christmas lending season as well" (Interviewee 7, credit union)

- **Increased loan delinquency is one of greatest risks** associated with the cost-of-living crisis, because loan loss provisioning one is of greatest costs facing sector

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6. Sector facing cost and income pressures, but impact on bottom line uneven

- **Lenders facing significant cost pressures**, such as supplier, and utility bills but especially in recruiting and retaining staff
- **Great uncertainty about how the cost-of-living crisis will develop** and how it will impact their bottom line and customers
- **Potential existential threat to some lenders** due to lower income, rising prices, increased bad debt & effects of Covid-19:

“When the banks collapsed in 2008…I remember at that time being really worried about the future of the credit union. I'm more worried this time than I was back then. I felt like back then it was we were in a better position…Otherwise, we're not going to be here in 5-10 years’ time.”
(Interviewee 11, credit union)

- **Others expect limited or no impact on bottom line** as they’re well capitalised, profitable to weather crisis or as they will shift lending to less risky, better off applicants

Concluding remarks

- **Too early to say something definitive** about the effect of the cost-of-living crisis on affordable credit sector
  - **Crisis still evolving** with further prices rises expected later in the year and next year
  - **Great uncertainty about global factors** affecting inflation (Ukraine, sanctions) and future Govt. policy and responses
  - **Uncertain if effects on (low-income) households will be short-lived** or affect their financial circumstances in long run
- Nevertheless, combined the quantitative and more anecdotal evidence provided by interviewees point to 2 main conclusions:
  - Combo of rising living costs, long-term financial precarity and Covid-19 **pushed many customers into financial difficulties**
  - **Impact on lenders is more uncertain and uneven**, but cost-of-living crisis is **an existential threat to some lenders**

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Concluding remarks and implications

- **Crisis has reduced access to affordable credit** – important to determine if short-lived or if access curtailed in long-run
- **Some credit, especially BNPL, worsened customers' financial difficulties** raising question about detriment and regulation
- **Many borrowers will likely emerge from crisis with higher debts, less savings and lower income** – how can affordable credit sector can help rebuild resilience, what support & products needed
- **Any closures may affect access affordable credit as lenders serve different market segments** – careful monitoring to ensure access not significantly worsened for some

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Full report available on:
https://hub.salford.ac.uk/cfs/affordable-credit-microfinance/

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DATA ON DEMAND

Simon Gregory – Sales Director

Who are we?

Data On Demand provide alternative UK consumer data, helping businesses that service people deliver better customer outcomes.

Sectors we serve include: Financial Services, Utilities & Telecoms, Public Sector, Gaming, Insurance.

Our data is used across the full customer lifecycle from on-boarding, through risk decisioning and account management and also into collections & recoveries.

Our core offering for Lenders is to help them identify and monitor risk and align with regulatory requirements including the identification and monitoring of customer vulnerability.

The Problem

Lending is a risk decision.

In times of volatility risk becomes more difficult to predict so access to credit is restricted.

Demand for borrowing due to the socio-economic issues is increasing. Consumers are in need of finance, but due to risk and regulatory factors a large proportion are unable to access it.

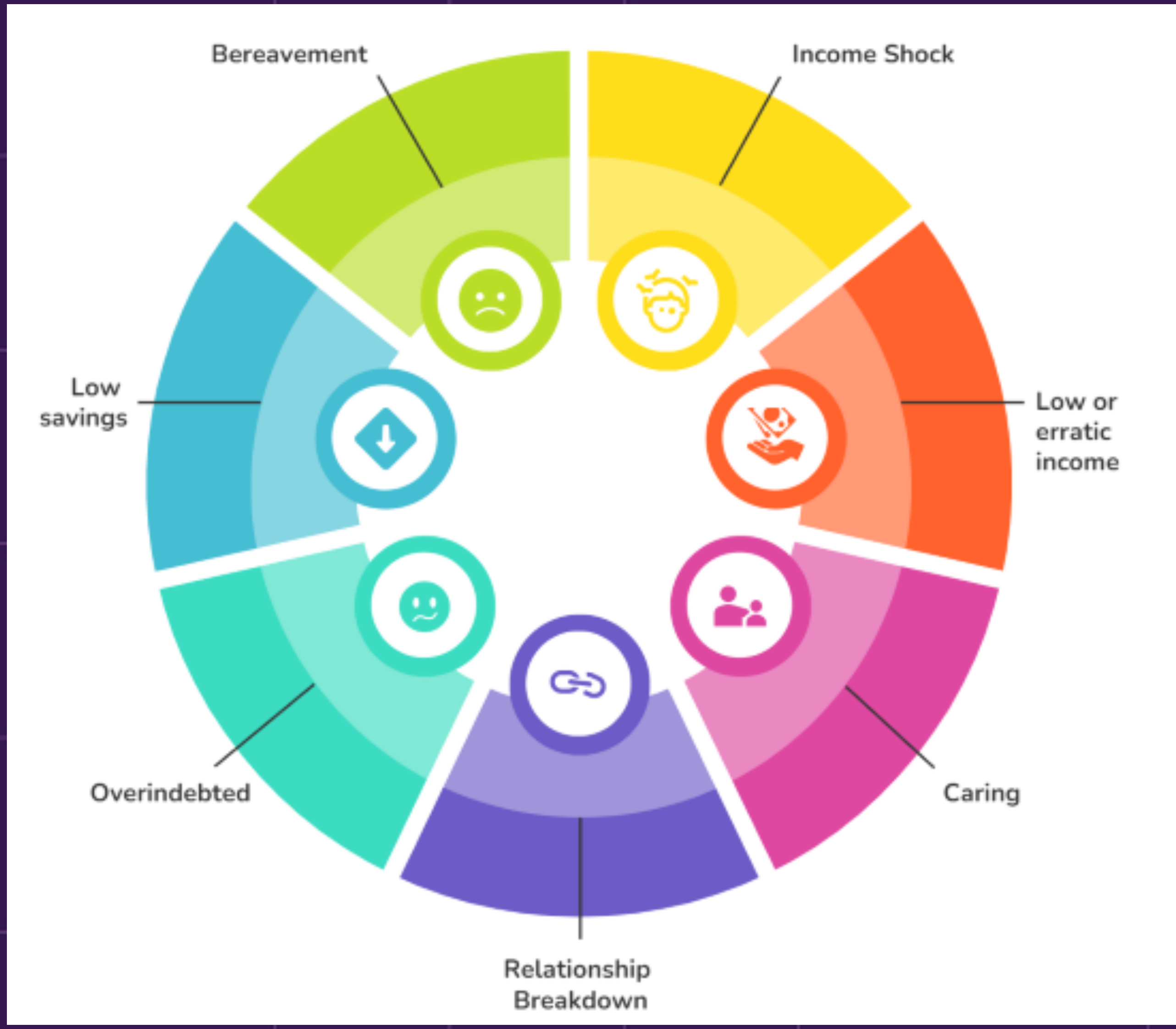
Now more than ever Lenders need to look to alternatives to ensure they have a clear view of the new customers they are underwriting and their customers changing circumstances.

UK Consumer Vulnerability – Research & Regulation

The FCA's "Financial Lives Survey" in 2020 identified 24 million Consumers with characteristics of vulnerability.

This was pre pandemic, pre Russian invasion & pre Cost of Living crisis.

Consumer Duty has now put even more onus on Financial Services providers to identify vulnerability and ensure they are delivering better customer outcomes.



ID.VU – Identification & Monitoring of Consumer Vulnerability

ID.VU collates data from High Cost Short Term loan applications and self-declared consumer Vulnerability via the Vulnerability Registration Service.

Built in line with FCA guidelines ID.VU provides high level vulnerability segmentation along with over 100 unique variables and trends.

Currently the database sits at 3.3 million UK consumers.

DATA ON DEMAND ID.VU

Worrying Current Trends

More people are turning to High Cost Short Term borrowing for the first time driven by either a change in circumstances, or tightened acceptance criteria.

Loan applications to support payment of household bills are increasing dramatically.

Applications remain highest within the 18-34 age bracket.

Loan Application Data	Apr-22	Jul-22
Loan Applications for HCST	193,000	250,000
Loans to pay Household Bills	19,254	137,110
Loans to pay Debt	6,568	13,511
Loans for Short Term Cash / Emergencies	9,280	14,293

THANK YOU!

www.dataondemand.co.uk

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DATA ON DEMAND

Community finance and the cost of living

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Kate Pender

Executive Director and Director of Growth Development and Programmes

What more can we do

Securing long term funding for financial inclusion will let us significantly expand our existing programmes to help more people access fair financial services

- **Significantly expand affordable credit** through further funding
- **Scale the No Interest Loan Scheme** assuming pilot successful
- **Roll out an affordable consolidation loan scheme** to reduce the burden of people's debts
- **Address appliance poverty** – increasing accessing to affordable appliances
- **Develop affordable insurance initiatives** – home, motor and income protection to improve access and address the poverty premium
- **Improve access** to people particularly excluded from the system

What's next

Please support our response and submit your own:
https://www.gov.uk/government/consultations/consultation-on-the-english-portion-of-dormant-assets-funding

- In September we'll share key messages and data points you can use in your own response
- We're drafting a financial inclusion theory of change, to show what we'll prioritise and how we will work with others
- We'll also share our response in advance

How else can we help?

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The Nearlys >>Nina Nearly

I live on my own in a rented house, lost my job during Covid and I'm not working at the moment. I always do my best to pay all my bills but its becoming impossible. It really stresses me to think I will fall behind on payments.

Nina Nearly

	Without Cost Increases	The winter ahead
	£	£
My monthly benefit income	334	334
Benefit income for my rent	350	385
Total income	684	719
My costs per month		
Rent and Council Tax	377	412
Utilities	80	176
Food	60	66
Other Essentials (Phone, Catalogues, Internet)	50	55
Non Essentials	20	22
My total costs per month	587	731
My extra cash per month	97	-12
My extra cash per week	**24**	**-3**
If I was still under 25 my extra cash per week	6	**-22**

Moneyline

Community finance and the cost of living

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nefirst CREDIT UNION

Joanne Angus

Chief Operating Officer

Cost of living crisis

What we are seeing at NEFirst Credit Union.

- Significant increase in low value loans received
- Increase in applications to assist with living expenses/household bills
- Increasing decline rates
- Underwriting difficult – Use of Buy now Pay Later and rising costs of utility and fuel bills, multiple bank accounts and gambling etc.
- Savings steady with only a 2% drop on last year.
- Delinquency levels up slightly, however, write off rates down.

August	Loan received	Granted	% Declined	Value Granted
2021	280	161	42%	74K
2022	979	322	67%	159K
Year				
2021	3248	1912	41%	1.3m
2022*	6337	2512	60%	1.6m

* End of year October 2022

Cost of living crisis

What are we doing

- Through the SOAR the banking platform, we use -

✓Inbuilt benefit checker

✓Open banking categorization and analysis

✓Sharing open banking outcome data with member

✓Signposting declines to relevant supporting organisations

- Multiple No interest Loan Schemes
- Partnerships with NE Local Authorities, Housing Associations Citizens Advice and Welfare assistance organisations etc.
- Marketing – High street presence, eco system of partnerships, social media, business development officer funded for two years.

nefirst CREDIT UNION

Challenges ahead

- The North East has the highest rate of poverty in the UK and people desperately need access to affordable credit.
- How can we look after those loyal and potential new members who no longer meet our affordability criteria due to the rise in cost of living?

✓ Increase Marketing?

✓ More No Interest loans?

✓ Debt Consolidation? (Comes with huge Risks)

- The biggest Risk to the CU's existence is **delinquency**.
- To supplement current signposting, an idea would be to raise funds to employ an Inhouse Debt Advisor to assist members in accessing potential benefits, assessing debt consolidation, assisting with budgeting and financial education and support.

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50%

Of our members are <u>very concerned</u> with the continual increases in cost of living and the overall impact on their personal financial position.*

**Based on an Annual Membership Survey conducted by Serve and Protect Credit Union in April 2022. A total of 4,628 responses were collected from members of Serve and Protect Credit Union.*

84%

84% of our members are concerned about the increasing energy costs.

48%

48% of our members are concerned about their ability to pay for fuel.

23%

23% are concerned about their ability to feed themselves and their family.

**Based on an Annual Membership Survey conducted by Serve and Protect Credit Union in April 2022. A total of 4,628 responses were collected from members of Serve and Protect Credit Union.*

AFFORDABLE TODAY

VS

AFFORDABLE TOMORROW

36% would need to take out a loan if they needed £2,000 for an emergency.

Based on 3,547 responses in our Financial Resilience Survey

62% would need to access their savings if they needed £2,000 for an emergency.

Based on 3,547 responses in our Financial Resilience Survey

Impact on Savings

Deposits

15.66% decrease in monthly amount deposited by Serve and Protect members.

Withdrawals

28.24% increase in monthly amount withdrawn by Serve and Protect members.

**Comparison between October 2021 and June 2022.*

Q&A

Thanks for joining the webinar

Please let us know if you have any questions, thoughts or ideas on anything we've covered

hello@fair4allfinance.org.uk