From the margins to the mainstream: scaling community investment in the UK.

Notes of the Community Investment Coalition Summit on 25th January 2013

The state of the sector and the scale of the challenge

Tony Greenham and Lynda Prieg, from the New Economics Foundation presented findings from European Union funded research on Stakeholder Banks: Benefits of Banking Diversity. This took data from 65 countries to identify successful alternatives to commercial banks. The key points raised were:

- That if the UK only has one kind of bank, profit making with shareholders, there is no reason to think that this will serve all people in the community.
- There are plenty of sustainable forms of banking provision that can fill the gaps and this is already the case on a small scale in the UK.
- The research looked around the globe at different forms of 'stakeholder banks' by surveying a range of stakeholders.
- These are banks that are sound commercially but serve parts of the community not otherwise served.
- The vision is for a more diversified sector.

Looking specifically at credit unions as one way to increase diversification, the research found that the advantages were:

- Democratic ownership structures (owned by customers not shareholders, one member one vote).
- Not just profit focused but offer other benefits, for example good customer service.
- Owners don't have a claim on profits of the bank, only on what they put in.
- They are lower risk-taking and there is less short-termism.
- They have generally lower returns but they are more stable.
- They have higher capital levels – because owners don't have a claim on profits, they are incentivised to put them aside for a rainy day and as an endowment for future generation.
- During the financial crisis they were able to increase lending while commercial banks contracted for example, American credit unions were able to increase lending by 7% in 2008 while commercial banks decreased lending by 7%.
- They tend to be better at being in tune with local people and needs because they are owned by them and can't move to another area. They are better at getting the soft information so they can lend more, but also have lower default rates, for example, Canadian Credit Unions have 17% of SME lending market although 5% of total banking market.

But challenges remain including:

- The UK is at a huge disadvantage in terms of history and regulation compared to other countries.
- The credit unions remain small and combine for some elements of what they do in the US and Canada.
- A centralised infrastructure has not emerged in the UK and Ireland and therefore it is hard for credit unions to be financially sustainable and offer certain services that are needed, for example, accessing payment systems.
- While they are owned by local institutions , as they grow they start to exert control over the institutions, there is a risk that they will take on a life of their own.
- The centrals in the US got into trouble while Canada didn't. This is because in US you can shop around for a central whereas in Canada you have to join the one that is local to you.
- It is plausible that Credit Unions could be a competitive force against commercial banks. They need regulation that protects them and recognises advantages.
- The sector needs to look at more collaboration but be aware of the pitfalls.

Nick Henry, GHK, presented CDFA research funded by RBS on CDFIs in the UK called 'Mind the Finance Gap'.

This research aimed to:

- Assess what is the scale and scope of community finance
- Estimate the demand.

And found that:

- There is a significant gap in community finance, with a potential market of £5.45 – £6.75 billion and only currently £0.7bn delivered into the market by the community finance sector.
- Which matters because of the social and economic benefits that would flow from increased lending.
- The under-served market includes business lending, civil society, personal lending and homeowners.

The challenges in expanding community finance include:

- Moving CDFAs from a nascent to a viable and established feature of the financial landscape.
- Language. Banks hate language like 'underserved market' and 'market failure'.
- The government won't do it alone.
- The challenge to the sector is that community finance as a concept is not well understood, it is an umbrella but needs an external clear message of what it means.

What does this mean for the sector? Panel debate

Ben Hughes, Chief Executive, CDFA

The evidence is exciting as it gives a road map of where we want to get to. Challenge is to make community finance part of the finance sector alongside mainstream banks, government, etc. This needs to be incentivised through a coherent policy framework.

The finance sector needs 'socialising' – the social sector is often told to act more like finance – why not the other way round?

The gap is not just financial, it is also lack of infrastructure – there is a big need for the sector to work together – develop integrated local infrastructure linked by support model.

There is also an issue about people in the street, most will know nothing about community finance, how do we raise awareness and create demand? Need to convert from need into evident demand. But we mustn't lose sight of why the sector started, serving those not served.

Nick Temple, Director of Business and Enterprise, Social Enterprise UK (also the policy lead to the Cabinet Office and chairman the social investment forum).

One of the tricky elements is the balance of local and national. These can easily go out of kilter particularly the influence of regulation and incentives. A related issue is the issue of governance, accountability and transparency, how do we avoid becoming commercialised as has happened in the social finance sector.

There is collective power in the sector, both in buying but also in savings.

Some of the principles of the USA's Community Reinvestment Act still apply, we are the leaders in social enterprise and Australia has 'second mover advantage', can we do something similar with CRA and learn from the US's experience?

The wider social investment market is nascent, fragmented, hard to navigate, complex and a bit slow. Risk capital is the big gap with more research needed. Crowd funding and community shares may be more of a route for social enterprises than SIBs. Big Society Capital is not a panacea as it has restrictions around it. Tripartite partnerships are important. The notion that banks only doing CSR is a bit outdated, they are engaging their businesses.

The sector needs to work together to communicate effectively, but how do you do this without losing the 'local' bit?

Bruce Davis Co-founder ZOPA and Abundance

The language of mainstream and margin is not helpful. In reality there is no such distinction. There are 'mainstream' banks that are subsidised and 'alternative' finance providers that aren't.

The problem arose because the UK allowed banks to take over other banks and there is no competition.

The goal of Abundance is financial inclusion. Peer to peer lending facilitates money going to where it needs to go.

Banks didn't get to where they are by being efficient. They got there by having a lot of power.

Angela Clements, City Save Credit Union:

The aim is for credit unions to have 5% of the personal banking sector in 5 years. Credit unions need a more supportive framework. A shared service centre could allow CUs to expand into business lending. Credit unions don't have the skills yet but personal lending is easier. The fall in personal lending is off set by arrears in rent, bills, etc. High cost lending is equally fuelled by promotion – they are creating the market.

Campaigning for reforms to:

- Access to a simple savings plan direct from income.
- Treasury solutions . The savings held by credit unions are growing but they cannot lend it because of legislation.
- Lending is easy but lending well is not – just because there is a gap, doesn't mean we should fill it.

Delegate participation

Delegates were asked to discuss the following questions in round table, facilitated groups:

1. Should community finance seek to scale up to address more of these under-served markets? If so, what do community providers need to do to reach scale?
2. What are the key barriers to achieving scale?
3. What sort of regulatory regime would help rather than hinder community investment?
4. How can community finance raise its public profile?

Comments and feedback are set out below

Should community finance seek to scale up to address more of these under-served markets? If so, what do community providers need to do to reach scale?

- CDFIs and credit unions should come together, puts pressure on for legislation.
- Technology has revolutionised and common platforms that are efficient, usable, etc. would have a genuine impact.
- Don't need new stuff and structures but to make what we have better.
- Collaboration , don't reinvent the wheel, its not about creating something new.
- Keep it local, relationship banking, there isn't funding for advice and support.
- More work needed around advice.

What are the key barriers to achieving scale?

- Not quite a level playing field in what's expected of the community finance sector.
- Get institutions to coalesce, strong view that new technology is a key driver.

What sort of regulatory regime would help rather than hinder community investment?

- Could be an intermediary that could lend to CDFI.
- Regulation and need to provide guarantees for funds invested.
- Credit Union has credit balances they'd like to use in different ways , with social return but can't without change.

How can community finance raise its public profile?

- Unpack what community finance is as a sector.
- What is community finance good at doing? Package up its about providing a service and giving back into local areas.
- Messaging – framework to convince policy makers but also customers.
- Customers are getting more savvy about where money is coming from and going to.
- Have an annual move your money campaign, focusing on where your money is going and what alternatives there might be.
- Get a story line in a soap opera.

An international perspective from the USA

Mark Pinsky, President and Chief Executive Officer, Opportunity Finance Network, USA

The community finance sector has come far since its origin a lot has been accomplished.

Two points to cover:

- Communications, messaging, brand and marketing
- Policy.

There are 500-700 CDFIs in the USA, about half of which are functioning well.

There are also:

- Community development credit unions
- Community development banks
- Community development loan funds
- Community development venture funds (very few of these).

They are mainly providing credit estimated at $40 billion mostly for housing but also for businesses, small, micro and non profit and 'community businesses' which can be both for profit and not for profit businesses. OFN has 200 CDFIs in their membership

In 2005 they did some research about the brand of CDFI. The term 'community development' was disliked by 100%. They gave a description of people who would potentially invest – with the word 'community development' in the title, it was not appealing to investors. So they rebranded to 'opportunity finance network'. This reflected what people said when they asked them what they liked about CDFIs 'you finance opportunity'. It gave CDFI's a tool to explain what they do. They worked in partnership with Starbucks who brought their marketing expertise. They distributed wristbands through the Starbucks stores, which made them realise they needed to change the language and the way they talked about themselves. They rebranded the whole CDFI industry in the US. They became 'a solution' and learned to tell that story.

The Reinvestment Act is necessary because it is the law of the land for CDFIs and partners, but it is not sufficient and is now outdated.

In the recession, CDFIs were able to say yes to lending when others said no. This performance changed the way people thought about CDFIs.

Ways to success:

- Humility – sometimes you need partners
- Discipline and performance
- Selective membership
- Institutional ego – ensure others think the work we do is as important as we think it is
- Data – tell your story.

Dan Letendre, Senior Vice President, Bank of America, USA

The Community Reinvestment Act no longer drives the Bank of America community investment it does it because it sees it as a good investment. The Act says that if you are a bank and accept then government's guarantee of covering your funds, you have to serve poor communities.

CDFIs are a way into funding innovative and unique local projects. A minority of CDFI clients are at or above a level that would be described as self-sustaining – i.e. break even or better.

80% need an alternative view of their viability.

1) Loan portfolio is more than sufficient to cover debt payments they take out
2) Able to fundraise to sustain their operations.

This is self-sustaining. They operate in the margin just outside where the mainstream banks leave off. It is not a constant market it is continuously changing so CDFI clients are continuously changing. Post 9/11 small businesses close to ground zero were on hold for 3 months while the clear up operation was underway. They needed a loan programme as no-one would loan to them. They expected a loss rate of 25% but this turned out to be 12%. Post-hurricane in New York, CDFIs could make quick loans. Bank of America lend to CDFIs because it is in their self-interest to do so.

Nick O'Donohoe, Chief Executive, Big Society Capital

Big Society Capital is using funds from dormant accounts. They are a 'social investment wholesaler'. They can lend to social investment intermediaries. They can lend to third sector organisations that have a social purpose. One difficulty for Big Society Capital working with CDFIs is that a lot of CDFI's lending is to SMEs. BSC cannot lend to them or to CDFIs that do personal lending.

The Community Reinvestment Act in the USA made a difference to US banks. It will be difficult to encourage UK banks to embrace CDFIs without it . The banks are still too big to fail, and taxpayers underwrite them. This gives us rights on transparency and to have a better idea on where they are lending. A lot of CDFI lending in the US is for affordable housing. So we need in the UK context to consider housing associations. There the 'gold standard' of sustainability is that all costs are covered. The Community Reinvestment Act opens the path but it needed equity / grants to support it. There will be a greater debate about this as the election approaches. In Australia they have relaunched Credit Unions and Cooperative banking but not called it this. The term 'customer owned bank' is preferred.

Delegates asked the panel a series of questions, which included:

- The need for equitable capital for CDFIs is exactly right. Work on small business development bank, green investment bank, covers CDFIs.
- Is it possible for a taskforce to work with CDFA to generate a CDFI fund?
- Couldn't Funding for Lending be opened up to CDFIs to get a short-term and long-term solution?
- Want to work with Big Society Capital to develop the narrative but should we rebrand CRA if we go down that route?
- The rebrand of CDFIs in the US, they already have in one place what the CDFIs etc. in the UK have separately. What is the bit before that needs to be in place before the rebrand?

In response, the following comments were made

- Small business development bank is going to have to lend in a genuinely sustainable way. CDFI fund was unlike anything else it was an investment in an intermediary and its strategy.
- Equity – unless the organisations can meet the gold standard, which they won't, will have to be a grant.
- CRA as it is written is not what you want – in US have made changes to pension laws that people put a small amount from pensions into investment. Need to have an affirmative obligation for all companies that benefit from government support to put some funds aside. CRA brand – if we are going to try for a CRA-like initiative we need to change the brand – copying name from US is probably not the right way – CRA in the US is not perfect.
- The term CDFI was not widely used until 1992in the US – the presidential candidate wanted to create CD banks and it didn't seem likely this could be achieved. We were defined by an opportunity and by risk. There was discussion about the term 'alternative lenders' but came up with CDFIs as they weren't alternatives as there was nothing there.

Where do we go from here? Irene Graham and Andrew Robinson talk about next steps

Irene Graham, Managing Director for Business, Finance and Strategy, British Banking Association

There is supply of finance but it is not as well connected as it could be. Different sources could be better joined up. Banks aren't the answer to everything. A number of banks are working with CDFA and CDFIs and there is a focus one working with the community sector

The business bank is seen as an opportunity to work jointly on policy. The BBA is engaged in a pilot where a customer comes in and the business bank can be a clearing exchange, so the customer is referred to the business bank can then be an independent referral mechanism into the appropriate funders in a community. Need collectively to look at whether the business bank can be used as a flow through to CDFIs?

Andrew Robinson, Director of Market Development, CCLA

Some percentage of people have no banking. The detail of the number is irrelevant but there is a problem that people, who need credit can't get it. It takes time to take an unbankable proposition and turn it into something that means the bank staff get their remuneration. There is a lack of professional and personal interest in getting credit to flow to the places it is needed but doesn't get there easily. In reacting to how we connect, if we don't get this then there's a problem. Don't know how to connect banks to CDFIs without some compulsion. What about business advice and support?

Irene Graham

Regarding transparency, banks will be producing lending statistics at postcode level.

If a business bank acts as a clearing stage then the amount of information coming through would mean more information available. Need Angel lending for start up. Need asset based finance for growth.

The BBA has a mentoring programme to ensure businesses are aware of what type of funding they need at what time and investment readiness for 'how do I present myself at any time to anyone I am looking for finance from?'. 1000 bank mentors – mentorsme.co.uk. Need to challenge the cultural aspect. It is not wrong to seek support. Some business opportunities do exist in 'deprived' areas.

Delegate comments

Delegates raised a number of issues including the need for more signposting of community finance products and providers; the need for a more coherent policy framework and action to raise these issues on the political agenda; that LEPs and local authorities could play a more proactive role; and the need for transparency of lending data to highlight the gaps in availability of affordable finance.

Key themes emerging from the summit

There were four key themes that emerged from the day:

- Communications and reputation management: The sector needs to significantly raise its profile and levels of confidence amongst a range of audiences, including potential customers and policy makers.
- The need for better joint and partnership working: to create a more cohesive sector.

- Improved infrastructure and more supportive legislation: to give community finance institutions more freedom to innovate and compete more effectively with high street banks.
- A clearer regulatory and policy framework to encourage and support a more diverse financial sector that offers a wider range of affordable and accessible finance.

Next steps

The Community Investment Coalition will build on the discussion and feedback from the summit and work to achieve the following goals:

- To develop a clearer narrative about community investment with place based case studies to provide context.
- To create a clearer framework for disclosure setting out who will benefit and data requirements, together with a suggested ratings framework and clear incentives / disincentives to encourage compliance.
- To campaign for improved infrastructure for community finance, including capital to get this in place.
- To continue to campaign for a clearer regulatory and policy framework to encourage and support a more diverse financial sector that offers a wider range of affordable and accessible finance.