CHASM | Centre on Household Assets and Savings Management

Briefing Paper

Are credit unions failing or are they repositioning themselves for the future?

In the past year, a number of credit unions (CUs) have closed – nine requiring the Financial Services Compensation Scheme to return deposits to members – raising concerns about the capability of the sector.

The sector has strong cross-party support and is benefiting from the Department of Work and Pensions' Credit Union Expansion Project. This is funding of £38million aimed at expanding the sector to provide financial services for 1 million more consumers by 2019, and enabling CUs to modernise and become financially sustainable.

Within the sector, this is seen as unambitious, lagging far behind its peers in other countries. In Canada 40% of the population use a CU and the sector operates with greater consumer benefit because of this challenge to its banking sector.

Like all other deposit-taking institutions including banks, CUs are closely regulated by the Financial Conduct Authority and the Prudential Regulation Authority. As the latter is a subsidiary of the Bank of England, presumably the incoming Governor of the Bank of England, Mark Carney will have strong views on the merits of a strong CU sector.

In the UK, there are around 400 credit unions of various shapes and sizes' some staffed by volunteers, while others employ highly experienced staff.

A key question is whether credit unions can provide ethical and affordable financial services while also running in a sustainable manner that does not require state aid.

In essence, the business of a CU is to offer savings accounts and promote thrift and financial wellbeing. These deposits are loaned back to its members at an affordable interest rate, which legislation dictates must be no higher than 26.8% APR. Surplus income is returned to saving members as a dividend. Therefore, any credit union that runs an efficient loan book should be able to operate in surplus.

Yet the annual accounts being released by CUs this year show that in many cases lending is reducing while bad debt and operational costs are rising.

Some CUs are doing well in building productive loan books and returning dividends from surpluses well in excess of building society saving rates.

Common links in successful CUs include expertise at board level and in key positions in the organisation, efficient systems and processes, particularly lending, and the emergence of strong collaborative links between CUs.

There appear to be three questions about how CUs can transition into credible and valuable community-based financial organisations:

- Can credit unions provide affordable credit despite the rising cost of debt-related fees?

- Can credit unions attract and retain skilled personnel and learn to share best practice?
- Can credit unions operate more collaboratively to maximise efficiency and resources?

Behind the headline-hitting failures, there is a clear emergence of some CUs investing well and partnering efficiently in their communities. In a sector that benefits from the wide support for each other, there are positive signs that some are poised to emerge from this current period of transition, better and stronger together.

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