Briefing Paper BP1-2017

An alternative to payday: Are credit unions the answer?

Dr Lindsey Appleyard, Centre of Business in Society, Coventry University

and CHASM External Associate

January 2017

(Originally published on CURB (Coventry University Research Blog) – October 2016)

Why is it that despite bad publicity, payday lending is growing, while many people still haven't heard of credit unions? The growth of payday lending over the last decade, and other forms of credit, is largely in response to income insecurity[1]. Credit is often used as a safety net when incomes do not cover all outgoing expenses. This is true of people both in and out of work. Research tells us that being in work is no guarantee of a stable income[2]. Indeed, many of us that experience insecure work such as zero hours contracts, self-employment, loss of employment, have resulted in many people using high-cost credit as a safety net as a result of financial exclusion and unwillingness of banks to help individuals in financial difficulties.

The regulation of payday loans in 2015 was deemed a great success by campaigners for borrowers. A payday loan is usually for a relatively small amount (on average around £260) for less than 31 days. The cost of a payday loan before the interest rate cap was £15-£35 per £100 borrowed for 30 days, equating to between 448% and 3,752% annual percentage rate (APR)[3]. Whilst the regulation of payday loans has been important to ensure greater affordability and responsible lending, it has diverted attention from other forms of high cost, sub-prime credit that are filling this space. The high cost of bank overdrafts, credit cards,

[1] Rowlingson, K. Appleyard, L. and Gardner, J. (2016) Payday lending in the UK: the regul(aris)ation of a necessary evil?. Journal of Social Policy, 45 (03) 527-543. http://journals.cambridge.org/repo_A10bt3rFszuauE

[2] Joseph Rowntree Foundation (2016) UK poverty: Causes, costs and solutions. https://www.jrf.org.uk/report/uk-poverty-causes-costs-and-solutions

[3] Office of Fair Trading (2013) Payday Lending Compliance Review Final Report, 6 March, http://webarchive.nationalarchives.gov.uk/20140402142426/http:/oft.gov.uk/shared_oft/Credit/oft1481.pdf

rent-to-buy products (such as Brighthouse), logbook loans and doorstep lending (e.g. Provident) also need greater scrutiny by regulators[4]. Meanwhile, some payday lenders have adapted their products to navigate around the interest rate cap. This tells us that regulation needs to be one step ahead to ensure that products are responsible and affordable to protect people from becoming unable to repay the loan and over-indebted.

However, while regulation is important, personal finance is often viewed as an individual issue and therefore an individual's responsibility to make informed decisions. Financial education is often promoted as giving us the knowledge and skills to veer away from (high-cost) borrowing and into saving so that we have reserves if there is an unexpected expense or in times of need. But financial education does not necessarily lead to increased financial capability or what may be considered 'good' financial decisions. For example, there are many reasons why people may borrow from a high-cost lender rather than an affordable lender. So, an awareness of alternative credit options such as credit unions is not necessarily the answer but this could help some.

So what is a credit union and why would you use them? Credit unions:

- have been in the UK since the 1960s/70s,
- are considered a responsible, affordable, financial alternative to high-cost credit,
- are designed for everyone,
- are financial cooperatives owned by their members,
- members share an annual dividend, based on any operating surplus,
- support the local community rather than shareholders.

Credit unions offer a core range of services including:

- savings,
- affordable loans,
- support with budgeting and planning expenditure.

They may also provide a number of additional services such as:

- payroll deductions to make regular savings directly from employers,

[4] Appleyard, L. Rowlingson, K. and Gardner, J. (2016) 'Variegated financialization of sub-prime credit markets'. *Competition & Change*, 20 (5) 297-313. DOI: 10.1177/1024529416657488 http://cch.sagepub.com/cgi/content/abstract/20/5/297

- a prepaid debit card (with cashback offers),
- life insurance, and
- many provide online and telephone banking so that lending decisions can be made quickly and effectively.

However, credit unions are a responsible lender and may not be able to lend to people without a track record of savings (although this is not always the case), or to help people that are already over-indebted and cannot afford to repay. Another limitation is that not all geographic areas of the UK are served by a credit union but there may be an employment based credit union that will allow you to join, such as the police or retail sector. In this way, they cannot replace the high-cost lending gap. This may explain why some credit union members seek credit from high-cost lenders and why alternative finance cannot always fill this space.

So are credit unions an alternative to payday? How about talking to your credit union to find out how they could help you beyond simply providing access to credit. Then talk to your family and friends to spread the word. That may be one way of increasing financial capability.

To find your Credit Union please visit: http://www.findyourcreditunion.co.uk/home

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