The Role of Credit Unions in Promoting Financial Inclusion in Rural Communities in Britain

Abstract

The growth in interest in the development of rural credit unions in Britain from the mid-90’s onwards was directly linked to a growing awareness of the number of rural households living in poverty or experiencing financial exclusion. Credit unions were established by local groups of volunteers in market towns and within dispersed rural areas with the aim of creating locally accessible, mutual and co-operative financial services, particularly for those who found it difficult to access mainstream financial providers.

In 2001, research was undertaken into the initial development of rural credit unions. The aim of the research was to strengthen their potential for growth given that many of the early rural credit unions had become economically vulnerable and, despite local commitment and good intentions, were struggling to make a significant impact in rural communities.

This paper explores the changing perceptions and understandings of rural credit unions and analyses the influence of what came to be known as ‘new model’ credit union development on their governance, management and performance. It re-examines the assumptions upon which current rural credit union development is based and investigates how credit unions can achieve their objective of becoming full service rural financial institutions with the capacity to serve rural communities effectively.

Keywords

Credit unions, financial inclusion, rurality, low income communities, financial services, organisational reform, co-operatives

JEL classification: G1, G2, I3

Introduction

Credit unions are self-help, financial cooperatives, established throughout the world to serve their members with accessible and affordable financial services. Grounded in co-operative values (WOCCU 2007), credit unions often exhibit a strong sense of social purpose (Hannon et al., 1994; Ferguson and McKillop, 1997; Fuller and Jonas, 2002; Goddard et al., 2002; Donnelly, 2004) and in many countries endeavour to serve those unserved or underserved by the mainstream banking sector. Unlike banks, they are owned entirely by their members and operate according to the democratic principle of one member one vote. Credit unions raise funds for lending predominantly from the savings of their members.

Credit unions were first introduced into Britain in the 1960s by immigrants from the Caribbean who struggled to find financial services appropriate to their needs (O’Connell,
2005, 2009; Decker and Jones, 2007). However, it was the poverty and financial exclusion of urban communities in the 1980s and 1990s that stimulated British credit union expansion (Jones 2008). During that period, political support for credit unions grew, and they came to be seen by local authorities as a vehicle for 'regenerating local economies, community development and as a means of the poor helping themselves' (Thomas and Balloch, 1994). By 1999, 83% of all community credit unions were formed with local authority support and with the express purpose of tackling poverty or providing services for disadvantaged people (Jones, 1999). From 1986 to 2000, the number of British credit unions grew from 96 to almost 700, the majority of which were in low-income neighbourhoods (Donnelly 2004).

However, by the end of the 1990s, even though credit unions were growing in number, this was not being matched by growth in members or in assets. The research report, Towards Sustainable Credit Union Development (Jones 1999), revealed that with few exceptions, the average membership of a community credit union in England and Wales was around 200 members, even after 9 to 12 years of development. In Scotland, average membership was a little higher at around 400, due mainly to a few larger credit unions in West Central Scotland (Donnelly 2004). Employee-based credit unions had performed better, recruiting on average 1,200 members but, even among these credit unions, growth was stalling. The result was that many credit unions, especially community credit unions, had become economically and organisationally vulnerable.

The 1999 report identified a number of reasons for poor credit union growth. These included inadequate British legislation and weak national trade bodies. Yet these two reasons alone could not explain poor growth in its totality, given the existence of some higher growth credit unions equally subject to the same legislation and ineffective trade bodies. The research analysis concluded that the main reason for poor credit union performance had been the widespread adoption of a development model that prioritised social goals to the exclusion of economic objectives. This traditional model of credit union development was based on an understanding of credit unions as small, socially-oriented, local volunteer-run community organisations established primarily to provide affordable loans to low-income people who lacked access to mainstream financial institutions. Little priority was given to business objectives or to the development of quality services necessary for long term sustainable development. The impact of this model was seen most clearly on community credit unions, but was also evident within employee credit unions, whose management and operations were similarly not conducive for growth (Jones 1999, 2008a; Decker and Jones 2008).

The 1998 report proved to be a catalyst for change within the British credit union movement. Its findings were recognised by UK central and local government (HMT 1999 a, b; LGA 2001) and by large sections of the credit union movement (O’Connell, 2005, 2009). It presented credit unions with a business model of development and stimulated a process of change that encouraged credit unions to adopt more professional and commercial approaches. The process of transformation is well documented in the literature (Jones 1999, 2001a, 2003, 2004a, b, 2007, 2008; McKillop and Wilson, J.O.S., 2003, 2008; Donnelly, 2004; Ryder 2009; Collard and Smith 2006; Goth et al., 2006, McKillop et al 2007) and it led to cultural shifts in understanding within a large part of the sector. Recent research (Jones 2008) has revealed how the impact of reform resulted in the tripling of credit union
membership and quadrupling of savings and loans since 1998. It is indicative, for example, that, in 2007, 23.25% of all British credit unions have over 2,000 members in comparison with only 3.6% in 1997 (Jones 2008). Of course, challenges remain, and evidence suggests that around 30% of British credit unions still remain economically and organisationally vulnerable (McKillop and Wilson 2008, Jones 2008), yet as Government and stakeholders recognise (HCSAC, 2009, CRC 2007, Ryder 2009), a significant process of strengthening has begun within the British credit union sector.

Rural credit union research

The 1999 report analysed credit union development according to common bond type (community or employee), national location (Scotland or England and Wales), size and rate of growth (Jones 1999). It made no specific reference to credit unions in rural areas and made no comparisons between their development and that of their urban counterparts. The reason focused on credit unions registered before 1994 and, prior to the mid-nineties, the development of community credit unions in rural areas was not possible. Some employee based credit unions served large rural areas but it was generally accepted by the Registry of Friendly Societies, the regulator at the time, that a viable community common bond, a prerequisite of credit union registration, was not possible in a rural area. The common bond, understood as network of social bonds and connections between members, was interpreted so strictly that it was considered that such social bonds could not really exist among disparate rural settlements. It was only under the pressure of groups in rural Britain campaigning for a more flexible interpretation of the common bond which led to the registration of the first credit union in a rural area in 1995 (Barker 1995).

This paper endeavours to explore the factors at play in the development of rural credit unions in Britain. Specific research literature on which to draw is sparse. Barker (1995) undertook a research study into the setting-up of some early rural credit unions in the Pennine Rural Development Area, and identified some of particular challenges they were facing, notably time and travel costs for volunteers; the more diverse nature of the rural population; and the scarcity of local banking facilities. With the increasing interest in credit unions in rural Wales, Butler (1996) explored the contribution credit unions could potentially make to the Welsh rural economy and argued that they would need to generate significant scale if they were to meet the financial needs of the agricultural community, given the high levels of farm household indebtedness. Several years later Lloyd and Brown (1999) carried out research into rural credit unions for the National Council for Voluntary Organisations revealed the difficulties faced by rural credit unions, including recruiting and retaining volunteers drawn from a wide area of scattered communities, the lack of a rural credit union profile, the distances involved and the scarcity of funds to finance credit union development. Lloyd and Brown (1999) concluded that rural credit unions were chronically undercapitalised, which severely limited their ability to grow, and that to succeed they would have to access the requisite investment and professional business support.

This paper is informed particularly by the two research reports, “From Small Acorns to Big Oaks – a study into the development of credit unions in rural England” (Jones 2001), undertaken for the then Countryside Agency, and the later “Creating Wealth in the West
Midlands through Sustainable Credit Unions” (Jones 2005), carried out for the regional development agency, Advantage West Midlands. The first report introduced the concept of new model credit union development, which had arisen through WOCCU co-operative strengthening programmes often with rural credit unions in Latin America, and which went beyond the basic business approaches recommended in the 1999 research report (Jones 1999). The second explores the implementation of the new model through a three-year Association of British Credit Unions (ABCUUL) strengthening project with a group of credit unions in the West Midlands, including those operating in rural and semi-rural locations.

These studies have been complemented by recent research into the progress of the British credit union movement since 1998 (Jones 2008d). This involved tracking the progress of the 17 rural credit unions that participated in the Countryside Agency study (Jones 2001). Progress was measured both statistically and through a series of surveys and interviews with directors, volunteers and staff members in the credit unions concerned.

Rural credit unions, poverty and financial exclusion

The relaxation in the interpretation of the common bond requirement in 1995 resulted in a growth in interest in the creation of credit unions in rural areas. One of the first, registered in 1995, was the Colne Valley Credit Union. It was established as part of the Barker (1995) research study by a group of 16 local volunteers and based on community networks within a 40 square mile rural area. The Registrar’s more flexible approach to the common bond still resulted in permission for only a modest geographical area.

In 1996, a new category of common bond was introduced and, for the first time, those who worked in an area could join a credit union alongside its residents (HM Treasury 1996). This ‘live or work’ common bond supported rural credit union development, as did the introduction of less onerous demands by the regulator to prove the existence of a common bond. This could now be stated by a credit union rather than demonstrated empirically. A turning point in rural credit union development was the acceptance of a rural common bond for the whole of the Isle of Wight with its 100,000 inhabitants in 1997. This opened the way for the registration of much larger common bonds and enabled credit unions, for the first time, to serve larger rural geographical areas.

By 2001, it was estimated that there were at least 62 community (residential common bond) or ‘live or work’ credit unions (out of a total of 698 in Britain) and 22 steering groups (those planning to start a credit union) in areas defined by the Countryside Agency as predominantly rural (Jones 2001). ABCUUL currently estimates that about 20% of credit unions (out of a total of 492) now serve predominately rural or semi-rural areas (CRC 2009).

As in urban areas, many rural credit unions were established as a direct response to the financial needs of people on low incomes (Jones, 2001; Barker, 1995). Typically, representatives of churches, Citizens Advice Bureaux, local authorities, housing associations, community organisations and concerned individuals came together in order to tackle rural poverty and financial exclusion. They were concerned about the number of bank and post office closures in rural areas and by the difficulties faced by the poor in accessing affordable financial services. In the 2001 research study (Jones 2001), 71% of rural credit union survey respondents indicated that their prime motivation for setting up a credit union
was to offer an alternative financial service to those in need or in difficulty (cf. Jones 1999). However the characteristics of rural poverty, as opposed to that found in urban areas, would present credit unions with some particular challenges.

Simmons (1997), McLaughlin (1986), Bradley (1987), Chapman et al (1998), Cloke et al. (1995) have analysed the harsh reality of rural poverty which often lies behind the idyllic images of a fair and prosperous countryside. In 1990, as recorded by Shucksmith (1999), one in four rural households in England and Wales, and one in three in Scotland, were living in or on the margins of poverty. In 2008, even though overall there is less poverty in rural than in urban areas (CRC 2008c), a Commission for Rural Communities (CRC) report (CRC 2008a) revealed that 22% of rural households in rural England still lived below the poverty line. Similar levels of poverty were found in Wales, with 25% of households living in poverty (Milbourne and Hughes, 2005) and in Scotland with just less than 20% (HCSAC, 2007).

However, measuring the level and extent of financial disadvantage in rural areas is often problematic. Standard metrics emphasise the geographical concentration of poverty, useful in urban areas, but which can be deceptive in large, sparsely populated rural areas, where poverty can be dispersed and hidden (CRC 2006). People on higher and lower incomes often live side by side, without there being the same visible concentrations of disadvantage so apparent in urban areas (CRC 2008). Moreover, poverty is not only hidden spatially, it can also be hidden conceptually and psychologically (CRC 2006). A culture of rural self-reliance and pride can lead the financially disadvantaged to avoid self-declaration, due to fears of marginalisation and alienation (CRC 2006). Shucksmith and Philip (2000), in reporting on research in rural Scotland, for example, drew attention to the fact that many households that experienced poverty and disadvantage actively rejected the objective assessment of their position.

Rural poverty is also less associated with the take up of welfare benefits, as it is in urban areas, and more with the working poor. Unemployment is lower, but so too are average incomes, and many people are subject to the insecurities of part-time and seasonal work. The 2006 Rural Disadvantage study (CRC 2006) highlighted the fact that that nearly half of the rural poor are in working households. The difficulties of life on a low income in a rural area are exacerbated by the increased costs of everyday items and services, such as food, fuel and transport, and the generally poor access to private and public services.

Financial exclusion also adds to the difficulties of life on a low income. With no access to, and no usage of, the mainstream financial services taken for granted by most people, financially excluded people have little option but to pay higher charges on transaction services to pay bills, are vulnerable to high-cost sub-prime lenders and often make poor money management decisions (Kempson and Whyley 1999, Kempson et al. 2000; Jones 2001b). Financial exclusion is often the result of poverty (JRF, 1998; Carbó et al., 2005) but it can also be its cause, and lead to even greater poverty and over-indebtedness. There are indications that overall financial exclusion is less in rural than in urban areas (DWP 2007), however, still in 2008, in rural England, 300,000 adults were unbanked (CRC 2008a), with a proportionately greater number in rural Scotland (SE 2007). Research also suggests access to affordable credit for many rural inhabitants is difficult with often a reliance on high-cost
sub-prime or even illegal lenders, even though exact figures cannot be ascertained (Jones and Barnes 2005, SQW 2007). The rise in the closure of rural bank branches and post offices has undoubtedly added to the feel of financial exclusion in the countryside. It was this reality that led groups of people in villages and market towns to create new credit unions as a co-operative solution to poverty and financial exclusion.

The traditional model of rural credit union development

When first established, rural credit unions were organised according to the same traditional, social model of development as previously adopted in urban areas (Jones 1999, 2001). They were small, local, volunteer-run organisations created, for the most part, to provide low-cost loans to people on low incomes. High priority was given to collective democracy, community involvement, member participation and the social and personal education of volunteers. Often they sought small grants, external subsidies or in-kind support from local authorities, charities or trust funds to assist with operational expenditure, premises, equipment and, in some cases, the costs of part-time staff (Jones 2001, 2005).

Among the volunteers, there was an emphasis on the development of local community and social bonds, with many credit unions being as much involved in community activities as in the provision of financial services. These credit unions arose out of what Fischer (1998) described as “spontaneous sociability”, which he argued was fundamental to the success of any financial co-operative. Day (1998) stresses how sustainable economic development in rural areas gains much “from building upon the strength of local social networks and institutional linkages, and in so doing, winning support from local cultural norms and values”. Early rural credit unions were embedded in such social networks, they reflected the cultural norms and values of life in the countryside and, in so doing, they hoped they would be able to create an effective financial service appropriate to the needs of rural communities.

Indeed, research findings (Jones 2001, 2005) recognised that these small voluntary credit unions, even the smallest, often contributed to the vitality of community life. They brought people together in a common endeavour and built social capital among volunteers and members, a characteristic identified by the Countryside Agency (2004) as often associated with rural social enterprise. Studley Credit Union, for example, in rural Warwickshire, was created by church workers and local activists to serve people on low incomes in the parish of Mappleborough Green, a community of five or six thousand adults. Registered in 1999, it was based in a village hall, had strong links with the Citizens Advice Bureau and formed part of the local community scene (Jones 2005). The problem was that at the end of 2004, five years after its registration, Studley Credit Union still only had 72 members, £21k in member savings and £9k out on loan. Similarly at the The Colne Valley Credit Union already mentioned above; by September 2001, six years after registration in 1995, the credit union had only 193 members with total savings of £65k and loans of £28k (Jones 2001). Economically both credit unions were to struggle and both have since transferred into larger County-wide credit unions.

The downside to the adoption of the traditional, social development model was that it resulted in small, undercapitalised and under-resourced rural credit unions, which, despite volunteer commitment to social goals and community life, found it difficult to provide an
efficient and accessible financial service to a sufficient number of members. They lacked the infrastructure and institutional capacity to develop as safe and secure financial organisations and to operate to modern commercial standards. Mostly borrower dominated and often suffering from a perception of being a “poor person’s bank”, they found they were unable to mobilise adequate amounts of savings and, perhaps more importantly in the rural context, make sufficient loans to generate income to build reserves and pay dividends to members. Volunteers were often overstretched and felt the strain of operating what was to become a complex financial business. Most of these credit unions offered a very limited service and were often only open for a few hours each week (Jones 1999).

There was an early recognition that the rural context makes a difference to credit union development. Positively the more heterogeneous nature of rural communities offered “an opportunity to involve a wider cross section of society in the credit union movement” (Barker 1995). Rural credit unions, it was considered, could potentially attract greater numbers of savers, build on strong local identities and benefit from the skills and abilities of rural volunteers. However, Barker (1995) also recognised that rural credit unions faced some particular and additional problems. Communication and transport difficulties, the increased costs of maintaining a service throughout a wide area, the lack of large employers to promote the credit union to their workforce and the hiddenness of rural poverty all combined to make rural credit union development more difficult than its urban counterpart. Later research (Lloyd and Brown 1999) similarly recorded the difficulties faced by rural credit unions. These included recruiting and retaining volunteers drawn from a wide area of scattered communities, the lack of a rural credit union profile, the distances involved and the scarcity of funds to finance credit union development.

The solution to the problem of slow growth among rural credit unions was seen by both Barker (1995) and Lloyd and Brown (1999) to be a more efficient implementation of the traditional credit union model. This entailed, they argued, the recruitment and training of more volunteers, better publicity and the additional support of external credit union development workers, often employed by local authorities or co-operative agencies to work with volunteer groups. The focus on the traditional model meant that, for Barker (1995), even successful rural credit unions would attract only 200 members, be totally organised by volunteers and would serve a common bond area with a population of less than 15,000. However, unlike Barker (1995), Lloyd and Brown (1999) did recognise that the employment of internal business development staff could be an important part of the future successful development of rural credit unions, even though the employment of paid staff was often a contested issue in small rural collective credit unions. This suggestion of employing staff was an early indication of a growing appreciation of the importance of a transition from traditional to a more business-like and professional approach.

With the limitations of the traditional model revealed in the 1999 research (Jones 1999), the question of the suitability of this model within the rural context became a live issue. Certainly, the traditional model was built on social goals and was adopted by local rural groups with a desire to combat poverty and financial exclusion. However, it was not built on the premiss that the achievement of social goals depended first on a realisation of key economic
objectives. In fact, the traditional model hardly focused at all on the achievement of the economic goals of savings mobilisation, income maximisation, capitalisation and delinquency control. The result was that many early rural credit unions found it difficult to achieve economic viability (Jones 2001). It was this reality and concern that led the Rural Development Commission, subsequently the Countryside Agency, to commission the 2001 research into the effective future development of credit unions in rural areas (Jones 2001).

‘From Small Acorns to Large Oaks’ – developing the new model approach

The ‘From Small Acorns to Large Oaks’ research study (Jones 2001) was a two-year participative action research project, commenced in 1999, which was aimed at finding solutions to the effective development of credit unions in rural areas. It involved staff and volunteers as co-researchers from two credit unions, both registered earlier in 1999; Penwith Credit Union which served a small rural region of Cornwall and First Dorset Credit Union which served Dorchester and its rural hinterland. It also involved as a co-researcher participant the emerging Just Credit Union, registered in 2001 at the end of the project, which aimed to serve the widely dispersed population of the county of Shropshire. An additional 12 rural credit unions were involved in the study though workshops, interviews and survey. At the end of the project (end 2001), Penwith Credit Union had 219 members and £62,095 in assets, and First Dorset Credit Union 330 members and £94,670 in assets.

Coterminous with this study, parallel research (Jones 2002) was being undertaken into the development of credit unions in Latin America, in particular in Guatemala, many of which operated in rural areas. The aim was to learn from international experience and strengthen a British understanding of sustainable credit union development. Despite the social, political and economic differences between Britain and Guatemala, credit unions in both countries had often been established for the poor according to a similar model of development that prioritised social over economic goals. In both cases, the result was that credit unions suffered financial, organisational and structural weaknesses. This was compounded often by dependence on external funding, in Britain mainly for operational and revenue costs and in Guatemala for on-lending (Branch 1992, 1993).

The Latin American study analysed the dynamics of a World Council of Credit Unions (WOCCU) co-operative strengthening programme, which over a seven year period transformed a group of inefficient and vulnerable Guatemalan credit unions, many serving rural communities, into competent and sound financial institutions. This revealed to British credit unions the possibility of reforming traditional model credit unions into effective financial institutions. It demonstrated that it would depend, however, not merely on the adoption of basic business practices, as envisaged in the 1999 report (Jones 1999), but rather on a radical financial, organisational and operational restructuring (Branch, and Cifuentes 2001).

This new radical restructuring is often referred to as ‘new model methodology’ (Arbuckle and Adams 2000, Richardson 2000a, b, Jones 2004a), and is understood as a sea-change in thinking in the way credit unions are organised and managed. In contrast to the traditional social development model, the ‘new model’ enshrines a rigorous, professional, market-oriented approach and focuses on the ability of credit unions to generate sufficient income to cover operating expenses, build reserves and pay attractive dividends on savings.
The rural study (Jones 2001) was the first action research project in Britain to engage systematically with 'new model' theory and methodology and to think through its application to credit union development thinking and practice. For rural credit unions of the time, given their tradition and culture, this presented them with a major challenge. For credit unions had still to face the paradox that if they were to achieve their social goals of serving the poor and combating financial exclusion, they had first to achieve economic viability and commercial success (Richardson and Lennon 2001).

For credit unions participating in the rural study, new model methodology raised complex and difficult issues, both conceptually and practically. Conceptually, the ideological perspective underpinning the 'new model' contrasted sharply with that of traditional practice, which appealed to a significant number of volunteers in rural areas. The vision of creating an alternative small scale financial service, founded on human, religious, environmental or social values engaged people in a way that discourse around the economic goals of asset quality, income and capital maximisation did not. In fact, in the rural research project, the two ideologies often clashed even though the emphasis moved increasingly towards 'new model' development as volunteers realised that much more could be achieved by credit unions if they grew into effective financial service providers. As Richardson points out, in referring to the Guatemalan strengthening project, “the long difficult process of changing the way people think is by far the most difficult aspect of modernisation” (Richardson 2000 b).

Practically, the 'new model' presented even more challenges. For engaging with 'new model' methodology involved considering simultaneous reform in all aspects of credit union management and organisation (Branch and Cifuentes 2001). It promoted change in management and organisation, in understanding the operating environment, in the approach to staffing and human resources, in the financial structure of the credit union, in the mobilisation of savings, in credit administration, in financial discipline and in marketing. Implementing reform in each of these areas, whether individually or simultaneously, presented rural credit unions with significant difficulties, given the physical, financial and human resources available. Table 1 outlines the key characteristics of 'new model' methodology, based on the WOCCU approach (Richardson 2000b), but as adapted through the rural study (Jones 2001).

Organisationally, for example, 'new model' methodology maintained that credit union strengthening depended on credit unions serving diverse income groups with the kinds of professional and accessible financial products and services that they wanted and required. Only by so doing, it was argued would credit unions build the capacity and financial viability to serve the poor effectively. However, the focus of most rural credit unions had been on providing a single linked savings and loan product for low income members. In fact, the rural study revealed that many moderate and higher income people joined the credit union, not because it could offer them a financial service they personally wanted, but so that they could help the poorer members of the community.

The challenge for credit unions was to develop as a financial service for all and offer the kinds of products and services that would attract both moderate and low income members. This was particularly significant in rural areas, as it was the rural poor above all who were
alienated by a service created solely to serve their needs. First Dorset volunteers were certain, for example, that the failure of a village collection point was due to the fact that local people were not prepared to declare themselves to be in financial need by joining a credit union. The juxtaposition of low, moderate and high income households in rural areas adds weight to the argument that, if rural credit unions are to succeed, they have to be regarded by the population at large as mutual financial institutions; not just serving the poor but offering a range of financial service that would attract an economically diverse membership.

This meant first researching the financial needs of the market and reforming the credit union approach to product development. Traditional social model credit unions were borrower-led organisations, yet lending policies and practices were restrictive. An obligatory twelve week savings period preceded any loan application, and the amount borrowed was limited to twice or three times the amount saved. Ironically, this lending practice prevented credit unions serving people on moderate incomes, who often found this practice inefficient and complex and who had other choices in the marketplace, as well as people on low incomes who were in need of an instant loan but who had been unable to build a sufficient savings balance (Jones 2004a). The modernisation of credit administration was central to the process of reform. Credit unions were encouraged to break the link between savings and loans and introduce more flexible and responsive capacity-based lending policies.

It might be argued that the obligation to save, and the linking of loans to savings balances meant that credit unions equally prioritised saving. However, this was not the case. For the most part, low income people saved only to borrow and moderate income people saved to support the poor. The widespread policy of not allowing a savings withdrawal, if savings were exceeded by a loan balance, actively deterred borrowers from saving more than they needed to access a loan. Many rural credit unions did have benefactor savers, but there would never be enough to build an economically sound organisation. The lack of a dividend on savings may not have deterred these benefactors but it prevented many moderate income savers investing significantly in credit unions. Attracting and maximising savings was, as described by Richardson (2000b), the ‘new model’ paradigm shift for without the mobilisation of savings, credit unions were destined to remain financially weak. Credit unions in the 2001 study were encouraged to make dividend payments on savings a priority.

The importance of building savings, however, goes beyond amassing credit union funds to on-lend and thereby generate income and build capital reserves. Building savings, or assets, directly contributes to moving people out of poverty, both economically and psychologically. As Sherraden (1991) argued, accumulating savings, or assets, results in a range of positive effects for people on low incomes which include planning for the future, health and well-being and increased participation in the community.

Much of the focus of new model methodology is on upgrading and achieving efficiencies in organisational processes and procedures. In fact, in addition to all the normal difficulties associated with creating any successful business, the rural context introduces additional challenges that arise from geography and distance, communication and transport problems and the rural economy itself. The lack of large employers, for example, hinders the recruitment of employee members through payroll deduction and, as has been already
argued, reaching those on low incomes is more complex given the rural pride and sensitivities and the fact that rural areas, although low wage economies, do not have the kind of high levels of concentrated disadvantage found in inner city areas. All these factors led the 2001 rural research study to the conclusion that rural credit unions must have in place an appropriate infrastructure, organisational systems, rigorous financial discipline, modern information technology, staffing and professional marketing and business development programmes if they are going to succeed in serving dispersed communities effectively and in attracting moderate and lower income members in sufficient numbers.

International credit union experience demonstrates that the development of rural credit unions, however, depends on the employment of high-quality paid managers and staff (cf. Almeyda and Branch 1999). The problem faced by rural credit unions in the 2001 study was that, even though a few had a part-time administrator, none had been able to employ managerial staff and all depended on volunteer labour. Barker (1995) had remarked that “rural volunteers are generally more skilled and from the middle of the socio-economic spectrum” (Barker 1995, and thus often competent contributors at board level, but also that many, although committed to the credit union, did not always have the time to devote to extensive involvement in day-to-day operations. Barker (1995) concluded that the solution to the problem was to recruit and train more volunteers. The new model approach depended, however, on the capacity to employ competent managers. Not only did this contribute to the professional operation of the business but freed volunteer directors to participate more fully in the governance and in setting the direction of the credit union.

The inability of rural credit unions to employ skilled managers was seen in the research to result from a lack of investment in credit unions in rural areas. All the credit unions in the rural study were suffering from under capitalisation and a lack of resources. Questionnaire returns revealed that the majority of rural credit unions were in receipt of some grant aid from local authorities, regeneration programmes or the private sector, mostly acquired for initial training and to cover basic minimal start up costs. For the most part, this grant aid was modest, with the average investment totalling £18,000 per credit union over a three year period. Only 21% of credit unions had received support for part time staff. The credit union receiving the most support was the Isle of Wight Credit Union which received funding for two part-time members of staff, IT and other equipment. Like most rural credit unions, however, the Isle of Wight’s funding was time limited and unstable.

In the 2001 rural study, however, staff and volunteers moved steadily in the direction of new model credit union development and to the conclusion that in order to operate successfully within a rural context, the structures, systems and resources outlined in the ‘new model’ were even more important than within the urban environment. This does not mean there is one single blueprint of credit union organisation and structure that would work in all circumstances and in every rural location. The ‘new model’, however, outlined a framework that was able to underpin the establishment of safe and sound rural financial co-operatives anywhere in the world.
<table>
<thead>
<tr>
<th>Area</th>
<th>Traditional focus</th>
<th>New model focus</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>1 Ideology</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Mentality</td>
<td>Social/business</td>
<td>Business/social</td>
</tr>
<tr>
<td>Attitude</td>
<td>Reactive</td>
<td>Entrepreneurial and competitive</td>
</tr>
<tr>
<td>Approach</td>
<td>Small is beautiful</td>
<td>Growth orientated</td>
</tr>
<tr>
<td><strong>2 Organisation</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Activity</td>
<td>Diverse community activities</td>
<td>Specialisation in financial services</td>
</tr>
<tr>
<td>Policies and standards</td>
<td>Diverse, locally developed and often containing</td>
<td>Standardised according to FSA requirements</td>
</tr>
<tr>
<td></td>
<td>inconsistencies</td>
<td></td>
</tr>
<tr>
<td>Membership</td>
<td>Lower income groups</td>
<td>Diverse income groups</td>
</tr>
<tr>
<td>Member service</td>
<td>Prioritises needs and convenience of credit union</td>
<td>Prioritises member service and responsive to member needs</td>
</tr>
<tr>
<td></td>
<td>volunteers</td>
<td></td>
</tr>
<tr>
<td>Image and market presence</td>
<td>Poor and unnoticed</td>
<td>Professional and accessible</td>
</tr>
<tr>
<td>Products</td>
<td>Credit and savings</td>
<td>Savings, credit, budget accounts, insurance</td>
</tr>
<tr>
<td>Technology</td>
<td>Manual or outdated IT.</td>
<td>Modern Information Technology</td>
</tr>
<tr>
<td>Information</td>
<td>Inadequate and difficult to find</td>
<td>Transparent, easily available and clear</td>
</tr>
<tr>
<td>Formal complaints</td>
<td>None</td>
<td>Clear procedure, made available to members, used to improve</td>
</tr>
<tr>
<td>procedure</td>
<td></td>
<td>services</td>
</tr>
<tr>
<td>Compensation Scheme</td>
<td>None</td>
<td>Contributory scheme to ensure savings are safe</td>
</tr>
<tr>
<td><strong>3 Operating Environment</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Credit union legislation</td>
<td>Outdated and restrictive</td>
<td>Modernised, permissive and designed for growth</td>
</tr>
<tr>
<td>Regulation</td>
<td>Inadequate – focused on registration rather than</td>
<td>Recognises unique characteristics of credit unions as mutuals.</td>
</tr>
<tr>
<td></td>
<td>regulation</td>
<td>Establishes prudent operating standards for all credit unions.</td>
</tr>
<tr>
<td>External environment</td>
<td>Isolated and lacking the active endorsement of other</td>
<td>Sponsored, supported by, and working in partnership, with key</td>
</tr>
<tr>
<td></td>
<td>organisations and agencies.</td>
<td>organisations and agencies. (e.g. Housing Associations, energy</td>
</tr>
<tr>
<td></td>
<td></td>
<td>companies, local authorities, large employers).</td>
</tr>
<tr>
<td>Area</td>
<td>Traditional focus</td>
<td>New model focus</td>
</tr>
<tr>
<td>-----------------------------</td>
<td>--------------------------------------------</td>
<td>---------------------------------------------------------------------------------</td>
</tr>
<tr>
<td>4 Human resources</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Governance</td>
<td>Volunteer Board</td>
<td>Corporate approach - volunteer board in partnership with the paid manager</td>
</tr>
<tr>
<td>Operational Staffing</td>
<td>Volunteers</td>
<td>Paid manager and employees</td>
</tr>
<tr>
<td>Technical knowledge</td>
<td>Insufficient</td>
<td>Well-trained</td>
</tr>
<tr>
<td>Business and financial experience</td>
<td>Inadequate</td>
<td>Competent and professional</td>
</tr>
<tr>
<td>Staff remuneration</td>
<td>Inadequate</td>
<td>Competitive</td>
</tr>
<tr>
<td>Volunteer and staff turnover</td>
<td>High</td>
<td>Low</td>
</tr>
<tr>
<td>5 Financial Structure</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Financing</td>
<td>Grant dependent</td>
<td>Mobilisation of savings</td>
</tr>
<tr>
<td>Capital Reserves</td>
<td>Inadequate</td>
<td>Exceeding minimum regulatory requirements</td>
</tr>
<tr>
<td>Initial Investment</td>
<td>Inadequate</td>
<td>Adequately resourced and capitalised</td>
</tr>
<tr>
<td>6 Savings</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Savings mobilisation</td>
<td>Low priority</td>
<td>First priority</td>
</tr>
<tr>
<td>Dividend</td>
<td>None or below market rate</td>
<td>Competitive dividend rate. Variable rates paid on different types of savings accounts</td>
</tr>
<tr>
<td>7 Credit</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Administration</td>
<td>Inflexible policies and administration</td>
<td>Efficient record keeping and market-oriented approach to lending</td>
</tr>
<tr>
<td>Interest rates</td>
<td>One interest rate for all</td>
<td>Competitive to market rates, particularly in relation to larger loans</td>
</tr>
<tr>
<td>Credit analysis</td>
<td>Limited assessment, based on a multiple of member’s savings</td>
<td>Based on affordability and capacity to repay as well as savings history</td>
</tr>
<tr>
<td>Credit checks</td>
<td>Never</td>
<td>If appropriate in relation to risk</td>
</tr>
<tr>
<td>Loan amounts</td>
<td>Restricted due to lack of funds</td>
<td>Within regulatory limits but flexible, based on risk</td>
</tr>
<tr>
<td>Guarantees (for secured loans)</td>
<td>Inadequate/not registered</td>
<td>Solid, convertible to cash, and registered</td>
</tr>
<tr>
<td>Area</td>
<td>Traditional focus</td>
<td>New model focus</td>
</tr>
<tr>
<td>------</td>
<td>-------------------</td>
<td>-----------------</td>
</tr>
<tr>
<td><strong>8 Financial discipline</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Accounting</td>
<td>In arrears and not balanced</td>
<td>Balanced and on time each month</td>
</tr>
<tr>
<td>Quarterly financial returns</td>
<td>Intermittent or late</td>
<td>Completed and submitted within prescribed deadline</td>
</tr>
<tr>
<td>Financial indicators</td>
<td>Diverse criteria</td>
<td>PEARLS Financial Monitoring System</td>
</tr>
<tr>
<td>Delinquency ratio calculation</td>
<td>Diverse calculations</td>
<td>Entire delinquent loan balance outstanding</td>
</tr>
<tr>
<td>Creation of bad debt provision</td>
<td>None or inadequate</td>
<td>Yearly write offs and 100% provision of net liability of debt more than 12 months in arrears. 35% provision for debts more than 3 months in arrears</td>
</tr>
<tr>
<td>Net income distribution</td>
<td>No dividend</td>
<td>Dividend after statutory transfer to reserves</td>
</tr>
<tr>
<td>Institution reserves</td>
<td>Inadequate</td>
<td>Reserve levels that meet FSA standards</td>
</tr>
<tr>
<td>Liquidity reserves</td>
<td>Not specifically allocated</td>
<td>Sufficient to meet operational needs and enable members’ demands for unattached share withdrawals</td>
</tr>
<tr>
<td>Internal audit</td>
<td>Not effective, exists in name only</td>
<td>Active and effective. Compliments the boards work in improving services</td>
</tr>
<tr>
<td>Annual external audit</td>
<td>Inadequate</td>
<td>Professional and appropriately qualified accounting firm</td>
</tr>
<tr>
<td>Annual business plan / strategic plan</td>
<td>Inadequate/none</td>
<td>Prepared annually and controlled monthly</td>
</tr>
<tr>
<td><strong>9 Marketing</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Premises</td>
<td>Inadequate, uninviting and often closed</td>
<td>New and well situated, comfortable. Open at regular times convenient to members.</td>
</tr>
<tr>
<td>Furniture and equipment</td>
<td>Old and worn out</td>
<td>Modern</td>
</tr>
<tr>
<td>Research</td>
<td>None/intermittent</td>
<td>Covering market area and used to inform marketing and business plans</td>
</tr>
<tr>
<td>Marketing plans</td>
<td>None/limited to promotions of publicity</td>
<td>Integrated with the business plan</td>
</tr>
<tr>
<td>Dress code</td>
<td>None</td>
<td>Professional</td>
</tr>
</tbody>
</table>

*Taken from “From Small Acorns to Large Oaks” (Jones 2001) and adapted for the English rural credit union context from the WOCCU credit union development model (Richardson 2000)*
Learning from the West Midlands – new model credit union development

The research project “Creating Wealth in the West Midlands through Sustainable Credit Unions” (Jones 2005) took place from 2002 to 2005 and was designed to assist credit unions to develop into ‘new model’ financial institutions. It was a multi-faceted project which included an intensive development programme for selected beacon credit unions, a regional educational programme and specialist technical support for vulnerable credit unions and those undergoing change. Just Credit Union (JCU), a participant in the 2001 rural research, was the beacon rural credit union and engaged to follow its rigorous development programme.

The West Midlands project aimed to build on the experience of the 2001 rural study and enable credit unions to serve the financial needs of the population at large, maximise savings by offering attractive dividend rates, diversify the portfolio of products and services, introduce operating efficiencies, commit to financial discipline, develop the governance systems and enable the assimilation of the financially excluded and people on low incomes into the mainstream (Richardson 2000a).

The learning generated on the West Midlands project convinced credit unions that to become quality financial institutions, they need to adopt customer and market led approaches to their development and to operate to commercial standards. With the support of the West Midlands credit unions action learning project, the directors and staff of Just Credit Union were able to identify a number of key learning outcomes arising from their experience of organising a credit union in a dispersed rural area. JCU concluded:

- Organising a county-wide credit union is more complex and demanding than the directors originally anticipated. Ensuring quality service delivery is particularly difficult with a small staff team and dispersed groups of volunteers. Just has learnt to target particular groups, communities, employers and organisations rather than trying to offer a service generally throughout the county.

- The importance of having a skilled and competent board of directors able to contribute to decision-making has become more evident. It is no longer appropriate to take onto the board anyone who volunteers. There needs to be effective monitoring and assessment through a nominating committee.

- Having a formal strategic planning process which leads to a robust business plan and specific resourced action plans is now seen as essential. The day-to-day demands of running a complex organisation often leaves little time for reflection and analysis. The board and staff have learnt the value of setting time aside for planning, often with the support of an outside facilitator.

- The development of staff and board skills in financial management has been a key outcome of beacon status within the West Midlands project. JCU now uses the PEARLS financial ratio system as a management tool (Richardson 2001). Financial analysis has demonstrated the importance of prioritising savings products within the credit union.

- The need to offer a professional and quality service is now seen as fundamental. This has involved training operational volunteers in member care and developing a sense of
mutual professional responsibility for the service that is offered. It has also meant that products and services respond to what members and potential members want from a credit union. Just has introduced customer focused lending policies based on a capacity to repay.

- The credit union has targeted organisations and communities but has learnt that it has had to have human and organisational resources in place to manage an influx of new members. Just has had to measure its growth to match resources within what is, in reality, an under-resourced organisation.

- Developing robust systems to support service delivery, particularly in lending and credit control has been a key learning experience. Just has developed standard procedures for credit application and granting. The same is true for credit control, where implementing standard practices in rural areas can be complex. Debt collection agencies, for example, do not often cover an entire rural area. Standard procedures are important when service delivery is through partner organisations. Service level agreements ensure good practice.

- A pilot study, supported by the West Midlands project, into the use of electronic cards for making deposits through post offices and retail shops has proved a success. Electronic deposits now account for 23% of all cash deposits into the credit union. Electronic access to cash is a goal of the credit union movement as a whole.

- Service delivery through partner organisations has been shown to be an important element of service delivery in rural areas. Just has only been able to maintain a network of credit union money points throughout the county with the support of housing associations, advice centres, community centres and other similar organisations.'New model' methodology furnished credit unions with a road-map for their transformation into more effective financial institutions. Credit unions following this map became known, in the British movement, as ‘quality credit unions’, a term that seemed less prescriptive than ‘new model’. As defined by ABCUL (2005), a quality credit union is one that:-

  - “has a strong capable board with the skills, sense of urgency and capacity to drive the credit union towards sustainability;

  - researches what its members want and seeks to provide services to meet those needs;

  - is a flexible lender – does not require people to save before they borrow;

  - is a responsible lender - assesses loan requests on the capacity to repay;

  - emphasises savings mobilisation recognising that sustainable financial intermediaries are built on member savings not external capital;

  - gives their members somewhere to deposit their wages or benefit and gives them easy access to their cash and a means of simply carrying out basic transactions”.

By 2005, there were good grounds for maintaining that rural credit unions had much greater awareness of what needed to be done to operate a credit union in a large rural area, the problem remained just how to do it in practice.
Rural credit unions – progress and development

Of the 15 credit unions that participated in the 2001 rural research study (Jones 2001), one is no longer trading, three have transferred engagements into other larger credit unions, two more are planning to transfer soon, one is planning to accept the transfer of another credit union, three are still operating as traditional volunteer-operated collectives, and five are endeavouring to grow the business according to new model methodology. All 15 rural credit unions are listed in Table Two. The average membership of the 15 credit unions at year end 2001 was 220 members, at year end 2008 it was 704, average assets were £72k in 2001 and £336k in 2008.

An assessment of the impact of credit unions within rural communities is complex. Most of the 15 credit unions that exist can demonstrate the attainment of social and community goals, normally at grass roots level, and often in terms of volunteer participation and training, of assisting individual members in financial difficulty and of contributing to community life and vitality. West Mendip Credit Union, for example, which serves 300 square miles of rural Somerset, is organised entirely by volunteers, has no premises of its own, operates through libraries and community centres and would claim to have generated a culture of mutuality and connectedness among its 354 members. Badingham and Neighbourhood Credit Union operated in a small Suffolk village and was formed by local people in response to the perceived hardship of families in the area. But “people were too proud to declare that they were poor”, a former director reported, and the credit union only ever recruited 72 members and made 5 loans. It closed in 2003 when credit unions came under the Financial Services Authority. But, as the director explained, ‘it had a low level altruistic feel about it and generated a lot camaraderie in the village”. As Fuller and Jonas (2002) argued, traditional credit union development often owed more to the concepts of social capital and community empowerment than it did to theories of economic development.

Since the publication of the 1999 report (Jones 1999) and the development of ‘new model methodology’, much greater attention has been given, when assessing credit union impact, to growth in members, savings, loans and assets and to the achievement of economic goals. For credit unions can only provide effective services for members, particularly for the financially excluded and those on low incomes, if they are developed, first and foremost, as strong and sustainable financial institutions. This is a position accepted by Government (HM Treasury 1999a, 1999b, 2004) and increasingly in the literature (McKillop and Wilson 2003 Collard and Kempson, 2005; Rossiter and Cooper, 2005; NCC 2005, Goth et al.2006.

Of the 15 credit unions, only three have grown to over 1,000 members, with an average asset size of £618,000. These are Just Credit Union, First Dorset Credit Union and Cornwall and The Scilly Isles Credit Union. The first two were action research participants in the 2001 rural study (Jones 2001) and Penwith Credit Union, the third participant in the study, transferred into Cornwall and The Scilly Isles Credit Union in 2007. These three leading rural credit unions have been able to develop a valuable financial service within the constraints of the resources available. However, given they serve large geographical areas, the challenge of delivering an effective financial service to all throughout the entire rural area remains.
Otherwise, among the group of 15 credit unions, growth in the number of members and in assets has remained relatively modest. Six of the 15 have, or will soon, disappear as independent credit unions. Over the period, they were unable to generate the organisational capacity and economic strength to continue as autonomous organisations. Teesdale Credit Union, for example, in rural County Durham, is soon to transfer into a county-wide credit union. Established by church groups and organised entirely by volunteers, the credit union endeavoured to serve ex-mining villages and hill-farming settlements in a 324 square mile rural area. However, after nine years of development the credit union was only able to recruit 130 members and, finally, was neither financially nor organisationally viable.

The organisational and economic vulnerability of many rural credit unions is recognised by Government (CRC 2009). As a recent Commission for Rural Communities Report (2009) noted:

“Credit unions in rural areas face substantial challenges linked to growth and becoming financially sustainable. Operating in a sparsely populated area, they find it difficult to reach the critical mass of membership base. Rural areas are also associated with increased time and travel costs for volunteers to oversee the ‘collection points’, and a scarcity of local banking facilities, which can make collection and transfer of cash difficult”.

Nevertheless, credit unions regarded by Government as important vehicles for combating poverty and financial exclusion in the countryside (SQW 2007, CRC 2008, 2009). In general, the potential of modernised, and later ‘new model’ credit unions to combat financial exclusion and to build wealth in communities has recognised by UK central and local government since 1999 (HMT 1999 a and b, LGA 2001, HCTC, 2006 a and b). In early 2005, following the publication of the report, “Promoting Financial Inclusion” (HM Treasury 2004), the Government established a Financial Inclusion Taskforce with the purpose of monitoring progress on its policy objectives of tackling financial exclusion, including supporting credit unions to maximise their impact within low income communities, including within rural areas.

**Financial Inclusion Growth Fund**

In October 2005, as direct support to the development of the credit union movement, HM Treasury announced a £120 million Financial Inclusion Fund which included a £36 million Growth Fund for credit unions and CDFI’s. The purpose of Growth Fund was to expand lending in low income communities and to enable financial excluded borrowers to migrate from sub-prime loan companies into credit union or CDFI membership. Initially, seventy-three credit unions were contracted by the Department of Work and Pensions, and an additional sixteen subcontracted by contracted credit unions or CDFIs, to deliver the Growth Fund, which was originally intended to operate from April 2006 for a two year period. This has now been extended into Growth Fund 1.5 and GF 2.

The Growth Fund has now been in operation for over two years and the results are beginning to emerge. Credit unions are lending 91% of total loans made under the Growth Fund. Initial success with the fund prompted the Government, in March 2007, to provide a further £6 million to support lending in under-served parts of the country, to invest in skills
and capacity-building programmes of staff and volunteers and to support credit unions to provide transactional banking services.

Government support for the introduction of current accounts, as part of the overall approach to tackling financial exclusion, has been particularly encouraging. Credit unions have only been able to offer current accounts since 2006 through a partnership arrangement with The Co-operative Bank but are now seen as essential to a pathway to financial inclusion (Jones 2008 a, c). In addition, in March 2007, HM Treasury announced that it intended to establish a new Financial Inclusion Fund “for new and ongoing initiatives to promote financial inclusion, maintaining the current level of intensity of action” (HMT 2007a). In December 2007, it was confirmed that the Financial Inclusion Fund would be extended until 2011 and a further £38 million made available to credit unions and CDFIs for on lending (HMT 2007d).

However, the lack of credit unions operating in rural areas, with a capacity to deliver, has meant a small number of applications to deliver Growth Fund loans in rural areas. Between 2006 and 2007, only 2.3% of Growth Fund loans were made to people living in rural areas (CRC 2009). However since 2007 the Growth Fund has supported the expansion of credit union services, in relation to the list of 15, at Just Credit Union and First Dorset Credit Union, as well as in Workshop and in Taunton.

**Did small acorns ever grow into large oaks?**

The original intention of the 2001 rural action research (Jones 2001), as it was of the 2005 West Midlands project (Jones 2005), was to support the growth of credit unions in rural areas from their small beginnings, small acorns, to their becoming self-sustainable co-operative financial institutions, large oaks. Just Credit Union and First Dorset Credit Union have made significant progress but many challenges remain.

**Just Credit Union**

JCU is the largest open-common bond rural credit union in Britain with over 1,600 members and serves the 1,234 square miles of the rural county of Shropshire, with its population of 240,000 adults. Eschewing proposals to establish a number of smaller traditional model credit unions throughout the county, the original founders decided to proceed with the creation of the first county-wide rural credit union in Britain. The primary focus was always on delivering financial services to the financially excluded, but the vision was to create a business-oriented financial institution that would be large enough to flourish. It was recognised from the outset that this involved competent management, paid staff, quality products and services, effective organisational systems and procedures, adequate finance and resources and professional marketing and promotion. JCU is the only rural credit union to have implemented WOCCU’s PEARLS monitoring system (Richardson 2001).

Since 2005, and JCU’s involvement in the West Midlands action research (Jones 2005) as a beacon credit union, JCU has focused on developing the professionalism of the business and develop member access to services through electronic payment deposit systems and the new Credit Union Current Account. JCU is the first rural credit union to introduce the current account. With the move to greater use of electronic systems, JCU has closed many of its volunteer-operated branches in community locations. Despite the loss of direct contact
with volunteers, JCU assessed that branches were not only costly to maintain but unproductive in ensuring a quality service for members. Apart from 5 remaining branches in market towns and collection points in five schools, all of JCU’s business is now conducted centrally from its head office the county town. Links with partner organisations, however, are strong and the credit union offers direct payroll payment services to County Council, hospital and housing association employees. Since its creation, JCY has had the active support of Shropshire County Council which has provided a central office and financial support for 2.5 staff members.

JCU considers that it is now at a cross-road. Through the delivery of the Financial Inclusion Fund Growth Fund, JCU has prioritised serving low income and financially excluded members. This has brought external income and capital into the credit union, but, according to the manager (Jones 2008), this has compromised building the business a going concern. Small loans made to high risk, low income members are not profitable in themselves, and heavily resource intensive; the challenge for JCU is to generate income from more profitable lending.

The fact that the level that income from the business does not yet cover costs is a critical issue for JCU. Operating expenses are high at 18% of average assets (WOCCU target is less than 5%) and other income from grants and subsidies to cover these expenses is 17% of average assets. JCU is dependent both on the income generated through the Growth Fund (ending in 2011) and through the support of Shropshire County Council. The challenge for Just is build the business by attracting an increasingly economically diverse membership. Currently over 13% of borrowers are on welfare benefits.

First Dorset Credit Union

Since 2001, First Dorset Credit Union’s (FDCU) strategy to grow as a viable co-operative enterprise has turned on developing more professional approaches to the business, on widening the common bond or area of operation, of moving into visible high street premises, on developing links with partner organisations and on participating in the HMT Financial Inclusion Growth Fund. Overall the aim has also been to diversify the membership and attract more moderate income members, as central to achieving long-term financial stability. For it was accepted that only by attracting a more diverse membership would the goal of serving the financially excluded be achieved. In the period 2001 to 2008, membership has increased by 325% and assets by 534%.

In 2001, the common bond was smaller than it is today, mainly defined by the county town of Dorchester and its surrounding rural hinterland. FDCU now serves all of rural Dorset. This has allowed the credit union to develop County-wide partnerships with housing associations, community organisations and local authorities. In fact, the move into professional high street premises in Dorchester was facilitated by a partner housing association. At the same time, to enable credit union access in the villages, ‘collection points’ or local branches have been increased to eight, established predominantly in church halls and housing association offices throughout the county. Current statistics demonstrate that active membership is now drawn equally from rural villages and settlements and from the county town Dorchester.
Operational management still remains a challenge. The credit union now has two full time members of staff, a manager and loans officer, which enables some of the directors to take a more strategic and policy oriented role. However, operational service delivery depends heavily still on the 100 volunteers who staff the main office and outlying collection points. The logistics of serving a large geographical area is hindered by FDCU’s lack of IT infrastructure, current account transaction facilities and electronic payment methods into the credit union. Nevertheless, with moves to encourage payroll deduction for employees and deposits by standing order, FDCU calculates that now only 40% of its members pay into branch offices in person.

The major decision in 2006 to participate in the Financial Inclusion Growth Fund was seen by FDCU as key its strategic development. By bringing in external capital into the credit union for on-lending, it enabled FDCU to serve a greater number of low income people. It also brought revenue resources to pay for one of the full time members of staff, the loan officer. One possible drawback has been that it possibly contributed to maintaining the image of the credit union as a financial institution for the poor.

In fact, in 2008, the overall profile of the active members tends still to be people on low income and/or on welfare benefits. FDCU has still not been able to diversify the membership base sufficiently and attract moderate income members in significant numbers who wish to use the credit union as a financial resource. There is still a noticeable number of “ethical savers” who are willing to save in the credit union, at no rate of return, in order to support the community. The problem is that the number of such ethical savers in any community is inevitably limited.

As with JCU, a critical issue for FDCU is that the credit union is not generating sufficient income to develop to pay all its costs. Even though both membership and assets have risen, so too have costs, as the credit union has had to engage staff to carry out the business. Operating expenses are 14% of average assets (WOCCU target is less than 5%) and other income from grants and subsidies to cover these expenses is 11% of average assets (year end 2007). Some immediate staffing costs are being met by Growth Fund revenue income and by a grant from a charitable trust, both of which will end in the next few years. Volunteers reported that they are seeking further grant aid from external sources, particularly as write offs and provisioning for bad debts have been on the increase. Some volunteer directors are sceptical of FDCU ever becoming fully sustainable without ongoing external support to provide a service to the community.

**Rural credit union development – challenges and opportunities**

*Developing the rural credit union infrastructure – the importance of new technology*

Establishing a modern, professional credit union anywhere is demanding. But it is more demanding in a rural area where added complexities arise from geography, distance and poor transport links. Not only does rurality add considerably to the challenge of managing the organisation, but it also adds to the costs. It is for this reason that rural credit unions have often pioneered new solutions to enabling people access credit union services. Building a network of partner organisations and agencies throughout a large rural area is one approach credit unions such as JCU and FDCU have found to be effective. People are
then able to access the credit union through their own organisation, whether this is a housing association, district council, community organisation, advice agency, faith community or other corporate community body.

Other credit unions have endeavoured to create networks of volunteer community branches. Norfolk Credit Union (NCU), for example, serves 300 square miles of the rural county of Norfolk through a volunteer-driven ‘community group and strategic partnership approach’. This involves the creation of multiple volunteer groups throughout the county, each of which is organised to deliver its own NCU branch branded locally as a ‘community bank’. This labour intensive solution is only possible, however, as all branches are staffed solely by volunteers.

As modernised credit unions endeavour to build efficiencies into service delivery, it often becomes evident, however, that they are unable to preserve branches or collection points in every town, village and settlement in a county. Not only is this costly, particularly if staff are employed to manage these alongside volunteers, it is difficult to ensure that products and services are of a standard and consistent quality. It was, for this reason that JCU moved in the direction of the introduction of new technology. To facilitate the making of deposits into the credit union, JCU undertook a pilot project, as part of the West Midlands research (Jones 2005), to introduce electronic deposit cards enabling members to make cash deposits in post offices and in retail outlets. This proved successful, with 23% of all cash deposits into the credit union being made by use of the card after only one year of operation (Jones 2005). This led JCU to offer the Credit Union Current Account enabling members to access cash machines, cash-back in shops and fully functional debit cards. This has proved to be a step forward in enabling people to access credit unions in rural areas. It resulted in JCU closing a number of its local collection points, however, regarded as necessary in advancing the efficiency of service delivery, even though this has meant some loss of contact with volunteers. The JCU experience in the introduction of new technology has been complemented by that of credit unions such as York Credit Union (YCU) which has pioneered a web-based system to enable members to access their accounts through library collection points throughout Yorkshire, the largest county in England.

The steps taken towards the introduction of new technology in credit unions such as JCU and YCU have been significant, and this has been followed by other credit unions also introducing electronic deposit systems and, in places, pre-paid debit cards. The most significant has been the introduction of the Credit Union Current Account at JCU. This has led the Commission for Rural Communities (CRC) to recommend to Government to establish a Financial Inclusion Technology Fund to support the development and use of new innovative delivery mechanisms to ease access to financial services within rural areas including the new Credit Union Current Account (CRC 2009). CRC also recommends that the Government should expand support through the Growth Fund to develop credit unions and in rural areas beyond 2011.

*The new Credit Union Current Account is a major step forward. However, with a set up cost of around £100,000 it remains beyond the reach of most credit unions. Furthermore, many rural communities still have no access to credit unions and/or*
Without access to appropriate and affordable credit there is an increasing risk that vulnerable people in these rural areas will turn to high interest doorstep lenders and illegal money lenders. (CRC 2009)

Of course, branch networks, new technology and delivery mechanisms alone do not attract people to credit unions. To succeed rural credit unions will have to provide the kinds of products and the kind of personal financial services that a large cross section of people in rural areas want and need.

Promoting financial inclusion

Credit unions have discovered that, despite commitments to serving the financially excluded, there is a particular rural challenge in serving low income and poorer members. Often isolated and living alongside their more prosperous neighbours, people on low incomes are often unwilling to be stereotyped as poor, and reject any financial service that appears established primarily for their needs as poor people. This image of a credit union as organisations established for the disadvantaged results in their not being attractive to the people they are designed to serve. In both 2001 and 2005 (Jones 2001, 2005) rural credit unions regularly reported that they were not reaching as many people on low incomes as they would like.

Paradoxically, this means that the needs of the rural financially excluded can only be met in credit unions that appeal to economically diverse sections of the population. This has entailed a cultural change within many socially-driven rural credit unions that traditionally focused primarily on low income groups. The challenge for rural credit unions is now, through effective marketing strategies, new technology and infrastructure and the development of quality products and services, to attract a much wider membership base.

Rural credit unions are indeed making moves to become more open and accessible to a larger cross section of society. The moves to high street premises for example, has enabled many credit unions to be more visible and to be seen as offering a financial service to the population at large. Indeed as the West Midlands project concluded (Jones 2005) credit unions will need to develop into the kind of professional financial organisation that can attract members through the quality of its products and services. Whether this can be done however remains to be seen. Nationally, the signs are promising and the British credit union movement as a whole has experienced a significant strengthening over the last 10 years (Jones 2008d). Yet some commentators remain sceptical and see little appetite among the general public for credit union products and services (McKillop and Wilson 2008).

Legislation and regulation

An important factor linked to new model credit union development is legislation reform. From the time of the Credit Unions Act 1979, British credit union legislation has been regarded as restrictive and has been seen as limited growth. Over the past ten years, advances in legislation change have occurred and in June 2007, the government launched a major consultation on cooperative and credit union legislation (HMT 2007c,). This has resulted in a commitment to introduce new legislation in 2009 that will enable more flexible common
bonds, corporate membership, and permission to pay interest on savings deposits among other significant changes (HMT 2009). All of which, it argued is central to building the capacity of rural credit unions to serve low income communities more effectively.

The key proposals of the 2009 HM Treasury legislation reform order relate to:

- **The common bond** - the proposal is to abolish the traditional "common bond" requirement for credit unions, in which some form of ‘commonality’ between members had to be established. This is to be replaced with a "field of membership" test, in which credit unions define the group of people it serves and demonstrate their capacity to do so. Credit unions will be allowed to serve multiple fields of membership, which, in fact, will still be called ‘common bonds’ for ease of reference. This will allow rural credit unions to serve people in a locality plus, for example, all the tenants of a particular housing association, no matter where they lived in the country. It will allow rural credit unions to amalgamate even though their common bond areas are not adjacent. It will make credit union membership more open, accessible and flexible.

- **Corporate membership** – At present credit unions can only offer membership to individuals. With the new legislation, credit unions will be able to accept corporate members, unincorporated associations or partnerships into membership, with certain provisos. This will allow, for example, housing associations, charities, private sector companies and foundations to invest in a credit union and create funds for lending within low income communities.

- **Interests on deposits** - Modernised credit unions need legislation to allow interest-bearing savings accounts to attract diverse groups of savers. This is critical to credit union success as financial strength depends ultimately on attracting member savings. For this reason, that all credit unions will be able to offer variable interest rates on savings deposits if they hold reserves of £50,000 or 5% of total assets, whichever is higher, providing certain conditions are met.

- **Attachment of shares to loans** – Credit unions traditionally did not allow borrowers to withdraw their savings if the balance of their loan account exceeded that of their savings account. This practice of freezing savings if a member has a higher-value loan had been strongly criticised in new model methodology as it results in members saving elsewhere if they have a loan outstanding. This attachment of shares to loans was enshrined in the 1979 Act. The new legislation will repeal the ‘attachment requirement’.

- **Charging for ancillary services** – The proposal to allow credit unions to charge market rates for ancillary services recognises the fact that credit unions are commercial businesses that must generate income to survive. At the moment credit unions can only pass on the cost of providing a service to a member, a difficult exercise as actual costs are not easy to calculate, with this proposal credit union will be able to charge properly for such services as managing a budget account, cheque cashing and bill payments.
Collaboration among credit unions

Most of the products and services required by a modern, co-operative credit union movement are now available to credit unions within the British credit union movement. These will be further upgraded and modernised with the advent of the new legislation. Credit unions can, or soon will with the change in legislation, be able to offer a current account, benefit direct accounts, savings accounts with variable interest rates, the Child Trust Fund, loan accounts with variable interest rates (up to 2% per month), multiple insurance products, bill payment accounts, transmission services, electronic payment systems, pre-paid cards, and internet banking. They could, if they had the capacity and requisite permissions, also offer mortgages. These products and services are available to all rural credit unions with the capacity to deliver them.

It is now recognised that the capacity to deliver enhanced products and services would be assisted by the development of collaborative back office services. The atomised business model of individualised credit union development, as delineated both in the 1999, 2001 and 205 research studies, is now seen as unlikely to generate sufficient scale and organisational capacity to deliver products and services within a competitive financial market. For this reason, more collaborative back office approaches to business development are seen to offer greater potential for economies of scale and the delivery of a wider and more diverse range of products and services. These could include administrative services, marketing, internal audit, treasury and liquidity management, current account and card management and even call centre support. A collaborative back office approach would depend; however, on a central IT platform which itself could be offered to all credit unions, including those in rural areas and maintained though a back office facility.

Rural credit unions are well placed to participate in a coordinated back office facility given the level of mutual support that exists in the sector. However, this would not be particularly a rural initiative as a wider UK back office facility for all credit unions would be much more productive. This would be necessary particularly in the case of the Credit Union Current Account, a back office for which could only be delivered UK-wide.

Collaborative bank office facilities are only applicable if credit unions have the organisational management and capacity to participate. Given the size and strength of some of the credit unions in rural areas, further transfers of engagements to create larger, more stable institutions will be required before all rural credit unions can participate productively in a back office facility. This is already happening in rural North Wales and undoubtedly will be considered in other regions as well.

The future of rural credit unions in Britain

The important role rural credit unions can play within rural communities continues to be recognised by Government and public bodies. A recent CRC report (CRC 2009) highlighted the ongoing reality of financial exclusion in rural areas, exacerbated by the effects of the recession, and stressed the contribution that can be made by community-based credit unions. The report highlighted how, of the 25 local authorities with the highest unmet demand for affordable credit, four are classified as rural and eight have significant rural populations, and how around 200,000 people in rural England do not yet have access to a
bank account. The recognition that the demand for financial services such as affordable 
credit is outstripping supply in rural areas is increasingly leading local government and 
agencies to look to the credit union movement to supply the gap. Recently, for example, the 
Scottish Highland Council’s Recession Action Plan included a commitment to explore the 
creation of a pan-Highland credit union to provide financial services, money advice and 
affordable credit across the Highlands, one of the most rural regions of Britain (Highland 
Council 2009).

However, the challenge this poses to rural credit unions is immense. The financial and 
human resources required to implement an effective financial service to low income people 
throughout a dispersed rural area are considerable. Nevertheless, credit union experience 
and research since 1999 has established a ‘new model’ route map to effective development 
based on good governance, effective management, financial discipline and a focus on 
quality in service delivery.

However, successful change and development in the rural credit union movement will 
depend ultimately on the quality of the leadership of credit union directors and managers. It 
will depend on the leadership and business expertise, credibility and skills of the people 
involved in credit unions. Finding proven leaders to drive forward the next stage of 
development will be challenging and will depend, not just on training existing personnel, but 
on recruiting new people to serve on boards and work in credit unions. Staff recruitment is a 
key issue as the growth and development of rural credit unions depend ultimately, not on 
external factors, but on the quality of their management. Credit unions need to employ senior 
managers with high-level skills in leadership, strategy, business and financial management. 
Employing managers who are primarily administrators, as many rural credit unions have 
been accustomed to doing, rarely results in achieving strategic objectives.
<table>
<thead>
<tr>
<th>Credit Union Name</th>
<th>Year Reg.</th>
<th>County</th>
<th>Year</th>
<th>Members</th>
<th>Assets</th>
<th>Savings</th>
<th>Loans</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Badingham and Neighbourhood Credit Union</td>
<td>2000</td>
<td>Sussex</td>
<td>2001</td>
<td>55</td>
<td>n/a*</td>
<td>£9,000</td>
<td>£300</td>
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<td>2. Breseley, Much Wenlock and District Credit Union</td>
<td>1997</td>
<td>Shropshire</td>
<td>2001</td>
<td>201</td>
<td>£58,455</td>
<td>£47,895</td>
<td>£25,395</td>
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<td>3. Colne Valley Credit Union</td>
<td>1995</td>
<td>Yorkshire</td>
<td>2001</td>
<td>193</td>
<td>£68,227</td>
<td>£64,973</td>
<td>£27,969</td>
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<td>4. First Dorset Credit Union</td>
<td>1999</td>
<td>Dorset</td>
<td>2001</td>
<td>330</td>
<td>£94,670</td>
<td>£78,000</td>
<td>£38,015</td>
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<td>5. Isle of Wight Credit Union</td>
<td>1997</td>
<td>Isle of Wight</td>
<td>2001</td>
<td>370</td>
<td>£122,722</td>
<td>£95,870</td>
<td>£57,850</td>
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<td>6. Just Credit Union Credit Union</td>
<td>Shropshire</td>
<td>2001</td>
<td>Registered as a credit union in 2002</td>
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<td>7. Mid Cornwall Credit Union</td>
<td>2000</td>
<td>Cornwall</td>
<td>2001</td>
<td>265</td>
<td>£65,174</td>
<td>£53,917</td>
<td>£34,273</td>
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<td>8. Penwith Credit Union</td>
<td>1999</td>
<td>Cornwall</td>
<td>2001</td>
<td>219</td>
<td>£62,095</td>
<td>£36,106</td>
<td>£22,067</td>
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<td>9. Plough and Share Credit Union</td>
<td>2000</td>
<td>Devon</td>
<td>2001</td>
<td>200</td>
<td>£24,666</td>
<td>£14,225</td>
<td>£5,409</td>
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<td>10. Stroud Valley Credit Union</td>
<td>1998</td>
<td>Gloucestershire</td>
<td>2001</td>
<td>162</td>
<td>£35,667</td>
<td>£26,268</td>
<td>£6,795</td>
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<td>11. Taunton Credit Union</td>
<td>1998</td>
<td>Somerset</td>
<td>2001</td>
<td>206</td>
<td>£40,000</td>
<td>£37,500</td>
<td>£17,000</td>
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<td>12. Teesdale Credit Union.</td>
<td>1999</td>
<td>Durham</td>
<td>2001</td>
<td>117</td>
<td>£22,674</td>
<td>£20,402</td>
<td>£8,267</td>
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<td>13. West Derwentside Credit Union</td>
<td>1997</td>
<td>Durham</td>
<td>2001</td>
<td>424</td>
<td>£96,210</td>
<td>£87,689</td>
<td>£8,612</td>
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<td>14. West Mendip Credit Union</td>
<td>2000</td>
<td>Somerset</td>
<td>2001</td>
<td>n/a</td>
<td>n/a</td>
<td>£4,823</td>
<td>n/a</td>
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<td>15. Workshop and District CU.</td>
<td>2000</td>
<td>Durham</td>
<td>2001</td>
<td>124</td>
<td>£31,172</td>
<td>£17,761</td>
<td>£12,476</td>
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